NO. S1510120
VANCOUVER REGISTRY

IN THE SUPREME COURT OF BRITISH COLUMBIA

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*
R.S.C. 1985, c. C-36, AS AMENDED

AND

IN THE MATTER OF THE *BUSINESS CORPORATIONS ACT,*
S.B.C. 2002, c. 57, AS AMENDED

AND

IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF WALTER ENERGY CANADA HOLDINGS, INC. AND THE OTHER PETITIONERS LISTED ON SCHEDULE "A"

PETITIONERS

UNITED MINE WORKERS OF AMERICA
1974 PENSION PLAN AND TRUST
BOOK OF AUTHORITIES RE: EXPERT REPORT OF JUDITH F. MAZO
(SERVED NOVEMBER 24, 2016)

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31 29 U.S.C.A. § 1423. Repealed

32 29 U.S.C.A. § 1424. Repealed

33 29 U.S.C.A. § 1425. Repealed

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34 2016 Annual Report of the Pension Benefit Guaranty Corporation

35 Opinion Letter of Pension Benefit Guaranty Corporation dated for reference May 5, 1997

470 F.Supp. 945
United States District Court, D. Massachusetts.

PENSION BENEFIT GUARANTY CORPORATION, Plaintiff,
and
United Rubber, Cork, Linoleum and Plastic Workers of America, Solomon, Reddix, and Alex Williams, Plaintiff-Intervenors,
v.
OUIMET CORPORATION, Ouimet Stay & Leather Company, Ouimet Welting Company, EmilR. Ouimet Wareham Trust, Avon Sole Company, Tenn-Ero Corporation and HerbertKahn, Trustee, Defendants.

Civ. A. Nos. 76-1314-T, 77-2005-T.
|
March 22, 1979.

Pension Benefit Guaranty Corporation brought action pursuant to ERISA to collect amount for which defendant companies were allegedly liable as result of termination of pension plan by two bankrupt affiliates. The Bankruptcy Judge ruled that PBGC could obtain reimbursement only from the direct employer, holding defendant companies free from liability. On appeal, the District Court, Tauro, J., held that: (1) when one member of a controlled group terminates an underfunded pension plan, entire group may be held liable by the PBGC for purposes of reimbursement under termination liability provisions of ERISA; (2) termination liability provisions of ERISA meet Fifth Amendment's requirement of due process, and (3) PBGC was not required to issue waiver merely because it received notification of termination of pension plan within statutory period.

Order accordingly.

Attorneys and Law Firms

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Richard Maloney, Maloney, Williams & Baer, Boston, Mass., for the Ouimet Group.

Bertram Diamond, Stamford, Conn., Harold B. Roitman, Boston, Mass., for intervenors, URW, Reddix and Williams.

OPINION

TAURO, District Judge.

At issue here is whether the defendants, several business entities under common control, [1] may be held jointly and severally liable for the termination of an underfunded pension plan by two of their bankrupt affiliates. The plaintiff is the Pension Benefit Guaranty Corporation (PBGC), a creature of Congress born under the provisions of the Employment Retirement Income Security Act (ERISA), 29 U.S.C. s 1302. The prime purpose of that Act is to insure that workers receive the benefits to which they are entitled under private pension plans established for them by their employers. Congress recognized that workers had been unfairly subjected to the loss of expected benefits when underfunded plans terminated. Under ERISA, Congress gave the PBGC the responsibility of administering terminated pension plans to the end that affected workers receive anticipated pension benefits promised them by their employers. It is the PBGC's attempt to administer certain terminated pension plans that underlies this litigation. [2]

I.

PROCEDURAL BACKGROUND

PBGC began this action in April, 1976, pursuant to ERISA, to collect the amount for which the defendant Ouimet companies are allegedly liable as a result of the termination of a pension plan by their two affiliates, the Avon Sole Company (Avon) and the Tenn-ERO corporation (Tenn-ERO). Those two corporations had been adjudicated bankrupt on March 22, 1976. On August

20, 1976, the case was referred to the Bankruptcy Judge sitting as a Master pursuant to Fed.R.Civ.P. 53.

In his report, the Bankruptcy Judge concluded that section 1362 of ERISA [3] permitted the PBGC to obtain reimbursement only from the direct employers, Avon and Tenn-ERO. The other members of the controlled group [4] were held to be free from liability arising out of the termination of Avon/Tenn-ERO's pension plan. The Bankruptcy Judge also determined that ***948** Avon and Tenn-ERO were not liable to the PBGC because they had no net worth. [5]

PBGC subsequently appealed the rulings of the Bankruptcy Judge to this court and has also moved to: (1) modify the Master's Report insofar as it finds no liability on the part of the defendant companies; (2) recommit the case to the Master for findings relative to the net worth of the Ouimet controlled group; and (3) enter partial summary judgment for PBGC.

II.

FACTUAL BACKGROUND

Avon operated a plant in Massachusetts until March, 1975. In 1973, it formed Tenn-ERO, a wholly owned subsidiary. The companies experienced severe operating losses and on March 22, 1976, were adjudicated bankrupts.

As of the time Avon's Massachusetts plant was closed in 1975, the company was a party to a pension plan agreement, dated May 4, 1959, covering its unionized employees. When Avon shut down its plant, it notified PBGC, as required by ERISA, [6] that it would soon discontinue operations in Massachusetts and would be required to terminate its pension plan.

Through no illegal or improper conduct on Avon's part, its plan was underfunded when terminated. The primary reasons for the underfunding were that the market value had fallen on certain of the investments comprising plan assets and that the amortization of past underfunded liabilities was not yet complete. See 29 U.S.C. s 1082.

III.

THE CONTROLLED GROUP

The ownership picture of the defendant companies, outlined in footnote 1 Supra, has significance because of PBGC's position that each of them may be held to make good the deficiencies of the Avon/Tenn-ERO pension plan. [7] PBGC's theory is that, for purposes of section 1362 liability, the term "employer" includes not only the direct employer of the covered employees, but also all trades or businesses under common control with the direct employer.

At a hearing held before this court on March 6, 1978, the parties agreed that Ouimet, Stay and Welting are a controlled group as that term is defined in the IRC. They also agreed that Brockton should not be so included. They dispute, however, whether the Trust may be considered a member of the controlled group.

Defendants seek to have the Trust excluded from the controlled group on the ground that it is not a trade or business within the meaning of section 4001(b) of ERISA, 29 U.S.C. s 1301(b). [8] The Trust, by ***949** its terms, is a typical Massachusetts business trust, authorizing the operation of a profit sharing enterprise business. See Morrissey v. Commissioner, 296 U.S. 344, 56 S.Ct. 289, 80 L.Ed. 263 (1935). Indeed, the Trust's tax returns show it to be engaged in the real estate business. One of its corporate affiliates, Stay, has a five year lease on a parcel of improved real estate owned and managed by the Trust.

[1] Defendants argue further that section 1301(b) applies only to trades or businesses with employees, and because the Trust has no employees, it may not be deemed an employer. That argument depends on tortured statutory interpretation. The first sentence of section 1301(b) makes it clear that the Trust could be included in the controlled group as an employer although it may have no employees:

> An individual who owns the entire interest in an unincorporated trade or business is treated as his own employer, ...

Emil Ouimet, who owns 100% Of the Trust, would be considered his own employer. This court therefore holds that section 1301(b) includes all trades or businesses that are under common control, regardless of whether they have employees.

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Given the parties' stipulation that Brockton should be excluded, and the fact that Stay owns only 50% Of that company,[9] this court finds that the Trust, Stay, Welting, Ouimet and Avon/Tenn-ERO are all members of the same controlled group of businesses.

IV.

CONTROLLED GROUP LIABILITY UNDER ERISA

[2] The issue of controlled group liability for termination of underfunded pension plans is one of first impression. Analysis of the statute and review of the legislative history[10] leads this court to conclude that when one member of a controlled group terminates an underfunded pension plan, the entire group may be held liable by the PBGC for purposes of reimbursement under section 1362 of ERISA.

A) The Statute

[3] **[4]** **[5]** As the governmental agency in charge of administering the statutory plan of ERISA, the PBGC has interpreted section 1362 as imposing liability on all trades and businesses under common control when an employer within the group terminates an underfunded plan. That determination is subject to challenge and judicial review. 29 U.S.C. s 1303(f); 5 U.S.C. ss 701, 702.[11] A ***950** reviewing court must be guided by the construction given a statute by the agency charged with its execution, unless there are compelling indications that it is wrong. Columbia Broadcasting System, Inc. v. Democratic National Committee, 412 U.S. 94, 121, 93 S.Ct. 2080, 36 L.Ed.2d 772 (1973). Here there are no such indications. Indeed, strong support for the agency's interpretation can be found on the face of the statute itself.

The second sentence of 29 U.S.C. s 1301(b) states:

> For purposes of this subchapter, under regulations prescribed by the corporation, all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer and all such trades and businesses as a single employer (emphasis added).[12]

The provisions of section 1301 are contained in the same subchapter as are those of section 1362, the section imposing liability for reimbursement upon an employer who maintains an underfunded plan at the time of termination. The PBGC argues that section 1301(b) defines "employer" as that term is used in section 1362. Under this theory, the entire control group would be an employer for purposes of section 1362 liability, regardless of whether each member of the group actually contributed to the pension plan. Thus, all members of the controlled group would be potentially liable, jointly and severally, should an affiliate terminate an underfunded plan.

Defendants urge contrary interpretations of sections 1301(b) and 1362.[13] They start by noting that, under section 1362, an employer must "maintain" a plan in order to be held liable. Maintaining a plan is viewed by defendants as being synonymous with contributing to a plan. Defendants conclude, therefore, that because members of the controlled group in this case did not contribute to the terminated plan, they cannot be held liable under section 1362.

This argument hinges upon defendants' contention that section 1301(b) is not a definition of "employer" for the purposes of section 1362, but was merely intended to supplement a provision in section 1301(a). Defendants' theory is based upon the following rationale. Section 1301(a)(3) of ERISA provides that a "multi-employer plan" means a "multi-employer plan" as defined in section 414(f) of the IRC. That IRC provision defines a multi-employer plan as one to which more than a single employer is required to contribute.[14] A significant "special rule" in that section provides, however, that all corporations which are members of a controlled group of corporations shall be deemed to be one employer. 26 U.S.C. s 414(f)(2)(B). Defendants argue that the purpose of section 1301(b) is to modify section 1301(a) by extending the "special rule" enunciated in section 414(f)(2)(B), to the end that all members of a controlled group, whether or not incorporated, are deemed to be one employer.

Under defendants' theory, therefore, section 1301(b) does not abrogate the section 1362 requirement that a member of a common controlled group must "maintain" a plan in order to be held liable. The controlled group defendants in this case did not contribute to the Avon plan. They argue, therefore, that they did not "maintain" that ***951** plan and so have no section 1362 termination liability.

Defendants' interpretations of sections 1301(b) and 1362 fall short for three reasons. First, section 1301, in both the codified and uncodified versions, is labelled as a definitional section. It is difficult to accept the theory that Congress fleshed out the definitions contained in section 1301(a), by adding a separate subsection, 1301(b), rather than simply adding necessary language to section 1301(a).

Second, the definition at issue in 1301(b) is prefaced by the language "For purposes of this subchapter. . . ." (emphasis added). This clear, unequivocal explanatory phrase supports PBGC's contention that the definitions of section 1301(b) were intended to apply to the entire subchapter, and not merely as a supplement to a definition in section 1301(a). Defendants read "(f)or the purposes of this subchapter" to mean "(f)or the purposes of this section." In doing so, they overindulge themselves with poetic license.

Finally, it is by no means apparent that the word "maintain" means only "contribute." Regrettably, "maintain" is not defined in the statute. Defendants, however, rely upon an earlier version of section 1362, proposed by the House of Representatives, in support of the argument that the terms "maintain" and "contribute" were intended to be interchangeable.

> SEC. 414 (a) Subject to subsection (e), where the employer or employers Contributing to the terminating plan or who terminated the plan are not insolvent . . . such employer or employers (or any successor in interest to such employer or employers) shall be liable to reimburse the Corporation (PBGC) for any insurance benefits paid by the Corporation . . . .

H.R. 2, 93d Cong., 2d Sess. s 414(a), 120 Cong.Rec. 4733 (1974) (emphasis added). [15]

Actually, that bit of legislative history cuts the other way. The fact that Congress expressly substituted the word "maintain" for the word "contributing" in the final draft of section 1362 serves to undermine defendants' claim that the two terms are synonymous. It is reasonable to infer that the substitution was substantive rather than merely cosmetic. This court interprets the substitution as being a recognition by Congress that it would be inconsistent to impose liability on a controlled group under section 1301, while at the same time limiting liability under section 1362 to those who actually contribute to a pension plan. [16]

Another argument advanced by defendants is that to incorporate by reference the definition in section 1301(b) into section 1362(a) would render superfluous subsection (d) of 1362. The latter subsection extends liability to successor corporations when the direct employer has ceased to exist by virtue of a reorganization, merger, consolidation or liquidation into a parent corporation. Under the view taken by defendants, this subsection is unnecessary if the term "employer," as used in section 1362(b), already includes both a subsidiary and its parent. Defendants' argument ignores, however, the fact that the term "parent" is not defined directly in ERISA. Rather, section 1563(a) of the Internal Revenue Code, which is indirectly referenced in ***952** section 1301(b) of ERISA, [17] requires that a parent own at least 80% Of the voting stock of a corporation for that combination to qualify as being controlled. Because section 1301(b) and section 1362(b) impose liability only upon controlled groups, and not parents, a parent cannot qualify as a single employer of a controlled group under sections 1301(b) and 1362(b) unless it owns at least 80% Of its subsidiary's stock. Other Treasury regulations, however, specifically define "parent" as an entity which owns as little as 50% Of the subsidiary's stock. See, e. g., Treas.Reg. 1.351-1(c)(4). Thus, section 1362(d)(2) does have independent significance in that it would trigger termination liability if a parent owned less than 80% Of a subsidiary's stock, and the other requirements of that subsection were satisfied. The defendants, therefore, are incorrect in their contention that the PBGC's interpretation of Title IV would deprive section 1362(d)(2) of any substantial meaning.

A further argument advanced by defendants is that PBGC's interpretation of section 1301(b) is incompatible with section 1107(d)(7) of ERISA. [18] That section limits

the percentage of employee pension funds that may be invested in the securities or real property of employer or employer-affiliates. The term employer-affiliate is defined as,

a member of any controlled group of corporations . . . of which the employer who maintains the plan is a member. 29 U.S.C. s 1107(d)(7).

This definition, however, does not conflict with the PBGC's view that the term "employer," as used in section 1362, includes controlled group affiliates of the direct employer. Section 1301(b) explicitly defines the term "employer" for the purposes of Title IV of the Act, which includes section 1362. Section 1107 is not contained in Title IV. A facially inconsistent definition of "employer" or "employer affiliate" contained in another Title of ERISA has little relevance to the provisions of Title IV which contains its own definitions of those terms.

Defendants assert that it would be unjust to hold them liable for a terminated plan to which they do not individually contribute because the Internal Revenue Code does not permit anyone but the direct employer to take deductions for contributions made to a pension plan.

Section 404(a) of the IRC, provides that, subject to certain limitations, contributions paid by an employer to an employee pension plan are deductible. Subsection (g) of 404 states that,

> For purposes of this section any amount paid by an employer under section 4062 . . . or 4064, (29 U.S.C. ss 1362, 1364) of the Employee Retirement Income Security Act of 1974 shall be treated as a contribution to which this section applies by such employer to or under a stock bonus, pension, profit-sharing, or annuity plan.

Although this subsection clearly covers termination liability payments under ERISA, defendants assert that this IRC provision does not allow an affiliated employer to deduct contributions made to a pension plan covering the employees of another member of a controlled group. In support of that interpretation they point to Revenue Ruling 69-35, 1969-1 C.B. 117, 118, which states:

> (A)mounts contributed under this plan by the corporation that is not the employer of those benefiting from the contribution are not deductible under section 404 of the Code unless they constitute 'make-up' contributions within the purview of section 404(a)(3)(B) and then only to the extent therein provided.

This ruling, however, was handed down in 1969, five years prior to the passage of ERISA, and clearly reflects the concern of the Treasury Department that affiliated corporations might vary annual contributions to a pension plan solely to maximize ***953** favorable tax consequences. Prior to ERISA, therefore, the Treasury Department did not allow affiliates to make tax deductible contributions unless they qualified as employers under the relevant provisions of the IRC.

With the enactment of ERISA in 1974, however, the Treasury Department modified its interpretation of section 404 of the IRC. In a letter to the PBGC, the Treasury Department has stated that reimbursement payments required to be made to the PBGC by an affiliate that is considered an employer under sections 1362 or 1364 by application of section 1301(b), may be deducted pursuant to section 404(g) of the Code. The letter notes that section 404(g) is limited by its literal terms to payments made to the PBGC. It goes on to state that the Internal Revenue Service agrees with the Treasury Department's interpretation of section 404(g). Thus, under the view taken by three government entities, the PBGC, the Treasury Department, and the Internal Revenue Service, payments made by a controlled group affiliate to the PBGC in response to ERISA termination liability are tax deductible. The IRC, therefore, recognizes the potential burden of imposing non-deductible termination liability upon a member of a controlled group, and makes provision to ease that burden.[19]

B) Legislative History

Although this court finds that the statutory language of ERISA is relatively clear and unambiguous, a review of the legislative history in this case only reinforces the court's conclusion. ERISA imposes termination liability

on all affiliates of a controlled group. Congressional intent is expressed clearly in the Report of the Conference Committee:

> In determining the employer who may be liable for the insurance coverage losses of the corporation (PBGC), all trades or businesses (whether or not incorporated) under common control are to be treated as a single employer.

H.Conf.Rep.No.93-1280, 93d Cong., 2d Sess. 376 (1974), Reprinted in 1974 U.S.Cong.Code & Admin.News pp. 4639, 5155.

The conferees again emphasized the controlled group concept when they discussed the termination liability provisions of 29 U.S.C. s 1364. Under section 1364, termination liability was extended to multi-employer plans, with the controlled group treated as a single employer for the purposes of determining the liability of each individual employer.[20] As the Report noted:

In this regard, it should be noted that the affiliated employer rules are to apply in ***954** this area. That is, if one member of an affiliated group has employer liability, then that liability is to extend to the entire affiliated group. Also, the 30-per-cent-of-net-assets limit is to apply with respect to the net assets of the entire group.

H.Conf.Rep.No.93-1280 at 380, 1974 U.S.Cong.Code & Admin.News at 5159. There is nothing in the Committee Report that lends support to defendants' contention that a controlled group employer must "contribute" to a plan in order for termination liability to attach. To the contrary, the Report demonstrates an intention to extend liability unconditionally to the entire affiliated group.

Defendants counter with the argument that because none of the early House and Senate bills mentioned the controlled group liability theory, the Conference Committee violated a congressional rule by considering and including in a report "matter not committed to (it) by either House." 2 U.S.C. s 190c. 2 U.S.C. s 190c permits the Conference Committee to make "germane modification of subjects in disagreement." One of the matters assigned to the Committee for mediation was a dispute between the two legislative bodies regarding the scope of employer liability. The House bill made an employer liable for 50% Of its net worth. The Senate wanted a liability provision for only 30%. The Conference Committee adopted the Senate version and went on to determine that an employer's net worth included the assets of all the companies in a controlled group. See H.Conf.Rep.No.93-1280 at 376, U.S.Cong.Code & Admin.News at 5155. Such a determination was within the scope of matters assigned to the Committee for resolution.

[6] **[7]** This court holds, therefore, that section 1301(b) defines the word " employer" for the purposes of determining section 1362 liability. Thus, the PBGC may impose termination liability, jointly and severally, on each member of a controlled group, whether or not such member contributed to the terminated pension plan.

V.

CONSTITUTIONAL ISSUES

Prior to ERISA, no federal law required pension plans to be fully funded. Defendants argue that imposing retrospective liability under ERISA on employers who established and maintained pension plans prior to its passage violated their Due Process rights under the Fifth Amendment.

[8] It is well established that "legislation readjusting rights and burdens is not unlawful solely because it upsets otherwise settled expectations." Usery v. Turner Elkhorn Mining Co., 428 U.S. 1, 16, 96 S.Ct. 2882, 2893, 49 L.Ed.2d 752 (1976). See also Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 98 S.Ct. 2716, 57 L.Ed.2d 727 (1978) (Brennan, J., dissenting). In determining the constitutionality of a statute with retrospective effect, a court must consider the nature and strength of the public interest served by the legislation. Hochman, The Supreme Court and the Constitutionality of Retroactive Legislation, 73 Harv.L.Rev. 692, 697 (1960). In Turner Elkhorn the Supreme Court upheld mining safety legislation imposing liability on employers for disabilities incurred by employees whose employment had terminated prior to the date of the enactment of the statute.[21] Finding the statute to be remedial ***955** in nature, the Court sustained it on the ground that it was a rational measure which transferred the consequences of employment from the injured employee to the employer who had profited from his labor. 428 U.S. at 18, 96 S.Ct. 2882.

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The Court in Turner Elkhorn distinguished Railroad Retirement Board v. Alton R. R. Co., 295 U.S. 330, 55 S.Ct. 758, 79 L.Ed. 1468 (1935), on which defendants rely. The Alton Court had invalidated as arbitrary a statute requiring employers to finance pensions for former employees of the railroads. The Court there found that such a requirement bore no rational relationship to the Act's underlying purpose of encouraging early retirement, but served only to supplement the salaries of former employees who had already retired.

[9] It is questionable, in any event, whether Alton retains vitality in light of the Court's recent approach to substantive due process analysis. [22] Remedial legislation is no longer subject to strict scrutiny. Plaintiffs need not demonstrate a compelling public interest to justify the change in employer responsibility imposed by ERISA.

The Fifth Amendment, in the field of federal activity, and the Fourteenth, as respects state action, do not prohibit governmental regulation for the public welfare. They merely condition the exertion of the admitted power, by securing that the end shall be accomplished by methods consistent with due process. And the guaranty of due process, as has often been held, demands only that the law shall not be unreasonable, arbitrary or capricious, and that the means selected shall have a real and substantial relation to the object sought to be attained.
Nebbia v. New York, 291 U.S. 502, 525, 54 S.Ct. 505, 510-511, 78 L.Ed. 940 (1934).

[10] **[11]** The Due Process Clause clearly places greater limitations upon Congress' power to legislate retrospectively rather than prospectively. Congressional acts, however, are presumed constitutional. The party challenging them has the burden of establishing that Congress acted in an arbitrary and irrational manner. Usery v. Turner Elkhorn Mining Co., 428 U.S. at 15, 96 S.Ct. 2882. Defendants here have failed to demonstrate that application of the controlled group liability concept would be arbitrary or unreasonable. ERISA was enacted to remedy a serious social problem, the loss and frustration experienced by employees deprived of vested benefits as a result of a pension plan termination. See S.Rep.No.93-383, 93d Cong., 2d Sess., Reprinted in 1974 U.S.Cong.Code & Admin.News at 4902. Cf. Hoefel v. Atlas Tack Corp., 581 F.2d 1, 4 (1st Cir. 1978).

One purpose of ERISA is to supplement and enforce federal labor law by preventing employers from promising more than they can deliver by way of benefits when negotiating collective bargaining agreements. The employer liability provisions of Title IV directly serve the primary goal of the pension reform effort, the voluntary continuation and maintenance of private pension plans. Application of the controlled group liability theory fosters that purpose by preventing employers from using corporate segmentation as a shield from termination liability. [23] The statute reflects Congress' judgment that, without controlled group liability, businesses could juggle their activities to eviscerate the termination liability provisions of ERISA. Such prophylactic legislation is valid when applied indiscriminately on an across-the-board basis.

(A) remedial provision (may require) some individuals to submit to regulation who do not participate in the conduct the legislation was intended to deter or control. (I)n defining a class subject to regulation, "(t)he inclusion of a reasonable ***956** margin, to insure effective enforcement, will not put upon a law, otherwise valid, the stamp of invalidity." Nothing else will meet the demands of our complex economic system.
Mourning v. Family Publications Service, Inc., 411 U.S. 356, 374, 93 S.Ct. 1652, 1663, 36 L.Ed.2d 318 (1973) (citations omitted).

The Supreme Court's decision in Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 98 S.Ct. 2716, 57 L.Ed.2d 727 (1978), does not undercut the PBGC's contention that the employer liability concepts of ERISA meet due process requirements. In Allied, the Court examined the constitutionality of a pre-ERISA Minnesota statute that imposed a charge on pension plans not funded sufficiently to cover employees who had worked at least ten years. The Minnesota Act was triggered if an employer either terminated a pension plan or closed a Minnesota office. The Court found the Minnesota statute impaired existing employer-employee obligations and, therefore, was unconstitutional under the provisions of the contract clause. [24] Allied is at least facially distinguishable, because ERISA is a federal law not subject to the strictures of the contract clause. In any event, the challenged provisions of ERISA meet the substantive tests imposed by Allied.

" 'Legislation adjusting the rights and responsibilities of contracting parties must be upon reasonable conditions

and of a character appropriate to the public purpose justifying its adoption.' " 438 U.S. at 244, 98 S.Ct. at 2722, Quoting United States Trust Co. v. New Jersey, 431 U.S. 1, 22, 97 S.Ct. 1505, 52 L.Ed.2d 92 (1977). The first inquiry under Allied is whether the challenged statute has substantially impaired a contractual obligation.

[12] **[13]** **[14]** Here, the provisions of the Avon pension plan gave the company the right to "amend, modify, suspend or terminate the Plan" and limited the benefits payable upon termination of the plan to "the assets then remaining in the Trust Fund." Public policy requires that pension plans be construed to avoid the forfeiture of rights earned by an employee through years of service. [25] Given that policy, this court holds that the imposition of termination liability for vested benefits in this case would not substantially impair the provisions of the Avon plan, certainly not to the degree that impairment was present in Allied. There, Minnesota law imposed employer liability to cover full pension benefits, whether or not vested, for all ten year employees. By contrast, ERISA imposes liability only for those benefits that have vested in accordance with the terms of a plan. [26]

The difference in contractual impairment between section 1362 of ERISA and the Minnesota statute is a significant one. The First Circuit has recently stated its support for the position that the promise of a pension constitutes an offer which, upon performance of the required services by the ***957** employee, becomes a binding obligation. Hoefel v. Atlas Tack Corp., 581 F.2d at 4. [27] Cf. International Union, United Automobile, Aerospace & Agricultural Implement Workers of America v. Atlas Tack Corp., 590 F.2d 384 at 386 (1st Cir. 1979). Thus, the vesting of benefits becomes a significant event that prevents the employer from revoking the offer. Other courts have also noted that the vesting of benefits changes a revocable offer into a binding obligation, and have refused to enforce disclaimer language similar to that in the Avon plan to deprive employees of vested benefits. See, e. g., Cantor v. Berkshire Life Insurance Co., 171 Ohio St. 405, 171 N.E.2d 518, 522 (1960).

Given this view of the law, it seems dubious that the imposition of termination liability for vested benefits would undermine any reliance interest that the defendants may have had in the disclaimer language of the Avon plan. The Minnesota statute in Allied, however, went much farther than ERISA in disrupting settled contractual expectations. As noted above, the statute imposed liability for benefits that had not vested under the terms of a plan. In essence, this meant that the employer was held to his promise before the consideration required by the offer had been rendered. The effect on reliance interests was significant. As the Supreme Court noted:

> The company . . . had no reason to anticipate that its employees' pension rights could become vested except in accordance with the terms of the plan. It relied heavily, and reasonably, on this legitimate contractual expectation in calculating its annual contributions to the pension fund.

438 U.S. at 245-246, 98 S.Ct. at 273. [28]

The negligible infringement of employer reliance interests distinguishes ERISA from the Minnesota statute at issue in Allied. It is appropriate, however, to note other differences between the two statutes. First, employer liability could be triggered under Minnesota law solely by a company closing its Minnesota office. The closing of an office was, in fact, the basis of liability in Allied. The statutory scheme of ERISA, however, bears a more substantial relation to the problem of termination liability. Under its terms, employer liability is triggered only by formal termination of an underfunded plan. [29] Second, under the ***958** Minnesota law an employer was held responsible for the full pensions of all employees if the plan was determined to be insufficient. By contrast, ERISA tempers the financial impact of termination liability by limiting it to no more than 30% Of the employer's statutory net worth and authorizing equitable deferred payment arrangements. 29 U.S.C. ss 1362(b)(2), 1367. Moreover, during the first nine months after ERISA was enacted, a period applicable to the termination of the Avon plan, the PBGC had the authority to reduce employer liability or waive it altogether in the case of unreasonable hardship. 29 U.S.C. s 1304(f)(4).

This court finds that the termination liability provisions of ERISA upset settled contractual expectations only to a minimal degree. This limited impairment, when balanced against a statutory purpose of protecting against unwarranted and unjust employee deprivation, contrasts sharply with the underlying circumstances in Allied.

Defendants' final constitutional claim is that the liability imposed by ERISA is in the nature of a tax or penalty. This contention fails in light of the enunciated purposes of ERISA, which show it to be entirely remedial in nature. See 29 U.S.C. s 1001.

[15] For the reasons stated above, this court holds that the termination liability provisions of ERISA meet the Fifth Amendment's requirement of due process.

VI.

Defendants assert that even if they are collectively liable as a controlled group under ERISA, the PBGC should have waived liability under 29 U.S.C. s 1304(f)(4). That section gave the agency discretion to waive or reduce employer liability for a plan which terminated within the first 270 days after enactment of the statute, provided the agency determined that the employer was not able to continue the plan and that an assessment of liability would result in unreasonable hardship. [30]

PBGC maintains that the Ouimet group is not eligible for a waiver or reduction of liability under section 1304(f)(4) because it did not request a waiver within the statutory period, although it did notify the agency that the plan would be terminated within that period. Such notification is required. 29 U.S.C. s 1341.

[16] Defendants are correct in observing that the Act does not require an employer to make a formal request for a waiver. They are incorrect, however, in interpreting section 1304(f)(4) to require the agency to issue a waiver merely because it received a notification of termination within the statutory period. The Act specifically grants the PBGC discretion to determine whether liability will be waived.

PBGC's position is that it received many notices of pending plan terminations within the first 270 days after enactment of ERISA. Given the relatively short amount of time available to assess the financial conditions of terminating employers, PBGC relied upon the employers themselves to assess their economic situations and request waivers if needed. PBGC then deployed its limited resources to investigate whether the companies requesting waivers met the statutory conditions. Under the circumstances, such an approach cannot be said to have been unreasonable.

[17] Defendants seek to have this issue remanded to the agency for a determination on the merits of their right to a waiver. Regardless of the equities of such an approach, this court has no power to do so. ERISA empowers the PBGC to absolve employers ***959** of liability "for Only the first 270 days" after enactment. 29 U.S.C. s 1304(f) (emphasis added). The time during which the agency had the authority to exercise its discretion has long since passed. [31]

CONCLUSION

For the reasons stated above, this court ORDERS that PBGC's motions for partial summary judgment and for relief from the automatic stay in bankruptcy are hereby granted. It is further ORDERED that this case is remanded to the Bankruptcy Court for a determination of the net worth of the defendant controlled group, as it has been defined in this opinion.

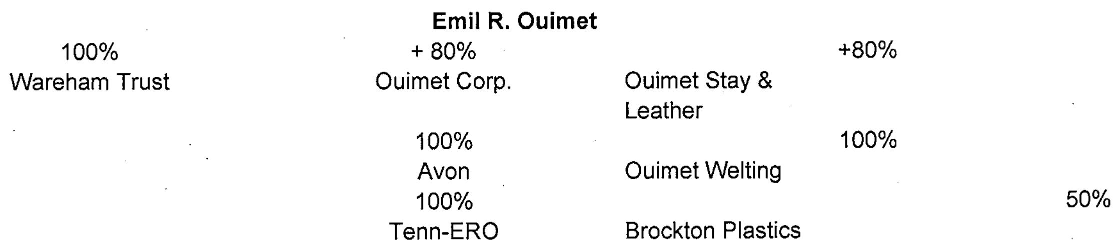
An order will issue.

All Citations

470 F.Supp. 945

Footnotes

1 The relationship of the defendant businesses is demonstrated in the diagram below:



2 The PBGC is funded primarily through the payment of insurance premiums by pension plan employers. It also receives funds by way of the reimbursement provisions of sections 4062-64 of the Act, 29 U.S.C. ss 1362-64. Section 1362, the provision at issue here, requires an employer terminating an underfunded plan to pay the PBGC either the deficit between the plan's guaranteed benefits and the plan's remaining assets or 30% Of the employer's remaining net worth, whichever is less.

3 29 U.S.C. s 1362 provides, in relevant part:

(a) This section applies to any employer who maintained a plan (other than a multiemployer plan) at the time it was terminated, ...

(b) Any employer to which this section applies shall be liable to the corporation, in an amount equal to the lesser of

(1) the excess of

(A) the current value of the plan's benefits guaranteed under this subchapter on the date of termination over

(B) the current value of the plan's assets allocable to such benefits on the date of termination, or

(2) 30 percent of the net worth of the employer determined as of a day, chosen by the corporation but not more than 120 days prior to the date of termination, computed without regard to any liability under this section.

4 The Ouimet Corporation (Ouimet), Ouimet Stay & Leather Company (Stay) and Ouimet Welting Company (Welting).

5 Since an employer's maximum liability under section 1362 cannot exceed 30% Of its net worth, See n. 2 Supra, a company which has no ascertainable net worth cannot be held liable to the PBGC for purposes of reimbursement.

6 See 29 U.S.C. s 1341.

7 The Bankruptcy Judge found that the relationship of the companies in the Ouimet group made them a controlled group within the meaning of 26 U.S.C. s 1563(a)(3). This section of the Internal Revenue Code (IRC) is indirectly incorporated by reference into ERISA by 29 U.S.C. s 1301(b) in the following manner: Section 1301(b) provides that all regulations promulgated by PBGC relative to controlled group employers shall be consistent with 26 U.S.C. s 414(c). Section 414(c) of the IRC provides that all employees of trades and businesses under common control, whether or not incorporated, are to be treated as employed by a single employer. It states that regulations prescribed under that subsection shall be based on principles similar to those which apply in section 414(b). That subsection states that all employees of corporations which are members of a controlled group of corporations are to be treated as employed by a single employer. It refers to 26 U.S.C. s 1563(a) for the definition of a controlled group.

8 Section 1301(b) provides:

An individual who owns the entire interest in an unincorporated trade or business is treated as his own employer, and a partnership is treated as the employer of each partner who is an employee within the meaning of section 401(c)(1) of Title 26. For purposes of this subchapter, under regulations prescribed by the corporation, all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer and all such trades and businesses as a single employer. The regulations prescribed under the preceding sentence shall be consistent and coextensive with regulations prescribed for similar purposes by the Secretary of the Treasury under section 414(c) of Title 26.

9 26 U.S.C. s 1563(a) provides that the common parent must hold at least 80% Of the voting stock of all the sibling subsidiaries for those subsidiaries to qualify as members of a controlled group.

10 Prior to examining legislative history, it is appropriate to first determine if the statutory language is clear and unambiguous. If it is, then there is no need to examine extrinsic sources, such as legislative history, to aid in statutory construction. Preterm Inc. v. Dukakis, 591 F.2d 121, 128, 135-136 (1st Cir. 1979).

11 Section 4003(f) of the Act, 29 U.S.C. s 1303(f), provides:

Any participant, beneficiary, plan administrator, or employee adversely affected by any action of the corporation, or by a receiver or trustee appointed by the corporation, with respect to a plan in which such participant, beneficiary, plan administrator or employer has an interest, may bring an action against the corporation, receiver, or trustee in the appropriate court. For purposes of this subsection the term "appropriate court" means the United States district court before which proceedings under sections 1341 or 1342 of this title are being conducted, or if no such proceedings are being conducted the United States district court for the district in which the plan has its principal office, or the United States district court for the District of Columbia. The district courts of the United States have jurisdiction of actions brought under this subsection without regard to the amount in controversy.

The second line of the above quoted section contains a typographical error. The section provides that "any participant, beneficiary, plan administrator or Employee " may bring suit in federal court against the PBGC, if adversely affected by a determination by that agency. The word "employee" should read "employer."

Section 10(a) of the Administrative Procedure Act, 5 U.S.C. s 702, grants the right of judicial review to anyone adversely affected or aggrieved by agency action unless another statute expressly or impliedly forbids the relief sought. The PBGC is clearly a governmental agency within the meaning of that section. See 5 U.S.C. s 701(b)(1).

12 The regulations promulgated by PBGC pursuant to the authority vested in the agency under section 1301(b) virtually echo the wording of the statute. See 29 C.F.R. ss 2612.1-.3.

13 The substance of defendants' first argument was advanced in a recent law review article. Note, Termination Liability Under Title IV of ERISA: Impact on Companies Under Common Control, 27 Case W.Res.L.Rev. 945 (1977).

14 Under certain provisions of ERISA, participants in multi-employer plans are treated differently from single employers who maintain plans. See note 20 Infra.

15 Cited in Note, Termination Liability Under ERISA, supra n. 13 at 957.

16 Defendants also argue that PBGC misconstrues the plain meaning of section 1301(b) by its reading that all trades or businesses under common control shall be treated as a single employer. This construction, according to defendants, fails to take into account the importance of the word "such" in the second sentence of that section. Under defendants' statutory analysis, the word "such" indicates that only "when employees of trades or businesses under common control are to be treated as employed by a single employer, then, and For that purpose only, shall the trades or businesses be treated as a single employer." Joint Memorandum of Law of Trustee in Bankruptcy and Defendants at 21. It is defendants' construction, and not plaintiff's, which strains the plain meaning of the statute. The term "such trades and businesses" clearly refers to the section's prior language "trades and businesses (whether or not incorporated) which are under common control."

17 See n. 7 Supra.

18 See Note, Termination Liability Under ERISA, supra n. 13 at 960.

19 This court's conclusion with respect to PBGC's right to proceed against all affiliates of a controlled group does not serve to disadvantage the creditors of the bankrupts, Avon and Tenn-ERO. PBGC may assert a claim for up to thirty percent of the net worth of the entire controlled group. By applying the net worth of the entire controlled group, the bankruptcy estate will probably be exhausted, and the unsecured general creditors will receive little or no dividend. This result, though painful to creditors, might occur even if the bankrupts were not included in the controlled group. PBGC's termination liability claims have priority over other creditors, and are to be treated "in the same manner as a tax due and owing to the United States for purposes of the Bankruptcy Act . . . ." 29 U.S.C. s 1368(c)(2). Under the Bankruptcy Act, 11 U.S.C. s 104, a tax claim owed to the United States is a priority debt, payable "in advance of the payment of dividends to creditors . . . ." The recent revision of the Bankruptcy Act also gives priority to a tax claim. See 11 U.S.C. s 507(a)(6) (1979) (effective October 1, 1979).

The practical consequence here, therefore, is that even if the PBGC were not permitted to assert a claim against the bankrupts for up to 30% Of the controlled group's net worth, it could, nonetheless, assert a priority lien in the bankruptcy court against the bankrupts and probably submerge any claims of general creditors.

20 Under section 1364, the PBGC is required to determine, in a manner consistent with section 1362, termination liability for multiple employers maintaining a plan. There are, however, several special rules for the determination of section 1364 liability. First, the amount of termination liability allocable to each individual employer is proportionate to the amount that the employer was required to contribute to the plan over the preceding five years. Second, the limitation of employer liability in section 1362(b)(2) (30% Of the employer's net worth) is applied to each employer separately under section 1364. 29 U.S.C. s 1364(b).

As noted above, section 1362 is the appropriate termination liability provision when the plan is maintained entirely within the controlled group. Section 1364 would be applicable when the controlled group maintained a plan in conjunction with employers outside the group. For the purposes of determining liability in a multiemployer plan, however, section 1301(b) requires that the controlled group be treated as a single employer.

The failure of Congress to apportion liability among members of a controlled group may be attributed either to legislative oversight or to a determination that such apportionment is better left as a business decision.

21 Unlike the legislation upheld in Turner Elkhorn, ERISA is not wholly retrospective in its operation. The debt to the government arises only if an employer, like defendants, decides to terminate its insufficiently funded plan after the enactment date of the Act.

22 See, e. g., Williamson v. Lee Optical Co., 348 U.S. 483, 75 S.Ct. 461, 99 L.Ed. 563 (1955). See also Usery v. Turner Elkhorn Mining Co., 428 U.S. at 19, 96 S.Ct. 2882.

23 The contention that Congress has no power to achieve statutory objectives by disregarding corporate form is a notion that has long been put to rest. See, e. g., Corn Products Refining Co. v. Benson, 232 F.2d 554, 565 (2d Cir. 1956);

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Asiatic Petroleum Co. v. Commissioner, 79 F.2d 234, 237-38 (2d Cir.), Cert. denied, 296 U.S. 645, 56 S.Ct. 248, 80 L.Ed. 459 (1935).

24 That clause, in relevant part, provides:
"No State shall . . . pass any . . . Law impairing the Obligation of Contracts, ..." U.S.Const. art. 1, s 10.

25 See Hoefel v. Atlas Tack Corp., 581 F.2d at 6.

26 Under section 1362, an employer is liable only for those benefits that are guaranteed under Title IV. 29 U.S.C. s 1362(a) states that only "nonforfeitable" benefits are guaranteed. It is clear that a benefit is only nonforfeitable when an employee has complied with all of the conditions required by him or her under the terms of a plan. Once that happens, the employee has a vested interest in the plan. The terms "nonforfeitable" and "vest" are, therefore, complementary. See Nachman Corp. v. Pension Benefit Guaranty Corp., 592 F.2d 947, 955 (7th Cir. 1979). See also the PBGC definition of "nonforfeitable" for Title IV purposes in 29 C.F.R. s 2605.6(a) (1978). The fact that a pension plan contains a clause relieving an employer from liability should the plan terminate does not mean that the benefits of the plan are forfeitable. Nachman, supra at 957, Rev'g, 436 F.Supp. 1334 (N.D.Ill.1977); In re Williamsport Milk Products Co., Inc., — F.Supp. ——(M.D.Pa.1978). But see A-T-O, Inc. v. Pension Benefit Guaranty Corporation, 456 F.Supp. 545 (N.D.Ohio 1978). After defendants attempted to argue that the benefits of the Avon plan were, under the Nachman district court opinion, forfeitable and thus not guaranteeable by the PBGC, this court permitted the union representing beneficiaries of the Avon plan, as well as several beneficiaries themselves, to intervene as plaintiffs on November 17, 1978.

27 In Hoefel, the First Circuit held that a clause in a pension plan which gave the employer the right to discontinue the plan was not effective in depriving employees of vested pension rights. The court determined that the subject employees reasonably believed they would be entitled to a lifetime pension upon retirement, provided they had served the company for a specified number of years. Hoefel involved facts not found here, including employer misrepresentations, but is instructive on this issue particularly in its discussion of Boase v. Lee Rubber & Tire Corp., 437 F.2d 527 (3d Cir. 1970). In Boase, the Third Circuit held that where an employer, in "clear and unambiguous" language reserves the right to terminate a pension plan, it can do so even in a manner which deprives retired employees of earned pension benefits. The First Circuit in Hoefel stated that it would decline to follow Boase in light of the public policy which requires that pension plans be construed to avoid the forfeiture of vested pension rights. 581 F.2d at 6.

28 This court's evaluation of the reliance interests at stake here is supported by a recent Seventh Circuit decision, Nachman Corp. v. Pension Benefit Guaranty Corporation, 592 F.2d 947 (7th Cir. 1979). The pension plan at issue in that case contained disclaimer language almost identical to that here and had also terminated prior to the minimum vesting standards of Title I. In examining the constitutionality of imposing termination liability under such circumstances, the court discussed the Allied decision, comparing the reliance interests in the Minnesota statute to those in ERISA. The court found that the Minnesota statute displaced employer reliance interests far more than Title IV because it imposed liability "for payment of benefits to employees who, since they had not fulfilled service requirements, had no vested rights under the plan." The court also found that Title IV protected employee reliance interests more than the state statute because it was applicable only to vested benefits, where the employee's expectation in retirement security is particularly strong. 592 F.2d at 961-962. As the circuit court noted, the Supreme Court in Allied was unwilling to speculate that employees without reliance interests. It is clear, however, that employees do have significant reliance interests in the payment of vested pension benefits.

29 Under limited circumstances, when the shutdown of a facility may signal impending plan termination, an employer may be required to post limited security. That security is refunded if the plan does not terminate in five years, and it may be waived in appropriate situations. 29 U.S.C. ss 1362(e), 1363.

30 29 U.S.C. s 1304(f)(4) provides:
In addition to its other powers under this subchapter, for only the first 270 days after September 2, 1974 the (PBGC) may (4) waive the application of the provisions of sections 1362, 1363 and 1364 of this title to, or reduce the liability imposed under such sections on, any employer with respect to a plan terminating during that 270 day period if the corporation determines that such waiver or reduction is necessary to avoid unreasonable hardship in any case in which the employer was not able, as a practical matter, to continue the plan.

31 Assuming Arguendo that the agency still had authority to consider defendants' need for a waiver, it is doubtful this court could review the agency's decision not to entertain the claim under the Administrative Procedure Act, since the decision is one committed to agency discretion by law. See 5 U.S.C. s 701(a)(2). But see 29 U.S.C. s 1303(f).
In this connection it is also worth noting that, in light of this court's holding, the PBGC, even if it had continuing authority to waive or reduce liability, might well refuse a waiver on the ground that the controlled group, including as it does solvent employers, has the ability to either continue the plan, or reimburse PBGC without undue hardship.

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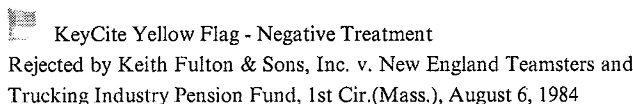

KeyCite Yellow Flag - Negative Treatment
Rejected by Keith Fulton & Sons, Inc. v. New England Teamsters and Trucking Industry Pension Fund, 1st Cir.(Mass.), August 6, 1984

630 F.2d 4
United States Court of Appeals,
First Circuit.

PENSION BENEFIT GUARANTY CORPORATION, Plaintiff-Appellee,
and
United Rubber, Cork, Linoleum and Plastic Workers of America, Solomon Reddix and Alex Williams, Plaintiffs-Intervenors-Appellees,
v.
OUIMET CORPORATION, Ouimet Stay & Leather Company, Ouimet Welting Company, Emil R. Ouimet Wareham Trust, Avon Sole Company, Tenn-ERO Corporation and Herbert Kahn, Trustee, Defendants-Appellants.

No. 79-1414.
|
Argued Dec. 4, 1979.
|
Decided Aug. 29, 1980.

Pension Benefit Guaranty Corporation brought action pursuant to ERISA to collect amount for which defendant companies were allegedly liable as result of termination of pension plan by two bankrupt affiliates. The Bankruptcy Judge ruled that PBGC could obtain reimbursement only from the direct employer, holding defendant companies free from liability. On appeal, the United States District Court for the District of Massachusetts, Joseph L. Tauro, J., 470 F.Supp. 945, found entire employer group liable and interlocutory appeal was taken. The Court of Appeals, Bownes, Circuit Judge, held that: (1) group of corporations which were under common control and which filed a consolidated tax return on which pension contributions of one corporation were deducted constituted one employer for purposes of section of ERISA governing pension plan termination insurance and it was not unfair to treat group as single employer and make it responsible for pension plan's deficit, and (2) retroactive impact of ERISA for underfunding liability was valid.

Affirmed.

Bownes, Circuit Judge, filed opinion concurring specially.

West Headnotes (8)

[1] **Labor and Employment**
Pension Benefits Guarantee Corporation; Termination Insurance

Under ERISA section dealing with common control employer for purposes of termination insurance, group of employers under common control is to be treated as single employer. Employee Retirement Income Security Act of 1974, §§ 4001(b), 4062(b), 29 U.S.C.A. §§ 1301(b), 1362(b).

5 Cases that cite this headnote

[2] **Labor and Employment**
Trade or Business Under Common Control

Term "employer" as used in a recent ERISA section dealing with liability of employer after termination of pension plan refers, in case of group under common control, to all the trades or businesses which are members of the group. Employee Retirement Income Security Act of 1974, §§ 4001(b), 4062(b), 29 U.S.C.A. §§ 1301(b), 1362(b).

27 Cases that cite this headnote

[3] **Labor and Employment**
Eligibility, Participation, and Coverage

Congress' intent to prevent evasion of ERISA was accomplished through antidiscrimination rules of Title II and vesting and participation minimums under Title I. Employee Retirement Income Security Act of 1974, §§ 2 et seq., 3001 et seq., 29 U.S.C.A. §§ 1001 et seq., 1301 et seq.

Cases that cite this headnote

[4] **Labor and Employment**

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Trade or Business Under Common Control

Congress in enacting the ERISA provision relating to control group employer intended such provision to apply to entire subchapter including section dealing with liability of employer when plan is terminated. Employee Retirement Income Security Act of 1974, §§ 4001(b), 4062(b), 29 U.S.C.A. §§ 1301(b), 1362(b).

16 Cases that cite this headnote

[5] **Labor and Employment**
Liability of Employer;Related or Successor Entities

Group of corporations which were under common control and which filed a consolidated tax return on which pension contributions of one corporation were deducted constituted one employer for purposes of section of ERISA governing pension plan termination insurance and it was not unfair to treat group as single employer and make it responsible under provisions relating to pension plan's deficit. Employee Retirement Income Security Act of 1974, §§ 407(d)(7), 4001(b), 4062, 4062(d)(2), 29 U.S.C.A. §§ 1107(d)(7), 1301(b), 1362, 1362(d)(2).

6 Cases that cite this headnote

[6] **Labor and Employment**
Retroactive Application;Effective Date

Even though pension plan contained provision limiting benefits on termination to the assets remaining in the trust fund, retroactive impact of ERISA for underfunding liability was not statutorily improper. Employee Retirement Income Security Act of 1974, § 4062(a, b), 29 U.S.C.A. § 1362(a, b).

Cases that cite this headnote

[7] **Constitutional Law**
Pensions and Benefits, Regulation Of

Labor and Employment
Retroactive Application;Effective Date

Retroactive impact of ERISA for underfunding liability did not violate employer's due process rights. Employee Retirement Income Security Act of 1974, § 4062(a, b), 29 U.S.C.A. § 1362(a, b); U.S.C.A.Const. Amends. 5, 14.

1 Cases that cite this headnote

[8] **Labor and Employment**
Proceedings

Where employer notified PBGC of intent to terminate plan and had some negotiations with PBGC during period of time when PBGC had authority to waive employer's liability under pension plan, but employer never timely filed application for waiver, denial of waiver was proper. Employee Retirement Income Security Act of 1974, § 4004(f), (f)(4), 29 U.S.C.A. § 1304(f), (f)(4).

5 Cases that cite this headnote

Attorneys and Law Firms

***6** Richard G. Maloney and Sidney Werlin, Boston, Mass., with whom Maloney, Williams & Baer, Richard M. Zinner, Friedman & Atherton, Paul P. Daley, Hale & Dorr, Richard E. Mikels, and Riemer & Braunstein, Boston, Mass., were on brief, for defendants-appellants.

Judith F. Mazo, Washington, D.C., with whom Henry Rose, James N. Dulcan and Burns, Jackson, Miller, Summit & Washington, Washington, D.C., were on brief, for Pension Benefit Guaranty Corp., plaintiff-appellee.

Bertram Diamond, Stamford, Conn., for United Rubber, Cork, Linoleum and Plastic Workers of America, Soloman Reddix and Alex Williams, plaintiffs-intervenors-appellees.

Before COFFIN, Chief Judge, CAMPBELL and BOWNES, Circuit Judges.

Opinion

BOWNES, Circuit Judge.

Jurisdiction in this interlocutory appeal from the United States District Court for the District of Massachusetts is predicated upon 28 U.S.C. s 1292(b).[1] The issue is one of first impression involving the interpretation of the Employee Retirement Income Security Act of 1974 (ERISA), Pub.L.No. 93-406, 88 Stat. 832, 29 U.S.C. ss 1001-1381.

The case[2] began with the bankruptcy of a corporation, Avon, and its wholly owned subsidiary, Tenn-ERO, which were part of a larger group of corporations, the Ouimet Group.[3] A brief prefatory explanation of ERISA, and the role in it of the Pension Benefits Guaranty Corporation (PBGC), is necessary to appreciate the issues. Under ERISA, PBGC assumes the administration and payment of benefits of a terminated pension plan whose assets are insufficient to cover all guaranteed benefits. PBGC may recover from the employer 30% of its net worth determined as of a date within one hundred twenty days of the plan termination, or the deficit, whichever is less. The bankrupts, here, had no positive net worth as of the valuation date. This means that, if the term "employer" is limited to the bankrupts, PBGC recovers nothing and a dividend will be paid to the creditors. If, on the other hand, "employer" is construed to mean the Ouimet Group of corporations, including the bankrupts, it is probable that PBGC will receive all of the bankrupts' assets with the creditors receiving nothing.

The Ouimet Group of Corporations

Over forty years ago, Emil R. Ouimet purchased the Brockton, Massachusetts shoe-trim manufacturing concern for which he had worked for several years. In 1940, he changed its name to Ouimet Leather *7 Company. He renamed it Ouimet Stay & Leather Company (Stay) when production expanded to include shoe upper strippings as well as other types of shoe findings.[4] In 1950, he founded Ouimet Corporation (Ouimet), a Delaware corporation with its principal place of business in Nashville, Tennessee. Ouimet manufactures shoe findings, laminations, and vinyl-coated fabrics. Emil also founded Brockton Plastics (Brockton), a Massachusetts corporation producing, among other things, shoe welting, and Ouimet Welting (Welting), a now-dormant corporation. In 1968, Ouimet purchased the Avon Sole Company (Avon), a shoe sole manufacturing factory located in Holbrook, Massachusetts. In 1972, Avon formed a wholly-owned subsidiary, Tenn-ERO, to operate a nonunion plant in Lawrenceburg, Tennessee.

In 1971, Emil Ouimet created the Wareham Trust (Trust) as a tax device. Its assets include the combined Stay-Brockton factory and the houses in which Emil and his son Richard reside.

Emil Ouimet owns 100% of Trust; 80% of Ouimet; and 80% of Stay. He owned all stock in Avon which, in turn, held 100% of Tenn-ERO's stock. Stay has a 100% interest in Ouimet Welting; and a 50% interest in Brockton. At all times pertinent to this litigation, Emil Ouimet was president of all Ouimet Group corporations except Ouimet and Stay, of which Richard was president.

The Plan

Pursuant to a collective bargaining agreement with the Rubber Workers Union and the International Brotherhood of Firemen and Oilers, Avon instituted a pension plan for its hourly workers in 1959. The plan provided for full vesting[5] after ten years of service, if certain age criteria were satisfied. It gave the company the right to "amend, modify, suspend or terminate the Plan" and limited the benefits payable upon termination of the plan to "the assets then remaining in the Trust Fund." Avon made all actuarily mandated contributions, but at all times the plan was underfunded. There were three reasons for this. (1) Initial underfunding occurred because credit was given for past years of service while no immediate contribution to the plan for this credit was required. Rather, the deficit was expected to be amortized over thirty years. (2) Ouimet negotiated several benefit increases which were not met by current contributions. (3) A decrease in the value of certain fund investments in 1974 and 1975 led to a devaluation of the plan assets. When Ouimet purchased Avon, the underfunding amounted to $92,000. By March 25, 1975, the day Avon closed its doors, it was $552,339.64.

Prior Proceedings

On June 18, 1975, Avon and Tenn-ERO filed Chapter XI bankruptcy petitions; on March 22, 1976, they were adjudicated bankrupts. When the plant shut-down appeared imminent, Avon notified PBGC of its intent to terminate the pension plan. [6] PBGC responded to Avon's request to terminate the plan with a letter stating:

> It has been determined that Avon Sole Company was the employer who maintained the Plant at the date of termination for purposes of Section 4062 of the Act, 29 U.S.C. s 1362.

It estimated Avon's liability to be $717,500 and filed a proof of claim in the Avon/Tenn-ERO bankruptcy proceeding for that amount. After examining the bankrupts' books, [7] PBGC determined that Ouimet, Stay, and Welting should also be ***8** considered employers who maintained the plan. It computed the liability of the five corporations at $552,339.64 [8] and filed an amended proof of claim in that amount in the bankruptcy proceedings. Ouimet and Stay filed proofs claiming that, if held liable, they should be subrogated to the rights of PBGC against Avon and Tenn-ERO. The bankruptcy trustee cross-claimed alleging that Ouimet and Stay should reimburse the estate for any payments which Avon and Tenn-ERO would be required to make to PBGC. On March 31, 1976, PBGC filed suit against the Ouimet Group in the United States District Court for the District of Massachusetts. [9] After filing suit against Ouimet, Stay, Welting, Avon, and Tenn-ERO, PBGC determined that Trust should be treated as an employer as well and it was joined as an additional defendant.

The district court named PBGC trustee of the Avon plant. [10] It appointed the bankruptcy judge sitting on the Avon/Tenn-ERO proceedings to serve as master. [11] Following a twelve-day trial in December, 1976, the bankruptcy judge recommended that no liability attach to the Group and that Avon/Tenn-ERO's negative net worth relieved them of liability to PBGC. After release of the bankruptcy judge's memorandum, Union moved to intervene to protect the interests of former Avon employees and the district court granted the motion. The court held a hearing on March 13, 1979. In its opinion, it ruled that ERISA imposes joint and several liability on all members of a controlled group of corporations. After a careful analysis of the statutory and constitutional issues, it granted PBGC's motions for partial summary judgment and for relief from the automatic stay in bankruptcy and remanded the case to the bankruptcy court for a determination of the net worth of the Ouimet Group of corporations. Pension Benefit Guaranty Corp. v. Ouimet Corp., 470 F.Supp. 945, 954, 958 (D.Mass.1979). We affirm, but on somewhat different grounds.

The Statutory Scheme

The employer-sponsored retirement income program, as one form of worker compensation, came into prominence in the 1940's. Expansion of coverage and a parallel increase in plan assets were marked in the ensuing decades. The field was unregulated by the federal government until the enactment, in 1958, of the Welfare and Pension Plans Disclosure Act. 29 U.S.C. s 301 et seq. Its purpose was to curb abuses by those to whom plan administration was entrusted. In 1962, criminalization of certain acts of malfeasance gave the earlier legislation some clout. Employee Retirement Income Act of 1974, H.R.Rep.No. 93-533, 93d Cong., 2d Sess., reprinted in (1974) U.S.Code Cong. & Admin.News pp. 4639, 4640-41. Plans administered jointly by employers and unions were under the dominion of the ***9** Labor Management Relations Act, 29 U.S.C. s 141 et seq. The tax advantages accruing to employers prompted Congress to enact Revenue Code provisions controlling plan contributions. 26 U.S.C. ss 401-404. Only a plan maintained "for the exclusive benefit of (the) employees or their beneficiaries" was deemed qualified. 26 U.S.C. s 401(a)(4). Of primary significance were antidiscrimination rules denying deductions if a plan was designed to benefit officers, shareholders, or highly compensated employees. Id.

By 1974, pension plans had burgeoned to include over thirty million workers; $150 billion in assets were held in trust for pensions, H.R.Rep.No. 533, supra, reprinted in (1974) U.S.Code Cong. & Ad.News at 4641, and twenty thousand workers were annually affected by pension plan failures. Employee Retirement Income Security Act of 1974, S.Rep.No. 383, 93 Cong.2d Sess., reprinted in (1974) U.S.Code Cong. & Ad.News, 4890, 5036. In many instances, benefits were subject to forfeiture "even when separated employees (were) within a few months, or even days, of qualifying for retirement." H.R.Rep.No. 533,

supra, reprinted in (1974) U.S.Code Cong. & Ad.News at 4643. The cloud of forfeitability was attributable to lack of uniformity in vesting, the Internal Revenue provisions requiring funding of current, but not past-service liabilities, and plan agreements which generally limited employee benefits to the corpus of the pension fund if a plan terminated prematurely.

Congress confronted these problems by enacting ERISA, a comprehensive statutory scheme detailing "minimum standards . . . assuring the equitable character of (pension) plans and their financial soundness." 29 U.S.C. s 1001(a).[12] 29 U.S.C. ss 1301-1381 created the Pension Benefit Guaranty Corporation and instituted a system of pension plan termination insurance. Designed to guarantee minimum pension benefits to workers whose employers discontinue pension plans, termination insurance is an industry-wide risk and cost-sharing program. From a pool of premiums contributed by employers who maintain plans, PBGC pays vested benefits to affected employees when a plan terminates. In addition to participation in the insurance program, which is mandatory in most instances, "any employer who maintained a plan (other than a multiemployer plan) at the time it was terminated," 29 U.S.C. s 1362(a), is liable to PBGC for the lesser of

> (1) the excess of-
> (A) the current value of the plan's benefits guaranteed under this subchapter on the date of termination over
>
> (B) the current value of the plan's assets allocable to such benefits on the date of termination, or
>
> (2) 30 percent of the net worth of the employer determined as of a day, chosen by the corporation but not more than 120 days prior to the date of termination, computed without regard to any liability under this section.

29 U.S.C. s 1362(b).

Who Is The Employer?

We start with the definition section of subchapter III-Plan Termination Insurance. 29 U.S.C. s 1301(b) provides in part:

> For purposes of this subchapter, under regulations prescribed by the corporation, all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer and all such trades and businesses as a single employer. The regulations prescribed under the preceding sentence shall be consistent and co-extensive with regulations prescribed for similar purposes by the Secretary of the Treasury under section 414(c) of Title 26[13] (emphasis added).

***10** Section 1301(b) applies, by its terms, only to groups "under common control" as that term is defined in regulations coextensive with the regulations under ***11** 26 U.S.C. s 414(c).[14] Those regulations define a group "under common control" as a parent-subsidiary group, brother-sister group, or combined group. The regulations go on to define these terms according to the degree and nature of common stock ownership. The Ouimet Group, with the exception of Brockton, which was excluded by stipulation, clearly meets the test of stock ownership in the regulations. The group is, therefore, under common control for purposes of section 1301(b).

[1] **[2]** The apparent meaning of section 1301(b) is that a group under common control is to be treated as a single employer for purposes of subchapter III, which is entitled Plan Termination Insurance. It appears, then, that the term "employer," as used in section 1362(b), which is part of subchapter III, refers, in the case of a group under common control, to all the "trades or businesses" which are members of the group. Under this reading of the statute, all members of the Ouimet Group would be jointly and severally liable to PBGC.

Ouimet argues, however, that section 1301(b) does not mean what it appears to mean. Rather, in Ouimet's view, this language was intended only to prevent employers from avoiding application of ERISA by shifting employees around among various corporate entities. Ouimet maintains that, in the absence of section

1301(b), an employer could avoid application of ERISA by dividing into several corporations, each with less than twenty-five employees. Alternatively, an employer could shift an individual employee among corporations so as to minimize his length of service in any one corporation to avoid allowing his benefits to become vested.

[3] **[4]** Ouimet is correct in asserting that Congress intended to prevent such evasion of ERISA. It is clear, however, that this was accomplished through the anti-discrimination rules of Title II and the vesting and participation minimums under Title I. If Congress had intended to limit the application of section 1301(b) to certain purposes, such as computing the number of employees for application of section 1321(b)(13), or the length of an employee's service for application of section 1322(b)(3)(A), it could have done so by referring specifically to the affected sections. Instead, Congress referred to "this subchapter." We must assume that Congress meant, by that phrase, the whole subchapter, including section 1362(b).

Ouimet argues that our reading of section 1301(b) renders section 1362(d)(2) superfluous. On this point, we agree with the district court's observation; since the definition of "parent" in the regulations under 26 U.S.C. s 414(c) is not incorporated into section 1362, there may be situations in which an employer is liquidated into a parent corporation which does not meet the definition of "parent" that is used to define a group under common control. In such a situation, section 1301(b) would not apply, and section 1362(d)(2) would be necessary to impose liability on the parent.

Ouimet also asserts that our reading of section 1301(b) is incompatible with section 1107(d)(7). Ouimet focuses on the words, "(a) corporation is an affiliate of an employer if it is a member of any controlled group of corporations . . . of which the employer who maintains the plan is a member," 29 U.S.C. s 1107(d)(7), and argues that this means that the employer cannot be the group. Again, we agree with the district court. This argument ignores the fact that section 1301(b) is in Title IV of the Act and applies only to subchapter III of that Title. The asserted incompatible language of section 1107(d)(7) is not in Title IV, let alone subchapter III. Defendants' construction mixes apples and oranges.

[5] We do not think it necessary to track in detail each of Ouimet's other arguments against application of the plain meaning of section 1301(b), since we consider ***12** them adequately addressed in the district court's opinion. We hold that the Ouimet Group, as a group under common control, is one employer for purposes of liability under section 1362.

We are not persuaded that, because only one of a group of corporations under common control contributes to a plan, it is unjust to make the group responsible for the plan's deficit. The facts of this case illustrate why such a group should be treated as an integrated whole. Ouimet purchased Avon with full knowledge of the plan and its funding requirements. Ouimet participated in the labor negotiations resulting in greater pension benefits that contributed to the deficit. The Ouimet Group filed a consolidated tax return on which the Avon contributions were deducted. We see nothing unfair in treating the Ouimet Group as a single employer.

We agree with the district court that the group under common control consists of Ouimet, Trust, Stay, Welting, and Avon/Tenn-ERO.

Retroactivity

[6] Defendants challenge the retroactive impact of ERISA for underfunding liability on both statutory and constitutional grounds. The Seventh Circuit confronted the same challenges in Nachman Corp. v. Pension Benefit Guar. Corp., 592 F.2d 947 (7th Cir. 1979). Its decision upholding the retroactivity features of the Act on both grounds was appealed. The Supreme Court granted certiorari, but limited its review to the statutory question. Nachman Corp. v. Pension Benefit Guar. Corp., 446 U.S. 359, 100 S.Ct. 1723, 64 L.Ed.2d 354 (1980). It stated the statutory question as follows:

> The question in this case is whether former employees of petitioner with vested interests in a plan that terminated the day before much of ERISA became fully effective are covered by the insurance program notwithstanding a provision in the plan limiting their benefits to the assets in the pension fund.

Id. at --, 100 S.Ct. at 1726. It held that, despite the retroactive effect on the Nachman Corporation, the pension benefits were "nonforfeitable" and that PBGC had a statutory right to reimbursement from the employer. Since the pension plan in this case terminated prior to December 31, 1975, and contains language substantially identical to the language in the Nachman plan, defendants' statutory retroactive challenge is foreclosed by the Supreme Court decision in Nachman. See (Powell J., dissenting). id. at 1744.

The constitutional challenge to the retroactive effects of ERISA on defendants is based on due process grounds. The battle lines are drawn around redoubtable cases. Defendants rely primarily on Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 98 S.Ct. 2716, 57 L.Ed.2d 727 (1978), and Railroad Retirement Bd. v. Alton R.R., 295 U.S. 330, 55 S.Ct. 758, 79 L.Ed. 1468 (1935). PBGC counters with Usery v. Turner Elkhorn Mining, 428 U.S. 1, 96 S.Ct. 2882, 49 L.Ed.2d 752 (1976). We agree with the Seventh Circuit that Turner Elkhorn carries the day.

[7] The record supporting the enactment of ERISA, wholly unlike that present in Allied Structural Steel, demonstrates that "the presumption favoring 'legislative judgment as to the necessity and reasonableness of a particular measure' " must be allowed to govern here. 438 U.S. at 247, 98 S.Ct. at 2724. Turner Elkhorn Mining, 428 U.S. at 18, 19, 96 S.Ct. 2882; Williamson v. Lee Optical Co., 348 U.S. 483, 488, 75 S.Ct. 461, (464) 99 L.Ed. 563 (1955). Title IV of ERISA satisfies Nachman's rights to Due Process.
Nachman Corp. v. Pension Benefit Guar. Corp., 596 F.2d at 963. We note that the Supreme Court quoted extensively in a footnote the analysis the Seventh Circuit used to distinguish ERISA from the Minnesota statute in Allied Structural Steel Co. v. Spannaus. Nachman Corp. v. Pension Benefit Guar. Corp., 446 U.S. at -- n. 12, 100 S.Ct. at 1729 n. 12. We hold that, despite the retroactivity inherent in the Act, there is no constitutional due process violation.

*13 *Waiver*

To temper the immediate impact of ERISA on employers terminating plans, Congress authorized PBGC to issue full or partial liability waivers in cases of extreme hardship during the first two hundred seventy days after ERISA's enactment. 29 U.S.C. s 1304(f)(4).[15] During the two hundred seventy day period, PBGC promulgated no guidelines relative to waiver application procedures, but, on May 30, 1975, the final day of its temporary authority, it waived liability in most cases in which it had received a letter requesting a waiver. These waivers were contingent upon subsequent investigation into qualification for hardship status. The sole procedural requirement of section 1304(f)(4) is that the plan terminate during the applicable period. Fulfilling that requirement triggers eligibility for consideration of relief from liability.

[8] On March 14, 1975, more than two months prior to the expiration of PBGC's temporary authority, Avon notified PBGC of its intent to terminate the plan on March 25, 1975. PBGC replied with a request for information about the plan and the reasons for its dissolution. Avon made a timely reply to the correspondence, outlining its poor financial condition. On May 29, 1975, Avon's plan administrator advised an Avon vice-president, Thomas Rosser, that Avon should forward a waiver request to PBGC "by registered mail on May 30." PBGC did not receive the letter, dated June 5, until the tenth of June and refused to consider the waiver request. The Ouimet Group now asserts that it is entitled to consideration for a hardship waiver, contending that it had no knowledge that PBGC would waive liability only if a specific request were made. It contends that the June 5th letter "indicates no more than the diligence of the actuary, who became concerned about the absence of any action by PBGC." Our reading of the record leads us to the contrary conclusion. The letter from the company plan administrator to Rosser states:

> Enclosed is a draft of the letter I mentioned in our telephone conversation which should be forwarded on Company stationery to the PBGC by registered mail on May 30, to meet the 270 day period from September 2, 1974.

It indicates that Avon knew PBGC had instituted a waiver-request procedure. Whether Avon learned this formally or informally, it failed to act during the requisite time period. Avon correctly states that the statute requires no specific request for a waiver; but, once it had knowledge of PBGC's housekeeping rules, it should have

followed them. Moreover, as the district court pointed out, the Act allowed waiver by PBGC "for only the first 270 days" after enactment. 29 U.S.C. s 1304(f)(4). That period has passed.

Affirmed.

BOWNES, Circuit Judge (concurring specially).
While I agree with the panel, I think its statutory analysis, like that of the district court, is incomplete. It glosses over, without addressing, the main statutory problem-that ERISA recognizes two groups of businesses: businesses (whether or not incorporated) which are under common control, and a controlled group of corporations. Each is defined separately and treated separately under the Act. Unfortunately, the parties and the district court, to some degree, have used the terms interchangeably. Since the key question is whether the single employer definition of businesses under ***14** common control under section 1301(b) [16] brings the Ouimet Group within the liability provisions of section 1362(a), [17] and, since section 1301 does not refer to controlled groups of corporations at all, it is necessary to examine the Act to determine how both entities are treated and into which category the Ouimet Group falls.

Congress defined controlled group by adopting the Internal Revenue Code definitions of 26 U.S.C. s 1563(a) [18] which make stock ownership the test. It did not, at the time it passed ERISA, define groups under common control in terms of any existing provisions of the Internal Revenue Code. In section 1301(b), it provided that, under regulations prescribed by PBGC, all employees with trades or businesses under common control are to be treated as employed by a single employer. It further directed that the PBGC regulations "shall be consistent and coextensive with regulations prescribed for similar purposes by the Secretary of the Treasury under section 414(c) of Title 26." The regulations promulgated by the Secretary of the Treasury after the enactment of ERISA under 26 U.S.C. s 414(c), see footnote 14, supra, defined groups under common control in the same terms as controlled groups. This, however, cannot change the separate treatment given these two entities under the Act.

The Ouimet Group fits into the definition of both entities; it is a group of businesses under common control and also a controlled group of corporations. The problem inherent in this dual role is that businesses under common control and a controlled group of corporations are not treated in the same manner throughout the Act.

That section defining a multiemployer plan states, "all corporations which are members of a controlled group of corporations . . . shall be deemed to be one employer." 29 U.S.C. s 1002(37)(B)(ii). There is no mention of trades or businesses under common control in this section of the ***15** Act. Multiemployer plans are exempted from the liability provisions of 29 U.S.C. s 1362(a). Liability is imposed under 29 U.S.C. s 1364(a) on "all employers who maintain a plan under which more than one employer makes contributions at the time such plan is terminated . . ." Since the plan here is not multiemployer and since Ouimet is a controlled group, it can be argued that only the employer (the bankrupts) who maintained the plan are liable.

For purposes of minimum participation, vesting and benefit accrual, a controlled group and businesses under common control receive separate but equal tandem treatment under 29 U.S.C. ss 1060(c) and (d). [19]

Disparate treatment of these entities does not, however, eliminate the common control definition of employer from the liability section of the Act. I would hold specifically that where, as here, there is a controlled group of corporations that also meets the definition of businesses under common control, section 1301(b) makes the group a single employer for liability purposes under section 1362(a).

All Citations

630 F.2d 4, 2 Employee Benefits Cas. 1911

Footnotes

1 In pertinent part, 28 U.S.C. s 1292(b) provides:

(b) When a district judge, in making in a civil action an order not otherwise appealable under this section, shall be of the opinion that such order involves a controlling question of law as to which there is substantial ground for

difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order. The Court of Appeals may thereupon, in its discretion, permit an appeal to be taken from such order, if application is made to it within ten days after the entry of the order . . . .

2 The opinion of the district court is reported at 470 F.Supp. 945.

3 The Ouimet Group challenges certain retroactively-applied provisions of ERISA. After oral argument in the instant case, the Supreme Court heard oral arguments in Nachman Corp. v. Pension Benefit Guar. Corp.,, --U.S. --, 100 S.Ct. 1723, 64 L.Ed.2d 354 (1980), which also involved a retroactivity challenge to the Act. Accordingly, we postponed our decision until the Supreme Court had decided Nachman.

4 A finding is a trim, decorative item, or small stripping stitched onto the upper portion of a shoe. The terms finding and stay are interchangeable.

5 Vesting is defined as the "nonforfeitable right of interest which an employee acquires in the pension fund." Employee Retirement Income Security Act of 1974, H.R.Rep.No. 533, reprinted in (1974) U.S.Code Cong. & Ad. News 4639, 4643.

6 29 U.S.C. s 1341(a) requires plan administrators to notify PBGC of proposed terminations at least ten days prior to the proposed termination date.

7 PBGC has broad investigatory authority under 29 U.S.C. s 1303(a)-(c).

8 Maximum liability to PBGC is the lesser of the pension underfunding or 30% of the employer's net worth. 29 U.S.C. s 1362(b). PBGC determined the net worth of the Ouimet Group, excluding Trust and Brockton, to be $1,875,283 on December 31, 1974. Because 30% of net worth ($562,601.70) exceeds the amount of pension underfunding ($552,339.64) the liability equals the pension fund deficit.

9 29 U.S.C. s 1303(e) authorizes PBGC to bring suit for legal and/or equitable relief. Jurisdiction is vested in the United States district courts.

After commencement of plan termination, if PBGC finds that the plan is unable to pay basic benefits, 29 U.S.C. s 1341(e) empowers PBGC to apply to the district court for a decree adjudicating that the plan must be terminated according to procedures outlined in 29 U.S.C. s 1342. Pending adjudication, "such court shall stay . . . any pending bankruptcy." 29 U.S.C. s 1342(f).

10 29 U.S.C. s 1342(b) authorizes the appointment by the district court of PBGC as trustee. The court named PBGC trustee of Avon's plan on April 20, 1976, ordering that the termination be effective as of March 25, 1975. PBGC now pays monthly benefits averaging $87 to 108 employees. An additional 150 workers will receive no pension because their rights were not vested when Avon went out of business.

11 A district court may appoint a special master "in matters of account and of difficult computation of damages." Fed.R.Civ.P. 53. The proceedings were consolidated because the issues in both cases were "substantially identical." PBGC v. Tenn-ERO Corp., No. 76-1314 (D.Mass. May 13, 1977).

12 29 U.S.C. ss 1001-1144 set out requirements of minimum participation, vesting, and funding. 26 U.S.C. ss 401-415 contain coordinate tax provisions. 29 U.S.C. ss 1201-1242 detail the procedure for the agencies to whom enforcement is relegated.

13 26 U.S.C. s 414(c) states in pertinent part, "all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer."

14 Temporary Treasury Regulations promulgated under 26 U.S.C. s 414(c) provides in part:

s 11.414(c)-2 Two or more trades or businesses under common control (TD 7388, filed 10-31-75).

(a) In general. For purposes of this section, the term "two or more trades or businesses under common control" means any group of trades or businesses which is either a "parent-subsidiary group of trades or businesses under common control" as defined in paragraph (b) of this section, a "brother-sister group of trades or businesses under common control" as defined in paragraph (c) of this section, or a "combined group of trades or businesses under common control" as defined in paragraph (d) of this section. For purposes of this section and ss 11.414(c)-3 and 11.414(c)-4, the term "organization" means a sole proprietorship, a partnership (as defined in section 7701(a)(2)), a trust, an estate, or a corporation.

(b) Parent-subsidiary group of trades or businesses under common control-(1) General. The term "parent-subsidiary group of trades or businesses under common control" means one or more chains of organizations conducting trades or businesses connected through ownership of a controlling interest with a common parent organization if-

(i) A controlling interest in each of the organizations, except the common parent organization, is owned (directly and with the application of s 11.414(c)-4(b)(1), relating to options) by one or more of the other organizations; and

(ii) The common parent organization owns (directly and with the application of s 11.414(c)-4(b)(1), relating to options) a controlling interest in at least one of the other organizations, excluding, in computing such controlling interest, any direct ownership interest by such other organizations.

(2) Controlling interest defined-(i) Controlling interest. For purposes of paragraphs (b) and (c) of this section, the phrase "controlling interest" means:

(A) In the case of an organization which is a corporation, ownership of stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote of such corporation or at least 80 percent of the total value of shares of all classes of stock of such corporation:

(B) In the case of an organization which is a trust or estate, ownership of an actuarial interest of at least 80 percent of such trust or estate:

(C) In the case of an organization which is a partnership, ownership of at least 80 percent of the profits interest or capital interest of such partnership; and

(D) In the case of an organization which is a sole proprietorship, ownership of such sole proprietorship.

(ii) Actuarial interest. For purposes of this section, the actuarial interest of each beneficiary of a trust or estate shall be determined by assuming the maximum exercise of discretion by the fiduciary in favor of such beneficiary. The factors and method prescribed in s 20.2031-10 of this chapter (Estate Tax Regulations) for use in ascertaining the value of an interest in property for estate tax purposes shall be used for purposes of this subdivision in determining a beneficiary's actuarial interest.

(c) Brother-sister group of trades or businesses under common control-(1) General. The term "brother-sister group of trades or businesses under common control" means two or more organizations conducting trades or businesses if (i) the same five or fewer persons who are individuals, estates, or trusts own (directly and with the application of s 11.414(c)-4), singly or in combination, a controlling interest of each organization, and (ii) taking into account the ownership of each such person only to the extent such ownership is identical with respect to each such organization, such persons are in effective control of each organization.

(2) Effective control defined. For purposes of this paragraph, persons are in "effective control" of an organization if-

(i) In the case of an organization which is a corporation, such persons own stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote of such corporation or more than 50 percent of the total value of shares of all classes of stock of such corporation:

(ii) In the case of an organization which is a trust or estate, such persons own an aggregate actuarial interest of more than 50 percent of such trust or estate:

(iii) In the case of an organization which is a partnership, such persons own an aggregate of more than 50 percent of the profits interest or capital interest of such partnership; and

(iv) In the case of an organization which is a sole proprietorship, such persons own such sole proprietorship.

(d) Combined group of trades or businesses under common control. The term "combined group-of-trades or businesses under common control" means any group of three or more organizations, if (1) each such organization is a member of either a parent-subsidiary group of trades or businesses under common control or a brother-sister group of trades or businesses under common control, and (2) at least one such organization is the common parent organization of a parent-subsidiary group of trades or businesses under common control and is also a member of a brother-sister group of trades or businesses under common control.

15 29 U.S.C. s 1304(f) in relevant portion provides:

In addition to its other powers under this subchapter, for only the first 270 days after September 2, 1974, the corporation may

(4) waive the application of the provisions of sections 1362, 1363, and 1364 of this title to, or reduce the liability imposed under such sections on, any employer with respect to a plan terminating during that 270 day period if the corporation determines that such waiver or reduction is necessary to avoid unreasonable hardship in any case in which the employer was not able, as a practical matter, to continue the plan.

16 29 U.S.C. s 1301(b) provides in pertinent part:

For purposes of this subchapter, under regulations prescribed by the corporation, all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer and all such trades and businesses as a single employer. The regulations prescribed under the preceding sentence shall be consistent and coextensive with regulations prescribed for similar purposes by the Secretary of the Treasury under section 414(c) of Title 26.

17 29 U.S.C. s 1362(a) provides in pertinent part: "This section applies to any employer who maintained a plan (other than a multi-employer plan) at the time it was terminated(.)"

18 29 U.S.C. s 1060(c) refers to 26 U.S.C. s 1563(a)(1)-(3) which contains the following definition of controlled group of corporations.

(a) Controlled group of corporations.-For purposes of this part, the term "controlled group of corporations" means any group of-

(1) Parent-subsidiary controlled group.-One or more chains of corporations connected through stock ownership with a common parent corporation if-

(A) stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote or at least 80 percent of the total value of shares of all classes of stock of each of the corporations, except the common parent corporation, is owned (within the meaning of subsection (d)(1)) by one or more of the other corporations; and

(B) the common parent corporation owns (within the meaning of subsection (d) (1)) stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote or at least 80 percent of the total value of shares of all classes of stock of at least one of the other corporations, excluding, in computing such voting power or value, stock owned directly by such other corporations.

(2) Brother-sister controlled group.-Two or more corporations if stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote or at least 80 percent of the total value of shares of all classes of stock of each of the corporations is owned (within the meaning of subsection (d)(2)) by one person who is an individual, estate, or trust.

(3) Combined group.-Three or more corporations each of which is a member of a group of corporations described in paragraph (1) or (2), and one of which-

(A) is a common parent corporation included in a group of corporations described in paragraph (1), and also

(B) is included in a group of corporations described in paragraph (2).

19 29 U.S.C. ss 1060(c) and (d) provide:

(c) For purposes of sections 1052, 1053, and 1054 of this title, all employees of all corporations which are members of a controlled group of corporations (within the meaning of section 1563(a) of Title 26, determined without regard to section 1563(a)(4) and (e)(3)(C) of Title 26) shall be treated as employed by a single employer. With respect to a plan adopted by more than one such corporation, the minimum funding standard of section 1082 of this title shall be determined as if all such employers were a single employer, and allocated to each employer in accordance with regulations prescribed by the Secretary of the Treasury.

(d) For purposes of sections 1052, 1053, and 1054 of this title, under regulations prescribed by the Secretary of the Treasury, all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer. The regulations prescribed under this subsection shall be based on principles similar to the principles which apply in the case of subsection (c) of this section.

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KeyCite Yellow Flag - Negative Treatment
Proposed Regulation

Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.401(a)–1, Treas. Reg. § 1.401(a)–1

§ 1.401(a)–1 Post–ERISA qualified plans and qualified trusts; in general.

Effective: May 22, 2007
Currentness

(a) Introduction—(1) In general. This section and the following regulation sections under section 401 reflect the provisions of section 401 after amendment by the Employee Retirement Income Security Act of 1974 (Pub.L. 93–406) ("ERISA").

(2) [Reserved]

(b) Requirements for pension plans—(1) Definitely determinable benefits. (i) In order for a pension plan to be a qualified plan under section 401(a), the plan must be established and maintained by an employer primarily to provide systematically for the payment of definitely determinable benefits to its employees over a period of years, usually for life, after retirement or attainment of normal retirement age (subject to paragraph (b)(2) of this section). A plan does not fail to satisfy this paragraph (b)(1)(i) merely because the plan provides, in accordance with section 401(a)(36), that a distribution may be made from the plan to an employee who has attained age 62 and who is not separated from employment at the time of such distribution.

(ii) Section 1.401–1(b)(1)(i), a pre-ERISA regulation, provides rules applicable to this requirement, and that regulation is applicable except as otherwise provided.

(iii) The use of the type of plan provision described in § 1.415(a)–1(d)(1) which automatically freezes or reduces the rate of benefit accrual or the annual addition to insure that the limitations of section 415 will not be exceeded, will not be considered to violate the requirements of this subparagraph provided that the operation of such provision precludes discretion by the employer.

(2) Normal retirement age—(i) General rule. The normal retirement age under a plan must be an age that is not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed.

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(ii) Age 62 safe harbor. A normal retirement age under a plan that is age 62 or later is deemed to be not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed.

(iii) Age 55 to age 62. In the case of a normal retirement age that is not earlier than age 55 and is earlier than age 62, whether the age is not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed is based on all of the relevant facts and circumstances.

(iv) Under age 55. A normal retirement age that is lower than age 55 is presumed to be earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed, unless the Commissioner determines that under the facts and circumstances the normal retirement age is not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed.

(v) Age 50 safe harbor for qualified public safety employees. A normal retirement age under a plan that is age 50 or later is deemed to be not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed if substantially all of the participants in the plan are qualified public safety employees (within the meaning of section 72(t)(10)(B)).

(3) Benefit distribution prior to retirement. For purposes of paragraph (b)(1)(i) of this section, retirement does not include a mere reduction in the number of hours that an employee works. Accordingly, benefits may not be distributed prior to normal retirement age solely due to a reduction in the number of hours that an employee works.

(4) Effective date. Except as otherwise provided in this paragraph (b)(4), paragraphs (b)(2) and (3) of this section are effective May 22, 2007. In the case of a governmental plan (as defined in section 414(d)), paragraphs (b)(2) and (3) of this section are effective for plan years beginning on or after January 1, 2009. In the case of a plan maintained pursuant to one or more collective bargaining agreements that have been ratified and are in effect on May 22, 2007, paragraphs (b)(2) and (3) of this section do not apply before the first plan year that begins after the last of such agreements terminate determined without regard to any extension thereof (or, if earlier, May 24, 2010. See § 1.411(d)–4, A–12, for a special transition rule in the case of a plan amendment that increases a plan's normal retirement age pursuant to paragraph (b)(2) of this section.

Credits

[T.D. 7748, 46 FR 1695, Jan. 7, 1981; T.D. 9319, 72 FR 16894, April 5, 2007; T.D. 9325, 72 FR 28606, May 22, 2007]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Notes of Decisions (457)

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.401(a)–2, Treas. Reg. § 1.401(a)–2

§ 1.401(a)–2 Impossibility of diversion under qualified plan or trust.

Effective: April 5, 2007
Currentness

(a) General rule. Section 401(a)(2) requires that in order for a trust to be qualified, it must be impossible under the trust instrument (in the taxable year and at any time thereafter before the satisfaction of all liabilities to employees or their beneficiaries covered by the trust) for any part of the trust corpus or income to be used for, or diverted to, purposes other than for the exclusive benefit of those employees or their beneficiaries. Section 1.401–2, a pre-ERISA regulation, provides rules under section 401(a)(2) and that regulation is applicable except as otherwise provided.

(b) Section 415 suspense account. Notwithstanding paragraph (a) of this section, a plan, or trust forming part of a plan, may provide for the reversion to the employer, upon termination of the plan, of amounts contributed to the plan that exceed the limitations imposed under section 415(c), to the extent set forth in rules prescribed by the Commissioner in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2) of this chapter).

Credits
[T.D. 7748, 46 FR 1696, Jan. 7, 1981; T.D. 9319, 72 FR 16894, April 5, 2007]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Notes of Decisions (24)

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.401(a)–4, Treas. Reg. § 1.401(a)–4

§ 1.401(a)–4 Optional forms of benefit (before 1994).

Currentness

Q–1: How does section 401(a)(4) apply to optional forms of benefits?

A–1: (a) In general—(1) Scope. The nondiscrimination requirements of section 401(a)(4) apply to the amount of contributions or benefits, optional forms of benefit, and other benefits, rights and features (e.g., actuarial assumptions, methods of benefit calculation, loans, social security supplements, and disability benefits) under a plan. This section addresses the application of section 401(a)(4) only to optional forms of benefit under a plan. Generally, the determination of whether an optional form is nondiscriminatory under section 401(a)(4) is made by reference to the availability of such optional form, and not by reference to the utilization or actual receipt of such optional form. See Q&A–2 of this section. Even though an optional form of benefit under a plan may be nondiscriminatory under section 401(a)(4) and this § 1.401(a)–4 because the availability of such optional form does not impermissibly favor employees in the highly compensated group, such plan may fail to satisfy section 401(a)(4) with respect to the amount of contributions or benefits or with respect to other benefits, rights and features if, for example, the method of calculation or the amount or value of benefits payable under such optional form impermissibly favors the highly compensated group. See § 1.411(d)–4, Q&A–1 for the definition of "optional form of benefit."

(2) Nondiscrimination requirements. Each optional form of benefit provided under a plan is subject to the nondiscrimination requirement of section 401(a)(4) and thus the availability of each optional form of benefit must not discriminate in favor of the employees described in section 401(a)(4) in whose favor discrimination is prohibited (the "highly compensated group"). See paragraph (b) of this Q&A–1 for a description of the employees included in such group. This is true without regard to whether a particular optional form of benefit is the actuarial equivalent of any other optional form of benefit under the plan. Thus, for example, a plan may not condition, or otherwise limit, the availability of a single sum distribution of an employee's benefit in a manner that impermissibly favors the highly compensated group.

(b) Highly compensated group. For plan years commencing prior to the applicable effective date for the amendment made to section 401(a)(4) by section 1114 of the Tax Reform Act of 1986 (TRA '86), the highly compensated group consists of those employees who are officers, shareholders, or highly compensated. For plan years beginning on or after the applicable effective date of the amendments to section 401(a)(4) made by TRA '86, the highly compensated group consists of those employees who are highly compensated within the meaning of section 414(q). The amendment to section 401(a)(4) made by section 1114 of TRA '86 is generally effective for plan years commencing after December 31, 1988. See section 1114(a) of TRA '86.

Q–2: How is it determined whether an optional form of benefit satisfies the nondiscrimination requirements of section 401(a)(4)?

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A–2: (a) Nondiscrimination requirement—(1) In general. An optional form of benefit under a plan is nondiscriminatory under section 401(a)(4) only if the requirements of paragraphs (a)(2) and (a)(3) of this Q&A–2 are satisfied with respect to such optional form. The determination of whether an optional form of benefit satisfies these requirements is made by reference to the availability of the optional form, and not by reference to the utilization or actual receipt of such optional form. Thus, an optional form of benefit that satisfies the requirements of paragraphs (a)(2) and (a)(3) of this Q&A–2 is nondiscriminatory under section 401(a)(2) even though the highly compensated group disproportionately utilizes such optional form. However, the composition of the group of employees who actually receive benefits in an optional form may be relevant in determining whether such optional form satisfies the requirement of paragraph (a)(3) of this Q&A–2 with respect to effective availability.

(2) Current availability—(i) Plan years prior to TRA '86 effective date. Except as provided in paragraph (a)(2)(iii) of this Q&A–2, for plan years prior to the effective date of the amendments made to section 401(b) by section 1112(a) of TRA '86, the requirement of this paragraph (a)(2) is satisfied only if the group of employees to whom the optional form is currently available satisfies either the seventy percent test of section 410(b)(1)(A) or the nondiscriminatory classification test of section 410(b)(1)(B).

(ii) Plan years commencing on or after TRA '86 effective date. Except as provided in paragraph (a)(2)(iii) of this Q&A–2, for plan years commencing on or after the effective date on which the amendments made to section 410(b) by section 1112(a) of TRA '86 first apply to a plan, the requirement of this paragraph (a)(2) is satisfied only if the group of employees to whom the optional form is currently available satisfies either the percentage test set forth in section 410(b)(1)(A), the ratio test set forth in section 410(b)(1)(B), or the nondiscriminatory classification test set forth in section 410(b)(2)(A)(i). The employer need not satisfy the average benefit percentage test in section 410(b)(2)(A)(ii) in order for the optional form to be currently available to a nondiscriminatory group of employees.

(iii) Special rule for certain governmental or church plans. Plans described in section 410(c) will be treated as satisfying the current availability test of this paragraph (a)(2) if the group of employees with respect to whom the optional form is currently available satisfies the requirements of section 401(a)(3) as in effect on September 1, 1974.

(iv) Effective data for TRA '86 amendments to section 410(b). The amendments to section 410(b) made by section 1112(a) of TRA '86 are generally effective for plan years commencing after December 31, 1988. See section 1112(e)(1) of TRA '86.

(v) Elimination of optional forms—(A) In general. Notwithstanding paragraphs (a)(2)(i) and (a)(2)(ii) of this Q&A–2, in the case of an optional form of benefit that has been eliminated under a plan with respect to specified employees for benefits accrued after the later of the eliminating amendment's adoption date or effective date, the determination of whether such optional form satisfies this paragraph (a)(2) with respect to such employees is to be made immediately prior to the elimination. Accordingly, if, as of the later of the adoption date or effective date of an amendment eliminating an optional form with respect to future benefit accruals, the current availability of such optional form immediately prior to such amendment satisfies this paragraph (a)(2), then the optional form will be treated as satisfying this paragraph (a)(2) for all subsequent years.

(B) Example. A profit-sharing plan that provides for a single sum distribution available to all employees on termination of employment is amended January 1, 1990, to eliminate such single sum optional form of benefit with respect to benefits accrued after January 1, 1991. As of January 1, 1991, the single sum optional form of benefit is available to a group of employees that satisfies the percentage test of section 410(b)(1)(A). As of January 1, 1995, all nonhighly compensated employees who were entitled to the single sum optional form of benefit have terminated from employment with the employer and taken a distribution of their benefits. The only remaining employees who have a right to take a portion of their benefits in the form of a single sum distribution on termination of employment are highly compensated employees. Because the availability of the single sum optional form of benefit satisfied the current availability test as of January

1, 1991, the availability of such optional form of benefit is deemed to continue to satisfy the current availability test of this paragraph (a)(2).

(3) Effective availability—(i) In general. The requirement of this paragraph (a)(3) is satisfied only if, based on the facts and circumstances, the group of employees to whom the optional form is effectively available does not substantially favor the highly compensated group. This is the case even if the optional form is, or has been, currently available to a group of employees that satisfies the applicable requirements in paragraph (a)(2)(i) or (ii) of this Q&A-2.

(ii) Examples. The provisions of paragraph (a)(3)(i) of this Q&A-2 can be illustrated by the following examples:

Example 1. Employer X maintains a defined benefit plan that covers both of the 2 highly compensated employees of the employer and 8 of the twelve nonhighly compensated employees of the employer. Plan X provides for a normal retirement benefit payable as an annuity and based on a normal retirement age of 65, and an early retirement benefit payable upon termination in the form of an annuity to employees who terminate from service with the employer on or after age 55 with 30 or more years of service. Each of the 2 employees of employer X who are in the highly compensated group currently meet the age and service requirement, or will have 30 years of service by the time they reach age 55. All but 2 of the 8 nonhighly compensated employees of employer X who are covered by the plan were hired on or after age 35 and thus, cannot qualify for the early retirement benefit provision. Even though the group of employees to whom the early retirement benefit is currently available does not impermissibly favor the highly compensated group by reason of disregarding age and service, these facts and circumstances indicate that the effective availability of the early retirement benefit in plan X substantially favors the highly compensated group.

Example 2. Assume the same facts as in Example 1 except that the early retirement benefit is added by a plan amendment first adopted, announced and effective December 1, 1991, and is available only to employees who terminate from employment with the employer prior to December 15, 1991. Further assume that all employees were hired prior to attaining age 25, and that the group of employees who have, or will have attained age 55 with 30 years of service, by December 15, 1991, satisfies the ratio test of section 410(b)(1)(B). Finally, assume that the only employees who terminate from employment with the employer during the two week period in which the early retirement benefit is available are employees in the highly compensated group. These facts and circumstances indicate that the effective availability of the early retirement benefit substantially favors the highly compensated group. This is the case even though the limitation of the early retirement benefit to a specified period satisfies section 411(d)(6).

Example 3. Employer Y amends plan Y on June 30, 1990, to provide for a single sum distribution for employees who terminate from employment with the employer after June 30, 1990, and prior to January 1, 1991. The availability of this single sum distribution is conditioned on the employee having a particular disability at the time of termination of employment. The only employee of the employer who meets this disability requirement at the time of the amendment and thereafter through December 31, 1990, is a highly compensated employee. Generally, a disability condition with respect to the availability of a single sum distribution may be disregarded in determining whether the current availability of such optional form of benefit is discriminatory. However, these facts and circumstances indicate that the effective availability of the optional form of benefit substantially favors the highly compensated group.

Example 4. Employer Z maintains a money purchase pension plan that covers all employees of the employer. The plan provides for distribution in the form of a joint and survivor annuity, a life annuity, or equal installments over 10 years. During the 1992 calendar year the employer winds up his business. In December of 1992, only two employees remain in the employment of the employer, both of whom are highly compensated. Employer Z then amends the plan to provide for a single sum distribution to employees who terminate from employment on or after the date of the amendment. Both highly compensated employees terminate from employment on December 31, 1992, taking a single sum distribution of their benefits. These facts and circumstances indicate that the effective availability of the single sum optional form of benefit substantially favors the highly compensated group.

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(b) Application of tests—(1) Current availability—(i) In general. Except as otherwise provided in this paragraph (b), in determining whether an optional form of benefit that is subject to specified eligibility conditions is currently available to an employee for purposes of paragraph (a) of this Q&A–2, the determination of current availability generally is to be based on the current facts and circumstances with respect to the employee (e.g., the employee's current compensation or the employee's current net worth). Thus, for example, the fact that an employee may, in the future, satisfy an eligibility condition generally does not cause an optional form of benefit to be treated as currently available to such employee.

(ii) Exceptions for age, service, employment termination and certain other conditions—(A) Age and service conditions. For purposes of applying paragraph (a)(2) of this Q&A–2, except as provided in paragraph (b)(1)(ii)(B) of this Q&A–2, an age condition, a service condition, or both are to be disregarded. For example, an employer that maintains a plan that provides for an early retirement benefit payable as an annuity for employees in division A, subject to a requirement that the employee has attained his or her 55th birthday and has at least twenty years of service with the employer, is to disregard the age and service conditions in determining the group of employees to whom the early retirement annuity benefit is currently available. Thus, the early retirement annuity benefit is treated as currently available to all employees of division A, without regard to their ages or years of service and without regard to whether they could potentially meet the age and service conditions prior to attaining the plan's normal retirement age.

(B) Exception for certain age and service conditions. Age and service conditions that must be satisfied within a specified period of time may not be disregarded pursuant to paragraph (b)(1)(ii)(A) of this Q&A–2. However, in determining the current availability of an optional form of benefit subject to such an age condition, service condition, or both, an employer may project the age and service of employees to the last date on which the optional form of benefit subject to the age condition or service condition (or both) is available under the plan. An employer's ability to protect age and service to the last date on which the optional form of benefit is available under the plan is not cut off by a plan termination occurring prior to that date. Thus, for example, assume that an employer maintaining a plan that permits employees terminating from employment on or after age 55 between June 1, 1991 to May 31, 1992, to elect a single sum distribution, decides to terminate the plan on December 31, 1991. In determining the group of employees to whom the single sum optional form of benefit is currently available, this employer may project employees' ages through May 31, 1992.

(C) Certain other conditions disregarded. Conditions on the availability of optional forms of benefit requiring termination of employment, death, satisfaction of a specified health condition (or failure to meet such condition), disability, hardship, marital status, default on a plan loan secured by a participant's account balance, or execution of a covenant not to compete may be disregarded in determining the group of employees to whom an optional form of benefit is currently available.

(2) Employees taken into account. For purposes of applying paragraph (a) of this Q&A–2, the tests are to be applied on the basis of the employer's nonexcludable employees (whether or not they are participants in the plan) in the same manner as such tests would be applied in determining whether the plan providing the optional form of benefit satisfies the tests under section 410(b).

(3) Definition of "plan". For purposes of applying paragraph (a) of this Q&A–2, the term "plan" has the meaning that such term has for purposes of determining whether the amount of contributions or benefits and whether other benefits, rights, and features are nondiscriminatory under section 401(a)(4).

(4) Restructuring optional forms of benefit—(i) In general. For purposes of applying paragraph (a) of this Q&A–2, the availability of two or more optional forms of benefit under a plan may be tested by restructuring such benefits into two or more restructured optional forms of benefit and testing the availability of such restructured optional forms of benefit. If two or more optional forms of benefit under a plan contain both common and distinct components, such optional forms of benefit may be restructured as a single optional form of benefit comprising the common component, and one

or more optional forms of benefit comprising each distinct component. Components of optional forms of benefit may be treated as common only if they are identical with respect to all characteristics taken into account under Q&A–1(b) of § 1.411(d)–4. The availability of each restructured optional form of benefit must satisfy the applicable nondiscrimination requirements of paragraph (a) of this Q&A–2.

(ii) Example. A profit-sharing plan covering all the employees of an employer provides a single sum distribution option upon termination from employment for all employees earning less than $50,000 and a single sum distribution option upon termination from employment after the attainment of age 55 for all employees earning $50,000 or more. These distribution options are identical in all other respects. For purposes of applying section 401(a)(4), such optional forms of benefit may be restructured into two different optional forms of benefit: (A) a single sum distribution option upon termination from employment after the attainment of age 55 for all employees (i.e., the common component), and (B) a single sum distribution option upon termination from employment before the attainment of age 55 for all employees earning less than $50,000. The availability of each of these restructured optional forms of benefit must satisfy section 401(a)(4).

(c) Commissioner may provide additional tests. The Commissioner may provide such additional factors, tests, and safe harbors as are necessary or appropriate for purposes of determining whether the availability of an optional form of benefit is discriminatory under section 401(a)(4). In addition, the Commissioner may provide that additional eligibility conditions not related directly or indirectly to compensation or wealth may be disregarded under paragraph (b)(1)(ii)(C) of this Q&A–2 in determining the current availability of an optional form of benefit. The Commissioner may provide such additional guidance only through the publication of revenue rulings, notices or other documents of general applicability.

Q–3: May a plan condition the availability of an optional form of benefit on employer discretion?

A–3: No. Even if the availability of an optional form of benefit that is conditioned on employer discretion satisfies the nondiscrimination requirements of section 401(a)(4), the plan providing the optional form of benefit will fail to satisfy certain other requirements of section 401(a), including, in applicable circumstances, the definitely determinable requirement of section 401(a) and the requirements of section 401(a)(25) and section 411(d)(6). See § 1.411(d)–4.

Q–4: Will a plan provision violate section 401(a)(4) merely because it requires that an employee who terminates from service with the employer receive a single sum distribution in the event that the present value of the employee's benefit is not more than $3,500, as permitted by sections 411(a)(11) and 417(e)?

A–4: No. A plan will not be treated as discriminatory under section 401(a)(4) merely because the plan mandates a single sum distribution when the present value of an employee's benefit is not more than $3,500, as permitted by sections 411(a)(11) and 417(e). This is an exception to the general principles of this section. (No similar provision exists excepting such single sum distributions from the limits on employer discretion under section 411(d)(6). See § 1.411(d)–4 Q&A–4.)

Q–5: If the availability of an optional form of benefit discriminates, or may reasonably be expected to discriminate, in favor of the highly compensated group, what acceptable alternatives exist for amending the plan without violating section 411(d)(6)?

A–5: (a) Transitional rules—(1) In general. The following rules apply for purposes of making necessary amendments to existing plans (as defined in Q&A–6 of this section) under which the availability of an optional form of benefit violates the nondiscrimination requirements of section 401(a)(4) or may reasonably be expected to violate such requirements. These transitional rules are provided under the authority of section 411(d)(6), which allows the elimination of certain optional forms of benefit if permitted by regulations, and section 7805(b).

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(2) Nondiscrimination—(i) In general. The determination of whether the availability of an optional form of benefit violates section 401(a)(4) is to be made in accordance with Q&A–2 of this section. In addition, the availability of a particular optional form of benefit may reasonably be expected to violate the nondiscrimination requirements of section 401(a)(4) if, under the applicable facts and circumstances, there is a significant possibility that the current availability of such optional form of benefit will impermissibly favor the highly compensated group. This determination must be made on the basis of the seventy percent test of section 410(b)(1)(A) or the nondiscriminatory classification test of section 410(b)(1)(B) as such tests existed prior to the effective date of the amendments made to section 410(b) by section 1112(a) of TRA '86. Thus, a condition may not reasonably be expected to discriminate for purposes of these rules merely because it results in a significant possibility that discrimination will result because of the amendments made to section 410(b) by section 1112(a) of TRA '86. In addition, the availability of an optional form of benefit may not reasonably be expected to discriminate merely because of an age or service condition that may be disregarded in determining the current availability of such optional form of benefit under paragraph (b)(1)(ii)(A) of Q&A–2 of this section. Similarly, the availability of an optional form of benefit may not reasonably be expected to discriminate merely because of an age or service condition that, after permitted projection, does not cause such optional form to fail to satisfy the requirement of this paragraph (a)(2).

(ii) Examples. The provisions of paragraph (a)(2)(i) of this Q&A–5 can be illustrated by the following examples:

Example 1. A plan provides that a single sum distribution option is available only to (A) employees earning $50,000 or more in the final year of employment, (B) employees who furnish evidence that they have a net worth above a certain specified amount, and (C) employees who present a letter from an accountant or attorney declaring that it is in the employee's best interest to receive a single sum distribution. Whether the availability of such optional form of benefit discriminates depends on whether it meets the requirements of Q&A–2 of this § 1.401(a)–4. However, each of the specified conditions limiting the availability of the optional form of benefit may reasonably be expected to discriminate in favor of the highly compensated group in operation because of the likelihood of a significant positive correlation between the ability to meet any of the specified conditions and membership in the highly compensated group.

Example 2. A plan limits the availability of a single sum distribution option to employees employed in one particular division of the employer's company. All the employees of the company are participants in the plan. During the 1988 plan year, the division employs individuals who represent a nondiscriminatory classification of that company's employees (under section 410(b)(1)(B) prior to the effective date of the amendments made to section 410(b) by section 1112(a) of TRA '86) and is unlikely to cease employing such a nondiscriminatory classification in the future. The availability of a single sum distribution under this plan does not result in discrimination during the 1988 plan year and may not reasonably be expected to do so.

(b) Transitional alternatives. If the availability of an optional form of benefit under an existing plan is discriminatory under section 401(a)(4), the plan must be amended either to eliminate the optional form of benefit or to make the availability of the optional form of benefit nondiscriminatory. For example, the availability of an optional form of benefit may be made nondiscriminatory by making such benefit available to sufficient additional employees who are not in the highly compensated group or by imposing nondiscriminatory objective criteria on its availability such that the group of employees to whom the benefit is available is nondiscriminatory. See Q&A–6 of § 1.411(d)–4 for requirements with respect to such objective criteria. If, under an existing plan, the availability of an optional form of benefit may reasonably be expected to discriminate, the plan may be amended in the same manner permitted where the availability of an optional form of benefit is discriminatory. See paragraph (d) of this Q&A–5 for rules limiting the period during which the availability of optional forms of benefit may be eliminated or reduced under this paragraph.

(c) Compliance and amendment date provisions—(1) Operational compliance requirement. On or before the applicable effective date for the plan (see Q&A–6 of this section), the plan sponsor must select one of the alternatives permitted under paragraph (b) of this Q&A–5 with respect to each affected optional form of benefit and the plan must be operated

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in accordance with this selection. This is an operational requirement and does not require a plan amendment prior to the period set forth in paragraph (c)(2) of this Q&A–5. There is no special reporting requirement under the Code or this section with respect to this selection.

(2) Deferred amendment date. If paragraph (c)(1) of this Q&A–5 is satisfied, a plan amendment conforming the plan to the particular alternative selected under paragraph (b) of this Q&A–5 must be adopted within the time period permitted for amending plans in order to meet the requirements of section 410(b) as amended by TRA '86. Such conforming amendment must be consistent with the sponsor's selection as reflected by plan practice during the period from the effective date to the date the amendment is adopted. Thus, for example, if an existing calendar year noncollectively bargained defined benefit plan has a single sum distribution form subject to a discriminatory condition, that was available as of January 30, 1986 (subject to such condition), and such employer makes one or more single sum distributions available on or after the first day of the first plan year commencing on or after January 1, 1989, and before the plan amendment, then such employer may not adopt a plan amendment eliminating the single sum distribution form. Instead, such employer must adopt an amendment making the distribution form available to a nondiscriminatory group of employees while retaining the availability of such distribution form with respect to the group of employees to whom the benefit is already available. Similarly, any objective criteria that are adopted as part of such amendment must be consistent with the plan practice for the applicable period prior to the amendment. A conforming amendment under this paragraph (c)(2) must be made with respect to each optional form of benefit for which such amendment is required and must be retroactive to the applicable effective date.

(d) Limitation on transitional alternatives. The transitional alternatives permitting the elimination or reduction of optional forms of benefit will not violate section 411(d)(6) during the period prior to the applicable effective date for the plan (see Q&A–6 of this section). After the applicable effective date, any amendment (other than one described in paragraph (c)(2) of this Q&A–5) that eliminates or reduces an optional form of benefit or imposes new objective criteria restricting the availability of such optional form of benefit will fail to qualify for the exception to section 411(d)(6) provided in this Q&A–5. This is the case without regard to whether the availability of the optional form of benefit is discriminatory or may reasonably be expected to be discriminatory.

Q–6: For what period are the rules of this section effective?

A–6: (a) General effective date—(1) In general. Except as otherwise provided in this section, the provisions of this section are effective January 30, 1986, and do not apply to plan years beginning on or after January 1, 1994. For rules applicable to plan years beginning on or after January 1, 1994, see §§ 1.401(a)(4)–1 through 1.401(a)(4)–13.

(2) Plans of tax-exempt organizations. In the case of plans maintained by organizations exempt from income taxation under section 501(a), including plans subject to section 403(b)(12)(A)(i) (nonelective plans), except as otherwise provided in this section, the provisions of this section are effective January 30, 1986, and do not apply to plan years beginning on or after January 1, 1996. For rules applicable to plan years beginning on or after January 1, 1996, see §§ 1.401(a)(4)–1 through 1.401(a)(4)–13.

(b) New plans—(1) In general. Unless otherwise provided in paragraph (b)(2) of this Q&A–6, plans that are either adopted or made effective on or after January 30, 1986, are "new plans". With respect to such new plans, this section is effective January 30, 1986. This effective date is applicable to such plans whether or not they are collectively bargained.

(2) Exception with respect to certain new plans. Plans that are new plans as defined in paragraph (b)(1) of this Q&A–6, under which the availability of an optional form of benefit is discriminatory or may reasonably be expected to be discriminatory, and that receive a favorable determination letter that covered such plan provisions with respect to an application submitted prior to July 11, 1988, will be treated as existing plans with respect to such optional form of benefit

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for purposes of the transitional rules of this section. Thus, such plans are eligible for the compliance and amendment alternatives set forth in the transitional rule in Q&A–5 of this section.

(c) Existing plans—(1) In general. Plans that are both adopted and in effect prior to January 30, 1986, are "existing plans". In addition, new plans described in paragraph (b)(2) of this Q&A–6 are treated as existing plans with respect to certain forms of benefit. Subject to the limitations in paragraph (d) of this Q&A–6, the effective dates set forth in paragraphs (c)(2) and (c)(3) of this Q&A–6 apply to these existing plans for purposes of this section.

(2) Existing noncollectively bargained plans. With respect to existing noncollectively bargained plans, this section is effective for the first day of the first plan year commencing on or after January 1, 1989.

(3) Existing collectively bargained plans. With respect to existing collectively bargained plans, this section is effective for the later of the first day of the first plan year commencing on or after January 1, 1989, or the first day of the first plan year that the requirements of section 410(b) as amended by TRA '86 apply to such plan.

(d) Delayed effective dates not applicable to new optional forms of benefit or conditions—(1) In general. The delayed effective dates in paragraph (c)(2) and (3) of this Q&A–6 for existing plans are applicable with respect to an optional form of benefit only if both the optional form of benefit and any applicable condition either causing the availability of such optional form of benefit to be discriminatory or making it reasonable to expect that the availability of such optional form will be discriminatory were both adopted and in effect prior to January 30, 1986. If the preceding sentence is not satisfied with respect to an optional form of benefit, this section is effective with respect to such optional form of benefit as if the plan were a new plan.

(2) Exception for certain amendments covered by a favorable determination letter. If a condition causing the availability of an optional form of benefit to be discriminatory, or to be reasonably expected to discriminate, was adopted or made effective on or after January 30, 1986, and a favorable determination letter that covered such plan provision is or was received with respect to an application submitted before July 11, 1988, the effective date of this section with respect to such provision is the applicable effective date determined under the rules with respect to existing plans, as though such provision had been adopted and in effect prior to January 30, 1986.

(e) Transitional rule effective date. The transitional rule provided in Q&A–5 of this section is effective January 30, 1986.

Credits

[T.D. 8212, 53 FR 26054, July 11, 1988; T.D. 8360, 56 FR 47536, Sept. 19, 1991; T.D. 8485, 58 FR 46778, Sept. 3, 1993; T.D. 8212, 61 FR 14247, April 1, 1996]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Notes of Decisions (2)

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit-Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.401(a)(5)-1, Treas. Reg. § 1.401(a)(5)-1

§ 1.401(a)(5)-1 Special rules relating to nondiscrimination requirements.

Currentness

(a) In general. Section 401(a)(5) sets out certain provisions that will not of themselves be discriminatory within the meaning of section 410(b)(2)(A)(i) or section 401(a)(4). The exceptions specified in section 401(a)(5) are not an exclusive enumeration, but are merely a recital of provisions frequently encountered that will not of themselves constitute prohibited discrimination in contributions or benefits. See section 401(a)(4) and the regulations thereunder for the basic nondiscrimination rules. See § 1.410(b)-4 for the rule of section 410(b)(2)(A)(i) (relating to the nondiscriminatory classification test that is part of the minimum coverage requirements) referred to in section 401(a)(5)(A). See paragraphs (b) through (f) of this section for special rules used in applying the section 401(a)(4) nondiscrimination requirements under the remaining provisions of section 401(a)(5).

(b) Salaried or clerical employees. A plan does not fail to satisfy the nondiscrimination requirements of section 401(a)(4) merely because contributions or benefits provided under the plan are limited to salaried or clerical employees.

(c) Uniform relationship to compensation. A plan does not fail to satisfy the nondiscrimination requirements of section 401(a)(4) merely because the contributions or benefits of, or on behalf of, the employees under the plan bear a uniform relationship to the compensation (within the meaning of section 414(s)) of those employees.

(d) Certain disparity permitted. Under section 401(a)(5)(C), a plan does not discriminate in favor of highly compensated employees (as defined in section 414(q)), within the meaning of section 401(a)(4), in the amount of employer-provided contributions or benefits solely because—

(1) In the case of a defined contribution plan, employer contributions allocated to the accounts of employees favor highly compensated employees in a manner permitted by section 401(l) (relating to permitted disparity in plan contributions and benefits), and

(2) In the case of a defined benefit plan, employer-provided benefits favor highly compensated employees in a manner permitted by section 401(l) (relating to permitted disparity in plan contributions and benefits).

See §§ 1.401(l)-1 through 1.401(l)-6 for rules under which a plan may satisfy section 401(l) for purposes of the safe harbors of §§ 1.401(a)(4)-2(b)(3) and 1.401(a)(4)-3(b).

(e) Defined benefit plans integrated with social security—(1) In general. Under section 401(a)(5)(D), a defined benefit plan does not discriminate in favor of highly compensated employees (as defined in section 414(q)) with respect to the amount of employer-provided contributions or benefits solely because the plan provides that, with respect to each employee, the employer-provided accrued retirement benefit under the plan is limited to the excess (if any) of—

(i) The employee's final pay from the employer, over

(ii) The employer-provided retirement benefit created under the Social Security Act and attributable to service by the employee for the employer.

(2) Final pay. For purposes of paragraph (e)(1)(i) of this section, an employee's final pay from the employer as of a plan year is the employee's compensation (as defined in section 414(q)(7)) for the year (ending with or within the 5–plan-year period ending with the plan year in which the employee terminates from employment with the employer) in which the employee receives the highest compensation from the employer. Notwithstanding the preceding sentence, final pay for each employee under the plan may be determined with reference to the 5–plan-year period ending with the plan year before the plan year in which the employee terminates from employment with the employer. In determining an employee's final pay, the plan may specify any 12–month period (ending with or within the applicable 5–plan-year period) as a year provided the specified 12–month period is uniformly and consistently applied with respect to all employees. In determining an employee's final pay, compensation for any year in excess of the applicable limit under section 401(a)(17) for the year may not be taken into account.

(3) Rules for determining amount of employer-provided social security retirement benefit. For purposes of paragraph (e)(1)(ii) of this section, the following rules apply.

(i) The employer-provided retirement benefit on which any reduction or offset in the employee's accrued retirement benefit is based is limited solely to the employer-provided primary insurance amount payable under section 215 of the Social Security Act attributable to service by the employee for the employer.

(ii) The employer-provided primary insurance amount attributable to service by the employee for the employer is determined by multiplying the employer-provided portion of the employee's projected primary insurance amount by a fraction (not exceeding 1), the numerator of which is the employee's number of complete years of covered service for the employer under the Social Security Act, and the denominator of which is 35.

(4) Projected primary insurance amount. (i) As of a plan year, an employee's projected primary insurance amount is the primary insurance amount, determined as of the close of the plan year (the "determination date"), payable to the employee upon attainment of the employee's social security retirement age (as determined under section 415(b)(8)), assuming the employee's annual compensation from the employer that is treated as wages for purposes of the Social Security Act remains the same from the plan year until the employee's attainment of social security retirement age. With respect to service by the employee for the employer before the determination date, the actual compensation paid to the employee by the employer during all periods of service of the employee for the employer covered by the Social Security Act must be used in determining an employee's projected primary insurance amount. With respect to years before the employee's commencement of service for the employer, in determining the employee's

projected primary insurance amount, it may be assumed that the employee received compensation in an amount computed by using a six-percent salary scale projected backwards from the determination date to the employee's 21st birthday. However, if the employee provides the employer with satisfactory evidence of the employee's actual past compensation for the prior years treated as wages under the Social Security Act at the time the compensation was earned and the actual past compensation results in a smaller projected primary insurance amount, the plan must use the actual past compensation. The plan administrator must give clear written notice to each employee of the employee's right to supply actual compensation history and of the financial consequences of failing to supply the history. The notice must be given each time the summary plan description is provided to the employee and must also be given upon the employee's separation from service. The notice must also state that the employee can obtain the actual compensation history from the Social Security Administration. In determining the employee's projected primary insurance amount, the employer may not take into account any compensation from any other employer while the employee is employed by the employer.

(ii) As of a plan year, the employer-provided portion of the employee's projected primary insurance amount under the Social Security Act is 50 percent of the employee's projected primary insurance amount (as determined under paragraph (e)(4)(i) of this section).

(5) Employer-provided accrued retirement benefit. For purposes of this section, the employee's employer-provided accrued retirement benefit as of a plan year is the employee's accrued retirement benefit under the plan (determined on an actual basis and not on a projected basis) attributable to employer contributions under the plan. With respect to plans that provide for employee contributions, see section 411(c) for rules relating to the allocation of accrued benefits between employer contributions and employee contributions.

(6) Additional rules. (i) As of a plan year, paragraph (e)(1) of this section does not apply to the extent that its application would result in a decrease in an employee's accrued benefit. See sections 411(b)(1)(G) and 411(d)(6).

(ii) Section 401(a)(5)(D) and this paragraph (e) do not apply to a plan maintained by an employer, determined for purposes of the Federal Insurance Contributions Act or the Railroad Retirement Tax Act, as applicable, that does not pay any wages within the meaning of section 3121(a) or compensation within the meaning of section 3231(e). For this purpose, a plan maintained for a self-employed individual within the meaning of section 401(c)(1), who is also subject to the tax under section 1401, is deemed to be a plan maintained by an employer that pays wages within the meaning of section 3121(a).

(iii) If a plan provides for the payment of an employee's accrued retirement benefit (whether or not subsidized) commencing before an employee's social security retirement age, the projected employer-provided primary insurance amount attributable to service by the employee for the employer (as determined under paragraphs (e)(3) and (e)(4) of this section) that may be applied as an offset to limit the employee's accrued retirement benefit must be reduced in accordance with § 1.401(l)–3(e)(1). The reduction is made by multiplying the employee's projected employer-provided primary insurance amount by a fraction, the numerator of which is the appropriate factor under § 1.401(l)–3(e)(1), and the denominator of which is 0.75 percent.

(iv) The Commissioner may, in revenue rulings, notices or other documents of general applicability, prescribe additional rules that may be necessary or appropriate to carry out the purposes of this section, including rules relating to the determination of an employee's projected primary insurance amount attributable to the employee's service for former employers and rules applying section 401(a)(5)(D) with respect to an employer that pays wages

within the meaning of section 3121(a) or compensation within the meaning of section 3231(e) for some years and not for other years.

(7) **Examples.** The following examples illustrate this paragraph (e).

Example 1. Employer Z maintains a noncontributory defined benefit plan that uses the calendar year as its plan year. The plan provides a normal retirement benefit, commencing at age 65, equal to $500 a year, multiplied by the employee's years of service for Z, limited to the excess of the amount of the employee's final pay from Z (as determined in accordance with paragraph (e)(2) of this section) over the employee's employer-provided primary insurance amount attributable to the employee's service for Z. If an employee's social security retirement age is greater than 65, the plan provides for reduction of the employee's employer-provided primary insurance amount in accordance with paragraph (e)(6)(iii) of this section. The plan provides no limitation on the number of years of service taken into account in determining benefits under the plan. Employee A retires on July 6, 1995, at A's social security retirement age of 65 with 35 years of service for Z. The plan uses the plan year as the 12–month period for determining an employee's year of final highest pay from the employer. A's compensation for A's final 5 plan years is as follows:

1995 plan year	$10,500
1994 plan year	$20,000
1993 plan year	$18,000
1992 plan year	$17,000
1991 plan year	$16,500

A's annual primary insurance amount under social security, determined as of A's social security retirement age, is $9,000, of which $4,500 is the employer-provided portion attributable to A's service for Z ($9,000 x 50 percent x 35/35). Under the plan's benefit formula (disregarding the final pay limitation), A would be entitled to receive a normal retirement benefit of $17,500 ($500 x 35 years). However, under the plan, A's otherwise determined normal retirement benefit of $17,500 is limited to the excess of the amount of A's final pay from Z over A's employer-provided primary insurance amount under social security attributable to A's service for Z. Accordingly, A's normal retirement benefit is determined to be $15,500 ($20,000 (A's final pay from Z) less $4,500 (A's employer-provided primary insurance amount attributable to A's service for Z)) rather than $17,500. The final pay limitation in Z's plan satisfies section 401(a)(5)(D) and this paragraph (e). Accordingly, the plan maintained by Z does not discriminate in favor of highly compensated employees within the meaning of section 401(a)(4) merely because of the final pay limitation contained in the plan.

Example 2. Assume the same facts as in Example 1, except that A has 32 years of service for Z when A retires at A's social security retirement age. Under the plan's benefit formula (disregarding the final pay limitation), A would be entitled to receive an annual normal retirement benefit of $16,000 ($500 x 32 years). However, the plan provides that A's normal retirement benefit of $16,000 will be limited to $15,500 ($20,000 (the amount of A's final pay from Z) less $4,500 (½ of A's primary insurance amount under the Social Security Act)). The final pay limitation does not satisfy this paragraph (e). The portion of A's employer-provided primary insurance amount under the Social Security Act attributable to A's service for Z is 32/35 x $4,500, or $4,114. Therefore, to satisfy this paragraph (e), the final pay provision in Z's plan may not limit A's otherwise determined normal retirement benefit of $16,000 to less than $15,886 ($20,000 (the amount of X's final pay) minus $4,114 (the portion of A's employer-provided primary insurance amount attributable to A's service for Z)).

Example 3. (a) Employer X maintains a noncontributory defined benefit plan that uses the calendar year as its plan year. The formula for determining benefits under the plan provides a normal retirement benefit at age 65 equal to 90 percent

of an employee's final average compensation, with the benefit reduced by 1/30th for each year of the employee's service less than 30 and limited to the employee's final pay (as determined in accordance with paragraph (e)(2) of this section) less the employee's employer-provided primary insurance amount under social security attributable to the employee's service for X. The plan determines an employee's employer-provided projected primary insurance amount under social security attributable to the employee's service for X in accordance with paragraph (e)(3) of this section and applies the reductions applicable under paragraph (e)(6)(iii) of this section if benefits commence before social security retirement age. The plan determines an employee's accrued benefit under the fractional accrual method of section 411(b)(1)(C).

(b) Employee A commences participation in the plan on January 1, 1990, when A is 35 years of age. A's social security retirement age is 67. As of the close of the 2014 plan year, A's final average compensation from X is $15,000; A's final pay from X is $15,400, and A's projected employer-provided annual primary insurance amount under social security attributable to A's service for X is $4,000 (after the reduction applicable under paragraph (e)(6)(iii) of this section). Under the plan formula, A's accrued benefit as of the close of the 2014 plan year is $11,250 (90 percent x $15,000 x 25/30). As of the close of the 2014 plan year, the plan's final pay limitation does not affect A's benefit because A's benefit under the plan as of the close of the plan year and before application of the final pay limitation ($11,250) does not exceed A's final pay of $15,400 from X, determined as of the close of the plan year, less A's employer-provided projected primary insurance amount under social security attributable to A's service for X ($4,000).

(c) Assume that, as of the close of the 2015 plan year, A's final average compensation from X is $14,500 and A's final pay from X is $15,400. Assume also that as of the close of the 2015 plan year, A's employer-provided primary insurance amount attributable to A's service for X is $4,200 (after the reduction applicable under paragraph (e)(6)(iii) of this section). Accordingly, A's benefit as of the close of the 2015 plan year and before application of the final pay limitation is $11,310 (90 percent x $14,500 x 26/30). Under the plan's final pay limitation, A's benefit of $11,310 would be limited to $11,200, the amount of A's final pay from X ($15,400), less A's employer-provided projected primary insurance amount under social security attributable to A's service for X ($4,200). However, the plan's final pay limitation may not be applied to limit A's accrued benefit for the 2015 plan year to an amount below $11,250, which was A's accrued benefit under the plan at the close of the prior plan year. The foregoing is further illustrated in the following table for the plan years presented above and for additional years of service performed by A for X.

Table

[In dollar amounts]

1	2	3	4	5	6	7
Years of service	**Final average compensation**	**Benefit under plan formula (Column 2 x 0.9 x years of service/ 30)**	**Final pay**	**Employer-provided projected primary insurance amount under social security attributable to service for employer**	**Benefit if final pay reduction is applied in full (Column 4 Column 5)**	**Benefit to which A is entitled (smaller of Column 6 or Column 3, but not less than Column 7 for prior year)**
25..	$15,000	$11,250	$15,400	$4,000	$11,400	$11,250
26..	14,500	11,310	15,400	4,200	11,200	11,250

27	15,500	12,555	15,800	4,400	11,400	11,400
28	15,500	13,020	16,000	4,500	11,500	11,500
29	15,000	13,050	16,000	4,800	11,200	11,500
30	14,500	13,050	16,000	5,000	11,000	11,500

(f) Certain benefits not taken into account. In determining whether a plan satisfies section 401(a)(4) and this section, other benefits created under state or federal law (e.g., worker's compensation benefits or black lung benefits) may not be taken into account.

(g) More than one plan treated as single plan. [Reserved]

(h) Effective date—(1) In general. Except as provided in paragraph (h)(2) of this section, this section is effective for plan years beginning on or after January 1, 1994.

(2) Plans of tax-exempt organizations. In the case of plans maintained by organizations exempt from income taxation under section 501(a), including plans subject to section 403(b)(12)(A)(i) (nonelective plans), this section is effective for plan years beginning on or after January 1, 1996.

(3) Compliance during transition period. For plan years beginning before the effective date of these regulations, as set forth in paragraphs (h)(1) and (h)(2) of this section, and on or after the first day of the first plan year to which the amendments made to section 401(a)(5) by section 1111(b) of the Tax Reform Act of 1986 (TRA '86) apply, a plan must be operated in accordance with a reasonable, good faith interpretation of section 401(a)(5), taking into account pre-existing guidance and the amendments made by TRA '86 to related provisions of the Code. Whether a plan is operated in accordance with a reasonable, good faith interpretation of section 401(a)(5) will generally be determined based on all of the relevant facts and circumstances, including the extent to which an employer has resolved unclear issues in its favor. A plan will be deemed to be operated in accordance with a reasonable, good faith interpretation of section 401(a)(5) if it is operated in accordance with the terms of this section.

Credits

[T.D. 8359, 56 FR 47614, Sept. 19, 1991; T.D. 8359, 57 FR 10817, 10818, March 30, 1992; T.D. 8359, 57 FR 10951, March 31, 1992; T.D. 8486, 58 FR 46830, Sept. 3, 1993]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
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Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.401(a)–11, Treas. Reg. § 1.401(a)–11

§ 1.401(a)–11 Qualified joint and survivor annuities.

Currentness

(a) General rule—(1) Required provisions. A trust, to which section 411 (relating to minimum vesting standards) applies without regard to section 411(e)(2), which is a part of a plan providing for the payment of benefits in any form of a life annuity (as defined in paragraph (b)(1) of this section), shall not constitute a qualified trust under section 401(a)(11) and this section unless such plan provides that:

(i) Unless the election provided in paragraph (c)(1) of this section has been made, life annuity benefits will be paid in a form having the effect of a qualified joint and survivor annuity (as defined in paragraph (b)(2) of this section) with respect to any participant who—

(A) Begins to receive payments under such plan on or after the date the normal retirement age is attained, or

(B) Dies (on or after the date the normal retirement age is attained) while in active service of the employer maintaining the plan, or

(C) In the case of a plan which provides for the payment of benefits before the normal retirement age, begins to receive payments under such plan on or after the date the qualified early retirement age (as defined in paragraph (b)(4) of this section) is attained, or

(D) Separates from service on or after the date the normal retirement age (or the qualified early retirement age) is attained and after satisfaction of eligibility requirements for the payment of benefits under the plan (except for any plan requirement that there be filed a claim for benefits) and thereafter dies before beginning to receive life annuity benefits;

(ii) Any participant may elect, as provided in paragraph (c)(1) of this section, not to receive life annuity benefits in the form of a qualified joint and survivor annuity; and

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(iii) If the plan provides for the payment of benefits before the normal retirement age, any participant may elect, as provided in paragraph (c)(2) of this section, that life annuity benefits be payable as an early survivor annuity (as defined in paragraph (b)(3) of this section) upon his death in the event that he—

(A) Attains the qualified early retirement age (as defined in paragraph (b)(4) of this section), and

(B) Dies on or before the day normal retirement age is attained while employed by an employer maintaining the plan.

(2) Certain cash-outs. A plan will not fail to satisfy the requirements of section 401(a)(11) and this section merely because it provides that if the present value of the entire nonforfeitable benefit derived from employer contributions of a participant at the time of his separation from service does not exceed $1,750 (or such smaller amount as the plan may specify), such benefit will be paid to him in a lump sum.

(3) Illustrations. The provisions of subparagraph (1) of this paragraph may be illustrated by the following examples:

Example 1. The X Corporation Defined Contribution Plan was established in 1960. As in effect on January 1, 1974, the plan provided that, upon the participant's retirement, the participant may elect to receive the balance of his account in the form of (1) a single-sum cash payment, (2) a single-sum distribution consisting of X Corporation stock, (3) five equal annual cash payments, (4) a life annuity, or (5) a combination of options (1) through (4). The plan also provided that, if a participant did not elect another form of distribution, the balance of his account would be distributed to him in the form of a single-sum cash payment upon his retirement. Assume that section 401(a)(11) and this section became applicable to the plan as of its plan year beginning January 1, 1976, with respect to persons who were active participants in the plan as of such date (see paragraph (f) of this section). If X Corporation Defined Contribution Plan continues to allow the life annuity payment option after December 31, 1975, it must be amended to provide that if a participant elects a life annuity option the life annuity benefit will be paid in a form having the effect of a qualified joint and survivor annuity, except to the extent that the participant elects another form of benefit payment. However, the plan can continue to provide that, if no election is made, the balance will be paid as a single-sum cash payment. If the trust is not so amended, it will fail to qualify under section 401(a).

Example 2. The Corporation Retirement Plan provides that plan benefits are payable only in the form of a life annuity and also provides that a participant may retire before the normal retirement age of 65 and receive a benefit if he has completed 30 years of service. Under this plan, an employee who begins employment at the age of 18 will be eligible to receive retirement benefits at the age of 48 if he then has 30 years of service. This plan must allow a participant to elect in the time and manner prescribed in paragraph (c)(2) of this section an early survivor annuity (defined in paragraph (b)(3) of this section) to be payable on the death of the participant if death occurs while the participant is in active service for the employer maintaining the plan and on or after the date the participant reaches the qualified early retirement age of 55 (the later of the date the participant reaches the earliest retirement age (age 48) or 10 years before normal retirement age (age 55)) but before the day after the day the participant reaches normal retirement age (age 65).

Example 3. Assume the same facts as in Example 2. A, B, and C began employment with Y Corporation when they each attained age 18. A retires and begins to receive benefit payments at age 48 after completing 30 years of service. The plan is not required to pay a qualified joint and survivor annuity to A and his spouse at any time. B does not elect an early survivor annuity at age 55, but retires at age 57 after completing 39 years of service. Unless B makes an election under subparagraph (1)(ii) of this paragraph, the plan is required to pay a qualified joint and survivor annuity to B and his

spouse. C makes no elections described in subparagraph (1) of this paragraph, and dies while in active service at age 66 after completing 48 years of service. The plan is required to pay a qualified survivor annuity to C's spouse.

(b) Definitions. As used in this section—(1) Life annuity. (i) The term "life annuity" means an annuity that provides retirement payments and requires the survival of the participant or his spouse as one of the conditions for any payment or possible payment under the annuity. For example, annuities that make payments for 10 years or until death, whichever occurs first or whichever occurs last, are life annuities.

(ii) However, the term "life annuity" does not include an annuity, or that portion of an annuity, that provides those benefits which, under section 411(a)(9), would not be taken into account in the determination of the normal retirement benefit or early retirement benefit. For example, "social security supplements" described in the fourth sentence of section 411(a)(9) are not considered to be life annuities for the purposes of this section, whether or not an early retirement benefit is provided under the plan.

(2) Qualified joint and survivor annuity. The term "qualified joint and survivor annuity" means an annuity for the life of the participant with a survivor annuity for the life of his spouse which is neither (i) less than one-half of, nor (ii) greater than, the amount of the annuity payable during the joint lives of the participant and his spouse. For purposes of the preceding sentence, amounts described in § 1.401(a)–11(b)(1)(ii) may be disregarded. A qualified joint and survivor annuity must be at least the actuarial equivalent of the normal form of life annuity or, if greater, of any optional form of life annuity offered under the plan. Equivalence may be determined, on the basis of consistently applied reasonable actuarial factors, for each participant or for all participants or reasonable groupings of participants, if such determination does not result in discrimination in favor of employees who are officers, shareholders, or highly compensated. An annuity is not a qualified joint and survivor annuity if payments to the spouse of a deceased participant are terminated, or reduced, because of such spouse's remarriage.

(3) Early survivor annuity. The term "early survivor annuity" means an annuity for the life of the participant's spouse the payments under which must not be less than the payments which would have been made to the spouse under the joint and survivor annuity if the participant had made the election described in paragraph (c)(2) of this section immediately prior to his retirement and if his retirement had occurred on the day before his death and within the period during which an election can be made under such paragraph (c)(2). For example, if a participant would be entitled to a single life annuity of $100 per month or a reduced amount under a qualified joint and survivor annuity of $80 per month, his spouse is entitled to a payment of at least $40 per month. However, the payments may be reduced to reflect the number of months of coverage under the survivor annuity pursuant to paragraph (e) of this section.

(4) Qualified early retirement age. The term "qualified early retirement age" means the latest of—

(i) The earliest date, under the plan, on which the participant could elect (without regard to any requirement that approval of early retirement be obtained) to receive retirement benefits (other than disability benefits).

(ii) The first day of the 120th month beginning before the participant reaches normal retirement age, or

(iii) The date on which the participant begins participation.

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(5) Normal retirement age. The term "normal retirement age" has the meaning set forth in section 411(a)(8).

(6) Annuity starting date. The term "annuity starting date" means the first day of the first period with respect to which an amount is received as a life annuity, whether by reason of retirement or by reason of disability.

(7) Day. The term "day" means a calendar day.

(c) Elections—(1) Election not to take joint and survivor annuity form—(i) In general. (A) A plan shall not be treated as satisfying the requirements of this section unless it provides that each participant may elect, during the election period described in subdivision (ii) of this subparagraph, not to receive a qualified joint and survivor annuity. However, if a plan provides that a qualified joint and survivor annuity is the only form of benefit payable under the plan with respect to a married participant, no election need be provided.

(B) The election shall be in writing and clearly indicate that the participant is electing to receive all or, if permitted by the plan, part of his benefits under the plan in a form other than that of a qualified joint and survivor annuity. A plan will not fail to meet the requirements of this section merely because the plan requires the participant to obtain the written approval of his spouse in order for the participant to make this election or if the plan provides that such approval is not required.

(ii) Election period. (A) For purposes of the election described in paragraph (c)(1)(i) of this section, the plan shall provide an election period which shall include a period of at least 90 days following the furnishing of all of the applicable information required by subparagraph (3)(i) of this paragraph and ending prior to commencement of benefits. In no event may the election period end earlier than the 90th day before the commencement of benefits. Thus, for example, the commencement of benefits may be delayed until the end of such election period because the amount of payments to be made to a participant cannot be ascertained before the end of such period; see § 1.401(a)–14(d).

If a participant makes a request for additional information as provided in subparagraph (3)(iii) of this paragraph on or before the last day of the election period, the election period shall be extended to the extent necessary to include at least the 90 calendar days immediately following the day the requested additional information is personally delivered or mailed to the participant. Notwithstanding the immediately preceding sentence, a plan may provide in cases in which the participant has been furnished by mail or personal delivery all of the applicable information required by subparagraph (3)(i) of this paragraph, that a request for such additional information must be made on or before a date which is not less than 60 days from the date of such mailing or delivery; and if the plan does so provide, the election period shall be extended to the extent necessary to include at least the 60 calendar days following the day the requested additional information is personally delivered or mailed to the participant.

(B) In the case of a participant in a plan to which this subparagraph applies who separated from service after section 401(a)(11) and this section became applicable to such plan with respect to such participant, and to whom an election required by this subparagraph has not been previously made available (and will not become available in normal course), the plan must provide an election to receive the balance of his benefits (properly adjusted, if applicable, for payments received, prior to the exercise of such election, in the form of a qualified joint and survivor annuity) in a form other than that of a qualified joint and survivor annuity. The provisions of paragraph (c)(1)(ii)(A) shall apply except that in no event shall the election period end before the 90th day

after the date on which notice of the availability of such election and the applicable information required by subparagraph (3)(i) of this paragraph is given directly to the participant. If such notice and information is given by mail, it shall be treated as given on the date of mailing. If such participant has died, such election shall be made available to such participant's personal representative.

(2) Election of early survivor annuity—(i) In general. (A) A plan described in subparagraph (a)(1)(iii) of this section shall not be treated as satisfying the requirements of this section unless it provides that each participant may elect, during the period described in subdivision (ii) of this subparagraph, an early survivor annuity as described in paragraph (a)(1)(iii) of this section. Breaks in service after the participant has attained the qualified early retirement age neither invalidate a previous election or revocation nor prevent an election from being made or revoked during the election period.

(B) The election shall be in writing and clearly indicate that the participant is electing the early survivor annuity form.

(C) A plan is not required to provide an election under this subparagraph if—

(1) The plan provides that an early survivor annuity is the only form of benefit payable under the plan with respect to a married participant who dies while employed by an employer maintaining the plan,

(2) In the case of a defined contribution plan, the plan provides a survivor benefit at least equal in value to the vested portion of the participant's account balance, if the participant dies while in active service with an employer maintaining the plan, or

(3) In the case of a defined benefit plan, the plan provides a survivor benefit at least equal in value to the present value of the vested portion of the participant's normal form of the accrued benefit payable at normal retirement age (determined immediately prior to death), if the participant dies while in active service with an employer maintaining the plan. Any present values must be determined in accordance with either the actuarial assumptions or factors specified in the plan, or a variable standard independent of employer discretion for converting optional benefits specified in the plan.

(ii) Election period. (A) For purposes of the election described in paragraph (c)(2)(i) of this section the plan shall provide an election period which, except as provided in the following sentence, shall begin not later than the later of either the 90th day before a participant attains the qualified early retirement age or the date on which his participation begins, and shall end on the date the participant terminates his employment. If such a plan contains a provision that any election made under this subparagraph does not become effective or ceases to be effective if the participant dies within a certain period beginning on the date of such election, the election period prescribed in this subdivision (ii) shall begin not later than the later of (1) a date which is 90 days plus such certain period before the participant attains the qualified early retirement age or (2) the date on which his participation begins. For example, if a plan provides that an election made under this subparagraph does not become effective if the participant dies less than 2 years after the date of such election, the period for making an election under this subparagraph must begin not later than the later of (1) 2 years and 90 days before the participant attains the qualified early retirement age, or (2) the date on which his participation begins. However, the election period for an individual who was an

active participant on the date this section became effective with regard to the plan need not begin earlier than such effective date.

(B) In the case of a participant in a plan to which this subparagraph applies who dies after section 401(a)(11) and this section became applicable to such plan with respect to such participant and to whom an election required by this subparagraph has not been previously made available, the plan must give the participant's surviving spouse or, if dead, such spouse's personal representative the option of electing an early survivor annuity. The plan may reduce the surviving spouse's annuity to take into account any benefits already received. The period for making such election shall not end before the 90th day after the date on which written notice of the availability of such election and applicable information required by subparagraph (3)(i) of this paragraph is given directly to such surviving spouse or personal representative. If such notice and information is given by mail, it shall be treated as given on the date of mailing.

(3) Information to be provided by plan. For rules regarding the information required to be provided with respect to the election to waive a QJSA or a QPSA, see § 1.417(a)(3)–1.

(4) Election is revocable. A plan to which this section applies must provide that any election made under this paragraph may be revoked in writing during the specified election period, and that after such election has been revoked, another election under this paragraph may be made during the specified election period.

(5) Election by surviving spouse. A plan will not fail to meet the requirements of section 401(a)(11) and this section merely because it provides that the spouse of a deceased participant may elect to have benefits paid in a form other than a survivor annuity. If the plan provides that such a spouse may make such an election, the plan administrator must furnish to this spouse, within a reasonable amount of time after a written request has been made by this spouse, a written explanation in non-technical language of the survivor annuity and any other form of payment which may be selected. This explanation must state the financial effect (in terms of dollars) of each form of payment. A plan need not respond to more than one such request.

(d) Permissible additional plan provisions—(1) In general. A plan will not fail to meet the requirements of section 401(a)(11) and this section merely because it contains one or more of the provisions described in paragraphs (d)(2) through (5) of this section.

(2) Claim for benefits. A plan may provide that as a condition precedent to the payment of benefits, a participant must express in writing to the plan administrator the form in which he prefers benefits to be paid and provide all the information reasonably necessary for the payment of such benefits. However, if a participant files a claim for benefits with the plan administrator and provides the plan administrator with all the information necessary for the payment of benefits but does not indicate a preference as to the form for the payment of benefits, benefits must be paid in the form of a qualified joint and survivor annuity if the participant has attained the qualified early retirement age unless such participant has made an effective election not to receive benefits in such form. For rules relating to provisions in a plan to the effect that a claim for benefits must be filed before the payment of benefits will commence, see § 1.401(a)–14.

(3) Marriage requirements. A plan may provide that a joint and survivor annuity will be paid only if—

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(i) The participant and his spouse have been married to each other throughout a period (not exceeding one year) ending on the annuity starting date.

(ii) The spouse of the participant is not entitled to receive a survivor annuity (whether or not the election described in paragraph (c)(2) of this section has been made) unless the participant and his spouse have been married to each other throughout a period (not exceeding one year) ending on the date of such participant's death.

(iii) The same spouse must satisfy the requirements of subdivisions (i) and (ii) of this subparagraph.

(iv) The participant must notify the plan administrator (as defined by section 414(g)) of his marital status within any reasonable time period specified in the plan.

(4) Effect of participant's death on an election or revocation of an election under paragraph (c). A plan may provide that any election described in paragraph (c) of this section or any revocation of any such election does not become effective or ceases to be effective if the participant dies within a period, not in excess of 2 years, beginning on the date of such election or revocation. However, a plan containing a provision described in the preceding sentence shall not satisfy the requirements of this section unless it also provides that any such election or any revocation of any such election will be given effect in any case in which—

(i) The participant dies from accidental causes,

(ii) A failure to give effect to the election or revocation would deprive the participant's survivor of a survivor annuity, and

(iii) Such election or revocation is made before such accident occurred.

(5) Benefit option approval by third party. **(i)** A plan may provide that an optional form of benefit elected by a participant is subject to the approval of an administrative committee or similar third party. However, the administrative committee cannot deny a participant any of the benefits required by section 401(a)(11). For example, if a plan offers a life annuity option, the committee may deny the participant a qualified joint and survivor annuity only by denying the participant access to all life annuity options without knowledge of whether the participant wishes to receive a qualified joint and survivor annuity. Alternatively, if the committee knows which form of life annuity the participant has chosen before the committee makes its decision, the committee cannot withhold its consent for payment of a qualified joint and survivor annuity even though it denies all other life annuity options. This subparagraph (5) only applies before the effective date of the amendment made to section 411(d)(6) by section 301 of the Retirement Equity Act of 1984. See section 411(d)(6) and the regulations thereunder for rules limiting employer discretion.

(ii) The provisions of this subparagraph may be illustrated by the following example:

Example. In 1980 plan M provides that the automatic form of benefit is a single sum distribution. The plan also permits, subject to approval by the administrative committee, the election of several optional forms of life annuity. On the

election form that is reviewed by the administrative committee the participant indicates whether any life annuity option is preferred, without indicating the particular life annuity chosen. Thus, the committee approves or disapproves the election without knowledge of whether a qualified joint and survivor annuity will be elected. The administrative committee approval provision in Plan M does not cause the plan to fail to satisfy this section. On the other hand, if the form indicates which form of life annuity is preferred, committee disapproval of any election of the qualified joint and survivor annuity would cause the plan to fail to satisfy this section.

(e) Costs of providing qualified joint and survivor annuity form or early survivor annuity form. A plan may take into account in any equitable manner consistent with generally accepted actuarial principles applied on a consistent basis any increased costs resulting from providing qualified joint and survivor annuity and early survivor annuity benefits. A plan may give a participant the option of paying premiums only if it provides another option under which an out-of-pocket expense by the participant is not required.

(f) Application and effective date. Section 401(a)(11) and this section shall apply to a plan only with respect to plan years beginning after December 31, 1975, and shall apply only if—

(1) The participant's annuity starting date did not fall within a plan year beginning before January 1, 1976, and

(2) The participant was an active participant in the plan on or after the first day of the first plan year beginning after December 31, 1975.

For purposes of this paragraph, the term "active participant" means a participant for whom benefits are being accrued under the plan on his behalf (in the case of a defined benefit plan), the employer is obligated to contribute to or under the plan on his behalf (in the case of a defined contribution plan other than a profit-sharing plan), or the employer either is obligated to contribute to or under the plan on his behalf or would have been obligated to contribute to or under the plan on his behalf if any contribution were made to or under the plan (in the case of a profit-sharing plan).

If benefits under a plan are provided by the distribution to the participants of individual annuity contracts, the annuity starting date will be considered for purposes of this paragraph to fall within a plan year beginning before January 1, 1976, with respect to any such individual contract that was distributed to the participant during a plan year beginning before January 1, 1976, if no premiums are paid with respect to such contract during a plan year beginning after December 31, 1975. In the case of individual annuity contracts that are distributed to participants before January 1, 1978, and which contain an option to provide a qualified joint and survivor annuity, the requirements of this section will be considered to have been satisfied if, not later than January 1, 1978, holders of individual annuity contracts who are participants described in the first sentence of this paragraph are given an opportunity to have such contracts amended, so as to provide for a qualified joint and survivor annuity in the absence of a contrary election, within a period of not less than one year from the date such opportunity was offered. In no event, however, shall the preceding sentence apply with respect to benefits attributable to premiums paid after December 31, 1977.

(g) Effect of REA 1984—(1) In general. The Retirement Equity Act of 1984 (REA 1984) significantly changed the qualified joint and survivor annuity rules generally effective for plan years beginning after December 31, 1984. The new survivor annuity rules are primarily in sections 401(a)(11) and 417 as revised by REA 1984 and §§ 1.401(a)–20 and 417(e)–1.

(2) Regulations after REA 1984. (i) REA and the regulations thereunder to the extent inconsistent with pre-REA 1984 section 401(a)(11) and this section are controlling for years to which REA 1984 applies. See e.g., paragraphs (a)(1) and (2) of this section, relating to required provisions and certain cash-outs, respectively and (e), relating to costs of providing annuities, for rules that are inconsistent with REA 1984 and, therefore, are not applicable to REA 1984 years.

(ii) To the extent that the pre-REA 1984 law either is the same as or consistent with REA 1984 and the new regulations hereunder, the rules in this section shall continue to apply for years to which REA 1984 applies. (See, e.g., paragraph (c) (relating to how information is furnished participants and spouses) and paragraph (b) (defining a life annuity) for some of the rules that apply to REA 1984 years.) The rules in this section shall not apply for such years to the extent that they are inconsistent with REA 1984 and the regulations thereunder.

(iii) The Commissioner may provide additional guidance as to the continuing effect of the various rules in this section for years to which REA 1984 applies.

(Authority: Secs. 401(a)(11), 7805 Internal Revenue Code of 1954, (88 Stat. 935, 68A Stat. 917; (26 U.S.C. 401(a)(11), 7805)))

Credits

[T.D. 7458, 42 FR 1466, Jan. 7, 1977; 42 FR 6367, Feb. 2, 1977, as amended by T.D. 7510, 42 FR 53956, Oct. 4, 1977; T.D. 8219, 53 FR 31841, Aug. 22, 1988; T.D. 8219, 53 FR 48534, Dec. 1, 1988; T.D. 9099, 68 FR 70144, Dec. 17, 2003]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Notes of Decisions (22)

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.401(a)–12, Treas. Reg. § 1.401(a)–12

§ 1.401(a)–12 Mergers and consolidations of plans and transfers of plan assets.

Currentness

A trust will not be qualified under section 401 unless the plan of which the trust is a part provides that in the case of any merger or consolidation with, or transfer of assets or liabilities to, another plan after September 2, 1974, each participant in the plan would receive a minimum benefit if the plan terminated immediately after the merger, consolidation, or transfer. This benefit must be equal to or greater than the benefit the participant would have been entitled to receive immediately before the merger, consolidation, or transfer if the plan in which he was a participant had then terminated. This section applies to a multiemployer plan only to the extent determined by the Pension Benefit Guaranty Corporation. For additional rules concerning mergers or consolidations of plans and transfers of plan assets, see section 414(l) and § 1.414(l)–1.

Credits

[T.D. 7638, 44 FR 48195, Aug. 17, 1979]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

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26 C.F.R. § 1.401(a)–13, Treas. Reg. § 1.401(a)–13

§ 1.401(a)–13 Assignment or alienation of benefits.

Currentness

(a) Scope of the regulations. This section applies only to plans to which section 411 applies without regard to section 411(e)(2). Thus, for example, it does not apply to a governmental plan, within the meaning of section 414(d); a church plan, within the meaning of section 414(e), for which there has not been made the election under section 410(a) to have the participation, vesting, funding, etc. requirements apply; or a plan which at no time after September 2, 1974, provided for employer contributions.

(b) No assignment or alienation—(1) General rule. Under section 401(a)(13), a trust will not be qualified unless the plan of which the trust is a part provides that benefits provided under the plan may not be anticipated, assigned (either at law or in equity), alienated or subject to attachment, garnishment, levy, execution or other legal or equitable process.

(2) Federal tax levies and judgments. A plan provision satisfying the requirements of subparagraph (1) of this paragraph shall not preclude the following:

(i) The enforcement of a Federal tax levy made pursuant to section 6331.

(ii) The collection by the United States on a judgment resulting from an unpaid tax assessment.

(c) Definition of assignment and alienation—(1) In general. For purposes of this section, the terms "assignment" and "alienation" include—

(i) Any arrangement providing for the payment to the employer of plan benefits which otherwise would be due the participant under the plan, and

(ii) Any direct or indirect arrangement (whether revocable or irrevocable) whereby a party acquires from a participant or beneficiary a right or interest enforceable against the plan in, or to, all or any part of a plan benefit payment which is, or may become, payable to the participant or beneficiary.

(2) Specific arrangements not considered an assignment or alienation. The terms "assignment" and "alienation" do not include, and paragraph (e) of this section does not apply to, the following arrangements:

(i) Any arrangement for the recovery of amounts described in section 4045(b) of the Employee Retirement Income Security Act of 1974, 88 Stat. 1027 (relating to the recapture of certain payments),

(ii) Any arrangement for the withholding of Federal, State or local tax from plan benefit payments,

(iii) Any arrangement for the recovery by the plan of overpayments of benefits previously made to a participant,

(iv) Any arrangement for the transfer of benefit rights from the plan to another plan, or

(v) Any arrangement for the direct deposit of benefit payments to an account in a bank, savings and loan association or credit union, provided such arrangement is not part of an arrangement constituting an assignment or alienation. Thus, for example, such an arrangement could provide for the direct deposit of a participant's benefit payments to a bank account held by the participant and the participant's spouse as joint tenants.

(d) Exceptions to general rule prohibiting assignments or alienations—(1) Certain voluntary and revocable assignments or alienations. Not withstanding paragraph (b)(1) of this section, a plan may provide that once a participant or beneficiary begins receiving benefits under the plan, the participant or beneficiary may assign or alienate the right to future benefit payments provided that the provision is limited to assignments or alienations which—

(i) Are voluntary and revocable;

(ii) Do not in the aggregate exceed 10 percent of any benefit payment; and

(iii) Are neither for the purpose, nor have the effect, of defraying plan administration costs.

For purposes of this subparagraph, an attachment, garnishment, levy, execution, or other legal or equitable process is not considered a voluntary assignment or alienation.

(2) Benefits assigned or alienated as security for loans. (i) Notwithstanding paragraph (b)(1) of this section, a plan may provide for loans from the plan to a participant or a beneficiary to be secured (by whatever means) by the participant's accrued nonforfeitable benefit provided that the following conditions are met.

(ii) The plan provision providing for the loans must be limited to loans from the plan. A plan may not provide for the use of benefits accrued or to be accrued under the plan as security for a loan from a party other than the plan, regardless of whether these benefits are nonforfeitable within the meaning of section 411 and the regulations thereunder.

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(iii) The loan, if made to a participant or beneficiary who is a disqualified person (within the meaning of section 4975(e)(2)), must be exempt from the tax imposed by section 4975 (relating to the tax imposed on prohibited transactions) by reason of section 4975(d)(1). If the loan is made to a participant or beneficiary who is not a disqualified person, the loan must be one which would be exempt from the tax imposed by section 4975 by reason of section 4975(d)(1) if the loan were made to a disqualified person.

(e) Special rule for certain arrangements—(1) In general. For purposes of this section and notwithstanding paragraph (c)(1) of this section, an arrangement whereby a participant or beneficiary directs the plan to pay all, or any portion, of a plan benefit payment to a third party (which includes the participant's employer) will not constitute an "assignment or alienation" if—

(i) It is revocable at any time by the participant or beneficiary; and

(ii) The third party files a written acknowledgement with the plan administrator pursuant to subparagraph (2) of this paragraph.

(2) Acknowledgement requirement for third party arrangements. In accordance with paragraph (e)(1)(ii) of this section, the third party is required to file a written acknowledgement with the plan administrator. This acknowledgement must state that the third party has no enforceable right in, or to, any plan benefit payment or portion thereof (except to the extent of payments actually received pursuant to the terms of the arrangement). A blanket written acknowledgement for all participants and beneficiaries who are covered under the arrangement with the third party is sufficient. The written acknowledgement must be filed with the plan administrator no later than the later of—

(i) August 18, 1978; or

(ii) 90 days after the arrangement is entered into.

(f) Effective date. Section 401(a)(13) is applicable as of January 1, 1976, and the plan provision required by this section must be effective as of that date. However, regardless of when the provision is adopted, it will not affect—

(1) Attachments, garnishments, levies, or other legal or equitable process permitted under the plan that are made before January 1, 1976;

(2) Assignments permitted under the plan that are irrevocable on December 31, 1975, including assignments made before January 1, 1976, as security for loans to a participant or beneficiary from a party other than the plan; and

(3) Renewals or extensions of loans described in subparagraph (2) of this paragraph, if—

(i) The principal amount of the obligation outstanding on December 31, 1975 (or, if less, the principal amount outstanding on the date of renewal or extension), is not increased;

(ii) The loan, as renewed or extended, does not bear a rate of interest in excess of the rate prevailing for similar loans at the time of the renewal or extensions; and

(iii) With respect to loans that are renewed or extended to bear a variable interest rate, the formula for determining the applicable rate is consistent with the formula for formulae prevailing for similar loans at the time of the renewal or extension. For purposes of subparagraphs (2) and (3) of this paragraph, a loan from a party other than the plan made after December 31, 1975, will be treated as a new loan. This is so even if the lender's security interest for the loan arises from an assignment of the participant's accrued nonforfeitable benefit made before that date.

(g) Special rules for qualified domestic relations orders—(1) Definition. The term "qualified domestic relations order" (QDRO) has the meaning set forth in section 414(p). For purposes of the Internal Revenue Code, a QDRO also includes any domestic relations order described in section 303(d) of the Retirement Equity Act of 1984.

(2) Plan amendments. A plan will not fail to satisfy the qualification requirements of section 401(a) or 403(a) merely because it does not include provisions with regard to a QDRO.

(3) Waiver of distribution requirements. A plan shall not be treated as failing to satisfy the requirements of sections 401(a) and (k) and 409(d) solely because of a payment to an alternate payee pursuant to a QDRO. This is the case even if the plan provides for payments pursuant to a QDRO to an alternate payee prior to the time it may make payments to a participant. Thus, for example, a pension plan may pay an alternate payee even though the participant may not receive a distribution because he continues to be employed by the employer.

(4) Coordination with section 417—(i) Former spouse. (A) In general. Under section 414(p)(5), a QDRO may provide that a former spouse shall be treated as the current spouse of a participant for all or some purposes under sections 401(a)(11) and 417.

(B) Consent. (1) To the extent a former spouse is treated as the current spouse of the participant by reason of a QDRO, any current spouse shall not be treated as the current spouse. For example, assume H is divorced from W, but a QDRO provides that H shall be treated as W's current spouse with respect to all of W's benefits under a plan. H will be treated as the surviving spouse under the QPSA and QJSA unless W obtains H's consent to waive the QPSA or QJSA or both. The fact that W married S after W's divorce from H is disregarded. If, however, the QDRO had provided that H shall be treated as W's current spouse only with respect to benefits that accrued prior to the divorce, then H's consent would be needed by W to waive the QPSA or QJSA with respect to benefits accrued before the divorce. S's consent would be required with respect to the remainder of the benefits.

(2) In the preceding examples, if the QDRO ordered that a portion of W's benefit (either through separate accounts or a percentage of the benefit) must be distributed to H rather than ordering that H be treated as W's spouse, the survivor annuity requirements of sections 401(a)(11) and 417 would not apply to the part of W's benefit awarded H. Instead, the terms of the QDRO would determine how H's portion of W's accrued benefit is paid. W is required to obtain S's consent if W elects to waive either the QJSA or QPSA with respect to the remaining portion of W's benefit.

(C) Amount of the QPSA or QJSA. (1) Where, because of a QDRO, more than one individual is to be treated as the surviving spouse, a plan may provide that the total amount to be paid in the form of a QPSA or survivor portion of a QJSA may not exceed the amount that would be paid if there were only one surviving spouse. The QPSA or survivor portion of the QJSA, as the case may be, payable to each surviving spouse must be paid as an annuity based on the life of each such spouse.

(2) Where the QDRO splits the participant's accrued benefit between the participant and a former spouse (either through separate accounts or percentage of the benefit), the surviving spouse of the participant is entitled to a QPSA or QJSA based on the participant's accrued benefit as of the date of death or the annuity starting date, less the separate account or percentage that is payable to the former spouse. The calculation is made as if the separate account or percentage had been distributed to the participant prior to the relevant date.

(ii) Current spouse. Under section 414(p)(5), even if the applicable election periods (i.e., the first day of the year in which the participant attains age 35 and 90 days before the annuity starting date) have not begun, a QDRO may provide that a current spouse shall not be treated as the current spouse of the participant for all or some purposes under sections 401(a)(11) and 417. A QDRO may provide that the current spouse waives all future rights to a QPSA or QJSA.

(iii) Effects on benefits. (A) A plan is not required to provide additional vesting or benefits because of a QDRO.

(B) If an alternate payee is treated pursuant to a QDRO as having an interest in the plan benefit, including a separate account or percentage of the participant's account, then the QDRO cannot provide the alternate payee with a greater right to designate a beneficiary for the alternate payee's benefit amount than the participant's right. The QJSA or QPSA provisions of section 417 do not apply to the spouse of an alternate payee.

(C) If the former spouse who is treated as a current spouse dies prior to the participant's annuity starting date, then any actual current spouse of the participant is treated as the current spouse, except as otherwise provided in a QDRO.

(iv) Section 415 requirements. Even though a participant's benefits are awarded to an alternate payee pursuant to a QDRO, the benefits are benefits of the participant for purposes of applying the limitations of section 415 to the participant's benefits.

Credits

[T.D. 7534, 43 FR 6943, Feb. 17, 1978; T.D. 8219, 53 FR 31850, Aug. 22, 1988; T.D. 8219, 53 FR 48534, Dec. 1, 1988]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Notes of Decisions (26)

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Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.410(b)–1, Treas. Reg. § 1.410(b)–1

§ 1.410(b)–1 Minimum coverage requirements (before 1994).

Currentness

(a) In general. A plan is not a qualified plan (and a trust forming a part of the plan is not a qualified trust) unless the plan satisfies section 410(b)(1). For plan years prior to the applicable effective date set forth in § 1.410(b)–10, a plan satisfies section 410(b)(1) if it satisfies the requirements of paragraph (b)(1) or (b)(2) of this section. See also § 1.410(b)–2 for plan years beginning on or after the applicable effective date set forth in § 1.410(b)–10.

(b) Coverage tests—(1) Percentage test. A plan satisfies the requirements of this subparagraph if it benefits—

(i) Seventy percent or more of all employees, or

(ii) Eighty percent or more of all employees who are eligible to benefit under the plan if 70 percent or more of all the employees are eligible to benefit under the plan,

excluding in each case employees who have not satisfied the minimum age and service requirements (if any) prescribed by the plan, as of the date coverage is tested, as a condition of participation and employees permitted to be excluded under paragraph (c) of this section. The percentage requirements of this subparagraph refer to a percentage of active employees, including employees temporarily on leave, such as those in the Armed Forces of the United States, if such employees are eligible under the plan.

(2) Classification test. A plan satisfies the requirements of section 410(b)(1) and this subparagraph if it benefits such employees as qualify under a classification of employees set up by the employer, which classification is found by the Internal Revenue Service not to be discriminatory in favor of employees who are officers, shareholders, or highly compensated. For purposes of this subparagraph, except as provided by paragraph (c) of this section, all active employees (including employees who do not satisfy the minimum age or service requirements of the plan) are taken into account.

(c) Exclusion of certain employees. Under section 410(b)(2), for purposes of section 410(b)(1) and paragraph (b) of this section, there shall be excluded from consideration employees described in subparagraphs (1), (2), and (3) of this paragraph.

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(1) Bargaining unit. Under section 410(b)(2)(A) and this paragraph, there may be excluded from consideration employees not included in the plan who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if the Internal Revenue Service finds that retirement benefits were the subject of good faith bargaining between such employee representatives and such employer or employers. For purposes of determining whether such bargaining occurred, it is not material that such employees are not covered by another plan or that the plan was not considered in such bargaining.

(2) Air pilots. Under section 410(b)(2)(B) and this paragraph there may be excluded from consideration, in the case of a plan established or maintained pursuant to an agreement which the Secretary of Labor finds to be a collective bargaining agreement between air pilots represented in accordance with title II of the Railway Labor Act and one or more employers all employees not covered by such agreement. Section 410(b)(2)(B) and this subparagraph do not apply to a plan if the plan provides contributions or benefits for employees whose principal duties are not customarily performed aboard aircraft in flight.

(3) Nonresident aliens. Under section 410(b)(2)(C) and this paragraph, there may be excluded from consideration employees who are nonresident aliens and who receive no earned income (within the meaning of section 911(b) and the regulations thereunder) from the employer which constitutes income from sources within the United States (within the meaning of section 861(a)(3) and the regulations thereunder).

(d) Special rules—(1) Highly compensated. The classification of an employee as highly compensated for purposes of section 410(b)(1)(B) and § 1.410(b)–1(b)(2) is made on the basis of the facts and circumstances of each case, taking into account the level of the employee's compensation and the level of compensation paid by the employer to other employees, whether or not covered by the plan. Average compensation levels determined on a local, regional, or national basis, are not relevant for this purpose. Further, the classification of an employee as highly compensated is not made solely on the basis of the number or percentage of employees whose compensation exceeds, or is exceeded by, the employee's.

(2) Discrimination. The determination as to whether a plan discriminates in favor of employees who are officers, shareholders, or highly compensated is made on the basis of the facts and circumstances of each case, allowing a reasonable difference between the ratio of such employees benefited by the plan to all such employees of the employer and the ratio of the employees (other than officers, shareholders, or highly compensated) of the employer benefited by the plan to all employees (other than officers, shareholders, or highly compensated). A showing that a specified percentage of employees covered by a plan are not officers, shareholders, or highly compensated, is not in itself sufficient to establish that the plan does not discriminate in favor of employees who are officers, shareholders, or highly compensated.

(3) Multiple plans—(i) An employer may designate two or more plans as constituting a single plan which is intended to qualify for purposes of section 410(b)(1) and this section, in which case all plans so designated shall be considered as a single plan in determining whether the requirements of such section are satisfied by each of the separate plans. A determination that the combination of plans so designated does not satisfy such requirements does not preclude a determination that one or more of such plans, considered separately, satisfies such requirements.

(ii) Notwithstanding subdivision (i) of this subparagraph, a plan which is subject to the limitations of section 401(a)(17) of the Code or section 301(d)(3) of the Tax Reduction Act of 1975 cannot be considered with any other plan which covers any employee covered by such plan.

(4) Profit-sharing plans. Employees under a profit-sharing plan who receive the amounts allocated to their accounts before the expiration of a period of time or the occurrence of a contingency specified in the plan shall not be considered covered by the plan. Thus, in case a plan permits employees to receive immediately the amounts allocated to their accounts, or to have such amounts paid to a profit-sharing plan for them, the employees who receive the shares immediately shall not be considered covered by the plan.

(5) Certain classifications. See section 401(a)(5) and the regulations thereunder for rules relating to classifications of employees which are not considered to be discriminatory per se for purposes of section 410(b)(1)(B) and § 1.410(b)–1(b)(2).

(6) Integration with Social Security Act. See section 401(a)(5) and the regulations thereunder for rules relating to integration of plans with the Social Security Act.

(7) Different age and service requirements—(i) Application. The rules of this subparagraph (7) apply to a plan which must satisfy the minimum age and service requirements of section 410(a)(1)(A) in order to be a qualified plan. Accordingly, the rules are inapplicable to plans described in section 410(c)(1) (see § 1.410(a)–1(c)(1)); plans satisfying the alternative minimum age and service requirements of section 410(a)(1)(B) but not satisfying the requirements of section 410(a)(1)(A); and plans which provide contributions or benefits for employees, some or all of whom are owner-employees (see section 401(a)(10)).

(ii) General rules. A provision for different age and service requirements for present and future employees either upon establishment or subsequent amendment is not, of itself, discriminatory under section 410(b)(1)(B) even though present employees who are officers, shareholders, or highly compensated cannot meet the age and service requirements for future employees at the time the plan is established or amended and even though present participants who are officers, shareholders, or highly compensated would not have satisfied the age and service requirements for future employees at the time they became participants in the plan. Furthermore, prohibited discrimination will be deemed not to arise in operation, solely because of such different requirements, when future employees are added to the employer's work force.

(8) Certain controlled groups. In applying the percentage test and classification test described in paragraph (b)(1) and (2) of this section for a year, all the employees of corporations or trades and businesses whose employees are treated as employed by a single employer by reason of section 414(b) or (c) must be taken into account. The preceding sentence shall apply for a plan year if, on 1 day in each quarter of such plan year, such corporations are members of a controlled group of corporations (within the meaning of section 414(b)) of such trades or businesses are under common control (within the meaning of section 414(c)).

(9) Transitional rule. In the case of a cash and deferred profit-sharing plan, in existence on June 27, 1974, the requirements of paragraph (b)(2) of this section are satisfied if over one-half of the participants in the plan are among the lowest paid two-thirds of all eligible employees. This subparagraph shall not apply after December 31, 1977.

(e) Example. The rules provided by this section are illustrated by the following example:

Example. An employer established a non-contributory defined benefit plan covering all employees of its ABC Division who are hired prior to age 60 and who are at least 25 years old. The normal retirement age under the plan is age 65. The employer has 100 employees including 20 employees who are under age 25 and 10 employees who were hired over age 60. The plan does not cover 15 employees who are over age 25 and were hired before age 60 because they are not in the ABC Division. Of these 15 excluded employees, 3 have less than 1 year of service. In addition, 12 of the 55 employees covered have less than one year of service. The plan can be shown not to satisfy the requirements of IRC section 410(b)(1)(A) as follows:

(i) Number of employees.......... 100

(ii) Number of employees excluded on account of minimum age and service.......... 20

(iii) (i)–(ii).......... 80

(iv) Number of employees who must be covered if plan is to satisfy IRC section 410(b)(1)(A), 70% of (iii).......... 56

(v) Number of employees actually covered.......... 55

Because the number of employees covered is less than the number of employees who must be covered, the plan does not satisfy the percentage coverage requirements of IRC section 410(b)(1)(A).

(Authority: Sec. 410 (88 Stat. 898; 26 U.S.C. 410))

Credits

[T.D. 7508, 42 FR 47197, Sept. 20, 1977, as amended by T.D. 7735, 45 FR 74722, Nov. 12, 1980; T.D. 8363, 56 FR 47643, Sept. 19, 1991; T.D. 8487, 58 FR 46839, Sept. 3, 1993]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

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Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.410(b)–2, Treas. Reg. § 1.410(b)–2

§ 1.410(b)–2 Minimum coverage requirements (after 1993).

Currentness

(a) In general. A plan is a qualified plan for a plan year only if the plan satisfies section 410(b) for the plan year. A plan satisfies section 410(b) for a plan year if and only if it satisfies paragraph (b) of this section with respect to employees for the plan year and paragraph (c) of this section with respect to former employees for the plan year. The rules in paragraphs (a), (b), and (c) of this section apply to all plans as a condition of qualification, including plans under which no employee is able to accrue any additional benefits (for example, frozen plans). Paragraphs (d), (e), and (f) of this section provide special rules for nonelective section 403(b) plans subject to section 403(b)(12)(A)(i), for governmental and church plans subject to section 410(c), and for certain acquisitions or dispositions, respectively. See § 1.410(b)–7 for rules for determining the "plan" subject to section 410(b).

(b) Requirements with respect to employees—(1) In general. A plan satisfies this paragraph (b) for a plan year if and only if it satisfies at least one of the tests in paragraphs (b)(2) through (b)(7) of this section for the plan year.

(2) Ratio percentage test—(i) In general. A plan satisfies this paragraph (b)(2) for a plan year if and only if the plan's ratio percentage for the plan year is at least 70 percent. This test incorporates both the percentage test of section 410(b)(1)(A) and the ratio test of section 410(b)(1)(B). See § 1.410(b)–9 for the definition of ratio percentage.

(ii) Examples. The following examples illustrate the ratio percentage test of this paragraph (b)(2).

Example 1. For a plan year, Plan A benefits 70 percent of an employer's nonhighly compensated employees and 100 percent of the employer's highly compensated employees. The plan's ratio percentage for the year is 70 percent (70 percent/100 percent), and thus the plan satisfies the ratio percentage test.

Example 2. For a plan year, Plan B benefits 40 percent of the employer's nonhighly compensated employees and 60 percent of the employer's highly compensated employees. Plan B fails to satisfy the ratio percentage test because the plan's ratio percentage is only 66.67 percent (40 percent/60 percent).

(3) Average benefit test. A plan satisfies this paragraph (b)(3) for a plan year if and only if the plan satisfies both the nondiscriminatory classification test of § 1.410(b)–4 and the average benefit percentage test of § 1.410(b)–5 for the plan year.

(4) Certain tax credit employee stock ownership plans. A plan satisfies this paragraph (b)(4) for a plan year if and only if the plan—

(i) Is a tax credit employee stock ownership plan (as defined in section 409(a)),

(ii) Is the only plan of the employer that is intended to qualify under section 401(a), and

(iii) Is a plan that satisfies the rule set forth in section 410(b)(6)(D).

This paragraph (b)(4) is available only for plan years for which the tax credit employee stock ownership plan receives contributions for which the employer is allowed a tax credit under section 41 (as in effect prior to its repeal by the Tax Reform Act of 1986) or section 48(n) (as in effect prior to its amendment by the Tax Reform Act of 1984). The requirement of this paragraph (b)(4) that the plan be the only plan of the employer that is intended to qualify under section 401(a) is not satisfied if the employer has only one plan, but that plan is treated as two or more separate plans under the mandatory disaggregation rules of § 1.410(b)–7(c).

(5) Employers with no nonhighly compensated employees. A plan satisfies this paragraph (b)(5) for a plan year if and only if the plan is maintained by an employer that has no nonhighly compensated employees at any time during the plan year.

(6) Plans benefiting no highly compensated employees. A plan satisfies this paragraph (b)(6) for a plan year if and only if the plan benefits no highly compensated employees for the plan year.

(7) Plans benefiting collectively bargained employees. A plan that benefits solely collectively bargained employees for a plan year satisfies this paragraph (b)(7) for the plan year. If a plan (within the meaning of § 1.410(b)–7(b)) benefits both collectively bargained employees and noncollectively bargained employees for a plan year, § 1.410(b)–7(c)(4) provides that the portion of the plan that benefits collectively bargained employees is treated as a separate plan from the portion of the plan that benefits noncollectively bargained employees. Thus, the mandatorily disaggregated portion of the plan that benefits the collectively bargained employees automatically satisfies this paragraph (b)(7) for the plan year and hence section 410(b). See § 1.410(b)–9 for the definitions of collectively bargained employee and noncollectively bargained employee.

(c) Requirements with respect to former employees—(1) Former employees tested separately. Former employees are tested separately from employees for purposes of section 410(b). Thus, former employees are disregarded in applying the ratio percentage test, the nondiscriminatory classification test, and the average benefit percentage test with respect to the coverage of employees under a plan, and employees are disregarded in applying this section with respect to the coverage of former employees under a plan.

(2) Testing former employees. A plan satisfies section 410(b) with respect to former employees if and only if, under all of the relevant facts and circumstances (including the group of nonexcludable former employees not benefiting under the plan), the group of former employees benefiting under the plan does not discriminate significantly in favor of highly compensated former employees.

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(d) Nonelective contributions under section 403(b) plans. For plan years beginning on or after January 1, 1989, a plan subject to section 403(b)(12)(A)(i) with respect to nonelective contributions (i.e., contributions not made pursuant to a salary reduction agreement) is treated as a plan subject to the requirements of this section. For this purpose, a plan described in the preceding sentence must satisfy the requirements of this section without regard to section 410(c) and paragraph (e) of this section. For plan years beginning before the effective date set forth in § 1.410(b)–10(d), any plan described in section 410(c)(1)(A) (regarding governmental plans) satisfies the requirements of this section.

(e) Certain governmental and church plans. The requirements of section 410(b) do not apply to a plan described in section 410(c)(1) (other than a plan subject to section 403(b)(12)(A)(i) or a plan with respect to which an election has been made under section 410(d)). Such a plan must satisfy section 401(a)(3) as in effect on September 1, 1974. For this purpose, a plan that satisfies section 410(b) (without regard to this paragraph (e)) is treated as satisfying section 401(a)(3) as in effect on September 1, 1974. For plan years beginning before the effective date set forth in § 1.410(b)–10(d), any plan described in section 410(c)(1)(A) (regarding governmental plans) satisfies the requirements of this section and is thus treated as satisfying the requirements of section 401(a)(3) as in effect on September 1, 1974. See § 1.410(b)–10(b)(2) for a special rule for plans of tax-exempt organizations.

(f) Certain acquisitions or dispositions. Section 410(b)(6)(C) (relating to certain acquisitions or dispositions) provides a special rule whereby a plan may be treated as satisfying section 410(b) for a limited period of time after an acquisition or disposition if it satisfies section 410(b) (without regard to the special rule) immediately before the acquisition or disposition and there is no significant change in the plan or in the coverage of the plan other than the acquisition or disposition. For purposes of section 410(b)(6)(C) and this paragraph (f), the terms "acquisition" and "disposition" refer to an asset or stock acquisition, merger, or other similar transaction involving a change in employer of the employees of a trade or business.

(g) Additional rules. The Commissioner may, in revenue rulings, notices, and other guidance of general applicability, provide any additional rules that may be necessary or appropriate in applying the minimum coverage requirements of section 410(b), including (without limitation) additional rules limiting or expanding the methods in § 1.410(b)–5(d) and (e) for determining employee benefit percentages.

Credits

[T.D. 8363, 56 FR 47643, Sept. 19, 1991; T.D. 8363, 57 FR 10817, March 31, 1992; T.D. 8487, 58 FR 46839, Sept. 3, 1993; T.D. 8548, 59 FR 32914, June 27, 1994]

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26 C.F.R. § 1.410(b)-3, Treas. Reg. § 1.410(b)-3

§ 1.410(b)-3 Employees and former employees who benefit under a plan.

Currentness

(a) Employees benefiting under a plan—(1) In general. Except as provided in paragraph (a)(2) of this section, an employee is treated as benefiting under a plan for a plan year if and only if for that plan year, in the case of a defined contribution plan, the employer receives an allocation taken into account under § 1.401(a)(4)-2(c)(2)(ii), or in the case of a defined benefit plan, the employee has an increase in a benefit accrued or treated as an accrued benefit under section 411(d)(6).

(2) Exceptions to allocation or accrual requirement—(i) Section 401(k) and 401(m) plans. Notwithstanding paragraph (a)(1) of this section, an employee is treated as benefiting under a section 401(k) plan for a plan year if and only if the employee is an eligible employee as defined in § 1.401(k)-6 under the plan. Similarly, an employee is treated as benefiting under a section 401(m) plan for a plan year if and only if the employee is an eligible employee as defined in § 1.401(m)-5 under the plan for the plan year.

(ii) Section 415 limits—(A) General rule for defined benefit plans. In determining whether an employee is treated as benefiting under a defined benefit plan for a plan year, plan provisions that implement the limits of section 415 are disregarded. Any plan provision that provides for increases in an employee's accrued benefit under the plan due solely to adjustments under section 415(d)(1), additional years of participation or service under section 415(b)(5), or changes in the defined contribution fraction under section 415(e) is also disregarded, but only if such provision applies uniformly to all employees in the plan.

(B) Defined benefit plans taking section 415 limits into account under section 401(a)(4) testing. Paragraph (a)(2)(ii)(A) of this section does not apply in the case of a defined benefit plan that uses the option in § 1.401(a)(4)-3(d)(2)(ii)(B) to take into account plan provisions implementing the provisions of section 415 in determining accrual rates under the section 401(a)(4) general test.

(C) Defined contribution plans. A defined contribution plan is permitted to apply the rule in the first sentence of paragraph (a)(2)(ii)(A) of this section in determining whether an employee is treated as benefiting under the plan, provided it applies the rule on a consistent basis for all employees in the plan.

(iii) Certain employees treated as benefiting—(A) In general. An employee is treated as benefiting under a plan for a plan year if the employee satisfies all of the applicable conditions for accruing a benefit or receiving an allocation

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for the plan year but fails to have an increase in accrued benefit or to receive an allocation solely because of one or more of the conditions set forth in paragraphs (a)(2)(iii)(B) through (F) of this section.

(B) Certain plan limits. The employee's benefit would otherwise exceed a limit that is applicable on a uniform basis to all employees in the plan. Thus, for example, if the formula under a defined benefit plan takes into account only the first 30 years of service for accrual purposes, an employee who has completed more than 30 years of service is still treated as benefiting under the plan.

(C) Benefits previously accrued. The benefit previously accrued by the employee is greater than the benefit that would be determined under the plan if the benefit previously accrued were disregarded. This could happen, for example, when the plan is applying the wear-away formula of § 1.401(a)(4)–13(c)(4)(ii) and the employee's frozen accrued benefit exceeds the benefit determined under the current formula.

(D) Benefit offset arrangements. The plan offsets the employee's current benefit accrual under an offset arrangement described in § 1.401(a)(4)–3(f)(9) (without regard to whether the offset is attributable to pre-participation service or past service).

(E) Target benefit plans. In the case of a target benefit plan that satisfies the nondiscriminatory amount requirement of § 1.401(a)(4)–1(b)(2) by satisfying the safe harbor in § 1.401(a)(4)–8(b)(3), the employee's theoretical reserve is greater than or equal to the actuarial present value of the fractional rule benefit.

(F) Post-normal retirement age adjustments. The employee has attained normal retirement age under a defined benefit plan and fails to accrue a benefit because of the provisions of section 411(b)(1)(H)(iii) regarding adjustments for delayed retirement.

(iv) Section 412(i) plans—(A) General rule. Notwithstanding paragraph (a)(1) of this section, an employee is treated as benefiting under an insurance contract plan within the meaning of section 412(i) for a plan year if and only if a premium is paid on behalf of the employee for the plan year.

(B) Exceptions. Notwithstanding paragraph (a)(2)(iv)(A) of this section, an employee is treated as benefiting under an insurance contract plan within the meaning of section 412(i) for a plan year if the sole reason that a premium is not paid on behalf of the employee is one of the reasons described in paragraph (a)(2)(iii) of this section. In addition, an employee is treated as benefiting under an insurance contract plan, within the meaning of section 412(i), that is a defined benefit plan if a premium is not paid on behalf of the employee solely because the insurance contracts that have previously been purchased on behalf of the employee guarantee to provide for the employee's projected normal retirement benefit without regard to future premium payments.

(3) Examples. The following examples illustrate the determination of whether an employee is benefiting under a plan for purposes of section 410(b).

Example 1. An employer has 35 employees who are eligible under a defined benefit plan. The plan requires 1,000 hours of service to accrue a benefit. Only 30 employees satisfy the 1,000–hour requirement and accrue a benefit. The five

employees who do not satisfy the 1,000–hour requirement during the plan year are taken into account in testing the plan under section 410(b) but are treated as not benefiting under the plan.

Example 2. An employer maintains a section 401(k) plan. Only employees who are at least age 21 and who complete one year of service are eligible employees under the plan within the meaning of § 1.401(k)–6. Under the rule of paragraph (a)(2)(i) of this section, only employees who have satisfied these age and service conditions are treated as benefiting under the plan.

Example 3. The facts are the same as in Example 2, except that the employer also maintains a section 401(m) plan that provides matching contributions contingent on elective contributions under the section 401(k) plan. The matching contributions are contingent on employment on the last day of the plan year. Under § 1.401(m)–5, because matching contributions are contingent on employment on the last day of the plan year, not all employees who are eligible employees under the section 401(k) plan are eligible employees under the section 401(m) plan. Thus, employees who have satisfied the age and service conditions but who do not receive a matching contribution because they are not employed on the last day of the plan year are treated as not benefiting under the section 401(m) portion of the plan.

(b) Former employees benefiting under a plan—(1) In general. A former employee is treated as benefiting for a plan year if and only if the plan provides an allocation or benefit increase described in paragraph (a)(1) of this section to the former employee for the plan year. Thus, for example, a former employee benefits under a defined benefit plan for a plan year if the plan is amended to provide an ad hoc cost-of-living adjustment in the former employee's benefits. In contrast, because an increase in benefits payable under a plan pursuant to an automatic cost-of-living provision adopted and effective before the beginning of the plan year is previously accrued, a former employee is not treated as benefiting in a subsequent plan year merely because the former employee receives an increase pursuant to such an automatic cost-of-living provision. Any accrual or allocation for an individual during the plan year that arises from the individual's status as an employee is treated as an accrual or allocation of an employee. Similarly, any accrual or allocation for an individual during the plan year that arises from the individual's status as a former employee is treated as an accrual or allocation of a former employee. It is possible for an individual to accrue a benefit both as an employee and as a former employee in a given plan year. During the plan year in which an individual ceases performing services for the employer, the individual is treated as an employee in applying section 410(b) with respect to employees and is treated as a former employee in applying section 410(b) with respect to former employees.

(2) Examples. The following examples illustrate the determination of whether a former employee benefits under a plan for purposes of section 410(b).

Example 1. Employer A amends its defined benefit plan in the 1995 plan year to provide an ad hoc cost-of-living increase of 5 percent for all retirees. Former employees who receive this increase are treated as benefiting under the plan for the 1995 plan year.

Example 2. Employer B maintains a defined benefit plan with a calendar plan year. In the 1995 plan year, Employer B amends the plan to provide that an employee who has reached early retirement age under the plan and who retires before July 31 of the 1995 plan year will receive an unreduced benefit, even though the employee has not yet reached normal retirement age. This early retirement window benefit is provided to employees based on their status as employees. Thus, although individuals who take advantage of the benefit become former employees, the window benefit is treated as provided to employees and is not treated as a benefit for former employees.

Example 3. The facts are the same as Example 2, except that on September 1, 1995, Employer B also amends the defined benefit plan to provide an ad hoc cost-of-living increase effective for all former employees. An individual who ceases performing services for the employer before July 31, 1995, under the early retirement window, and then receives the ad

hoc cost-of-living increase, is treated as benefiting for the 1995 plan year both as an employee with respect to the early retirement window, and as a former employee with respect to the ad hoc COLA.

Credits

[T.D. 8363, 56 FR 47644, Sept. 19, 1991; T.D. 8363, 57 FR 10954, March 31, 1992; T.D. 8487, 58 FR 46839, Sept. 3, 1993; T.D. 9169, 69 FR 78153, 78154, Dec. 29, 2004]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

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Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.410(b)–4, Treas. Reg. § 1.410(b)–4

§ 1.410(b)–4 Nondiscriminatory classification test.

Currentness

(a) In general. A plan satisfies the nondiscriminatory classification test of this section for a plan year if and only if, for the plan year, the plan benefits the employees who qualify under a classification established by the employer in accordance with paragraph (b) of this section, and the classification of employees is nondiscriminatory under paragraph (c) of this section.

(b) Reasonable classification established by the employer. A classification is established by the employer in accordance with this paragraph (b) if and only if, based on all the facts and circumstances, the classification is reasonable and is established under objective business criteria that identify the category of employees who benefit under the plan. Reasonable classifications generally include specified job categories, nature of compensation (i.e., salaried or hourly), geographic location, and similar bona fide business criteria. An enumeration of employees by name or other specific criteria having substantially the same effect as an enumeration by name is not considered a reasonable classification.

(c) Nondiscriminatory classification—(1) General rule. A classification is nondiscriminatory under this paragraph (c) for a plan year if and only if the group of employees included in the classification benefiting under the plan satisfies the requirements of either paragraph (c)(2) or (c)(3) of this section for the plan year.

(2) Safe harbor. A plan satisfies the requirement of this paragraph (c)(2) for a plan year if and only if the plan's ratio percentage is greater than or equal to the employer's safe harbor percentage, as defined in paragraph (c)(4)(i) of this section. See § 1.410(b)–9 for the definition of a plan's ratio percentage.

(3) Facts and circumstances—(i) General rule. A plan satisfies the requirements of this paragraph (c)(3) if and only if—

(A) The plan's ratio percentage is greater than or equal to the unsafe harbor percentage, as defined in paragraph (c)(4)(ii) of this section, and

(B) The classification satisfies the factual determination of paragraph (c)(3)(ii) of this section.

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(ii) Factual determination. A classification satisfies this paragraph (c)(3)(ii) if and only if, based on all the relevant facts and circumstances, the Commissioner finds that the classification is nondiscriminatory. No one particular fact is determinative. Included among the facts and circumstances relevant in determining whether a classification is nondiscriminatory are the following—

(A) The underlying business reason for the classification. The greater the business reason for the classification, the more likely the classification is to be nondiscriminatory. Reducing the employer's cost of providing retirement benefits is not a relevant business reason.

(B) The percentage of the employer's employees benefiting under the plan. The higher the percentage, the more likely the classification is to be nondiscriminatory.

(C) Whether the number of employees benefiting under the plan in each salary range is representative of the number of employees in each salary range of the employer's workforce. In general, the more representative the percentages of employees benefiting under the plan in each salary range, the more likely the classification is to be nondiscriminatory.

(D) The difference between the plan's ratio percentage and the employer's safe harbor percentage. The smaller the difference, the more likely the classification is to be nondiscriminatory.

(E) The extent to which the plan's average benefit percentage (determined under § 1.410(b)–5) exceeds 70 percent.

(4) Definitions—(i) Safe harbor percentage. The safe harbor percentage of an employer is 50 percent, reduced by ¾ of a percentage point for each whole percentage point by which the nonhighly compensated employee concentration percentage exceeds 60 percent. See paragraph (c)(4)(iv) for a table that illustrates the safe harbor percentage and unsafe harbor percentage.

(ii) Unsafe harbor percentage. The unsafe harbor percentage of an employer is 40 percent, reduced by ¾ of a percentage point for each whole percentage point by which the nonhighly compensated employee concentration percentage exceeds 60 percent. However, in no case is the unsafe harbor percentage less than 20 percent.

(iii) Nonhighly compensated employee concentration percentage. The nonhighly compensated employee concentration percentage of an employer is the percentage of all the employees of the employer who are nonhighly compensated employees. Employees who are excludable employees for purposes of the average benefit test are not taken into account.

(iv) Table. The following table sets forth the safe harbor and unsafe harbor percentages at each nonhighly compensated employee concentration percentage:

Nonhighly compensated employee concentration	Safe harbor percentage	Unsafe harbor

percentage		percentage
0-60	50.00	40.00
61	49.25	39.25
62	48.50	38.50
63	47.75	37.75
64	47.00	37.00
65	46.25	36.25
66	45.50	35.50
67	44.75	34.75
68	44.00	34.00
69	43.25	33.25
70	42.50	32.50
71	41.75	31.75
72	41.00	31.00
73	40.25	30.25
74	39.50	29.50
75	38.75	28.75
76	38.00	28.00
77	37.25	27.25
78	36.50	26.50
79	35.75	25.75
80	35.00	25.00
81	34.25	24.25
82	33.50	23.50
83	32.75	22.75
84	32.00	22.00
85	31.25	21.25
86	30.50	20.50
87	29.75	20.00

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88	29.00	20.00
89	28.25	20.00
90	27.50	20.00
91	26.75	20.00
92	26.00	20.00
93	25.25	20.00
94	24.50	20.00
95	23.75	20.00
96	23.00	20.00
97	22.25	20.00
98	21.50	20.00
99	20.75	20.00

(5) Examples. The following examples illustrate the rules in this paragraph (c).

Example 1. Employer A has 200 nonexcludable employees, of whom 120 are nonhighly compensated employees and 80 are highly compensated employees. Employer A maintains a plan that benefits 60 nonhighly compensated employees and 72 highly compensated employees. Thus, the plan's ratio percentage is 55.56 percent ([60/120]/[72/80]=50% /90% =0.5556), which is below the percentage necessary to satisfy the ratio percentage test of § 1.410(b)–2(b)(2). The employer's nonhighly compensated employee concentration percentage is 60 percent (120/200); thus, Employer A's safe harbor percentage is 50 percent and its unsafe harbor percentage is 40 percent. Because the plan's ratio percentage is greater than the safe harbor percentage, the plan's classification satisfies the safe harbor of paragraph (c)(2) of this section.

Example 2. The facts are the same as in Example 1, except that the plan benefits only 40 nonhighly compensated employees. The plan's ratio percentage is thus 37.03 percent ([40/120]/[72/80]=33.33% /90% =0.3703). Under these facts, the plan's classification is below the unsafe harbor percentage and is thus considered discriminatory.

Example 3. The facts are the same as in Example 1, except that the plan benefits 45 nonhighly compensated employees. The plan's ratio percentage is thus 41.67 percent ([45/120]/[72/80]=37.50% /90% =0.4167), above the unsafe harbor percentage (40 percent) and below the safe harbor percentage (50 percent). The Commissioner may determine that the classification is nondiscriminatory after considering all the relevant facts and circumstances.

Example 4. Employer B has 10,000 nonexcludable employees, of whom 9,600 are nonhighly compensated employees and 400 are highly compensated employees. Employer B maintains a plan that benefits 600 nonhighly compensated employees and 100 highly compensated employees. Thus, the plan's ratio percentage is 25.00 percent ([600/9,600]/[100/400]=6.25% /25% =0.2500), which is below the percentage necessary to satisfy the ratio percentage test of § 1.410(b)–2(b)(2). Employer B's nonhighly compensated employee concentration percentage is 96 percent (9,600/10,000); thus, Employer B's safe harbor percentage is 23 percent, and its unsafe harbor percentage is 20 percent. Because the plan's ratio percentage (25.00 percent) is greater than the safe harbor percentage (23.00 percent), the plan's classification satisfies the safe harbor of paragraph (c)(2) of this section.

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Example 5. The facts are the same as in Example 4, except that the plan benefits only 400 nonhighly compensated employees. The plan's ratio percentage is thus 16.67 percent ([400/9,600]/[100/400] =4.17% /25% =0.1667). The plan's ratio percentage is below the unsafe harbor percentage and thus the classification is considered discriminatory.

Example 6. The facts are the same as in Example 4, except that the plan benefits 500 nonhighly compensated employees. The plan's ratio percentage is thus 20.83 percent ([500/9,600]/[100/400]=5.21% /25% =0.2083), above the unsafe harbor percentage (20 percent) and below the safe harbor percentage (23 percent). The Commissioner may determine that the classification is nondiscriminatory after considering all the facts and circumstances.

Credits

[T.D. 8363, 56 FR 47645, Sept. 19, 1991; T.D. 8363, 57 FR 10954, March 31, 1992]

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26 C.F.R. § 1.410(b)-5, Treas. Reg. § 1.410(b)-5

§ 1.410(b)-5 Average benefit percentage test.

Currentness

(a) General rule. A plan satisfies the average benefit percentage test of this section for a plan year if and only if the average benefit percentage of the plan for the plan year is at least 70 percent. A plan is deemed to satisfy this requirement if it satisfies paragraph (f) of this section for the plan year.

(b) Determination of average benefit percentage. The average benefit percentage of a plan for a plan year is the percentage determined by dividing the actual benefit percentage of the nonhighly compensated employees in plans in the testing group for the testing period that includes the plan year by the actual benefit percentage of the highly compensated employees in plans in the testing group for that testing period. See paragraph (d)(3)(ii) of this section for the definition of testing period.

(c) Determination of actual benefit percentage. The actual benefit percentage of a group of employees for a testing period is the average of the employee benefit percentages, calculated separately with respect to each of the employees in the group for the testing period. All nonexcludable employees of the employer are taken into account for this purpose, even if they are not benefiting under any plan that is taken into account.

(d) Determination of employee benefit percentages—(1) Overview. This paragraph (d) provides rules for determining employee benefit percentages. See paragraph (e) of this section for alternative methods for determining employee benefit percentages.

(2) Employee contributions and employee-provided benefits disregarded. Only employer-provided contributions and benefits are taken into account in determining employee benefit percentages. Therefore, employee contributions (including both employee contributions allocated to separate accounts and employee contributions not allocated to separate accounts), and benefits derived from such contributions, are not taken into account in determining employee benefit percentages.

(3) Plans and plan years taken into account—(i) Testing group. All plans included in the testing group under § 1.410(b)-7(e)(1), and only those plans, are taken into account in determining an employee's employee benefit percentage.

(ii) Testing period. An employee's employee benefit percentage is determined on the basis of plan years ending with or within the same calendar year. These plan years are referred to in this section as the relevant plan years or, in the aggregate, as the testing period.

(4) Contributions or benefits basis. Employee benefit percentages may be determined on either a contributions or a benefits basis. Employee benefit percentages for any testing period must be determined on the same basis (contributions or benefits) for all plans in the testing group.

(5) Determination of employee benefit percentage—(i) General rule. The employee benefit percentage for an employee for a testing period is the rate that would be determined for that employee for purposes of applying the general test for nondiscrimination in §§ 1.401(a)(4)–2, 1.401(a)(4)–3, 1.401(a)(4)–8 or 1.401(a)(4)–9, if all the plans in the testing group were aggregated for purposes of section 410(b). Thus, if employee benefit percentages are determined on a contributions basis, each employee's employee benefit percentage is the aggregate normal allocation rate that would be determined for the employee under § 1.401(a)(4)–9(b)(2)(ii)(A) (if the plans in the testing group include both defined benefit and defined contribution plans), the allocation rate that would be determined for the employee under § 1.401(a)(4)–2(c)(2) (if the plans in the testing group include only defined contribution plans), or the equivalent normal allocation rate that would be determined for the employee under § 1.401(a)(4)–8(c)(2) (if the plans in the testing group include only defined benefit plans). Similarly, if employee benefit percentages are determined on a benefits basis, each employee's employee benefit percentage is the aggregate normal accrual rate that would be determined for the employee under § 1.401(a)(4)–9(b)(2)(ii)(B), the normal accrual rate that would be determined for the employee under § 1.401(a)(4)–3(d), or the equivalent accrual rate that would be determined for the employee under § 1.401(a)(4)–8(b)(2), depending on whether the plans in the testing group include both defined benefit and defined contribution plans, only defined benefit plans, or only defined contribution plans.

(ii) Plans with differing plan years. If not all the plans in the testing group share the same plan year, § 1.410(b)–7(d)(5) would ordinarily prohibit them from being aggregated for purposes of section 410(b). In such a case, employee benefit percentages are determined by applying the rules of paragraph (d)(5)(i) of this section separately to each subset of plans in the testing group that share the same plan year (or the same accrual computation period) and aggregating the results for all plans in the testing group. Thus, an employee's employee benefit percentage is determined as the sum of these separate employee benefit percentages that are determined consistently for all the plans in the testing group (except for differences attributable solely to the differences in plan years).

(iii) Options and consistency requirements. In determining employee benefit percentages under this paragraph (d)(5), any optional or alternative methods or rules available for determining rates in §§ 1.401(a)(4)–2, 1.401(a)(4)–3, 1.401(a)(4)–8, or 1.401(a)(4)–9, whichever is applicable, may be applied. Thus, for example, employee benefit percentages may generally be calculated using any of the alternative methods of determining average annual compensation or plan year compensation under § 1.401(a)(4)–12, and using any underlying definition of compensation that satisfies section 414(s). Except as otherwise specifically permitted, the determination of employee benefit percentages must be made on a consistent basis for all employees and for all plans in the testing group as required by §§ 1.401(a)(4)–2(c)(2)(vi), 1.401(a)(4)–3(d)(2)(i), 1.401(a)(4)–8(b)(2)(iv), 1.401(a)(4)–8(c)(2)(iv) or 1.401(a)(4)–9(b)(2)(iv).

(6) Permitted disparity—(i) In general. Permitted disparity may be imputed in determining employee benefit percentages as provided in §§ 1.401(a)(4)–2, 1.401(a)(4)–3, 1.401(a)(4)–8, or 1.401(a)(4)–9, whichever is applicable. When separate employee benefit percentages are determined for individual plans under paragraph (e)(2) of this

section (or for subsets of plans that have the same plan year as described in paragraph (d)(5)(ii) of this section), permitted disparity may be imputed for an employee only in one individual plan (or subset of plans) and may not be imputed for the same employee in another individual plan (or subset of plans). However, if the same average annual compensation or plan year compensation is used to determine employee benefit percentages in more than one plan, the employee's employee benefit percentages for those plans may be summed prior to imputing permitted disparity.

(ii) Plans which may not use permitted disparity. Permitted disparity may be reflected in the determination of rates only to the extent that the plans for which rates are being determined are plans for which the permitted disparity of section 401(l) is available. Thus, for example, if a section 401(k) plan is included in the testing group and permitted disparity is imputed under § 1.401(a)(4)–2(c)(iv), then employee benefit percentages are determined by first calculating an adjusted allocation rate (within the meaning of § 1.401(a)(4)–7(b)(1)) without regard to the amount of allocations under the section 401(k) plan and adding to it the allocation rate for the section 401(k) plan. See § 1.401(l)–1(a)(4) for a list of types of plans for which permitted disparity is not available.

(7) Requirements for certain plans providing early retirement benefits—(i) General rule. If any defined benefit plan in the testing group provides for early retirement benefits in addition to normal retirement benefits to any highly compensated employee, and the average actuarial reduction for any one of these benefits commencing in the five years prior to the plan's normal retirement age is less than four percent per year, then the aggregate most valuable allocation rate, equivalent most valuable allocation rate, aggregate most valuable accrual rate, or most valuable accrual rate must be substituted for the related normal rates in paragraph (d)(5) of this section.

(ii) Exception. Paragraph (d)(7)(i) of this section does not apply if early retirement benefits with average actuarial reductions described in that paragraph are currently available, within the meaning of § 1.401(a)(4)–4(b), under plans in the testing group to a percentage of nonhighly compensated employees that is at least 70 percent of the percentage of highly compensated employees to whom these benefits are currently available.

(e) Additional optional rules—(1) Overview. This paragraph (e) contains various alternative methods for determining employee benefit percentages for a testing period.

(2) Determination of employee benefit percentages as the sum of separately determined rates—(i) In general. Employee benefit percentages may be determined as the sum of separately determined employee benefit percentages for each of the plans in the testing group that are aggregated under paragraphs (d)(5)(i) or (ii) of this section, provided that these employee benefit percentages are determined on a consistent basis for all of these plans pursuant to paragraph (d)(5)(iii) of this section.

(ii) Exception from consistency requirement. The consistency requirement of paragraph (e)(2)(i) of this section is not violated merely because employee benefit percentages are not determined in a consistent manner for all of the plans in the testing group and the inconsistencies in determination of rates among plans are described in paragraph (e)(2)(iii) of this section. The exception in this paragraph (e)(2)(ii) applies only if it is reasonable to believe that the inconsistencies do not result in an average benefit percentage that is significantly higher than the average benefit percentage that would be determined had employee benefit percentages been determined on a consistent basis pursuant to paragraph (d)(5)(iii) of this section.

(iii) Permitted inconsistencies. The following inconsistencies between plans are permitted under this paragraph (e)(2)—

(A) Use of different underlying definitions of section 414(s) compensation in the determination of rates;

(B) Use of different definitions of average annual compensation;

(C) Use of different testing ages;

(D) Use of different fresh-start dates;

(E) Use of different actuarial assumptions for normalization; or

(F) Disregard of actuarial increases after normal retirement age and QPSA charges without regard to any requirement for uniformity in the actuarial increases or QPSA charges.

(3) Determination of employee benefit percentages without regard to plans of another type—(i) General rule. Employee benefit percentages may be determined under plans of one type (i.e., defined benefit plans or defined contribution plans) by treating all plans of the other type (i.e., defined contribution plans or defined benefit plans, respectively) as if they were not part of the testing group, using the method provided in this paragraph (e)(3). If this method is used to determine whether a defined contribution plan satisfies the average benefit percentage test, employee benefit percentages under all defined contribution plans in the testing group must be determined on a contributions basis, and benefits under any defined benefit plans may not be included in the employee benefit percentage. Similarly, if this method is used to determine whether a defined benefit plan satisfies the average benefit percentage test, employee benefit percentages under all defined benefit plans in the testing group must be determined on a benefits basis, and allocations under any defined contribution plans may not be included in the employee benefit percentage.

(ii) Restriction on use of separate testing group determination method. A plan does not satisfy the average benefit percentage test using the method provided in this paragraph (e)(3) unless each of the plans in the testing group of the other type (i.e., defined benefit plan or defined contribution plan) than the plan being tested satisfies the average benefit test of § 1.410(b)–2(b)(3) using the method in this paragraph (e)(3) or satisfies the ratio percentage test of § 1.410(b)–2(b)(2).

(iii) Treatment of permitted disparity. Although under the general rule of this paragraph (e)(3) plans of another type are disregarded in determining employee benefit percentages, the permitted disparity used by those plans (including any permitted disparity that is used by those plans to satisfy § 1.401(a)(4)–1(b)(2)) is nonetheless taken into account in determining the extent to which permitted disparity may be used in determining employee benefit percentages.

(iv) Example. The following example illustrates the rules of this paragraph (e)(3):

Example. Employer A maintains two defined benefit plans, neither of which covers a group of employees that satisfies the ratio percentage test of § 1.410(b)–2(b)(2), and a profit-sharing plan and a section 401(k) plan, each of which benefits a group of employees that satisfies the ratio percentage test of § 1.410(b)–2(b)(2). The defined benefit plans will satisfy the average benefit percentage test if the actual benefit percentage of all nonexcludable nonhighly compensated employees, computed on a benefits basis without regard to contributions under the profit-sharing plan or the section 401(k) plan, is at least 70 percent of the actual benefit percentage of all nonexcludable highly compensated employees, computed on a benefits basis without regard to contributions under the profit-sharing plan or the section 401(k) plan.

(4) Simplified method for determining employee benefit percentages for certain defined benefit plans—(i) In general. An employee's employee benefit percentage with respect to a plan may be determined under the simplified method of paragraph (e)(4)(ii) of this section, provided the following conditions are satisfied:

(A) The only plans included in the testing group are defined benefit plans, and employee benefit percentages under these plans are determined on a benefits basis.

(B) Employee benefit percentages under the plans in the testing group are not required to be determined by taking into account early retirement benefits under paragraph (d)(7) of this section.

(C) The plan is a safe harbor defined benefit plan described in § 1.401(a)(4)–3(b).

(ii) Simplified method—(A) Section 401(l) plans. Under the simplified method of this paragraph (e)(4)(ii), an employee's employee benefit percentage with respect to a section 401(l) plan described in § 1.401(a)(4)–3(b)(3) (i.e., a unit credit plan) may be deemed equal to the employee's excess benefit percentage or gross benefit percentage (as defined in § 1.401(l)–1(c) (14) or (18), respectively), whichever is applicable under the plan's benefit formula in the plan year. In the case of a section 401(l) plan described in § 1.401(a)(4)–3(b)(4) (i.e., a fractional accrual plan), an employee's employee benefit percentage with respect to that plan may be deemed equal to the rate at which the excess or gross benefit, whichever is applicable, accrues for the employee in the plan year, taking into account the plan's benefit formula and the employee's projected service at normal retirement age. The use of this simplified method will be treated as an imputation of permitted disparity. See paragraph (d)(6) of this section for a restriction on multiple use of permitted disparity.

(B) Other plans. Under the simplified method of this paragraph (e)(4)(ii), an employee's employee benefit percentage with respect to a plan described in § 1.401(a)(4)–3(b)(3) that is not a section 401(l) plan and that is not imputing permitted disparity may be deemed equal to the employee's benefit rate in the plan year under the plan's benefit formula. In the case of a plan described in § 1.401(a)(4)–3(b)(4) that is not a section 401(l) plan and that is not imputing permitted disparity, an employee's employee benefit percentage with respect to that plan may be deemed equal to the rate at which the benefit accrues for the employee in the plan year, taking into account the plan's benefit formula and an employee's projected service at normal retirement age.

(5) Three-year averaging period. An employee's employee benefit percentage may be determined for a testing period as the average of the employee's employee benefit percentages determined separately for the testing period and for the immediately preceding one or two testing periods (referred to in this section as an averaging period). Employee benefit percentages of a particular employee that are averaged together within an averaging period must be determined on a consistent basis for all testing periods within the averaging period.

(6) Alternative methods of determining compensation. Employee benefit percentages may be determined on the basis of any definition of compensation that satisfies § 1.414(s)–1(d) (without regard to whether the definition satisfies § 1.414(s)–1(d)(3)), provided that the same definition is used for all employees and it is reasonable to believe that the definition does not result in an average benefit percentage that is significantly higher than the average benefit percentage that would be determined had employee benefit percentages been determined using a definition of compensation that also satisfies § 1.414(s)–1(d)(3).

(f) Special rule for certain collectively bargained plans. A plan (as determined without regard to the mandatory disaggregation rule of § 1.410(b)–7(c)(5)) that benefits both collectively bargained employees and noncollectively bargained employees is deemed to satisfy the average benefit percentage test of this section if—

(1) The provisions of the plan applicable to each employee in the plan are identical to the provisions of the plan applicable to every other employee in the plan, including the plan benefit or allocation formula, any optional forms of benefit, any ancillary benefit, and any other right or feature under the plan, and

(2) The plan would satisfy the ratio percentage test of § 1.410(b)–2(b)(2), if §§ 1.410(b)–6(d) and 1.410(b)–7(c)(5) (the excludable employee and mandatory disaggregation rules for collectively bargained and noncollectively bargained employees) did not apply.

Credits

[T.D. 8363, 56 FR 47646, Sept. 19, 1991; T.D. 8363, 57 FR 10817, March 31, 1992; T.D. 8363, 57 FR 10954, March 31, 1992; T.D. 8487, 58 FR 46840, Sept. 3, 1993]

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26 C.F.R. § 1.410(b)–6, Treas. Reg. § 1.410(b)–6

§ 1.410(b)–6 Excludable employees.

Effective: July 21, 2006
Currentness

(a) Employees—(1) In general. For purposes of applying section 410(b) with respect to employees, all employees of the employer, other than the excludable employees described in paragraphs (b) through (i) of this section, are taken into account. Excludable employees are not taken into account with respect to a plan even if they are benefiting under the plan, except as otherwise provided in paragraph (b) of this section.

(2) Rules of application. Except as specifically provided otherwise, excludable employees are determined separately with respect to each plan for purposes of testing that plan under section 410(b). Thus, in determining whether a particular plan satisfies the ratio percentage test of § 1.410(b)–2(b)(2), paragraphs (b) through (i) of this section are applied solely with reference to that plan. Similarly, in determining whether two or more plans that are permissively aggregated and treated as a single plan under § 1.410(b)–7(d) satisfy the ratio percentage test of § 1.410(b)–2(b)(2), paragraphs (b) through (i) of this section are applied solely with reference to the deemed single plan. In determining whether a plan satisfies the average benefit percentage test of § 1.410(b)–5, the rules of this section are applied by treating all plans in the testing group as a single plan.

(b) Minimum age and service exclusions—(1) In general. If a plan applies minimum age and service eligibility conditions permissible under section 410(a)(1) and excludes all employees who do not meet those conditions from benefiting under the plan, then all employees who fail to satisfy those conditions are excludable employees with respect to that plan. An employee is treated as meeting the age and service requirements on the date that any employee with the same age and service (including service permitted to be taken into account for purposes of nondiscrimination testing under § 1.401(a)(4)–11(d)(3)) would be eligible to commence participation in the plan, as provided in section 410(b)(4)(C).

(2) Multiple age and service conditions. If a plan, including a plan for which an employer chooses the treatment under paragraph (b)(3) of this section, has two or more different sets of minimum age and service eligibility conditions, those employees who fail to satisfy all of the different sets of age and service conditions are excludable employees with respect to the plan. Except as provided in paragraph (b)(3) of this section, an employee who satisfies any one of the different sets of conditions is not an excludable employee with respect to the plan. Differences in the manner in which service is credited (e.g., hours of service calculated in accordance with 29 CFR 2530.200b–2 for hourly employees and elapsed time calculated in accordance with § 1.410(a)–7 for salaried employees) for purposes of applying a service condition are not taken into account in determining whether multiple age and service eligibility conditions exist.

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(3) Plans benefiting certain otherwise excludable employees—(i) In general. An employer may treat a plan benefiting otherwise excludable employees as two separate plans, one for the otherwise excludable employees and one for the other employees benefiting under the plan. See § 1.410(b)–7(c)(3) regarding permissive disaggregation of plans benefiting otherwise excludable employees. The effect of this rule is that employees who would be excludable under paragraph (b)(1) of this section (applied without regard to section 410(a)(1)(B)) but for the fact that the plan does not apply the greatest permissible minimum age and service conditions may be treated as excludable employees with respect to the plan. This treatment is available only if the plan satisfies section 410(b) and § 1.410(b)–2 with respect to these otherwise excludable employees in the manner described in paragraph (b)(3)(ii) of this section.

(ii) Testing portion of plan benefiting otherwise excludable employees. In determining whether the plan that benefits employees who would otherwise be excludable under paragraph (b)(1) of this section (applied without regard to section 410(a)(1)(B)) satisfies section 410(b) and § 1.410(b)–2, employees who have satisfied the greatest permissible minimum age and service conditions with respect to the plan are excludable employees. In addition, if the plan being tested applies minimum age and service conditions and those conditions are less than the maximum permissible minimum age and service conditions, employees who have not satisfied the lower minimum age and service conditions actually provided for in the plan are excludable employees. Thus, for example, if the plan requires attainment of age 18 and 3 months of service, employees who have not attained age 18 or 3 months of service with the employer are excludable employees.

(4) Examples. The following examples illustrate the minimum age and service condition rules of this paragraph (b). In each example, the employer is not treated as operating qualified separate lines of business under section 414(r).

Example 1. An employer maintains Plan A for hourly employees and Plan B for salaried employees. Plan A has no minimum age or service condition. Plan B has no minimum age condition and requires 1 year of service. The employer treats Plans A and B as a single plan for purposes of section 410(b). Because Plan A imposes no minimum age or service condition, all employees of the employer automatically satisfy the minimum age and service conditions of Plan A. Therefore, no employees are excludable under this paragraph (b) in testing Plans A and B for purposes of section 410(b).

Example 2. An employer maintains three plans. Plan C benefits employees in Division C who satisfy the plan's minimum age and service condition of age 21 and 1 year of service. Plan D benefits employees in Division D who satisfy the plan's minimum age and service condition of age 18 and 1 year of service. Plan E benefits employees in Division E who satisfy the plan's minimum age and service condition of age 21 and 6 months of service. The employer treats Plans D and E as a single plan for purposes of section 410(b). In testing Plan C under the ratio percentage test or the nondiscriminatory classification test of section 410(b), employees who are not at least age 21 or who do not have at least 1 year of service are excludable employees under paragraph (b)(1) of this section. In testing Plans D and E, employees who do not satisfy the age and service requirements of either of the two plans are excludable employees under paragraph (b)(2) of this section. Thus, an employee is excludable with respect to Plans D and E only if the employee is not at least age 18 with at least 1 year of service or is not at least age 21 with at least 6 months of service. Thus, an employee who is 19 years old and has 11 months of service is excludable. Similarly, an employee who is 17 years old and has performed 2 years of service is also excludable.

Example 3. An employer maintains three plans. Plan F benefits all employees in Division F (the plan does not apply any minimum age or service condition). Plan G benefits employees in Division G who satisfy the plan's minimum age and service condition of age 18 and 1 year of service. Plan H benefits employees in Division H who satisfy the plan's minimum age and service condition of age 21 and 6 months of service. In testing the employer's plans under the average benefit percentage test provided in § 1.410(b)–5, Plans F, G, and H are treated as a single plan and, as such, use the lowest

minimum age and service condition under the rule of paragraph (b)(2) of this section. Therefore, because Plan F does not apply any minimum age or service condition, no employee is excludable under this paragraph (b).

Example 4. An employer maintains Plan J, which does not apply any minimum age or service conditions. Plan J benefits all employees in Division 1 but does not benefit employees in Division 2. Although Plan J has no minimum age or service condition, the employer wants to exclude employees whose age and service is below the permissible minimums provided in section 410(b)(1)(A). The employer has 110 employees who either do not have 1 year of service or are not at least age 21. Of these 110 employees, 10 are highly compensated employees and 100 are nonhighly compensated employees. Five of these highly compensated employees, or 50 percent, work in Division 1 and thus benefit under Plan J. Thirty-five of these nonhighly compensated employees, or 35 percent, work in Division 1 and thus benefit under Plan J. Plan J satisfies the ratio percentage test of section 410(b) with respect to employees who do not satisfy the greatest permissible minimum age and service requirement because the ratio percentage of that group of employees is 70 percent. Thus, in determining whether or not Plan J satisfies section 410(b), the 110 employees may be treated as excludable employees in accordance with paragraph (b)(3)(i) of this section.

(c) Certain nonresident aliens—(1) General rule. An employee who is a nonresident alien (within the meaning of section 7701(b)(1)(B)) and who receives no earned income (within the meaning of section 911(d)(2)) from the employer that constitutes income from sources within the United States (within the meaning of section 861(a)(3)) is treated as an excludable employee.

(2) Special treaty rule. In addition, an employee who is a nonresident alien (within the meaning of section 7701(b)(1)(B)) and who does receive earned income (within the meaning of section 911(d)(2)) from the employer that constitutes income from sources within the United States (within the meaning of section 861(a)(3)) is permitted to be excluded, if all of the employee's earned income from the employer from sources within the United States is exempt from United States income tax under an applicable income tax convention. This paragraph (c)(2) applies only if all employees described in the preceding sentence are so excluded.

(d) Collectively bargained employees—(1) General rule. A collectively bargained employee is an excludable employee with respect to a plan that benefits solely noncollectively bargained employees. If a plan (within the meaning of § 1.410(b)–7(b)) benefits both collectively bargained employees and noncollectively bargained employees for a plan year, § 1.410(b)–7(c)(4) provides that the portion of the plan that benefits the collectively bargained employees is treated as a separate plan from the portion of the plan that benefits the noncollectively bargained employees. Thus, a collectively bargained employee is always an excludable employee with respect to the mandatorily disaggregated portion of any plan that benefits noncollectively bargained employees.

(2) Definition of collectively bargained employee—(i) In general. A collectively bargained employee is an employee who is included in a unit of employees covered by an agreement that the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, provided that there is evidence that retirement benefits were the subject of good faith bargaining between employee representatives and the employer or employers. An employee is a collectively bargained employee regardless of whether the employee benefits under any plan of the employer. See section 7701(a)(46) and § 301.7701–17T of this chapter for additional requirements applicable to the collective bargaining agreement. An employee who performs hours of service during the plan year as both a collectively bargained employee and a noncollectively bargained employee is treated as a collectively bargained employee with respect to the hours of service performed as a collectively bargained employee and a noncollectively bargained employee with respect to the hours of service performed as a noncollectively

bargained employee. See § 1.410(b)–7(c) for disaggregation rules for plans benefiting collectively bargained and noncollectively bargained employees.

(ii) Special rules for certain employees in multiemployer plans—(A) In general. For purposes of this paragraph (d), in testing the disaggregated portion of a multiemployer plan benefiting noncollectively bargained employees, a noncollectively bargained employee who benefits under the plan may be treated as a collectively bargained employee with respect to all of the employee's hours of service under the rules of paragraphs (d)(2)(ii)(B) through (E) of this section, if the employee is or was a member of a unit of employees covered by a collective bargaining agreement and that agreement or a successor agreement provides for the employee to benefit under the plan in the current plan year. For this purpose, provisions of a participation agreement or similar document are taken into account in determining whether a collective bargaining agreement provides for an employee to benefit under a multiemployer plan.

(B) Employees who were collectively bargained employees during a portion of the current plan year. An employee described in paragraph (d)(2)(ii)(A) of this section who performs services for one or more employers that are parties to the collective bargaining agreement, for the plan, or for the employee representative both as a collectively bargained employee and as a noncollectively bargained employee during a plan year may be treated as a collectively bargained employee for the plan year, provided that at least half of the employee's hours of service during the plan year are performed as a collectively bargained employee.

(C) Employees who were collectively bargained employees during the collective bargaining agreement. An employee described in paragraph (d)(2)(ii)(A) of this section who was a collectively bargained employee with respect to all of the employee's hours of service during a plan year (including employees who are treated as collectively bargained employees with respect to all of their hours of service during a plan year under paragraph (d)(2)(ii)(B) or (E) of this section) may be treated as a collectively bargained employee with respect to all of the employee's hours of service for the duration of the collective bargaining agreement applicable for such plan year or, if later, until the end of the following plan year. For this purpose, a collective bargaining agreement is applicable for a plan year if it provided for the employee to benefit in the plan and was effective for any portion of that plan year. This paragraph (d)(2)(ii)(C) does not apply unless the terms of the plan providing for benefit accruals treat the employee in a manner that is generally no more favorable than similarly-situated employees who are collectively bargained employees.

(D) Employees who previously were collectively bargained employees. An employee who was treated as a collectively bargained employee pursuant to paragraph (d)(2)(ii)(C) of this section may be treated as a collectively bargained employee with respect to all of the employee's hours of service after the end of the period described in paragraph (d)(2)(ii)(C) of this section, provided that the employee is performing services for one or more employers that are parties to the collective bargaining agreement, for the plan, or for the employee representative. This paragraph (d)(2)(ii)(D) does not apply unless the terms of the plan providing for benefit accruals treat the employee in a manner that is generally no more favorable than similarly-situated employees who are collectively bargained employees, and no more than five percent of the employees covered under the multiemployer plan are noncollectively bargained employees (determined without regard to this paragraph (d)(2)(ii)(D)). In determining whether more than five percent of the employees covered under the multiemployer plan are noncollectively bargained employees, those employees who are described in paragraphs (d)(2)(ii)(B) and (C) of this section are treated as collectively bargained employees.

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(E) Transition rule. For a plan year beginning before the applicable effective date of these regulations as set forth in § 1.410(b)-10 (b) or (d), any employee described in paragraph (d)(2)(ii)(A) of this section may be treated as a collectively bargained employee with respect to all of the employee's hours of service for that plan year.

(F) Consistency requirement. The rules in paragraphs (d)(2)(i) and (ii) of this section must be applied to all employees on a reasonable and consistent basis for the plan year.

(iii) Covered by a collective bargaining agreement—(A) General rule. For purposes of paragraph (d)(2)(i) of this section, an employee is included in a unit of employees covered by a collective bargaining agreement if and only if the employee is represented by a bona fide employee representative that is a party to the collective bargaining agreement under which the plan is maintained. Thus, for example, an employee of either a plan or the employee representative that is a party to the collective bargaining agreement under which the plan is maintained is not included in a unit of employees covered by the collective bargaining agreement under which the plan is maintained merely because the employee is covered under the plan pursuant to an agreement entered into by the plan or employee representative on behalf of the employee (other than in the capacity of an employee representative with respect to the employee). This is the case even if all of such employees benefiting under the plan constitute only a de minimis percentage of the total employees benefiting under the plan.

(B) Plans covering professional employees—(1) In general. An employee is not considered included in a unit of employees covered by a collective bargaining agreement for a plan year for purposes of paragraph (d)(2)(iii)(A) of this section if, for the plan year, more than 2 percent of the employees who are covered pursuant to the agreement are professionals. This rule applies to all employees under the agreement, nonprofessionals as well as professionals. Thus, no employees covered by such an agreement are excludable employees with respect to employees who are not covered by a collective bargaining agreement.

(2) Multiple collective bargaining agreements. This paragraph (d)(2)(iii)(B) is applied separately with respect to each collective bargaining agreement. Thus, for example, if a plan benefits two groups of employees, one included in a unit of employees covered by collective bargaining agreement X, more than 2 percent of whom are professionals, and another included in a unit of employees covered by collective bargaining agreement Y, none of whom are professionals, the group covered by agreement X is not considered covered by a collective bargaining agreement and the group covered by agreement Y is considered covered by a collective bargaining agreement.

(3) Application of minimum coverage tests. If a plan covers more than 2 percent professional employees, no employees in the plan are treated as covered by a collective bargaining agreement. A plan that covers more than 2 percent professional employees must satisfy section 410(b) without regard to section 413(b) and the special rule in § 1.410(b)-2(b)(7) of this section (regarding collectively bargained plans). In such cases, all nonexcludable employees must be taken into account. For this purpose, employees included in other collective bargaining units are excludable employees. However, the employees who are not covered by a collective bargaining agreement and the employees who are covered by an agreement that has more than 2 percent professionals are not excludable employees.

(iv) Examples. The following examples illustrate the collective bargaining unit rules of this section.

Example 1. An employer has 700 collectively bargained employees (none of whom is a professional employee) and 300 noncollectively bargained employees (200 of whom are highly compensated employees). For purposes of applying the ratio percentage test of § 1.410(b)–2(b)(2) to Plan X, which benefits only the 300 noncollectively bargained employees, the 700 collectively bargained employees are treated as excludable employees pursuant to paragraph (d) of this section.

Example 2. (i) An employer has 1,500 employees in the following categories:

	Noncollectively bargained employees	Collectively bargained employees	Total
Highly compensated employees	100	100	200
Nonhighly compensated employees	900	400	1,300
Total	1,000	500	1,500

The employer maintains Plan Y, which benefits 1,100 employees, including all of the noncollectively bargained employees (except for 100 nonhighly compensated employees who are noncollectively bargained employees), and 200 of the collectively bargained employees (including the 100 highly compensated employees who are collectively bargained employees). There are no professional employees covered by the collective bargaining agreement. In accordance with § 1.410(b)–7(c)(4), the employer must apply the ratio percentage test of § 1.410(b)–2(b)(2) to Plan Y as if the plan were two separate plans, one benefiting the noncollectively bargained employees and the other benefiting the collectively bargained employees.

(ii) In testing the portion of Plan Y that benefits the noncollectively bargained employees, the collectively bargained employees are excludable employees. That portion's ratio percentage is 88.89 percent ([800/900]/[100/100] = 88.89% /100% = 0.8889), and thus it satisfies the ratio percentage test. The portion of Plan Y that benefits collectively bargained employees automatically satisfies section 410(b) under the special rule in § 1.410(b)–2(b)(7).

(e) Employees of qualified separate lines of business. If an employer is treated as operating qualified separate lines of business for purposes of section 410(b) in accordance with § 1.414(r)–1(b), in testing a plan that benefits employees of one qualified separate line of business, the employees of the other qualified separate lines of business of the employer are treated as excludable employees. The rule in this paragraph (e) does not apply for purposes of satisfying the nondiscriminatory classification requirement of section 410(b)(5)(B). See §§ 1.414(r)–1(c)(2) and 1.414(r)–8 (separate application of section 410(b) to the employees of a qualified separate line of business). In addition, the rule in this paragraph (e) does not apply to a plan that is tested under the special rule for employer-wide plans in § 1.414(r)–1(c)(2)(ii) for a plan year.

(f) Certain terminating employees—(1) In general. An employee may be treated as an excludable employee for a plan year with respect to a particular plan if—

(i) The employee does not benefit under the plan for the plan year,

(ii) The employee is eligible to participate in the plan,

(iii) The plan has a minimum period of service requirement or a requirement that an employee be employed on the last day of the plan year (last-day requirement) in order for an employee to accrue a benefit or receive an allocation for the plan year,

(iv) The employee fails to accrue a benefit or receive an allocation under the plan solely because of the failure to satisfy the minimum period of service or last-day requirement,

(v) The employee terminates employment during the plan year with no more than 500 hours of service, and the employee is not an employee as of the last day of the plan year (for purposes of this paragraph (f)(1)(v), a plan that uses the elapsed time method of determining years of service may use either 91 consecutive calendar days or 3 consecutive calendar months instead of 500 hours of service, provided it uses the same convention for all employees during a plan year), and

(vi) If this paragraph (f) is applied with respect to any employee with respect to a plan for a plan year, it is applied with respect to all employees with respect to the plan for the plan year.

(2) Hours of service. For purposes of this paragraph (f), the term "hours of service" has the same meaning as provided for such term by 29 CFR 2530.200b–2 under the general method of crediting service for the employee. If one of the equivalencies set forth in 29 CFR 2530.200b–3 is used for crediting service under the plan, the 500–hour requirement must be adjusted accordingly.

(3) Examples. The following examples illustrate the provision of this paragraph (f).

Example 1. An employer has 35 employees who are eligible to participate under a defined contribution plan. The plan provides that an employee will not receive an allocation of contributions for a plan year unless the employee is employed by the employer on the last day of the plan year. Only 30 employees are employed by the employer on the last day of the plan year. Two of the five employees who terminated employment before the last day of the plan year had 500 or fewer hours of service during the plan year, and the remaining three had more than 500 hours of service during the year. Of the five employees who were no longer employed on the last day of the plan year, the two with 500 hours of service or less during the plan year are treated as excludable employees for purposes of section 410(b), and the remaining three who had over 500 hours of service during the plan year are taken into account in testing the plan under section 410(b) but are treated as not benefiting under the plan.

Example 2. An employer has 30 employees who are eligible to participate under a defined contribution plan. The plan requires 1,000 hours of service to receive an allocation of contributions or forfeitures. Ten employees do not receive an allocation because of their failure to complete 1,000 hours of service. Three of the 10 employees who failed to satisfy the minimum service requirement completed 500 or fewer hours of service and terminated their employment. Two of the employees completed more than 500, but fewer than 1,000 hours of service and terminated their employment. The remaining five employees did not terminate employment. Under the rule in paragraph (f) of this section, the three terminated employees who completed 500 or fewer hours of service are treated as excludable employees for the portion of the plan year they are employed. The other seven employees who do not receive an allocation are taken into account in testing the plan under section 410(b) but are treated as not benefiting under the plan.

Example 3. An employer maintains two plans, Plan A for salaried employees and Plan B for hourly employees. Of the 100 salaried employees, two do not receive an allocation under Plan A for the plan year because they terminate employment

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before completing 500 hours of service. Of the 300 hourly employees, 50 do not receive an allocation under Plan B for the plan year because they terminate employment before completing 500 hours. In applying section 410(b) to Plan A, the two employees who did not receive an allocation under Plan A are excludable employees, but the 50 who did not receive an allocation under Plan B are not excludable employees, because they were not eligible to participate under Plan A.

(g) Employees of certain governmental or tax-exempt entities—(1) Plans covered. For purposes of testing either a section 401(k) plan, or a section 401(m) plan that is provided under the same general arrangement as a section 401(k) plan, an employer may treat as excludable those employees described in paragraphs (g)(2) and (3) of this section.

(2) Employees of governmental entities. Employees of governmental entities who are precluded from being eligible employees under a section 401(k) plan by reason of section 401(k)(4)(B)(ii) may be treated as excludable employees if more than 95 percent of the employees of the employer who are not precluded from being eligible employees by reason of section 401(k)(4)(B)(ii) benefit under the plan for the year.

(3) Employees of tax-exempt entities. Employees of an organization described in section 403(b)(1)(A)(i) who are eligible to make salary reduction contributions under section 403(b) may be treated as excludable with respect to a section 401(k) plan, or a section 401(m) plan that is provided under the same general arrangement as a section 401(k) plan, if—

(i) No employee of an organization described in section 403(b)(1)(A)(i) is eligible to participate in such section 401(k) plan or section 401(m) plan; and

(ii) At least 95 percent of the employees who are neither employees of an organization described in section 403(b)(1)(A)(i) nor employees of a governmental entity who are precluded from being eligible employees under a section 401(k) plan by reason of section 401(k)(4)(B)(ii) are eligible to participate in such section 401(k) plan or section 401(m) plan.

(h) Former employees—(1) In general. For purposes of applying section 410(b) with respect to former employees, all former employees of the employer are taken into account, except that the employer may treat a former employee described in paragraph (h)(2) or (h)(3) of this section as an excludable former employee. If either (or both) of the former employee exclusion rules under paragraphs (h)(2) and (h)(3) of this section is applied, it must be applied to all former employees for the plan year on a consistent basis.

(2) Employees terminated before a specified date. The employer may treat a former employee as excludable if—

(i) The former employee became a former employee either prior to January 1, 1984, or prior to the tenth calendar year preceding the calendar year in which the current plan year begins, and

(ii) The former employee became a former employee in a calendar year that precedes the earliest calendar year in which any former employee who benefits under the plan in the current plan year became a former employee.

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(3) Previously excludable employees. The employer may treat a former employee as excludable if the former employee was an excludable employee (or would have been an excludable employee if these regulations had been in effect) under the rules of paragraphs (b) through (g) of this section during the plan year in which the former employee became a former employee. If the employer treats a former employee as excludable pursuant to this paragraph (h)(3), the former employee is not taken into account with respect to a plan even if the former employee is benefiting under the plan.

(i) Former employees treated as employees. An employer may treat as excludable employees all formerly nonhighly compensated employees who are treated as employees of the employer under § 1.410(b)–9 solely because they have increases in accrued benefits under a defined benefit plan that are based on ongoing service or compensation credits (including imputed service or compensation) after they cease to perform services for the employer.

Credits

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit-Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.410(b)-7, Treas. Reg. § 1.410(b)-7

§ 1.410(b)-7 Definition of plan and rules governing plan disaggregation and aggregation.

Currentness

(a) In general. This section provides a definition of "plan." First, this section sets forth a definition of plan within the meaning of section 401(a) or 403(a). Then certain mandatory disaggregation and permissive aggregation rules are applied. The result is the definition of plan that applies for purposes of sections 410(b) and 401(a)(4). Thus, in general, the term "plan" as used in this section initially refers to a plan described in section 414(l) and to an annuity plan described in section 403(a), and the term "plan" as used in other sections under these regulations means the plan determined after application of this section. Paragraph (b) of this section provides that each single plan under section 414(l) is treated as a single plan for purposes of section 410(b). Paragraph (c) of this section describes the rules for certain plans that must be treated as comprising two or more separate plans, each of which is a single plan subject to section 410(b). Paragraph (d) of this section provides a rule permitting an employer to aggregate certain separate plans to form a single plan for purposes of section 410(b). Paragraph (e) of this section provides rules for determining the testing group of plans taken into account in determining whether a plan satisfies the average benefit percentage test of § 1.410(b)-5.

(b) Separate asset pools are separate plans. Each single plan within the meaning of section 414(l) is a separate plan for purposes of section 410(b). See § 1.414(l)-1(b). For example, if only a portion of the assets under a defined benefit plan is available, on an ongoing basis, to provide the benefits of certain employees, and the remaining assets are available only in certain limited cases to provide such benefits (but are available in all cases for the benefit of other employees), there are two separate plans. Similarly, the defined contribution portion of a plan described in section 414(k) is a separate plan from the defined benefit portion of that same plan. A single plan under section 414(l) is a single plan for purposes of section 410(b), even though the plan comprises separate written documents and separate trusts, each of which receives a separate determination letter from the Internal Revenue Service. A defined contribution plan does not comprise separate plans merely because it includes more than one trust, or merely because it provides for separate accounts and permits employees to direct the investment of the amounts allocated to their accounts. Further, a plan does not comprise separate plans merely because assets are separately invested in individual insurance or annuity contracts for employees.

(c) Mandatory disaggregation of certain plans—(1) Section 401(k) and 401(m) plans. The portion of a plan that is a section 401(k) plan and the portion that is not a section 401(k) plan are treated as separate plans for purposes of section 410(b). Similarly, the portion of a plan that is a section 401(m) plan and the portion that is not a section 401(m) plan are treated as separate plans for purposes of section 410(b). Thus, a plan that consists of elective contributions under a section 401(k) plan, employee and matching contributions under a section 401(m) plan, and contributions other than elective, employee, or matching contributions is treated as three separate plans for purposes of section 410(b). In addition, the portion of a plan that consists of contributions described in § 1.401(k)-2(a)(5) (i.e., contributions that fail to satisfy the allocation or compensation requirements applicable to elective contributions and are therefore required to be tested separately) and

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the portion of the plan that does not consist of such contributions are treated as separate plans for purposes of section 410(b). Similarly, the portion of a plan that consists of contributions described in § 1.410(m)–1(b)(4)(ii) (i.e., matching contributions that fail to satisfy the allocation and other requirements applicable to matching contributions and are therefore required to be tested separately) and the portion of the plan that does not consist of such contributions are treated as separate plans for purposes of section 410(b).

(2) ESOPs and non–ESOPs. The portion of a plan that is an ESOP and the portion of the plan that is not an ESOP are treated as separate plans for purposes of section 410(b), except as otherwise permitted under § 54.4975–11(e) of this Chapter.

(3) Plans benefiting otherwise excludable employees. If an employer applies section 410(b) separately to the portion of a plan that benefits only employees who satisfy age and service conditions under the plan that are lower than the greatest minimum age and service conditions permissible under section 410(a), the plan is treated as comprising separate plans, one benefiting the employees who have satisfied the lower minimum age and service conditions but not the greatest minimum age and service conditions permitted under section 410(a) and one benefiting employees who have satisfied the greatest minimum age and service conditions permitted under section 410(a). See § 410(b)–6(b)(3)(ii) for rules about testing otherwise excludable employees.

(4) Plans benefiting certain disaggregation populations of employees—(i) In general—(A) Single plan must be treated as separate plans. If a plan (*i.e.*, a single plan within the meaning of section 414(l)) benefits employees of more than one disaggregation population, the plan must be disaggregated and treated as separate plans, each separate plan consisting of the portion of the plan benefiting the employees of each disaggregation population. See paragraph (c)(4)(ii) of this section for the definition of disaggregation population.

(B) Benefit accruals or allocations attributable to current status. Except as otherwise provided in paragraph (c)(4)(i)(C) of this section, in applying the rule of paragraph (c)(4)(i)(A) of this section, the portion of the plan benefiting employees of a disaggregation population consists of all benefits accrued by, or all allocations made to, employees while they were members of the disaggregation population.

(C) Exceptions for certain benefit accruals—(1) Attribution of benefits to first disaggregation population. If employees benefiting under a plan change from one disaggregation population to a second disaggregation population, benefits they accrue while members of the second disaggregation population that are attributable to years of service previously credited while the employees were members of the first disaggregation population may be treated as provided to them in their status as members of the first disaggregation population and thus included in the portion of the plan benefiting employees of the first disaggregation population. This special treatment is available only if it is applied on a consistent basis, if it does not result in significant discrimination in favor of highly compensated employees, and if the plan provision providing the additional benefits applies on the same terms to all similarly-situated employees. For example, if all formerly collectively bargained employees accrue additional benefits under a plan after becoming noncollectively bargained employees, then those benefit increases may be treated as included in the portion of the plan benefiting collectively bargained employees if they are attributable to years of service credited while the employees were collectively bargained (e.g., where the additional benefits result from compensation increases that occur while the employees are noncollectively bargained or from plan amendments affecting benefits earned while collectively bargained that are adopted while the employees are noncollectively bargained) and if such treatment does not result in significant discrimination in favor of highly compensated employees.

(2) Attribution of benefits to current disaggregation population. If employees benefiting under a plan change from one disaggregation population to another disaggregation population, benefits they accrue while members of the first disaggregation population may be treated as provided to them in their current status and thus included in the portion of the plan benefiting employees of the disaggregation population of which they are currently members. This special treatment is available only if it is applied on a consistent basis and if it does not result in significant discrimination in favor of highly compensated employees.

(D) Change in disaggregation populations—(1) Reasonable treatment. If, in previous years, the configuration of a plan's disaggregation populations differed from their configuration for the current year, for purposes of the benefits accrued by, or allocations made to, an employee for those years, the employee's status as a member of a current disaggregation population for those years must be determined on a reasonable basis. A different configuration occurs, for example, if disaggregation populations exist for the first time, such as when an employer is first treated as operating qualified separate lines of business, or if the existing disaggregation populations change, such as when an employer redesignates its qualified separate lines of business.

(2) Example. The following example illustrates the application of this paragraph (c)(4)(i)(D).

Example. (a) Employer X operates Divisions M and N, which are treated as qualified separate lines of business for the first time in 1998. Thus, the disaggregation populations of employees of Division M and employees of Division N exist for the first time. Since 1981 Employer X has maintained a defined benefit plan, Plan P, for employees of Division M. Plan P provides a normal retirement benefit of one percent of average annual compensation for each year of service up to 25. Employee A has worked for Division M since 1981 and has never worked for Division N. Employee B has worked for Division N since 1989 and worked for Division M from 1981 to 1988. Employee C has worked in the headquarters of Employer X since 1981. For the period 1981 to 1988 Employee C was credited with years of service under Plan P.

(b) For purposes of the benefits accrued by Employee A under Plan P during years 1981 through 1997, Employee A is reasonably treated as having been a member of the Division M disaggregation population for those years. For purposes of the benefits accrued by Employee B under Plan P during years 1981 through 1988, Employee B is reasonably treated as having been a member of the Division M disaggregation population for 1981 through 1988 and as having changed to the Division N disaggregation population for 1989 through 1997. For purposes of the benefits accrued by Employee C under Plan P during years 1981 through 1988, Employee C is reasonably treated as having been a member of the Division M disaggregation population for those years. Moreover, any benefit accruals for Employee B and Employee C in years after 1988, that result from increases in average annual compensation after 1988 and that are attributable to years of service credited for 1981 through 1988, may be treated as provided to Employee B and Employee C in their status as members of the Division M disaggregation population if the requirements of paragraph (c)(4)(i)(C)(1) of this section are otherwise met.

(ii) Definition of disaggregation population—(A) Plan benefiting employees of qualified separate lines of business. If an employer is treated as operating qualified separate lines of business for purposes of section 410(b) in accordance with § 1.414(r)–1(b), and a plan benefits employees of more than one qualified separate line of business, the employees of each qualified separate line of business are separate disaggregation populations. In this case, the portion of the plan benefiting the employees of each qualified separate line of business is treated as a separate plan maintained by that qualified separate line of business. However, employees of different qualified separate lines of business who are benefiting under a plan that is tested under the special rule for employer-wide plans in § 1.414(r)–1(c)(2)(ii) for a plan year are not separate disaggregation populations merely because they are employees of different qualified separate lines of business.

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(B) Plan benefiting collectively bargained employees. If a plan benefits both collectively bargained employees and noncollectively bargained employees, the collectively bargained employees are one disaggregation population and the noncollectively bargained employees are another disaggregation population. If the population of collectively bargained employees includes employees covered under different collective bargaining agreements, the population of employees covered under each collective bargaining agreement is also a separate disaggregation population.

(C) Plan maintained by more than one employer. If a plan benefits employees of more than one employer, the employees of each employer are separate disaggregation populations. In this case, the portion of the plan benefiting the employees of each employer is treated as a separate plan maintained by that employer, which must satisfy section 410(b) by reference only to that employer's employees. However, for purposes of this paragraph (c)(4)(ii)(C), if the plan of one employer (or, in the case of a plan maintained by more than one employer, the plan provisions applicable to the employees of one employer) treats compensation or service with another employer as compensation or service with the first employer, then the current accruals attributable to that compensation or service are treated as provided to an employee of the first employer under the plan of the first employer (or the portion of a plan maintained by more than one employer benefiting employees of the first employer), and the provisions of paragraph (c)(4)(i)(C) of this section do not apply to those accruals. Thus, for example, if Plan A maintained by Employer X imputes service or compensation for an employee of Employer Y, then Plan A is not treated as benefiting the employees of more than one employer merely because of this imputation.

(5) Additional rule for plans benefiting employees of more than one qualified separate line of business. If a plan benefiting employees of more than one qualified separate line of business satisfies the reasonable classification requirement of § 1.410(b)–4(b) before the application of paragraph (c)(4) of this section, then any portion of the plan that is treated as a separate plan as a result of the application of paragraphs (c)(4)(i)(A) and (ii)(A) of this section is deemed to satisfy that requirement.

(d) Permissive aggregation for ratio percentage and nondiscriminatory classification tests—(1) In general. Except as provided in paragraphs (d)(2) and (d)(3) of this section, for purposes of applying the ratio percentage test of § 1.410(b)–2(b)(2) or the nondiscriminatory classification test of § 1.410(b)–4, an employer may designate two or more separate plans (determined after application of paragraph (b) of this section) as a single plan. If an employer treats two or more separate plans as a single plan under this paragraph, the plans must be treated as a single plan for all purposes under sections 401(a)(4) and 410(b).

(2) Rules of disaggregation. An employer may not aggregate portions of a plan that are disaggregated under the rules of paragraph (c) of this section. Similarly, an employer may not aggregate two or more separate plans that would be disaggregated under the rules of paragraph (c) of this section if they were portions of the same plan. In addition, an employer may not aggregate an ESOP with another ESOP, except as permitted under § 54.4975–11(e) of this Chapter.

(3) Duplicative aggregation. A plan may not be combined with two or more plans to form more than one single plan. Thus, for example, an employer that maintains plans A, B, and C may not aggregate plans A and B and plans A and C to form two single plans. However, the employer may apply the permissive aggregation rules of this paragraph

(d) to form any one (and only one) of the following combinations: plan ABC, plans AB and C, plans AC and B, or plans A and BC.

(4) Special rule for plans benefiting employees of a qualified separate line of business. For purposes of paragraph (d)(1) of this section, an employer that is treated as operating qualified separate lines of business for purposes of section 410(b) in accordance with § 1.414(r)–1(b) is permitted to aggregate the portions of two or more plans that benefit employees of the same qualified separate line of business (regardless of whether the employer elects to aggregate the portions of the same plans that benefit employees of the other qualified separate lines of business of the employer), provided that none of the plans is tested under the special rule for employer-wide plans in § 1.414(r)–1(c)(2)(ii). Thus, the employer is permitted to apply paragraph (d)(1) of this section with respect to two or more separate plans determined after the application of paragraphs (b) and (c)(4) of this section, but may not aggregate a plan that is tested under the special rule for employer-wide plans in § 1.414(r)–1(c)(2)(ii) for a plan year with any portion of a plan that does not rely on that special rule for the plan year. In all other respects, the provisions of this paragraph (d) regarding permissive aggregation apply, including (but not limited to) the disaggregation rules under paragraph (d)(2) of this section (including the mandatory disaggregation rule of paragraph (c)(4) of this section), and the prohibition on duplicative aggregation under paragraph (d)(3) of this section. This paragraph (d)(4) applies only in the case of an employer that is treated as operating qualified separate lines of business for purposes of section 410(b) in accordance with § 1.414(r)–1(b). See §§ 1.414(r)–1(c)(2) and 1.414(r)–8 (separate application of section 410(b) to the employees of a qualified separate line of business).

(5) Same plan year requirement. Two or more plans may not be aggregated and treated as a single plan under this paragraph (d) unless they have the same plan year.

(e) Determination of plans in testing group for average benefit percentage test—(1) In general. For purposes of applying the average benefit percentage test of § 1.410(b)–5 with respect to a plan, all plans in the testing group must be taken into account. For this purpose, the plans in the testing group are the plan being tested and all other plans of the employer that could be permissively aggregated with that plan under paragraph (d) of this section. Whether two or more plans could be permissively aggregated under paragraph (d) of this section is determined (i) without regard to the rule in paragraph (d)(4) of this section that portions of two or more plans benefiting employees of the same line of business may not be aggregated if any of the plans is tested under the special rule for employer-wide plans in § 1.414(r)–1(c)(2)(ii), (ii) without regard to paragraph (d)(5) of this section, and (iii) by applying paragraph (d)(2) of this section without regard to paragraphs (c)(1) and (c)(2) of this section.

(2) Examples. The following example illustrates the rules of this paragraph (e).

Example 1. Employer X is treated as operating two qualified separate lines of business for purposes of section 410(b) in accordance with section 414(r), QSLOB1 and QSLOB2. Employer X must apply the rules in § 1.414(r)–8 to determine whether its plans satisfy section 410(b) on a qualified-separate-line-of-business basis. Employer X maintains the following plans:

(a) Plan A, the portion of Employer X' s employer-wide section 401(k) plan that benefits all noncollectively bargained employees of QSLOB1,

(b) Plan B, the portion of Employer X' s employer-wide section 401(k) plan that benefits all noncollectively bargained employees of QSLOB2,

(c) Plan C, a defined benefit plan that benefits all hourly noncollectively bargained employees of QSLOB1,

(d) Plan D, a defined benefit plan that benefits all collectively bargained employees of QSLOB1,

(e) Plan E, an ESOP that benefits all noncollectively bargained employees of QSLOB1,

(f) Plan F, a profit-sharing plan that benefits all salaried noncollectively bargained employees of QSLOB1.

Assume that Plan F does not satisfy the ratio percentage test of § 1.410(b)–2(b)(2) on a qualified-separate-line-of-business basis, but does satisfy the nondiscriminatory classification test of § 1.410(b)–4 on both an employer-wide and a qualified-separate-line-of-business basis. Therefore, to satisfy section 410(b), Plan F must satisfy the average benefit percentage test of § 1.410(b)–5 on a qualified-separate-line-of-business basis. The plans in the testing group used to determine whether Plan F satisfies the average benefit percentage test of § 1.410(b)–5 are Plans A, C, E, and F.

Example 2. The facts are the same as in Example 1, except that Employer X applies the special rule for employer-wide plans in § 1.414(r)–1(c)(2)(ii) to its employer-wide section 401(k) plan. To satisfy section 410(b), Plan F must satisfy the average benefit percentage test of § 1.410(b)–5. Since paragraph (c)(4) of this section no longer applies to Plans A and B, they are treated as a single plan (Plan AB). The plans in the testing group used to determine whether Plan F satisfies the average benefit percentage test of § 1.410(b)–5 are therefore Plans A, B, C, E, and F. However, the employees of QSLOB 2 continue to be excludable employees for purposes of determining whether Plan F satisfies the average benefit percentage test. See § 1.410(b)–6(e).

(f) Section 403(b) plans. In determining whether a plan satisfies section 410(b), a plan subject to section 403(b)(12)(A)(i) is disregarded. However, in determining whether a plan subject to section 403(b)(12)(A)(i) satisfied section 410(b), plans that are not subject to section 403(b)(12)(A)(i) may be taken into account.

Credits

[T.D. 8363, 56 FR 47655, Sept. 19, 1991; T.D. 8376, 56 FR 63433, Dec. 4, 1991; T.D. 8363, 57 FR 10817, March 31, 1992; T.D. 8363, 57 FR 10954, March 31, 1992; T.D. 8487, 58 FR 46843, Sept. 3, 1993; T.D. 8548, 59 FR 32914, June 27, 1994; T.D. 9169, 69 FR 78153, Dec. 29, 2004]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

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Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.410(b)–8, Treas. Reg. § 1.410(b)–8

§ 1.410(b)–8 Additional rules.

Currentness

(a) Testing methods—(1) In general. A plan must satisfy section 410(b) for a plan year using one of the testing options in paragraphs (a)(2) through (a)(4) of this section. Whichever testing option is used for the plan year must also be used for purposes of applying section 401(a)(4) to the plan for the plan year. The annual testing option in paragraph (a)(4) of this section must be used in applying section 410(b) to a section 401(k) plan or a section 401(m) plan, and in applying the average benefit percentage test of § 1.410(b)–5. For purposes of this paragraph (a), the plan provisions and other relevant facts as of the last day of the plan year regarding which employees benefit under the plan for the plan year are applied to the employees taken into account under the testing option used for the plan year. For this purpose, amendments retroactively correcting a plan in accordance with § 1.401(a)(4)–11(g) are taken into account as plan provisions in effect as of the last day of the plan year.

(2) Daily testing option. A plan satisfies section 410(b) for a plan year if it satisfies § 1.410(b)–2 on each day of the plan year, taking into account only those employees (or former employees) who are employees (or former employees) on that day.

(3) Quarterly testing option. A plan is deemed to satisfy section 410(b) for a plan year if the plan satisfies § 1.410(b)–2 on at least one day in each quarter of the plan year, taking into account for each of those days only those employees (or former employees) who are employees (or former employees) on that day. The preceding sentence does not apply if the plan's eligibility rules or benefit formula operate to cause the four quarterly testing days selected by the employer not to be reasonably representative of the coverage of the plan over the entire plan year.

(4) Annual testing option. A plan satisfies section 410(b) for a plan year if it satisfies § 1.410(b)–2 as of the last day of the plan year, taking into account all employees (or former employees) who were employees (or former employees) on any day during the plan year.

(5) Example. The following example illustrates this paragraph (a).

Example. Plan A is a defined contribution plan that is not a section 401(k) plan or a section 401(m) plan, and that conditions allocations on an employee's employment on the last day of the plan year. Plan A is being tested for the 1995 calendar plan year using the daily testing option in paragraph (a)(2) of this section. In testing the plan for compliance with section 410(b) on March 11, 1995, Employee X is taken into account because he was an employee on that day and

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was not an excludable employee with respect to Plan A on that day. Employee X was a participant in Plan A on March 11, 1995, was employed on December 31, 1995, and received an allocation under Plan A for the 1995 plan year. Under these facts, Employee X is treated as benefiting under Plan A on March 11, 1995, even though Employee X had not satisfied all of the conditions for receiving an allocation on that day, because Employee X satisfied all of those conditions as of the last day of the plan year.

(b) Family member aggregation rule. For purposes of section 410(b), and in accordance with section 414(q)(6), a highly compensated employee who is a 5–percent owner or one of the ten most highly compensated employees and any family member (or members) of such a highly compensated employee who is also an employee of the employer are to be treated as a single highly compensated employee. If any member of that group is benefiting under a plan, the deemed single employee is treated as benefiting under the plan. If no member of that group is benefiting under a plan, the deemed single employee is treated as not benefiting under the plan.

Credits

[T.D. 8363, 56 FR 47656, Sept. 19, 1991]

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Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.410(b)–9, Treas. Reg. § 1.410(b)–9

§ 1.410(b)–9 Definitions.

Currentness

In applying this section and §§ 1.410(b)–2 through 1.410(b)–10, the definitions in this section govern unless otherwise provided.

Collectively bargained employee. Collectively bargained employee means a collectively bargained employee within the meaning of § 1.410(b)–6(d)(2).

Defined benefit plan. Defined benefit plan means a defined benefit plan within the meaning of section 414(j). The portion of a plan described in section 414(k) that does not consist of separate accounts is treated as a defined benefit plan.

Defined contribution plan. Defined contribution plan means a defined contribution plan within the meaning of section 414(i). The portion of a plan described in section 414(k) that consists of separate accounts is treated as a defined contribution plan.

Employee. Employee means an individual who performs services for the employer who is either a common law employee of the employer, a self-employed individual who is treated as an employee pursuant to section 401(c)(1), or a leased employee (not excluded under section 414(n)(5)) who is treated as an employee of the employer-recipient under section 414(n)(2) or 414(o)(2). Individuals that an employer treats as employees under section 414(n) pursuant to the requirements of section 414(o) are considered to be leased employees for purposes of this rule. In addition, an individual must be treated as an employee with respect to allocations under a defined contribution plan taken into account under § 1.401(a)(4)–2(c)(ii) and with respect to increases in accrued benefits (within the meaning of 411(a)(7)) under a defined benefit plan that are based on ongoing service or compensation (including imputed service or compensation) credits.

Employer. Employer means the employer maintaining the plan and those employers required to be aggregated with the employer under sections 414(b), (c), (m), or (o). An individual who owns the entire interest of an unincorporated trade or business is treated as an employer. Also, a partnership is treated as the employer of each partner and each employee of the partnership.

ESOP. ESOP or employee stock ownership plan means an employee stock ownership plan within the meaning of section 4975(e)(7) or a tax credit employee stock ownership plan within the meaning of section 409(a).

Former employee. Former employee means an individual who was, but has ceased to be, an employee of the employer (i.e., the individual has ceased performing services as an employee for the employer). An individual is treated as a former employee beginning on the day after the day on which the individual ceases performing services as an employee for the

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employer. Thus, an individual who ceases performing services as an employee for an employer during a plan year is both an employee and a former employee for the plan year. Notwithstanding the foregoing, an individual is an employee (and not a former employee) to the extent that the individual is treated as an employee with respect to the plan for the plan year under the definition of employee in this section.

Highly compensated employee. Highly compensated employee means an employee who is a highly compensated employee within the meaning of section 414(q) or a former employee treated as an employee under the definition of employee in this section who is a highly compensated former employee within the meaning of section 414(q).

Highly compensated former employee. Highly compensated former employee means a former employee who is a highly compensated former employee within the meaning of section 414(q).

Multiemployer plan. Multiemployer plan means a multiemployer plan within the meaning of section 414(f).

Noncollectively bargained employee. Noncollectively bargained employee means an employee who is not a collectively bargained employee.

Nonhighly compensated employee. Nonhighly compensated employee means an employee who is not a highly compensated employee.

Nonhighly compensated former employee. Nonhighly compensated former employee means a former employee who is not a highly compensated former employee.

Plan year. Plan year means the plan year of the plan as defined in the written plan document. In the absence of a specifically designated plan year, the plan year is deemed to be the calendar year.

Plan year compensation. Plan year compensation means plan year compensation within the meaning of § 1.401(a)(4)–12.

Professional employee. Professional employee means any highly compensated employee who, on any day of the plan year, performs professional services for the employer as an actuary, architect, attorney, chiropodist, chiropractor, dentist, executive, investment banker, medical doctor, optometrist, osteopath, podiatrist, psychologist, certified or other public accountant, stockbroker, or veterinarian, or in any other professional capacity determined by the Commissioner in a notice or other document of general applicability to constitute the performance of services as a professional.

Ratio percentage. With respect to a plan for a plan year, a plan's ratio percentage means the percentage (rounded to the nearest hundredth of a percentage point) determined by dividing the percentage of the nonhighly compensated employees who benefit under the plan by the percentage of the highly compensated employees who benefit under the plan. The percentage of the nonhighly compensated employees who benefit under the plan is determined by dividing the number of nonhighly compensated employees benefiting under the plan by the total number of nonhighly compensated employees of the employer. The percentage of the highly compensated employees who benefit under the plan is determined by dividing the number of highly compensated employees benefiting under the plan by the total number of highly compensated employees of the employer.

Section 401(k) plan. Section 401(k) plan means a plan consisting of elective contributions described in § 1.401(k)–1(g)(3) [1] under a qualified cash or deferred arrangement described in § 1.401(k)–1(a)(4)(i). Thus, a section 401(k) plan does not include a plan (or portion of a plan) that consists of contributions under a nonqualified cash or deferred arrangement, or qualified nonelective or qualified matching contributions treated as elective contributions under § 1.401(k)–1(a)(6).

Section 401(l) plan. Section 401(l) plan means a plan that—

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(1) Provides for a disparity in employer-provided benefits or contributions that satisfies section 401(l) in form, and

(2) Relies on one of the safe harbors of § 1.401(a)(4)–2(b)(2), 1.401(a)(4)–3(b), 1.401(a)(4)–8(b)(3), or 1.401(a)(4)–8(c)(3)(iii)(B) to satisfy section 401(a)(4).

Section 401(m) plan. Section 401(m) plan means a plan consisting of employee contributions described in § 1.401(m)–1(f)(12)[2] or matching contributions described in § 1.401(m)–1(a)(2), or both. Thus, a section 401(m) plan does not include a plan (or portion of a plan) that consists of elective contributions or qualified nonelective contributions treated as matching contributions under § 1.401(m)–1(b)(5).

Credits

[T.D. 8363, 56 FR 47657, Sept. 19, 1991; T.D. 8363, 57 FR 10817, March 31, 1992; T.D. 8363, 57 FR 10954, March 31, 1992; T.D. 8487, 58 FR 46843, Sept. 3, 1993; T.D. 9169, 69 FR 78153, Dec. 29, 2004]

Editorial Note: By T.D. 9169, 69 FR 78153, Dec. 29, 2004, the Internal Revenue Service published a document in the Federal Register, attempting to amend 1.410(b)–9 by removing "1.401(k)–1(g)(3) and 1.401(m)–1(f)(12)" and inserting "1.401(k)–6 and 1.401(m)–1(f)(12)". However, because of inaccurate language, this amendment could not be incorporated.

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

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Footnotes

1 See Editorial Note following this section.

2 See Editorial Note following this section.

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26 C.F.R. § 1.410(b)–10, Treas. Reg. § 1.410(b)–10

§ 1.410(b)–10 Effective dates and transition rules.

Effective: July 21, 2006
Currentness

(a) Statutory effective dates—(1) In general. Except as set forth in paragraph (a)(2) of this section, the minimum coverage rules of section 410(b) as amended by section 1112 of the Tax Reform Act of 1986 apply to plan years beginning on or after January 1, 1989.

(2) Special statutory effective date for collective bargaining agreements—(i) In general. As provided for by section 1112(e)(2) of the Tax Reform Act of 1986, in the case of a plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified before March 1, 1986, the minimum coverage rules of section 410(b) as amended by section 1112 of the Tax Reform Act of 1986 do not apply to employees covered by any such agreement in plan years beginning before the earlier of—

(A) January 1, 1991; or

(B) The later of January 1, 1989, or the date on which the last of such collective bargaining agreements terminates (determined without regard to any extension thereof after February 28, 1986). For purposes of this paragraph (a)(2), any extension or renegotiation of a collective bargaining agreement, which extension or renegotiation is ratified after February 28, 1986, is to be disregarded in determining the date on which the agreement terminates.

(ii) Example. The following example illustrates this paragraph (a)(2).

Example. Employer A maintains Plan 1 pursuant to a collective bargaining agreement. Plan 1 covers 100 of Employer A's noncollectively bargained employees and 900 of Employer A's collectively bargained employees. Employer A also maintains Plan 2, which covers Employer A's other 400 noncollectively bargained employees. The collective bargaining agreement under which Plan 1 is maintained was entered into on January 1, 1986, and expires December 31, 1992. Because Plan 1 is a plan maintained pursuant to a collective bargaining agreement, section 410(b) applies to the first plan year beginning on or after January 1, 1991. In applying section 410(b) to Plan 2, the 100 noncollectively bargained employees in Plan 1 must be taken into account. The deferred effective date for plans maintained pursuant to a collective bargaining agreement is not applicable in determining how section 410(b) is applied to a plan that is not maintained pursuant to a collective bargaining agreement.

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(iii) Plan maintained pursuant to a collective bargaining agreement. For purposes of this paragraph (a)(2), a plan is maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers, if one or more of the agreements were ratified before March 1, 1986. Only plans maintained pursuant to agreements that the Secretary of Labor finds to be collective bargaining agreements and that satisfy section 7701(a)(46) are eligible for the deferred effective date under this paragraph (a)(2). A plan will not be treated as a plan maintained pursuant to one or more collective bargaining agreements eligible for the deferred effective date under this paragraph (a)(2) unless the plan would be a plan maintained pursuant to one or more collective bargaining agreements under the principles applied under section 1017(c) of the Employee Retirement Income Security Act of 1974. See H.R. Rep. No. 1280, 93rd Cong. 2d Sess. 266 (1974).

(b) Regulatory effective dates—(1) In general. Except as otherwise provided in this section, §§ 1.410(b)–2 through 1.410(b)–9 apply to plan years beginning on or after January 1, 1994.

(2) Plans of tax-exempt organizations. In the case of plans maintained by organizations exempt from income taxation under section 501(a), including plans subject to section 403(b)(12)(A)(i) (nonelective plans), §§ 1.410(b)–2 through 1.410(b)–9 apply to plan years beginning on or after January 1, 1996, to the extent such plans are subject to section 410(b).

(c) Compliance during transition period. For plan years beginning before the effective date of these regulations, as set forth in paragraph (b) of this section, and on or after the statutory effective date as set forth in paragraph (a) of this section, a plan must be operated in accordance with a reasonable, good faith interpretation of section 410(b). Whether a plan is operated in accordance with a reasonable, good faith interpretation of section 410(b) will generally be determined based on all of the relevant facts and circumstances, including the extent to which an employer has resolved unclear issues in its favor. If a plan's classification has been determined by the Commissioner to be nondiscriminatory and there have been no significant changes in or omissions of a material fact, the classification will be treated as nondiscriminatory for the relevant plan year. A plan will be deemed to be operated in accordance with a reasonable, good faith interpretation of section 410(b) if it is operated in accordance with the terms of §§ 1.410(b)–2 through 1.410(b)–9.

(d) Effective date for governmental plans. In the case of governmental plans described in section 414(d), including plans subject to section 403(b)(12)(A)(i) (nonelective plans) § 1.410(b)–2 through § 1.410(b)–10 apply to plan years beginning on or after January 1, 1996, or 90 days after the opening of the first legislative session beginning on or after January 1, 1996, of the governing body with authority to amend the plan, if that body does not meet continuously. Such plans are deemed to satisfy section 410(b) (and in the case of such plans that are not subject to section 403(b)(12)(A)(i), section 401(a)(3) as in effect on September 1, 1974) for plan years before that effective date. For purposes of this section, the governing body with authority to amend the plan is the legislature, board, commission, council, or other governing body with authority to amend the plan. See § 1.410(b)–2(d) and (e).

(e) Effective date for provisions relating to exclusion of employees of certain tax-exempt entities. The provisions in § 1.410(b)–6(g) apply to plan years beginning after December 31, 1996. For plan years to which § 1.410(b)–6 applies that begin before January 1, 1997, § 1.410(b)–6(g) (as it appeared in the April 1, 2005 edition of 26 CFR part 1) applies.

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[T.D. 8363, 56 FR 47658, Sept. 19, 1991; T.D. 8363, 57 FR 10954, March 31, 1992; T.D. 8487, 58 FR 46844, Sept. 3, 1993; T.D. 9275, 71 FR 41359, July 21, 2006]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.414(c)–3, Treas. Reg. § 1.414(c)–3

§ 1.414(c)–3 Exclusion of certain interests or stock in determining control.

Currentness

(a) In general. For purposes of § 1.414(c)–2(b) (2) (i) and (c)(2), the term "interest" and the term "stock" do not include an interest which is treated as not outstanding under paragraph (b) of this section in the case of a parent-subsidiary group of trades or businesses under common control or under paragraph (c) of this section in the case of a brother-sister group of trades or businesses under common control. In addition, the term "stock" does not include treasury stock or nonvoting stock which is limited and preferred as to dividends. For definitions of certain terms used in this section, see paragraph (d) of this section.

(b) Parent-subsidiary group of trades or businesses under common control—(1) In general. If an organization (hereinafter in this section referred to as "parent organization") owns (within the meaning of paragraph (b)(2) of this section)—

(i) In the case of a corporation, 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of such corporation.

(ii) In the case of a trust or an estate, an actuarial interest (within the meaning of § 1.414(c)–2(b)(2)(ii)) of 50 percent or more of such trust or estate, and

(iii) In the case of a partnership, 50 percent or more of the profits or capital interest of such partnership, then for purposes of determining whether the parent organization or such other organization (hereinafter in this section referred to as "subsidiary organization") is a member of a parent-subsidiary group of trades or businesses under common control, an interest in such subsidiary organization excluded under paragraph (b) (3), (4), (5), or (6) of this section shall be treated as not outstanding.

(2) Ownership. For purposes of paragraph (b)(1) of this section, a parent organization shall be considered to own an interest in or stock of another organization which it owns directly or indirectly with the application of § 1.414(c)–4(b)(1) and—

(i) In the case of a parent organization which is a partnership, a trust, or an estate, with the application of paragraphs (b) (2), (3), and (4) of § 1.414(c)–4, and

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(ii) In the case of a parent organization which is a corporation, with the application of § 1.414(c)–4(b)(4).

(3) Plan of deferred compensation. An interest which is an interest in or stock of the subsidiary organization held by a trust which is part of a plan of deferred compensation (within the meaning of section 406(a)(3) and the regulations thereunder) for the benefit of the employees of the parent organization or the subsidiary organization shall be excluded.

(4) Principal owners, officers, etc. An interest which is an interest in or stock of the subsidiary organization owned (directly and with the application of § 1.414(c)–4) by an individual who is a principal owner, officer, partner, or fiduciary of the parent organization shall be excluded.

(5) Employees. An interest which is an interest in or stock of the subsidiary organization owned (directly and with the application of § 1.414(c)–4) by an employee of the subsidiary organization shall be excluded if such interest or such stock is subject to conditions which substantially restrict or limit the employee's right (or if the employee constructively owns such interest or such stock, the direct or record owner's right) to dispose of such interest or such stock and which run in favor of the parent or subsidiary organization.

(6) Controlled exempt organization. An interest which is an interest in or stock of the subsidiary organization shall be excluded if owned (directly and with the application of § 1.414(c)–4) by an organization (other than the parent organization):

(i) To which section 501 (relating to certain educational and charitable organizations which are exempt from tax) applies, and

(ii) Which is controlled directly or indirectly (within the meaning of paragraph (d)(7) of this section) by the parent organization or subsidiary organization, by an individual, estate, or trust that is a principal owner of the parent organization, by an officer, partner, or fiduciary of the parent organization, or by any combination thereof.

(c) Brother-sister group of trades or businesses under common control—(1) In general. If five or fewer persons (hereinafter in this section referred to as "common owners") who are individuals, estates, or trusts own (directly and with the application of § 1.414(c)–4)—

(i) In the case of a corporation, 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock or such corporation,

(ii) In the case of a trust or an estate, an actuarial interest (within the meaning of § 1.414(c)–2(b)(2)(ii)) of 50 percent or more of such trust or estate, and

(iii) In the case of a partnership, 50 percent or more of the profits or capital interest of such partnership, then for purposes of determining whether such organization is a member of a brother-sister group of trades or businesses

under common control, an interest in such organization excluded under paragraph (c) (2), (3), or (4) of this section shall be treated as not outstanding.

(2) Exempt employees' trust. An interest which is an interest in or stock of such organization held by an employees' trust described in section 401(a) which is exempt from tax under section 501(a) shall be excluded if such trust is for the benefit of the employees of such organization.

(3) Employees. An interest which is an interest in or stock of such organization owned (directly and with the application of § 1.414(c)–4) by an employee of such organization shall be excluded if such interest or stock is subject to conditions which run in favor of a common owner of such organization or in favor of such organization and which substantially restrict or limit the employee's right (or if the employee constructively owns such interest or stock, the direct or record owner's right) to dispose of such interest or stock.

(4) Controlled exempt organization. An interest which is an interest in or stock of such organization shall be excluded if owned (directly and with the application of § 1.414(c)–4) by an organization:

(i) To which section 501(c)(3) (relating to certain educational and charitable organizations which are exempt from tax) applies, and

(ii) Which is controlled directly or indirectly (within the meaning of paragraph (d)(7) of this section) by such organization, by an individual, estate, or trust that is a principal owner of such organization, by an officer, partner, or fiduciary of such organization, or by any combination thereof.

(d) Definitions—(1) Employee. For purposes of this section, the term "employee" has the same meaning such term is given in section 3306(i) of the Code (relating to definitions for purposes of the Federal Unemployment Tax Act).

(2) Principal owner. For purposes of this section, the term "principal owner" means a person who owns (directly and with the application of § 1.414(c)–4)—

(i) In the case of a corporation, 5 percent or more of the total combined voting power of all classes of stock entitled to vote in such corporation or 5 percent of more of the total value of shares of all classes of stock of such corporation;

(ii) In the case of a trust or estate, an actuarial interest of 5 percent or more of such trust or estate; or

(iii) In the case of a partnership, 5 percent or more of the profits or capital interest of such partnership.

(3) Officer. For purposes of this section, the term "officer" includes the president, vice-presidents, general manager, treasurer, secretary, and comptroller of a corporation, and any other person who performs duties corresponding to those normally performed by persons occupying such positions.

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(4) Partner. For purposes of this section, the term "partner" means any person defined in section 7701(a)(2) (relating to definitions of partner).

(5) Fiduciary. For purposes of this section and § 1.414(c)–4, the term "fiduciary" has the same meaning as such term is given in section 7701(a)(6) and the regulations thereunder.

(6) Substantial conditions. (i) In general. For purposes of this section, an interest in or stock of an organization is subject to conditions which substantially restrict or limit the right to dispose of such interest or stock and which run in favor of another person if the condition extends directly or indirectly to such person preferential rights with respect to the acquisition of the direct owner's (or the record owner's) interest or stock. For a condition to be in favor of another person it is not necessary that such person be extended a discriminatory concession with respect to price. A right of first refusal with respect to an interest or stock in favor of another person is a condition which substantially restricts or limits the direct or record owner's right of disposition which runs in favor of such person. Further, any legally enforceable condition which prohibits the direct or record owner from disposing of his or her interest or stock without the consent of another person will be considered to be a substantial limitation running in favor of such person.

(ii) Special rule. For purposes of paragraph (c)(3) of this section only, if a condition which restricts or limits an employee's right (or direct or record owner's right) to dispose of his or her interest or stock also applies to the interest or stock in such organization held by a common owner pursuant to a bonafide reciprocal purchase arrangement, such condition shall not be treated as a substantial limitation or restriction. An example of a reciprocal purchase arrangement is an agreement whereby a common owner and the employee are given a right of first refusal with respect to stock of the employer corporation owned by the other party. If, however, the agreement also provides that the common owner has the right to purchase the stock of the employer corporation owned by the employee in the event the corporation should discharge the employee for reasonable cause, the purchase arrangement would not be reciprocal within the meaning of this subdivision.

(7) Control. For purposes of paragraphs (b)(6) and (c)(4) of this section, the term "control" means control in fact. The determination of whether there exists control in fact will depend upon all of the facts and circumstances of each case, without regard to whether such control is legally enforceable and irrespective of the method by which such control is exercised or exercisable.

(e) Examples. The provisions of this section may be illustrated by the following examples:

Example 1. ABC Partnership owns 70 percent of the capital interest and of the profits interest in the DEF Partnership. The remaining capital interest and profits interest in DEF is owned as follows: 4 percent by A (a general partner in ABC), and 26 percent by D (a limited partner in ABC). ABC satisfies the 50–percent capital interest or profits interest ownership requirement of paragraph (b)(1)(iii) of this section with respect to DEF. Since A and D are partners of ABC, under paragraph (b)(4) of this section the capital and profits interests in DEF owned by A and D are treated as not outstanding for purposes of determining whether ABC and DEF are members of a parent-subsidiary group of trades or businesses under common control under § 1.414 (c)–2(b). Thus, ABC is considered to own 100 percent (70÷70) of the capital interest and profits interest in DEF. Accordingly, ABC and DEF are members of a parent-subsidiary group of trades or businesses under common control.

Example 2. Assume the same facts as in example (1) and assume further that A owns 15 shares of the 100 shares of the only class of stock of S Corporation and DEF Partnership owns 75 shares of such stock. ABC satisfies the 50 percent stock requirement of paragraph (b)(1)(i) of this section with respect to S since ABC is considered as owning 52.5 percent (70 percentx75 percent) of the S stock with the application of § 1.414 (c)–4(b)(2). Since A is a partner of ABC, the S stock owned by A is treated as not outstanding for purposes of determining whether S is a member of a parent-subsidiary group of trades or businesses under common control. Thus, DEF Partnership is considered to own stock possessing 88.2 percent (75÷85) of the voting power and value of the S stock. Accordingly, ABC Partnership, DEF Partnership, and S Corporation are members of a parent-subsidiary group of trades or businesses under common control.

Example 3. ABC Partnership owns 60 percent of the only class of stock of Corporation Y. D, the president of Y, owns the remaining 40 percent of the stock of Y. D has agreed that if she offers her stock in Y for sale she will first offer the stock to ABC at a price equal to the fair market value of the stock on the first date the stock is offered for sale. Since D is an employee of Y within the meaning of section 3306(i) of the Code and her stock in Y is subject to a condition which substantially restricts or limits her right to dispose of such stock and runs in favor of ABC Partnership, under paragraph (b)(5) of this section such stock is treated as not outstanding for purposes of determining whether ABC and Y are members of a parent-subsidiary group of trades or businesses under common control. Thus, ABC Partnership is considered to own stock possessing 100 percent of the voting power and value of the stock of Y. Accordingly, ABC Partnership and Y Corporation are members of a parent-subsidiary group of trades or businesses under common control. The result would be the same if D's husband, instead of D, owned directly the 40 percent stock interest in Y and such stock was subject to a right of first refusal running in favor of ABC Partnership.

(f) Exception—(1) In general. If an interest in an organization (including stock of a corporation) is owned by a person directly or with the application of the rules of paragraph (b) of § 1.414(c)–4 and such ownership results in the membership of that organization in a group of two or more trades or businesses under common control for any period, then the interest will not be treated as an excluded interest under paragraph (b) or (c) of this section if the result of applying such provisions is that the organization is not a member of a group of two or more trades or businesses under common control for the period.

(2) Example. The provisions of this paragraph may be illustrated by the following example:

Example. Corporation P owns directly 50 of the 100 shares of the only class of stock of corporation S. A, an officer of P, owns directly 30 shares of S stock which P has an option to acquire. If, under paragraph (b)(4) of this section, the 30 shares owned directly by A are treated as not outstanding, P would be treated as owning stock possessing only 71 percent (50/70) of the total voting power and value of S stock, and S should not be a member of a parent-subsidiary group of trades or businesses under common control. However, because the 30 shares owned by A that P has an option to purchase are considered as owned by P under paragraph (b)(2) of this section, and that ownership plus P's direct ownership of 50 shares result in S's membership in a parent-subsidiary group of trades or businesses under common control for 1985, the provisions of this paragraph apply. Therefore, A's stock is not treated as an excluded interest and S is a member of a parent-subsidiary group consisting of P and S.

Credits

[T.D. 8179, 53 FR 6607, March 2, 1988; T.D. 8179, 53 FR 8302, March 14, 1988]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Notes of Decisions (2)

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.414(c)–4, Treas. Reg. § 1.414(c)–4

§ 1.414(c)–4 Rules for determining ownership.

Currentness

(a) In general. In determining the ownership of an interest in an organization for purposes of § 1.414(c)–2 and § 1.414(c)–3, the constructive ownership rules of paragraph (b) of this section shall apply, subject to the operating rules contained in paragraph (c). For purposes of this section the term "interest" means: in the case of a corporation, stock; in the case of a trust or estate, an actuarial interest; in the case of a partnership, an interest in the profits or capital; and in the case of a sole proprietorship, the proprietorship.

(b) Constructive ownership—(1) Options. If a person has an option to acquire any outstanding interest in an organization, such interest shall be considered as owned by such person. For this purpose, an option to acquire an option, and each one of a series of such options shall be considered as an option to acquire such interest.

(2) Attribution from partnerships—(i) General. An interest owned, directly or indirectly, by or for a partnership shall be considered as owned by any partner having an interest of 5 percent or more in either the profits or capital of the partnership in proportion to such partner's interest in the profits or capital, whichever such proportion is greater.

(ii) Example. The provisions of paragraph (b)(2)(i) of this section may be illustrated by the following example:

Example. A, B, and C, unrelated individuals, are partners in the ABC Partnership. The partners' interest in the capital and profits of ABC are as follows:

(In percent)

Partner	Capital	Profits
A	36	25
B	60	71
C	4	4

The ABC Partnership owns the entire outstanding stock (100 shares) of X Corporation. Under paragraph (b)(2)(i) of this section, A is considered to own the stock of X owned by the partnership in proportion to his interest

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in capital (36 percent) or profits (25 percent), whichever such proportion is greater. Therefore, A is considered to own 36 shares of X stock. Since B has a greater interest in the profits of the partnership than in the capital, B is considered to own X stock in proportion to his interest in such profits. Therefore, B is considered to own 71 shares of X stock. Since C does not have an interest of 5 percent or more in either the capital or profits of ABC, he is not considered to own any shares of X stock.

(3) Attribution from estates and trusts—(i) In general. An interest in an organization (hereinafter called an "organization interest") owned, directly or indirectly, by or for an estate or trust shall be considered as owned by any beneficiary of such estate or trust who has an actuarial interest of 5 percent or more in such organization interest, to the extent of such actuarial interest. For purposes of this subparagraph, the actuarial interest of each beneficiary shall be determined by assuming the maximum exercise of discretion by the fiduciary in favor of such beneficiary and the maximum use of the organization interest to satisfy the beneficiary's rights. A beneficiary of an estate or trust who cannot under any circumstances receive any part of an organization interest held by the estate or trust, including the proceeds from the disposition thereof, or the income therefrom, does not have an actuarial interest in such organization interest. Thus, where stock owned by a decedent's estate has been specifically bequeathed to certain beneficiaries and the remainder of the estate has been specifically bequeathed to other beneficiaries, the stock is attributable only to the beneficiaries to whom it is specifically bequeathed. Similarly a remainderman of a trust who cannot under any circumstances receive any interest in the stock of a corporation which is a part of the corpus of the trust (including any accumulated income therefrom or the proceeds from a disposition thereof) does not have an actuarial interest in such stock. However, an income beneficiary of a trust does have an actuarial interest in stock if he has any right to the income from such stock even though under the terms of the trust instrument such stock can never be distributed to him. The factors and methods prescribed in § 20.2031–7 or, for certain prior periods, § 20.2031–7A (Estate Tax Regulations) for use in ascertaining the value of an interest in property for estate tax purposes shall be used for purposes of this subdivision in determining a beneficiary's actuarial interest in an organization interest owned directly or indirectly by or for an estate or trust.

(ii) Special rules for estates. (A) For purposes of this paragraph (b)(3) with respect to an estate, property of a decedent shall be considered as owned by his or her estate if such property is subject to administration by the executor or administrator for the purposes of paying claims against the estate and expenses of administration notwithstanding that, under local law, legal title to such property vests in the decedent's heirs, legatees or devisees immediately upon death.

(B) For purposes of this paragraph (b)(3) with respect to an estate, the term "beneficiary" includes any person entitled to receive property of a decedent pursuant to a will or pursuant to laws of descent and distribution.

(C) For purposes of this paragraph (b)(3) with respect to an estate, a person shall no longer be considered a beneficiary of an estate when all the property to which he or she is entitled has been received by him or her, when he or she no longer has a claim against the estate arising out of having been a beneficiary, and when there is only a remote possibility that it will be necessary for the estate to seek the return of property from him or her or to seek payment from him or her by contribution or otherwise to satisfy claims against the estate or expenses of administration.

(iii) Grantor trusts, etc. An interest owned, directly or indirectly, by or for any portion of a trust of which a person is considered the owner under subpart E, part I, subchapter J of the Code (relating to grantors and others treated as substantial owners) is considered as owned by such person.

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(4) Attribution from corporations—(i) General. An interest owned, directly or indirectly, by or for a corporation shall be considered as owned by any person who owns (directly and, in the case of a parent-subsidiary group of trades or businesses under common control, with the application of paragraph (b)(1) of this section, or in the case of a brother-sister group of trades or business under common control, with the application of this section), 5 percent or more in value of the stock in that proportion which the value of the stock which such person so owns bears to the total value of all the stock in such corporation.

(ii) Example. The provisions of paragraph (b)(4)(i) of this section may be illustrated by the following example:

Example. B, an individual, owns 60 of the 100 shares of the only class of outstanding stock of corporation P. C, an individual, owns 4 shares of the P stock, and corporation X owns 36 shares of the P stock. Corporation P owns, directly and indirectly, 50 shares of the stock of corporation S. Under this subparagraph, B is considered to own 30 shares of the S stock (60/100 x 50), and X is considered to own 18 shares of S stock (36/100 x 50). Since C does not own 5 percent or more in the value of P stock, he is not considered as owning any of the S stock owned by P. If in this example, C's wife had owned directly 1 share of the P stock, C and his wife would each be considered as owning 5 shares of the P stock, and therefore C and his wife would be considered as owning 2.5 shares of the S stock (5/100 x 50).

(5) Spouse—(i) General rule. Except as provided in paragraph (b)(5)(ii) of this section, an individual shall be considered to own an interest owned, directly or indirectly, by or for his or her spouse, other than a spouse who is legally separated from the individual under a decree of divorce, whether interlocutory or final, or a decree of separate maintenance.

(ii) Exception. An individual shall not be considered to own an interest in an organization owned, directly or indirectly, by or for his or her spouse on any day of a taxable year of such organization, provided that each of the following conditions are satisfied with respect to such taxable year:

(A) Such individual does not, at any time during such taxable year, own directly any interest in such organization;

(B) Such individual is not a member of the board of directors, a fiduciary, or an employee of such organization and does not participate in the management of such organization at any time during such taxable year;

(C) Not more than 50 percent of such organization's gross income for such taxable year was derived from royalties, rents, dividends, interest, and annuities; and

(D) Such interest in such organization is not, at any time during such taxable year, subject to conditions which substantially restrict or limit the spouse's right to dispose of such interest and which run in favor of the individual or the individual's children who have not attained the age of 21 years. The principles of § 1.414(c)–3(d)(6)(i) shall apply in determining whether a condition is a condition described in the preceding sentence.

(iii) Definitions. For purposes of paragraph (b)(5)(ii)(C) of this section, the gross income of an organization shall be determined under section 61 and the regulations thereunder. The terms “interest”, “royalties”, “rents”, “dividends”,

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and "annuities" shall have the same meaning such terms are given for purposes of section 1244(c) and § 1.1244(c)–1(e)(1).

(6) Children, grandchildren, parents, and grandparents—(i) Children and parents. An individual shall be considered to own an interest owned, directly or indirectly, by or for the individual's children who have not attained the age of 21 years, and if the individual has not attained the age of 21 years, an interest owned, directly or indirectly, by or for the individual's parents.

(ii) Children, grandchildren, parents, and grandparents. If an individual is in effective control (within the meaning of § 1.414(c)–2(c)(2)), directly and with the application of the rules of this paragraph without regard to this subdivision, of an organization, then such individual shall be considered to own an interest in such organization owned, directly or indirectly, by or for the individual's parents, grandparents, grandchildren, and children who have attained the age of 21 years.

(iii) Adopted children. For purposes of this section, a legally adopted child of an individual shall be treated as a child of such individual.

(iv) Example. The provisions of this subparagraph (6) may be illustrated by the following example:

Example: (A) Facts. Individual F owns directly 40 percent of the profits interest of the DEF Partnership. His son, M, 20 years of age, owns directly 30 percent of the profits interest of DEF, and his son, A, 30 years of age, owns directly 20 percent of the profits interest of DEF. The 10 percent remaining of the profits interest and 100 percent of the capital interest of DEF is owned by an unrelated person.

(B) F's ownership. F owns 40 percent of the profits interest in DEF directly and is considered to own the 30 percent profits interest owned directly by M. Since, for purposes of the effective control test contained in paragraph (b)(6)(ii) of this section, F is treated as owning 70 percent of the profits interest of DEF, F is also considered as owning the 20 percent profits interest of DEF owned by his adult son, A. Accordingly, F is considered as owning a total of 90 percent of the profits interest in DEF.

(C) M's ownership. Minor son, M. owns 30 percent of the profits interest in DEF directly, and is considered to own the 40 percent profits interest owned directly by his father, F. However, M is not considered to own the 20 percent profits interest of DEF owned directly by his brother, A, and constructively by F, because an interest constructively owned by F by reason of family attribution is not considered as owned by him for purposes of making another member of his family the constructive owner of such interest. (See paragraph (c)(2) of this section.) Accordingly, M is considered as owning a total of 70 percent of the profits interest of the DEF Partnership.

(D) A's ownership. Adult son, A, owns 20 percent of the profits interest in DEF directly. Since, for purposes of determining whether A effectively controls DEF under paragraph (b)(6)(ii) of this section, A is treated as owning only the percentage of profits interest he owns directly, he does not satisfy the condition precedent for the attribution of the DEF profits interest from his father. Accordingly, A is considered as owning only the 20 percent profits interest in DEF which he owns directly.

(c) Operating rules—(1) In general. Except as provided in paragraph (c)(2) of this section, an interest constructively owned by a person by reason of the application of paragraph (b) (1), (2), (3), (4), (5), or (6) of this section shall, for the purposes of applying such paragraph, be treated as actually owned by such person.

(2) Members of family. An interest constructively owned by an individual by reason of the application of paragraph (b) (5) or (6) of this section shall not be treated as owned by such individual for purposes of again applying such subparagraphs in order to make another the constructive owner of such interest.

(3) Precedence of option attribution. For purposes of this section, if an interest may be considered as owned under paragraph (b)(1) of this section (relating to option attribution) and under any other subparagraph of paragraph (b) of this section, such interest shall be considered as owned by such person under paragraph (b)(1) of this section.

(4) Examples. The provisions of this paragraph may be illustrated by the following examples:

Example 1. A, 30 years of age, has a 90 percent interest in the capital and profits of DEF Partnership. DEF owns all the outstanding stock of corporation X and X owns 60 shares of the 100 outstanding shares of corporation Y. Under paragraph (c)(1) of this section, the 60 shares of Y constructively owned by DEF by reason of paragraph (b)(4) of this section are treated as actually owned by DEF for purposes of applying paragraph (b)(2) of this section. Therefore, A is considered as owning 54 shares of the Y stock (90 percent of 60 shares).

Example 2. Assume the same facts as in example (1). Assume further that B, who is 20 years of age and the brother of A, directly owns 40 shares of Y stock. Although the stock of Y owned by B is considered as owned by C (the father of A and B) under paragraph (b)(6)(i) of this section, under paragraph (c)(2) of this section such stock may not be treated as owned by C for purposes of applying paragraph (b)(6)(ii) of this section in order to make A the constructive owner of such stock.

Example 3. Assume the same facts as in example (2), and further assume that C has an option to acquire the 40 shares of Y stock owned by his son, B. The rule contained in paragraph (c)(2) of this section does not prevent the reattribution of such 40 shares to A because, under paragraph (c)(3) of this section, C is considered as owning the 40 shares by reason of option attribution and not by reason of family attribution. Therefore, since A is in effective control of Y under paragraph (b)(6)(ii) of this section, the 40 shares of Y stock constructively owned by C are reattributed to A. A is considered as owning a total of 94 shares of Y stock.

Credits

[T.D. 8179, 53 FR 6609, March 2, 1988; T.D. 8179, 53 FR 8302, March 14, 1988; T.D. 8540, 59 FR 30102, June 10, 1994]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Current through December 8, 2016; 81 FR 88972.

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Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Deferred Compensation, Etc.
Pension, Profit–Sharing, Stock Bonus Plans, Etc.

26 C.F.R. § 1.414(c)–5, Treas. Reg. § 1.414(c)–5

§ 1.414(c)–5 Certain tax-exempt organizations.

Effective: September 25, 2007
Currentness

(a) Application. This section applies to an organization that is exempt from tax under section 501(a). The rules of this section only apply for purposes of determining when entities are treated as the same employer for purposes of section 414(b), (c), (m), and (o) (including the sections referred to in section 414(b), (c), (m), (o), and (t)), and are in addition to the rules otherwise applicable under section 414(b), (c), (m), and (o) for determining when entities are treated as the same employer. Except to the extent set forth in paragraphs (d), (e), and (f) of this section, this section does not apply to any church, as defined in section 3121(w)(3)(A), or any qualified church-controlled organization, as defined in section 3121(w)(3)(B).

(b) General rule. In the case of an organization that is exempt from tax under section 501(a) (an exempt organization) whose employees participate in a plan, the employer with respect to that plan includes the exempt organization whose employees participate in the plan and any other organization that is under common control with that exempt organization. For this purpose, common control exists between an exempt organization and another organization if at least 80 percent of the directors or trustees of one organization are either representatives of, or directly or indirectly controlled by, the other organization. A trustee or director is treated as a representative of another exempt organization if he or she also is a trustee, director, agent, or employee of the other exempt organization. A trustee or director is controlled by another organization if the other organization has the general power to remove such trustee or director and designate a new trustee or director. Whether a person has the power to remove or designate a trustee or director is based on facts and circumstances. To illustrate the rules of this paragraph (b), if exempt organization A has the power to appoint at least 80 percent of the trustees of exempt organization B (which is the owner of the outstanding shares of corporation C, which is not an exempt organization) and to control at least 80 percent of the directors of exempt organization D, then, under this paragraph (b) and § 1.414(b)–1, entities A, B, C, and D are treated as the same employer with respect to any plan maintained by A, B, C, or D for purposes of the sections referenced in section 414(b), (c), (m), (o), and (t).

(c) Permissive aggregation with entities having a common exempt purpose—(1) General rule. For purposes of this section, exempt organizations that maintain a plan to which section 414(c) applies that covers one or more employees from each organization may treat themselves as under common control for purposes of section 414(c) (and, thus, as a single employer for all purposes for which section 414(c) applies) if each of the organizations regularly coordinates their day-to-day exempt activities. For example, an entity that provides a type of emergency relief within one geographic region and another exempt organization that provides that type of emergency relief within another geographic region may treat themselves as under common control if they have a single plan covering employees of both entities and regularly coordinate their day-to-day exempt activities. Similarly, a hospital that is an exempt organization and another exempt

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organization with which it coordinates the delivery of medical services or medical research may treat themselves as under common control if there is a single plan covering employees of the hospital and employees of the other exempt organization and the coordination is a regular part of their day-to-day exempt activities.

(2) Authority to permit aggregation. (i) For determining when entities are treated as the same employer under section 414(b), (c), (m), and (o), the Commissioner may issue rules of general applicability, in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter), permitting other types of combinations of entities that include exempt organizations to elect to be treated as under common control for one or more specified purposes if:

(A) There are substantial business reasons for maintaining each entity in a separate trust, corporation, or other form; and

(B) Such treatment would be consistent with the anti-abuse standards in paragraph (f) of this section.

(ii) For example, this authority might be exercised in any situation in which the organizations are so integrated in their operations as to effectively constitute a single coordinated employer for purposes of section 414(b), (c), (m), and (o), including common employee benefit plans.

(d) Permissive disaggregation between qualified church controlled organizations and other entities. In the case of a church plan (as defined in section 414(e)) to which contributions are made by more than one common law entity, any employer may apply paragraphs (b) and (c) of this section to those entities that are not a church (as defined in section 403(b)(12)(B) and § 1.403(b)–2 separately from those entities that are churches. For example, in the case of a group of entities consisting of a church (as defined in section 3121(w)(3)(A)), a secondary school (that is treated as a church under § 1.403(b)–2), and several nursing homes each of which receives more than 25 percent of its support from fees paid by residents (so that none of them is a qualified church-controlled organization under § 1.403(b)–2 and section 3121(w)(3)(B)), the nursing homes may treat themselves as being under common control with each other, but not as being under common control with the church and the school, even though the nursing homes would be under common control with the school and the church under paragraph (b) of this section.

(e) Application to certain church entities under section 3121(w)(3). [Reserved]

(f) Anti-abuse rule. In any case in which the Commissioner determines that the structure of one or more exempt organizations (which may include an exempt organization and an entity that is not exempt from income tax) or the positions taken by those organizations has the effect of avoiding or evading any requirements imposed under section 401(a), 403(b), or 457(b), or any applicable section (as defined in section 414(t)), or any other provision for which section 414(c) applies, the Commissioner may treat an entity as under common control with the exempt organization.

(g) Examples. The provisions of this section are illustrated by the following examples:

Example 1. (i) Facts. Organization A is a tax-exempt organization under section 501(c)(3) which owns 80% or more of the total value of all classes of stock of corporation B, which is a for profit organization.

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(ii) Conclusion. Under paragraph (a) of this section, this section does not alter the rules of section 414(b) and (c), so that organization A and corporation B are under common control under § 1.414(c)–2(b).

Example 2. (i) Facts. Organization M is a hospital which is a tax-exempt organization under section 501(c)(3) and organization N is a medical clinic which is also a tax-exempt organization under section 501(c)(3). N is located in a city and M is located in a nearby suburb. There is a history of regular coordination of day-to-day activities between M and N, including periodic transfers of staff, coordination of staff training, common sources of income, and coordination of budget and operational goals. A single section 403(b) plan covers professional and staff employees of both the hospital and the medical clinic. While a number of members of the board of directors of M are also on the board of directors of N, there is less than 80% overlap in board membership. Both organizations have approximately the same percentage of employees who are highly compensated and have appropriate business reasons for being maintained in separate entities.

(ii) Conclusion. M and N are not under common control under this section, but, under paragraph (c) of this section, may chose to treat themselves as under common control, assuming both of them act in a manner that is consistent with that choice for purposes of § 1.403(b)–5(a), sections 401(a), 403(b), and 457(b), and any other applicable section (as defined in section 414(t)), or any other provision for which section 414(c) applies.

Example 3. (i) Facts. Organizations O and P are each tax-exempt organizations under section 501(c)(3). Each organization maintains a qualified plan for its employees, but one of the plans would not satisfy section 410(b) (or section 401(a)(4)) if the organizations were under common control. The two organizations are closely related and, while the organizations have several trustees in common, the common trustees constitute fewer than 80 percent of the trustees of either organization. Organization O has the power to remove any of the trustees of P and to select the slate of replacement nominees.

(ii) Conclusion. Under these facts, pursuant to paragraphs (b) and (f) of this section, the Commissioner treats the entities as under common control.

(h) Applicable date. This section applies for plan years beginning after December 31, 2008.

Credits

[T.D. 9340, 72 FR 41158, July 26, 2007; 72 FR 54352, Sept. 25, 2007]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

Current through December 8, 2016; 81 FR 88972.

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26 C.F.R. § 1.414(c)–5, Treas. Reg. § 1.414(c)–5

§ 1.414(c)–5 Certain tax-exempt organizations.

Effective: September 25, 2007
Currentness

(a) Application. This section applies to an organization that is exempt from tax under section 501(a). The rules of this section only apply for purposes of determining when entities are treated as the same employer for purposes of section 414(b), (c), (m), and (o) (including the sections referred to in section 414(b), (c), (m), (o), and (t)), and are in addition to the rules otherwise applicable under section 414(b), (c), (m), and (o) for determining when entities are treated as the same employer. Except to the extent set forth in paragraphs (d), (e), and (f) of this section, this section does not apply to any church, as defined in section 3121(w)(3)(A), or any qualified church-controlled organization, as defined in section 3121(w)(3)(B).

(b) General rule. In the case of an organization that is exempt from tax under section 501(a) (an exempt organization) whose employees participate in a plan, the employer with respect to that plan includes the exempt organization whose employees participate in the plan and any other organization that is under common control with that exempt organization. For this purpose, common control exists between an exempt organization and another organization if at least 80 percent of the directors or trustees of one organization are either representatives of, or directly or indirectly controlled by, the other organization. A trustee or director is treated as a representative of another exempt organization if he or she also is a trustee, director, agent, or employee of the other exempt organization. A trustee or director is controlled by another organization if the other organization has the general power to remove such trustee or director and designate a new trustee or director. Whether a person has the power to remove or designate a trustee or director is based on facts and circumstances. To illustrate the rules of this paragraph (b), if exempt organization A has the power to appoint at least 80 percent of the trustees of exempt organization B (which is the owner of the outstanding shares of corporation C, which is not an exempt organization) and to control at least 80 percent of the directors of exempt organization D, then, under this paragraph (b) and § 1.414(b)–1, entities A, B, C, and D are treated as the same employer with respect to any plan maintained by A, B, C, or D for purposes of the sections referenced in section 414(b), (c), (m), (o), and (t).

(c) Permissive aggregation with entities having a common exempt purpose—(1) General rule. For purposes of this section, exempt organizations that maintain a plan to which section 414(c) applies that covers one or more employees from each organization may treat themselves as under common control for purposes of section 414(c) (and, thus, as a single employer for all purposes for which section 414(c) applies) if each of the organizations regularly coordinates their day-to-day exempt activities. For example, an entity that provides a type of emergency relief within one geographic region and another exempt organization that provides that type of emergency relief within another geographic region may treat themselves as under common control if they have a single plan covering employees of both entities and regularly coordinate their day-to-day exempt activities. Similarly, a hospital that is an exempt organization and another exempt

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organization with which it coordinates the delivery of medical services or medical research may treat themselves as under common control if there is a single plan covering employees of the hospital and employees of the other exempt organization and the coordination is a regular part of their day-to-day exempt activities.

(2) Authority to permit aggregation. (i) For determining when entities are treated as the same employer under section 414(b), (c), (m), and (o), the Commissioner may issue rules of general applicability, in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter), permitting other types of combinations of entities that include exempt organizations to elect to be treated as under common control for one or more specified purposes if:

(A) There are substantial business reasons for maintaining each entity in a separate trust, corporation, or other form; and

(B) Such treatment would be consistent with the anti-abuse standards in paragraph (f) of this section.

(ii) For example, this authority might be exercised in any situation in which the organizations are so integrated in their operations as to effectively constitute a single coordinated employer for purposes of section 414(b), (c), (m), and (o), including common employee benefit plans.

(d) Permissive disaggregation between qualified church controlled organizations and other entities. In the case of a church plan (as defined in section 414(e)) to which contributions are made by more than one common law entity, any employer may apply paragraphs (b) and (c) of this section to those entities that are not a church (as defined in section 403(b)(12)(B) and § 1.403(b)–2) separately from those entities that are churches. For example, in the case of a group of entities consisting of a church (as defined in section 3121(w)(3)(A)), a secondary school (that is treated as a church under § 1.403(b)–2), and several nursing homes each of which receives more than 25 percent of its support from fees paid by residents (so that none of them is a qualified church-controlled organization under § 1.403(b)–2 and section 3121(w)(3)(B)), the nursing homes may treat themselves as being under common control with each other, but not as being under common control with the church and the school, even though the nursing homes would be under common control with the school and the church under paragraph (b) of this section.

(e) Application to certain church entities under section 3121(w)(3). [Reserved]

(f) Anti-abuse rule. In any case in which the Commissioner determines that the structure of one or more exempt organizations (which may include an exempt organization and an entity that is not exempt from income tax) or the positions taken by those organizations has the effect of avoiding or evading any requirements imposed under section 401(a), 403(b), or 457(b), or any applicable section (as defined in section 414(t)), or any other provision for which section 414(c) applies, the Commissioner may treat an entity as under common control with the exempt organization.

(g) Examples. The provisions of this section are illustrated by the following examples:

Example 1. (i) Facts. Organization A is a tax-exempt organization under section 501(c)(3) which owns 80% or more of the total value of all classes of stock of corporation B, which is a for profit organization.

(ii) Conclusion. Under paragraph (a) of this section, this section does not alter the rules of section 414(b) and (c), so that organization A and corporation B are under common control under § 1.414(c)–2(b).

Example 2. (i) Facts. Organization M is a hospital which is a tax-exempt organization under section 501(c)(3) and organization N is a medical clinic which is also a tax-exempt organization under section 501(c)(3). N is located in a city and M is located in a nearby suburb. There is a history of regular coordination of day-to-day activities between M and N, including periodic transfers of staff, coordination of staff training, common sources of income, and coordination of budget and operational goals. A single section 403(b) plan covers professional and staff employees of both the hospital and the medical clinic. While a number of members of the board of directors of M are also on the board of directors of N, there is less than 80% overlap in board membership. Both organizations have approximately the same percentage of employees who are highly compensated and have appropriate business reasons for being maintained in separate entities.

(ii) Conclusion. M and N are not under common control under this section, but, under paragraph (c) of this section, may chose to treat themselves as under common control, assuming both of them act in a manner that is consistent with that choice for purposes of § 1.403(b)–5(a), sections 401(a), 403(b), and 457(b), and any other applicable section (as defined in section 414(t)), or any other provision for which section 414(c) applies.

Example 3. (i) Facts. Organizations O and P are each tax-exempt organizations under section 501(c)(3). Each organization maintains a qualified plan for its employees, but one of the plans would not satisfy section 410(b) (or section 401(a)(4)) if the organizations were under common control. The two organizations are closely related and, while the organizations have several trustees in common, the common trustees constitute fewer than 80 percent of the trustees of either organization. Organization O has the power to remove any of the trustees of P and to select the slate of replacement nominees.

(ii) Conclusion. Under these facts, pursuant to paragraphs (b) and (f) of this section, the Commissioner treats the entities as under common control.

(h) Applicable date. This section applies for plan years beginning after December 31, 2008.

Credits

[T.D. 9340, 72 FR 41158, July 26, 2007; 72 FR 54352, Sept. 25, 2007]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, unless otherwise noted.

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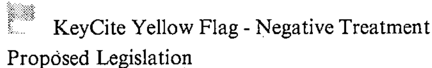
KeyCite Yellow Flag - Negative Treatment
Proposed Legislation

United States Code Annotated
Title 11. Bankruptcy (Refs & Annos)
Chapter 11. Reorganization (Refs & Annos)
Subchapter I. Officers and Administration (Refs & Annos)

11 U.S.C.A. § 1112

§ 1112. Conversion or dismissal

Effective: December 22, 2010
Currentness

(a) The debtor may convert a case under this chapter to a case under chapter 7 of this title unless--

(1) the debtor is not a debtor in possession;

(2) the case originally was commenced as an involuntary case under this chapter; or

(3) the case was converted to a case under this chapter other than on the debtor's request.

(b)(1) Except as provided in paragraph (2) and subsection (c), on request of a party in interest, and after notice and a hearing, the court shall convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause unless the court determines that the appointment under section 1104(a) of a trustee or an examiner is in the best interests of creditors and the estate.

(2) The court may not convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter if the court finds and specifically identifies unusual circumstances establishing that converting or dismissing the case is not in the best interests of creditors and the estate, and the debtor or any other party in interest establishes that--

(A) there is a reasonable likelihood that a plan will be confirmed within the timeframes established in sections 1121(e) and 1129(e) of this title, or if such sections do not apply, within a reasonable period of time; and

(B) the grounds for converting or dismissing the case include an act or omission of the debtor other than under paragraph (4)(A)--

(i) for which there exists a reasonable justification for the act or omission; and

(ii) that will be cured within a reasonable period of time fixed by the court.

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(3) The court shall commence the hearing on a motion under this subsection not later than 30 days after filing of the motion, and shall decide the motion not later than 15 days after commencement of such hearing, unless the movant expressly consents to a continuance for a specific period of time or compelling circumstances prevent the court from meeting the time limits established by this paragraph.

(4) For purposes of this subsection, the term "cause" includes--

(A) substantial or continuing loss to or diminution of the estate and the absence of a reasonable likelihood of rehabilitation;

(B) gross mismanagement of the estate;

(C) failure to maintain appropriate insurance that poses a risk to the estate or to the public;

(D) unauthorized use of cash collateral substantially harmful to 1 or more creditors;

(E) failure to comply with an order of the court;

(F) unexcused failure to satisfy timely any filing or reporting requirement established by this title or by any rule applicable to a case under this chapter;

(G) failure to attend the meeting of creditors convened under section 341(a) or an examination ordered under rule 2004 of the Federal Rules of Bankruptcy Procedure without good cause shown by the debtor;

(H) failure timely to provide information or attend meetings reasonably requested by the United States trustee (or the bankruptcy administrator, if any);

(I) failure timely to pay taxes owed after the date of the order for relief or to file tax returns due after the date of the order for relief;

(J) failure to file a disclosure statement, or to file or confirm a plan, within the time fixed by this title or by order of the court;

(K) failure to pay any fees or charges required under chapter 123 of title 28;

(L) revocation of an order of confirmation under section 1144;

(M) inability to effectuate substantial consummation of a confirmed plan;

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(N) material default by the debtor with respect to a confirmed plan;

(O) termination of a confirmed plan by reason of the occurrence of a condition specified in the plan; and

(P) failure of the debtor to pay any domestic support obligation that first becomes payable after the date of the filing of the petition.

(c) The court may not convert a case under this chapter to a case under chapter 7 of this title if the debtor is a farmer or a corporation that is not a moneyed, business, or commercial corporation, unless the debtor requests such conversion.

(d) The court may convert a case under this chapter to a case under chapter 12 or 13 of this title only if--

(1) the debtor requests such conversion;

(2) the debtor has not been discharged under section 1141(d) of this title; and

(3) if the debtor requests conversion to chapter 12 of this title, such conversion is equitable.

(e) Except as provided in subsections (c) and (f), the court, on request of the United States trustee, may convert a case under this chapter to a case under chapter 7 of this title or may dismiss a case under this chapter, whichever is in the best interest of creditors and the estate if the debtor in a voluntary case fails to file, within fifteen days after the filing of the petition commencing such case or such additional time as the court may allow, the information required by paragraph (1) of section 521(a), including a list containing the names and addresses of the holders of the twenty largest unsecured claims (or of all unsecured claims if there are fewer than twenty unsecured claims), and the approximate dollar amounts of each of such claims.

(f) Notwithstanding any other provision of this section, a case may not be converted to a case under another chapter of this title unless the debtor may be a debtor under such chapter.

CREDIT(S)

(Pub.L. 95-598, Nov. 6, 1978, 92 Stat. 2630; Pub.L. 98-353, Title III, § 505, July 10, 1984, 98 Stat. 384; Pub.L. 99-554, Title II, §§ 224, 256, Oct. 27, 1986, 100 Stat. 3102, 3114; Pub.L. 103-394, Title II, § 217(c), Oct. 22, 1994, 108 Stat. 4127; Pub.L. 109-8, Title IV, § 442(a), Apr. 20, 2005, 119 Stat. 115; Pub.L. 111-327, § 2(a)(33), Dec. 22, 2010, 124 Stat. 3561.)

Notes of Decisions (861)

11 U.S.C.A. § 1112, 11 USCA § 1112
Current through P.L. 114-248.

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KeyCite Yellow Flag - Negative Treatment
Proposed Legislation

United States Code Annotated
Title 26. Internal Revenue Code (Refs & Annos)
Subtitle A. Income Taxes (Refs & Annos)
Chapter 1. Normal Taxes and Surtaxes (Refs & Annos)
Subchapter D. Deferred Compensation, Etc. (Refs & Annos)
Part I. Pension, Profit-Sharing, Stock Bonus Plans, Etc. (Refs & Annos)
Subpart A. General Rule (Refs & Annos)

26 U.S.C.A. § 401, I.R.C. § 401

§ 401. Qualified pension, profit-sharing, and stock bonus plans

Effective: December 19, 2014
Currentness

(a) Requirements for qualification.--A trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of his employees or their beneficiaries shall constitute a qualified trust under this section--

(1) if contributions are made to the trust by such employer, or employees, or both, or by another employer who is entitled to deduct his contributions under section 404(a)(3)(B) (relating to deduction for contributions to profit-sharing and stock bonus plans), or by a charitable remainder trust pursuant to a qualified gratuitous transfer (as defined in section 664(g)(1)), for the purpose of distributing to such employees or their beneficiaries the corpus and income of the fund accumulated by the trust in accordance with such plan;

(2) if under the trust instrument it is impossible, at any time prior to the satisfaction of all liabilities with respect to employees and their beneficiaries under the trust, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, purposes other than for the exclusive benefit of his employees or their beneficiaries (but this paragraph shall not be construed, in the case of a multiemployer plan, to prohibit the return of a contribution within 6 months after the plan administrator determines that the contribution was made by a mistake of fact or law (other than a mistake relating to whether the plan is described in section 401(a) or the trust which is part of such plan is exempt from taxation under section 501(a), or the return of any withdrawal liability payment determined to be an overpayment within 6 months of such determination).;[1]

(3) if the plan of which such trust is a part satisfies the requirements of section 410 (relating to minimum participation standards); and

(4) if the contributions or benefits provided under the plan do not discriminate in favor of highly compensated employees (within the meaning of section 414(q)). For purposes of this paragraph, there shall be excluded from consideration employees described in section 410(b)(3)(A) and (C).

(5) Special rules relating to nondiscrimination requirements.--

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(A) Salaried or clerical employees.--A classification shall not be considered discriminatory within the meaning of paragraph (4) or section 410(b)(2)(A)(i) merely because it is limited to salaried or clerical employees.

(B) Contributions and benefits may bear uniform relationship to compensation.--A plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the contributions or benefits of, or on behalf of, the employees under the plan bear a uniform relationship to the compensation (within the meaning of section 414(s)) of such employees.

(C) Certain disparity permitted.--A plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the contributions or benefits of, or on behalf of, the employees under the plan favor highly compensated employees (as defined in section 414(q)) in the manner permitted under subsection (l).

(D) Integrated defined benefit plan.--

(i) In general.--A defined benefit plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the plan provides that the employer-derived accrued retirement benefit for any participant under the plan may not exceed the excess (if any) of--

(I) the participant's final pay with the employer, over

(II) the employer-derived retirement benefit created under Federal law attributable to service by the participant with the employer.

For purposes of this clause, the employer-derived retirement benefit created under Federal law shall be treated as accruing ratably over 35 years.

(ii) Final pay.--For purposes of this subparagraph, the participant's final pay is the compensation (as defined in section 414(q)(4)) paid to the participant by the employer for any year--

(I) which ends during the 5-year period ending with the year in which the participant separated from service for the employer, and

(II) for which the participant's total compensation from the employer was highest.

(E) 2 or more plans treated as single plan.--For purposes of determining whether 2 or more plans of an employer satisfy the requirements of paragraph (4) when considered as a single plan--

(i) Contributions.--If the amount of contributions on behalf of the employees allowed as a deduction under section 404 for the taxable year with respect to such plans, taken together, bears a uniform relationship to the compensation (within the meaning of section 414(s)) of such employees, the plans shall not be considered

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discriminatory merely because the rights of employees to, or derived from, the employer contributions under the separate plans do not become nonforfeitable at the same rate.

(ii) Benefits.--If the employees' rights to benefits under the separate plans do not become nonforfeitable at the same rate, but the levels of benefits provided by the separate plans satisfy the requirements of regulations prescribed by the Secretary to take account of the differences in such rates, the plans shall not be considered discriminatory merely because of the difference in such rates.

(F) Social security retirement age.--For purposes of testing for discrimination under paragraph (4)--

(i) the social security retirement age (as defined in section 415(b)(8)) shall be treated as a uniform retirement age, and

(ii) subsidized early retirement benefits and joint and survivor annuities shall not be treated as being unavailable to employees on the same terms merely because such benefits or annuities are based in whole or in part on an employee's social security retirement age (as so defined).

(G) Governmental plans.--Paragraphs (3) and (4) shall not apply to a governmental plan (within the meaning of section 414(d)).

(6) A plan shall be considered as meeting the requirements of paragraph (3) during the whole of any taxable year of the plan if on one day in each quarter it satisfied such requirements.

(7) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part satisfies the requirements of section 411 (relating to minimum vesting standards).

(8) A trust forming part of a defined benefit plan shall not constitute a qualified trust under this section unless the plan provides that forfeitures must not be applied to increase the benefits any employee would otherwise receive under the plan.

(9) Required distributions.--

(A) In general.--A trust shall not constitute a qualified trust under this subsection unless the plan provides that the entire interest of each employee--

(i) will be distributed to such employee not later than the required beginning date, or

(ii) will be distributed, beginning not later than the required beginning date, in accordance with regulations, over the life of such employee or over the lives of such employee and a designated beneficiary (or over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and a designated beneficiary).

(B) Required distribution where employee dies before entire interest is distributed.--

(i) Where distributions have begun under subparagraph (A)(ii).--A trust shall not constitute a qualified trust under this section unless the plan provides that if--

(I) the distribution of the employee's interest has begun in accordance with subparagraph (A)(ii), and

(II) the employee dies before his entire interest has been distributed to him,

the remaining portion of such interest will be distributed at least as rapidly as under the method of distributions being used under subparagraph (A)(ii) as of the date of his death.

(ii) 5-year rule for other cases.--A trust shall not constitute a qualified trust under this section unless the plan provides that, if an employee dies before the distribution of the employee's interest has begun in accordance with subparagraph (A)(ii), the entire interest of the employee will be distributed within 5 years after the death of such employee.

(iii) Exception to 5-year rule for certain amounts payable over life of beneficiary.--If--

(I) any portion of the employee's interest is payable to (or for the benefit of) a designated beneficiary,

(II) such portion will be distributed (in accordance with regulations) over the life of such designated beneficiary (or over a period not extending beyond the life expectancy of such beneficiary), and

(III) such distributions begin not later than 1 year after the date of the employee's death or such later date as the Secretary may by regulations prescribe,

for purposes of clause (ii), the portion referred to in subclause (I) shall be treated as distributed on the date on which such distributions begin.

(iv) Special rule for surviving spouse of employee.--If the designated beneficiary referred to in clause (iii)(I) is the surviving spouse of the employee--

(I) the date on which the distributions are required to begin under clause (iii)(III) shall not be earlier than the date on which the employee would have attained age 70 ½, and

(II) if the surviving spouse dies before the distributions to such spouse begin, this subparagraph shall be applied as if the surviving spouse were the employee.

(C) Required beginning date.--For purposes of this paragraph--

(i) In general.--The term "required beginning date" means April 1 of the calendar year following the later of--

(I) the calendar year in which the employee attains age 70 ½, or

(II) the calendar year in which the employee retires.

(ii) Exception.--Subclause (II) of clause (i) shall not apply--

(I) except as provided in section 409(d), in the case of an employee who is a 5-percent owner (as defined in section 416) with respect to the plan year ending in the calendar year in which the employee attains age 70 ½, or

(II) for purposes of section 408(a)(6) or (b)(3).

(iii) Actuarial adjustment.--In the case of an employee to whom clause (i)(II) applies who retires in a calendar year after the calendar year in which the employee attains age 70 ½, the employee's accrued benefit shall be actuarially increased to take into account the period after age 70 ½ in which the employee was not receiving any benefits under the plan.

(iv) Exception for governmental and church plans.--Clauses (ii) and (iii) shall not apply in the case of a governmental plan or church plan. For purposes of this clause, the term "church plan" means a plan maintained by a church for church employees, and the term "church" means any church (as defined in section 3121(w)(3)(A)) or qualified church-controlled organization (as defined in section 3121(w)(3)(B)).

(D) Life expectancy.--For purposes of this paragraph, the life expectancy of an employee and the employee's spouse (other than in the case of a life annuity) may be redetermined but not more frequently than annually.

(E) Designated beneficiary.--For purposes of this paragraph, the term "designated beneficiary" means any individual designated as a beneficiary by the employee.

(F) Treatment of payments to children.--Under regulations prescribed by the Secretary, for purposes of this paragraph, any amount paid to a child shall be treated as if it had been paid to the surviving spouse if such amount will become payable to the surviving spouse upon such child reaching majority (or other designated event permitted under regulations).

(G) Treatment of incidental death benefit distributions.--For purposes of this title, any distribution required under the incidental death benefit requirements of this subsection shall be treated as a distribution required under this paragraph.

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[(H) **Repealed.** Pub.L. 113-295, Div. A, Title II, § 221(a)(52), Dec. 19, 2014, 128 Stat. 4045]

(10) Other requirements.--

(A) Plans benefiting owner-employees.--In the case of any plan which provides contributions or benefits for employees some or all of whom are owner-employees (as defined in subsection (c)(3)), a trust forming part of such plan shall constitute a qualified trust under this section only if the requirements of subsection (d) are also met.

(B) Top-heavy plans.--

(i) In general.--In the case of any top-heavy plan, a trust forming part of such plan shall constitute a qualified trust under this section only if the requirements of section 416 are met.

(ii) Plans which may become top-heavy.--Except to the extent provided in regulations, a trust forming part of a plan (whether or not a top-heavy plan) shall constitute a qualified trust under this section only if such plan contains provisions--

(I) which will take effect if such plan becomes a top-heavy plan, and

(II) which meet the requirements of section 416.

(iii) Exemption for governmental plans.--This subparagraph shall not apply to any governmental plan.

(11) Requirement of joint and survivor annuity and preretirement survivor annuity.--

(A) In general.--In the case of any plan to which this paragraph applies, except as provided in section 417, a trust forming part of such plan shall not constitute a qualified trust under this section unless--

(i) in the case of a vested participant who does not die before the annuity starting date, the accrued benefit payable to such participant is provided in the form of a qualified joint and survivor annuity, and

(ii) in the case of a vested participant who dies before the annuity starting date and who has a surviving spouse, a qualified preretirement survivor annuity is provided to the surviving spouse of such participant.

(B) Plans to which paragraph applies.--This paragraph shall apply to--

(i) any defined benefit plan,

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(ii) any defined contribution plan which is subject to the funding standards of section 412, and

(iii) any participant under any other defined contribution plan unless--

(I) such plan provides that the participant's nonforfeitable accrued benefit (reduced by any security interest held by the plan by reason of a loan outstanding to such participant) is payable in full, on the death of the participant, to the participant's surviving spouse (or, if there is no surviving spouse or the surviving spouse consents in the manner required under section 417(a)(2), to a designated beneficiary),

(II) such participant does not elect a payment of benefits in the form of a life annuity, and

(III) with respect to such participant, such plan is not a direct or indirect transferee (in a transfer after December 31, 1984) of a plan which is described in clause (i) or (ii) or to which this clause applied with respect to the participant.

Clause (iii)(III) shall apply only with respect to the transferred assets (and income therefrom) if the plan separately accounts for such assets and any income therefrom.

(C) Exception for certain ESOP benefits.--

(i) In general.--In the case of--

(I) a tax credit employee stock ownership plan (as defined in section 409(a)), or

(II) an employee stock ownership plan (as defined in section 4975(e)(7)),

subparagraph (A) shall not apply to that portion of the employee's accrued benefit to which the requirements of section 409(h) apply.

(ii) Nonforfeitable benefit must be paid in full, etc.--In the case of any participant, clause (i) shall apply only if the requirements of subclauses (I), (II), and (III) of subparagraph (B)(iii) are met with respect to such participant.

(D) Special rule where participant and spouse married less than 1 year.--A plan shall not be treated as failing to meet the requirements of subparagraphs (B)(iii) or (C) merely because the plan provides that benefits will not be payable to the surviving spouse of the participant unless the participant and such spouse had been married throughout the 1-year period ending on the earlier of the participant's annuity starting date or the date of the participant's death.

(E) Exception for plans described in section 404(c).--This paragraph shall not apply to a plan which the Secretary has determined is a plan described in section 404(c) (or a continuation thereof) in which participation is substantially limited to individuals who, before January 1, 1976, ceased employment covered by the plan.

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(F) Cross reference.--For--

(i) provisions under which participants may elect to waive the requirements of this paragraph, and

(ii) other definitions and special rules for purposes of this paragraph,

see section 417.

(12) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that in the case of any merger or consolidation with, or transfer of assets or liabilities to, any other plan after September 2, 1974, each participant in the plan would (if the plan then terminated) receive a benefit immediately after the merger, consolidation, or transfer which is equal to or greater than the benefit he would have been entitled to receive immediately before the merger, consolidation, or transfer (if the plan had then terminated). The preceding sentence does not apply to any multiemployer plan with respect to any transaction to the extent that participants either before or after the transaction are covered under a multiemployer plan to which title IV of the Employee Retirement Income Security Act of 1974 applies.

(13) Assignment and alienation.--

(A) In general.--A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that benefits provided under the plan may not be assigned or alienated. For purposes of the preceding sentence, there shall not be taken into account any voluntary and revocable assignment of not to exceed 10 percent of any benefit payment made by any participant who is receiving benefits under the plan unless the assignment or alienation is made for purposes of defraying plan administration costs. For purposes of this paragraph a loan made to a participant or beneficiary shall not be treated as an assignment or alienation if such loan is secured by the participant's accrued nonforfeitable benefit and is exempt from the tax imposed by section 4975 (relating to tax on prohibited transactions) by reason of section 4975(d)(1). This paragraph shall take effect on January 1, 1976 and shall not apply to assignments which were irrevocable on September 2, 1974.

(B) Special rules for domestic relations orders.--Subparagraph (A) shall apply to the creation, assignment, or recognition of a right to any benefit payable with respect to a participant pursuant to a domestic relations order, except that subparagraph (A) shall not apply if the order is determined to be a qualified domestic relations order.

(C) Special rule for certain judgments and settlements.--Subparagraph (A) shall not apply to any offset of a participant's benefits provided under a plan against an amount that the participant is ordered or required to pay to the plan if--

(i) the order or requirement to pay arises--

(I) under a judgment of conviction for a crime involving such plan,

(II) under a civil judgment (including a consent order or decree) entered by a court in an action brought in connection with a violation (or alleged violation) of part 4 of subtitle B of title I of the Employee Retirement Income Security Act of 1974, or

(III) pursuant to a settlement agreement between the Secretary of Labor and the participant, or a settlement agreement between the Pension Benefit Guaranty Corporation and the participant, in connection with a violation (or alleged violation) of part 4 of such subtitle by a fiduciary or any other person,

(ii) the judgment, order, decree, or settlement agreement expressly provides for the offset of all or part of the amount ordered or required to be paid to the plan against the participant's benefits provided under the plan, and

(iii) in a case in which the survivor annuity requirements of section 401(a)(11) apply with respect to distributions from the plan to the participant, if the participant has a spouse at the time at which the offset is to be made--

(I) either such spouse has consented in writing to such offset and such consent is witnessed by a notary public or representative of the plan (or it is established to the satisfaction of a plan representative that such consent may not be obtained by reason of circumstances described in section 417(a)(2)(B)), or an election to waive the right of the spouse to either a qualified joint and survivor annuity or a qualified preretirement survivor annuity is in effect in accordance with the requirements of section 417(a),

(II) such spouse is ordered or required in such judgment, order, decree, or settlement to pay an amount to the plan in connection with a violation of part 4 of such subtitle, or

(III) in such judgment, order, decree, or settlement, such spouse retains the right to receive the survivor annuity under a qualified joint and survivor annuity provided pursuant to section 401(a)(11)(A)(i) and under a qualified preretirement survivor annuity provided pursuant to section 401(a)(11)(A)(ii), determined in accordance with subparagraph (D).

A plan shall not be treated as failing to meet the requirements of this subsection, subsection (k), section 403(b), or section 409(d) solely by reason of an offset described in this subparagraph.

(D) Survivor annuity.--

(i) In general.--The survivor annuity described in subparagraph (C)(iii)(III) shall be determined as if--

(I) the participant terminated employment on the date of the offset,

(II) there was no offset,

(III) the plan permitted commencement of benefits only on or after normal retirement age,

(IV) the plan provided only the minimum-required qualified joint and survivor annuity, and

(V) the amount of the qualified preretirement survivor annuity under the plan is equal to the amount of the survivor annuity payable under the minimum-required qualified joint and survivor annuity.

(ii) Definition.--For purposes of this subparagraph, the term "minimum-required qualified joint and survivor annuity" means the qualified joint and survivor annuity which is the actuarial equivalent of the participant's accrued benefit (within the meaning of section 411(a)(7)) and under which the survivor annuity is 50 percent of the amount of the annuity which is payable during the joint lives of the participant and the spouse.

(14) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that, unless the participant otherwise elects, the payment of benefits under the plan to the participant will begin not later than the 60th day after the latest of the close of the plan year in which--

(A) the date on which the participant attains the earlier of age 65 or the normal retirement age specified under the plan,

(B) occurs the 10th anniversary of the year in which the participant commenced participation in the plan, or

(C) the participant terminates his service with the employer.

In the case of a plan which provides for the payment of an early retirement benefit, a trust forming a part of such plan shall not constitute a qualified trust under this section unless a participant who satisfied the service requirements for such early retirement benefit, but separated from the service (with any nonforfeitable right to an accrued benefit) before satisfying the age requirement for such early retirement benefit, is entitled upon satisfaction of such age requirement to receive a benefit not less than the benefit to which he would be entitled at the normal retirement age, actuarially, reduced under regulations prescribed by the Secretary.

(15) a [2] trust shall not constitute a qualified trust under this section unless under the plan of which such trust is a part--

(A) in the case of a participant or beneficiary who is receiving benefits under such plan, or

(B) in the case of a participant who is separated from the service and who has nonforfeitable rights to benefits,

such benefits are not decreased by reason of any increase in the benefit levels payable under title II of the Social Security Act or any increase in the wage base under such title II, if such increase takes place after September 2, 1974, or (if later) the earlier of the date of first receipt of such benefits or the date of such separation, as the case may be.

(16) A trust shall not constitute a qualified trust under this section if the plan of which such trust is a part provides for benefits or contributions which exceed the limitations of section 415.

(17) Compensation limit.--

(A) In general.-- A trust shall not constitute a qualified trust under this section unless, under the plan of which such trust is a part, the annual compensation of each employee taken into account under the plan for any year does not exceed $200,000.

(B) Cost-of-living adjustment.--The Secretary shall adjust annually the $200,000 amount in subparagraph (A) for increases in the cost-of-living at the same time and in the same manner as adjustments under section 415(d); except that the base period shall be the calendar quarter beginning July 1, 2001, and any increase which is not a multiple of $5,000 shall be rounded to the next lowest multiple of $5,000.

[(18) Repealed. Pub.L. 97-248, Title II, § 237(b), Sept. 3, 1982, 96 Stat. 511]

(19) A trust shall not constitute a qualified trust under this section if under the plan of which such trust is a part any part of a participant's accrued benefit derived from employer contributions (whether or not otherwise nonforfeitable), is forfeitable solely because of withdrawal by such participant of any amount attributable to the benefit derived from contributions made by such participant. The preceding sentence shall not apply to the accrued benefit of any participant unless, at the time of such withdrawal, such participant has a nonforfeitable right to at least 50 percent of such accrued benefit (as determined under section 411). The first sentence of this paragraph shall not apply to the extent that an accrued benefit is permitted to be forfeited in accordance with section 411(a)(3)(D)(iii) (relating to proportional forfeitures of benefits accrued before September 2, 1974, in the event of withdrawal of certain mandatory contributions).

(20) A trust forming part of a pension plan shall not be treated as failing to constitute a qualified trust under this section merely because the pension plan of which such trust is a part makes 1 or more distributions within 1 taxable year to a distributee on account of a termination of the plan of which the trust is a part, or in the case of a profit-sharing or stock bonus plan, a complete discontinuance of contributions under such plan. This paragraph shall not apply to a defined benefit plan unless the employer maintaining such plan files a notice with the Pension Benefit Guaranty Corporation (at the time and in the manner prescribed by the Pension Benefit Guaranty Corporation) notifying the Corporation of such payment or distribution and the Corporation has approved such payment or distribution or, within 90 days after the date on which such notice was filed, has failed to disapprove such payment or distribution. For purposes of this paragraph, rules similar to the rules of section 402(a)(6)(B) (as in effect before its repeal by section 521 of the Unemployment Compensation Amendments of 1992) shall apply.

[(21) Repealed. Pub.L. 99-514, Title XI, § 1171(b)(5), Oct. 22, 1986, 100 Stat. 2513]

(22) If a defined contribution plan (other than a profit-sharing plan)--

(A) is established by an employer whose stock is not readily tradable on an established market, and

(B) after acquiring securities of the employer, more than 10 percent of the total assets of the plan are securities of the employer,

any trust forming part of such plan shall not constitute a qualified trust under this section unless the plan meets the requirements of subsection (e) of section 409. The requirements of subsection (e) of section 409 shall not apply to any employees of an employer who are participants in any defined contribution plan established and maintained by such employer if the stock of such employer is not readily tradable on an established market and the trade or business of such employer consists of publishing on a regular basis a newspaper for general circulation. For purposes of the preceding sentence, subsections (b), (c), (m), and (o) of section 414 shall not apply except for determining whether stock of the employer is not readily tradable on an established market.

(23) A stock bonus plan shall not be treated as meeting the requirements of this section unless such plan meets the requirements of subsections (h) and (o) of section 409, except that in applying section 409(h) for purposes of this paragraph, the term "employer securities" shall include any securities of the employer held by the plan.

(24) Any group trust which otherwise meets the requirements of this section shall not be treated as not meeting such requirements on account of the participation or inclusion in such trust of the moneys of any plan or governmental unit described in section 818(a)(6).

(25) Requirement that actuarial assumptions be specified.--A defined benefit plan shall not be treated as providing definitely determinable benefits unless, whenever the amount of any benefit is to be determined on the basis of actuarial assumptions, such assumptions are specified in the plan in a way which precludes employer discretion.

(26) Additional participation requirements.--

(A) In general.--In the case of a trust which is a part of a defined benefit plan, such trust shall not constitute a qualified trust under this subsection unless on each day of the plan year such trust benefits at least the lesser of--

(i) 50 employees of the employer, or

(ii) the greater of--

(I) 40 percent of all employees of the employer, or

(II) 2 employees (or if there is only 1 employee, such employee).

(B) Treatment of excludable employees.--

(i) In general.--A plan may exclude from consideration under this paragraph employees described in paragraphs (3) and (4)(A) of section 410(b).

(ii) Separate application for certain excludable employees.--If employees described in section 410(b)(4)(B) are covered under a plan which meets the requirements of subparagraph (A) separately with respect to such

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employees, such employees may be excluded from consideration in determining whether any plan of the employer meets such requirements if--

(I) the benefits for such employees are provided under the same plan as benefits for other employees,

(II) the benefits provided to such employees are not greater than comparable benefits provided to other employees under the plan, and

(III) no highly compensated employee (within the meaning of section 414(q)) is included in the group of such employees for more than 1 year.

(C) Special rule for collective bargaining units.--Except to the extent provided in regulations, a plan covering only employees described in section 410(b)(3)(A) may exclude from consideration any employees who are not included in the unit or units in which the covered employees are included.

(D) Paragraph not to apply to multiemployer plans.--Except to the extent provided in regulations, this paragraph shall not apply to employees in a multiemployer plan (within the meaning of section 414(f)) who are covered by collective bargaining agreements.

(E) Special rule for certain dispositions or acquisitions.--Rules similar to the rules of section 410(b)(6)(C) shall apply for purposes of this paragraph.

(F) Separate lines of business.--At the election of the employer and with the consent of the Secretary, this paragraph may be applied separately with respect to each separate line of business of the employer. For purposes of this paragraph, the term "separate line of business" has the meaning given such term by section 414(r) (without regard to paragraph (2)(A) or (7) thereof).

(G) Exception for governmental plans.--This paragraph shall not apply to a governmental plan (within the meaning of section 414(d)).

(H) Regulations.--The Secretary may by regulation provide that any separate benefit structure, any separate trust, or any other separate arrangement is to be treated as a separate plan for purposes of applying this paragraph.

(27) Determinations as to profit-sharing plans.--

(A) Contributions need not be based on profits.--The determination of whether the plan under which any contributions are made is a profit-sharing plan shall be made without regard to current or accumulated profits of the employer and without regard to whether the employer is a tax-exempt organization.

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(B) Plan must designate type.--In the case of a plan which is intended to be a money purchase pension plan or a profit-sharing plan, a trust forming part of such plan shall not constitute a qualified trust under this subsection unless the plan designates such intent at such time and in such manner as the Secretary may prescribe.

(28) Additional requirements relating to employee stock ownership plans.--

(A) In general.--In the case of a trust which is part of an employee stock ownership plan (within the meaning of section 4975(e)(7)) or a plan which meets the requirements of section 409(a), such trust shall not constitute a qualified trust under this section unless such plan meets the requirements of subparagraphs (B) and (C).

(B) Diversification of investments.--

(i) In general.--A plan meets the requirements of this subparagraph if each qualified participant in the plan may elect within 90 days after the close of each plan year in the qualified election period to direct the plan as to the investment of at least 25 percent of the participant's account in the plan (to the extent such portion exceeds the amount to which a prior election under this subparagraph applies). In the case of the election year in which the participant can make his last election, the preceding sentence shall be applied by substituting "50 percent" for "25 percent".

(ii) Method of meeting requirements.--A plan shall be treated as meeting the requirements of clause (i) if--

(I) the portion of the participant's account covered by the election under clause (i) is distributed within 90 days after the period during which the election may be made, or

(II) the plan offers at least 3 investment options (not inconsistent with regulations prescribed by the Secretary) to each participant making an election under clause (i) and within 90 days after the period during which the election may be made, the plan invests the portion of the participant's account covered by the election in accordance with such election.

(iii) Qualified participant.--For purposes of this subparagraph, the term "qualified participant" means any employee who has completed at least 10 years of participation under the plan and has attained age 55.

(iv) Qualified election period.--For purposes of this subparagraph, the term "qualified election period" means the 6-plan-year period beginning with the later of--

(I) the 1st plan year in which the individual first became a qualified participant, or

(II) the 1st plan year beginning after December 31, 1986.

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For purposes of the preceding sentence, an employer may elect to treat an individual first becoming a qualified participant in the 1st plan year beginning in 1987 as having become a participant in the 1st plan year beginning in 1988.

(v) Exception.--This subparagraph shall not apply to an applicable defined contribution plan (as defined in paragraph (35)(E)).

(C) Use of independent appraiser.--A plan meets the requirements of this subparagraph if all valuations of employer securities which are not readily tradable on an established securities market with respect to activities carried on by the plan are by an independent appraiser. For purposes of the preceding sentence, the term "independent appraiser" means any appraiser meeting requirements similar to the requirements of the regulations prescribed under section 170(a)(1).

(29) Benefit limitations.--In the case of a defined benefit plan (other than a multiemployer plan or a CSEC plan) to which the requirements of section 412 apply, the trust of which the plan is a part shall not constitute a qualified trust under this subsection unless the plan meets the requirements of section 436.

(30) Limitations on elective deferrals.--In the case of a trust which is part of a plan under which elective deferrals (within the meaning of section 402(g)(3)) may be made with respect to any individual during a calendar year, such trust shall not constitute a qualified trust under this subsection unless the plan provides that the amount of such deferrals under such plan and all other plans, contracts, or arrangements of an employer maintaining such plan may not exceed the amount of the limitation in effect under section 402(g)(1)(A) for taxable years beginning in such calendar year.

(31) Direct transfer of eligible rollover distributions.--

(A) In general.--A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that if the distributee of any eligible rollover distribution--

(i) elects to have such distribution paid directly to an eligible retirement plan, and

(ii) specifies the eligible retirement plan to which such distribution is to be paid (in such form and at such time as the plan administrator may prescribe),

such distribution shall be made in the form of a direct trustee-to-trustee transfer to the eligible retirement plan so specified.

(B) Certain mandatory distributions.--

(i) In general.--In case of a trust which is part of an eligible plan, such trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that if--

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(I) a distribution described in clause (ii) in excess of $ 1,000 is made, and

(II) the distributee does not make an election under subparagraph (A) and does not elect to receive the distribution directly,

the plan administrator shall make such transfer to an individual retirement plan of a designated trustee or issuer and shall notify the distributee in writing (either separately or as part of the notice under section 402(f)) that the distribution may be transferred to another individual retirement plan.

(ii) Eligible plan.--For purposes of clause (i), the term "eligible plan" means a plan which provides that any nonforfeitable accrued benefit for which the present value (as determined under section 411(a)(11)) does not exceed $5,000 shall be immediately distributed to the participant.

(C) Limitation.--Subparagraphs (A) and (B) shall apply only to the extent that the eligible rollover distribution would be includible in gross income if not transferred as provided in subparagraph (A) (determined without regard to sections 402(c), 403(a)(4), 403(b)(8), and 457(e)(16)). The preceding sentence shall not apply to such distribution if the plan to which such distribution is transferred--

(i) is a qualified trust which is part of a plan which is a defined contribution plan and agrees to separately account for amounts so transferred, including separately accounting for the portion of such distribution which is includible in gross income and the portion of such distribution which is not so includible, or

(ii) is an eligible retirement plan described in clause (i) or (ii) of section 402(c)(8)(B).

(D) Eligible rollover distribution.--For purposes of this paragraph, the term "eligible rollover distribution" has the meaning given such term by section 402(f)(2)(A).

(E) Eligible retirement plan.--For purposes of this paragraph, the term "eligible retirement plan" has the meaning given such term by section 402(c)(8)(B), except that a qualified trust shall be considered an eligible retirement plan only if it is a defined contribution plan, the terms of which permit the acceptance of rollover distributions.

(32) Treatment of failure to make certain payments if plan has liquidity shortfall.--

(A) In general.--A trust forming part of a pension plan to which section [3] 430(j)(4) or 433(f)(5) applies shall not be treated as failing to constitute a qualified trust under this section merely because such plan ceases to make any payment described in subparagraph (B) during any period that such plan has a liquidity shortfall (as defined in section [3] 430(j)(4) or 433(f)(5)).

(B) Payments described.--A payment is described in this subparagraph if such payment is--

(i) any payment, in excess of the monthly amount paid under a single life annuity (plus any social security supplements described in the last sentence of section 411(a)(9)), to a participant or beneficiary whose annuity starting date (as defined in section 417(f)(2)) occurs during the period referred to in subparagraph (A),

(ii) any payment for the purchase of an irrevocable commitment from an insurer to pay benefits, and

(iii) any other payment specified by the Secretary by regulations.

(C) Period of shortfall.--For purposes of this paragraph, a plan has a liquidity shortfall during the period that there is an underpayment of an installment under section 430(j)(3) or 433(f) by reason of section 430(j)(4)(A) or 433(f)(5), respectively.

(33) Prohibition on benefit increases while sponsor is in bankruptcy.--

(A) In general.--A trust which is part of a plan to which this paragraph applies shall not constitute a qualified trust under this section if an amendment to such plan is adopted while the employer is a debtor in a case under Title 11, United States Code, or similar Federal or State law, if such amendment increases liabilities of the plan by reason of--

(i) any increase in benefits,

(ii) any change in the accrual of benefits, or

(iii) any change in the rate at which benefits become nonforfeitable under the plan,

with respect to employees of the debtor, and such amendment is effective prior to the effective date of such employer's plan of reorganization.

(B) Exceptions.--This paragraph shall not apply to any plan amendment if--

(i) the plan, were such amendment to take effect, would have a funding target attainment percentage (as defined in section 430(d)(2)) of 100 percent or more,

(ii) the Secretary determines that such amendment is reasonable and provides for only de minimis increases in the liabilities of the plan with respect to employees of the debtor,

(iii) such amendment only repeals an amendment described in section 412(d)(2), or

(iv) such amendment is required as a condition of qualification under this part.

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(C) Plans to which this paragraph applies.--This paragraph shall apply only to plans (other than multiemployer plans or CSEC plans) covered under section 4021 of the Employee Retirement Income Security Act of 1974.

(D) Employer.--For purposes of this paragraph, the term "employer" means the employer referred to in section 412(b)(1), without regard to section 412(b)(2).

(34) Benefits of missing participants on plan termination.--In the case of a plan covered by title IV of the Employee Retirement Income Security Act of 1974, a trust forming part of such plan shall not be treated as failing to constitute a qualified trust under this section merely because the pension plan of which such trust is a part, upon its termination, transfers benefits of missing participants to the Pension Benefit Guaranty Corporation in accordance with section 4050 of such Act.

(35) Diversification requirements for certain defined contribution plans.--

(A) In general.--A trust which is part of an applicable defined contribution plan shall not be treated as a qualified trust unless the plan meets the diversification requirements of subparagraphs (B), (C), and (D).

(B) Employee contributions and elective deferrals invested in employer securities.--In the case of the portion of an applicable individual's account attributable to employee contributions and elective deferrals which is invested in employer securities, a plan meets the requirements of this subparagraph if the applicable individual may elect to direct the plan to divest any such securities and to reinvest an equivalent amount in other investment options meeting the requirements of subparagraph (D).

(C) Employer contributions invested in employer securities.--In the case of the portion of the account attributable to employer contributions other than elective deferrals which is invested in employer securities, a plan meets the requirements of this subparagraph if each applicable individual who--

(i) is a participant who has completed at least 3 years of service, or

(ii) is a beneficiary of a participant described in clause (i) or of a deceased participant,

may elect to direct the plan to divest any such securities and to reinvest an equivalent amount in other investment options meeting the requirements of subparagraph (D).

(D) Investment options.--

(i) In general.--The requirements of this subparagraph are met if the plan offers not less than 3 investment options, other than employer securities, to which an applicable individual may direct the proceeds from the divestment of employer securities pursuant to this paragraph, each of which is diversified and has materially different risk and return characteristics.

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(ii) Treatment of certain restrictions and conditions.--

(I) Time for making investment choices.--A plan shall not be treated as failing to meet the requirements of this subparagraph merely because the plan limits the time for divestment and reinvestment to periodic, reasonable opportunities occurring no less frequently than quarterly.

(II) Certain restrictions and conditions not allowed.--Except as provided in regulations, a plan shall not meet the requirements of this subparagraph if the plan imposes restrictions or conditions with respect to the investment of employer securities which are not imposed on the investment of other assets of the plan. This subclause shall not apply to any restrictions or conditions imposed by reason of the application of securities laws.

(E) Applicable defined contribution plan.--For purposes of this paragraph--

(i) In general.--The term "applicable defined contribution plan" means any defined contribution plan which holds any publicly traded employer securities.

(ii) Exception for certain ESOPs.--Such term does not include an employee stock ownership plan if--

(I) there are no contributions to such plan (or earnings thereunder) which are held within such plan and are subject to subsection (k) or (m), and

(II) such plan is a separate plan for purposes of section 414(l) with respect to any other defined benefit plan or defined contribution plan maintained by the same employer or employers.

(iii) Exception for one participant plans.--Such term does not include a one-participant retirement plan.

(iv) One-participant retirement plan.--For purposes of clause (iii), the term "one-participant retirement plan" means a retirement plan that on the first day of the plan year--

(I) covered only one individual (or the individual and the individual's spouse) and the individual (or the individual and the individual's spouse) owned 100 percent of the plan sponsor (whether or not incorporated), or

(II) covered only one or more partners (or partners and their spouses) in the plan sponsor.

(F) Certain plans treated as holding publicly traded employer securities.--

(i) In general.--Except as provided in regulations or in clause (ii), a plan holding employer securities which are not publicly traded employer securities shall be treated as holding publicly traded employer securities if any employer

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corporation, or any member of a controlled group of corporations which includes such employer corporation, has issued a class of stock which is a publicly traded employer security.

(ii) Exception for certain controlled groups with publicly traded securities.--Clause (i) shall not apply to a plan if--

(I) no employer corporation, or parent corporation of an employer corporation, has issued any publicly traded employer security, and

(II) no employer corporation, or parent corporation of an employer corporation, has issued any special class of stock which grants particular rights to, or bears particular risks for, the holder or issuer with respect to any corporation described in clause (i) which has issued any publicly traded employer security.

(iii) Definitions.--For purposes of this subparagraph, the term--

(I) "controlled group of corporations" has the meaning given such term by section 1563(a), except that "50 percent" shall be substituted for "80 percent" each place it appears,

(II) "employer corporation" means a corporation which is an employer maintaining the plan, and

(III) "parent corporation" has the meaning given such term by section 424(e).

(G) Other definitions.--For purposes of this paragraph--

(i) Applicable individual.--The term "applicable individual" means--

(I) any participant in the plan, and

(II) any beneficiary who has an account under the plan with respect to which the beneficiary is entitled to exercise the rights of a participant.

(ii) Elective deferral.--The term "elective deferral" means an employer contribution described in section 402(g)(3)(A).

(iii) Employer security.--The term "employer security" has the meaning given such term by section 407(d)(1) of the Employee Retirement Income Security Act of 1974.

(iv) Employee stock ownership plan.--The term "employee stock ownership plan" has the meaning given such term by section 4975(e)(7).

(v) Publicly traded employer securities.--The term "publicly traded employer securities" means employer securities which are readily tradable on an established securities market.

(vi) Year of service.--The term "year of service" has the meaning given such term by section 411(a)(5).

(H) Transition rule for securities attributable to employer contributions.--

(i) Rules phased in over 3 years.--

(I) In general.--In the case of the portion of an account to which subparagraph (C) applies and which consists of employer securities acquired in a plan year beginning before January 1, 2007, subparagraph (C) shall only apply to the applicable percentage of such securities. This subparagraph shall be applied separately with respect to each class of securities.

(II) Exception for certain participants aged 55 or over.--Subclause (I) shall not apply to an applicable individual who is a participant who has attained age 55 and completed at least 3 years of service before the first plan year beginning after December 31, 2005.

(ii) Applicable percentage.--For purposes of clause (i), the applicable percentage shall be determined as follows:

Plan year to which subparagraph (C) applies:	The applicable percentage is:
1st	33
2d	66
3d and following	100.

(36) Distributions during working retirement.--A trust forming part of a pension plan shall not be treated as failing to constitute a qualified trust under this section solely because the plan provides that a distribution may be made from such trust to an employee who has attained age 62 and who is not separated from employment at the time of such distribution.

(37) Death benefits under USERRA-qualified active military service.--A trust shall not constitute a qualified trust unless the plan provides that, in the case of a participant who dies while performing qualified military service (as defined in section 414(u)), the survivors of the participant are entitled to any additional benefits (other than benefit accruals relating to the period of qualified military service) provided under the plan had the participant resumed and then terminated employment on account of death.

Paragraphs (11), (12), (13), (14), (15), (19), and (20) shall apply only in the case of a plan to which section 411 (relating to minimum vesting standards) applies without regard to subsection (e)(2) of such section.

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(b) Certain retroactive changes in plan.--A stock bonus, pension, profit-sharing, or annuity plan shall be considered as satisfying the requirements of subsection (a) for the period beginning with the date on which it was put into effect, or for the period beginning with the earlier of the date on which there was adopted or put into effect any amendment which caused the plan to fail to satisfy such requirements, and ending with the time prescribed by law for filing the return of the employer for his taxable year in which such plan or amendment was adopted (including extensions thereof) or such later time as the Secretary may designate, if all provisions of the plan which are necessary to satisfy such requirements are in effect by the end of such period and have been made effective for all purposes for the whole of such period.

(c) Definitions and rules relating to self-employed individuals and owner-employees.--For purposes of this section--

(1) Self-employed individual treated as employee.--

(A) In general.--The term "employee" includes, for any taxable year, an individual who is a self-employed individual for such taxable year.

(B) Self-employed individual.--The term "self-employed individual" means, with respect to any taxable year, an individual who has earned income (as defined in paragraph (2)) for such taxable year. To the extent provided in regulations prescribed by the Secretary, such term also includes, for any taxable year--

(i) an individual who would be a self-employed individual within the meaning of the preceding sentence but for the fact that the trade or business carried on by such individual did not have net profits for the taxable year, and

(ii) an individual who has been a self-employed individual within the meaning of the preceding sentence for any prior taxable year.

(2) Earned income.--

(A) In general.--The term "earned income" means the net earnings from self-employment (as defined in section 1402(a)), but such net earnings shall be determined--

(i) only with respect to a trade or business in which personal services of the taxpayer are a material income-producing factor,

(ii) without regard to paragraphs (4) and (5) of section 1402(c),

(iii) in the case of any individual who is treated as an employee under sections [4] 3121(d)(3)(A), (C), or (D), without regard to paragraph (2) of section 1402(c),

(iv) without regard to items which are not included in gross income for purposes of this chapter, and the deductions properly allocable to or chargeable against such items,

(v) with regard to the deductions allowed by section 404 to the taxpayer, and

(vi) with regard to the deduction allowed to the taxpayer by section 164(f).

For purposes of this subparagraph, section 1402, as in effect for a taxable year ending on December 31, 1962, shall be treated as having been in effect for all taxable years ending before such date. For purposes of this part only (other than sections 419 and 419A), this subparagraph shall be applied as if the term "trade or business" for purposes of section 1402 included service described in section 1402(c)(6).

[**(B) Repealed.** Pub.L. 89-809, Title II, § 204(c), Nov. 13 1966, 80 Stat. 1577]

(C) Income from disposition of certain property.--For purposes of this section, the term "earned income" includes gains (other than any gain which is treated under any provision of this chapter as gain from the sale or exchange of a capital asset) and net earnings derived from the sale or other disposition of, the transfer of any interest in, or the licensing of the use of property (other than good will) by an individual whose personal efforts created such property.

(3) Owner-employee.--The term "owner-employee" means an employee who--

(A) owns the entire interest in an unincorporated trade or business, or

(B) in the case of a partnership, is a partner who owns more than 10 percent of either the capital interest or the profits interest in such partnership.

To the extent provided in regulations prescribed by the Secretary, such term also means an individual who has been an owner-employee within the meaning of the preceding sentence.

(4) Employer.--An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer of each partner who is an employee within the meaning of paragraph (1).

(5) Contributions on behalf of owner-employees.--The term "contribution on behalf of an owner-employee" includes, except as the context otherwise requires, a contribution under a plan--

(A) by the employer for an owner-employee, and

(B) by an owner-employee as an employee.

(6) Special rule for certain fishermen.--For purposes of this subsection, the term "self-employed individual" includes an individual described in section 3121(b)(20) (relating to certain fishermen).

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(d) Contribution limit on owner-employees.--A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the plan provides that contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established.

[**(e) Repealed.** Pub.L. 98-369, div. A, Title VII, § 713(d)(3), July 18, 1984, 98 Stat. 958]

(f) Certain custodial accounts and contracts.--For purposes of this title, a custodial account, an annuity contract, or a contract (other than a life, health or accident, property, casualty, or liability insurance contract) issued by an insurance company qualified to do business in a State shall be treated as a qualified trust under this section if--

(1) the custodial account or contract would, except for the fact that it is not a trust, constitute a qualified trust under this section, and

(2) in the case of a custodial account the assets thereof are held by a bank (as defined in section 408(n)) or another person who demonstrates, to the satisfaction of the Secretary, that the manner in which he will hold the assets will be consistent with the requirements of this section.

For purposes of this title, in the case of a custodial account or contract treated as a qualified trust under this section by reason of this subsection, the person holding the assets of such account or holding such contract shall be treated as the trustee thereof.

(g) Annuity defined.--For purposes of this section and sections 402, 403, and 404, the term "annuity" includes a face-amount certificate, as defined in section 2(a)(15) of the Investment Company Act of 1940 (15 U.S.C., sec. 80a-2); but does not include any contract or certificate issued after December 31, 1962, which is transferable, if any person other than the trustee of a trust described in section 401(a) which is exempt from tax under section 501(a) is the owner of such contract or certificate.

(h) Medical, etc., benefits for retired employees and their spouses and dependents.--Under regulations prescribed by the Secretary, and subject to the provisions of section 420, a pension or annuity plan may provide for the payment of benefits for sickness, accident, hospitalization, and medical expenses of retired employees, their spouses and their dependents, but only if--

(1) such benefits are subordinate to the retirement benefits provided by the plan,

(2) a separate account is established and maintained for such benefits,

(3) the employer's contributions to such separate account are reasonable and ascertainable,

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(4) it is impossible, at any time prior to the satisfaction of all liabilities under the plan to provide such benefits, for any part of the corpus or income of such separate account to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of such benefits,

(5) notwithstanding the provisions of subsection (a)(2), upon the satisfaction of all liabilities under the plan to provide such benefits, any amount remaining in such separate account must, under the terms of the plan, be returned to the employer, and

(6) in the case of an employee who is a key employee, a separate account is established and maintained for such benefits payable to such employee (and his spouse and dependents) and such benefits (to the extent attributable to plan years beginning after March 31, 1984, for which the employee is a key employee) are only payable to such employee (and his spouse and dependents) from such separate account.

For purposes of paragraph (6), the term "key employee" means any employee, who at any time during the plan year or any preceding plan year during which contributions were made on behalf of such employee, is or was a key employee as defined in section 416(i). In no event shall the requirements of paragraph (1) be treated as met if the aggregate actual contributions for medical benefits, when added to actual contributions for life insurance protection under the plan, exceed 25 percent of the total actual contributions to the plan (other than contributions to fund past service credits) after the date on which the account is established. For purposes of this subsection, the term "dependent" shall include any individual who is a child (as defined in section 152(f)(1)) of a retired employee who as of the end of the calendar year has not attained age 27.

(i) Certain union-negotiated pension plans.--In the case of a trust forming part of a pension plan which has been determined by the Secretary to constitute a qualified trust under subsection (a) and to be exempt from taxation under section 501(a) for a period beginning after contributions were first made to or for such trust, if it is shown to the satisfaction of the Secretary that--

(1) such trust was created pursuant to a collective bargaining agreement between employee representatives and one or more employers,

(2) any disbursements of contributions, made to or for such trust before the time as of which the Secretary determined that the trust constituted a qualified trust, substantially complied with the terms of the trust, and the plan of which the trust is a part, as subsequently qualified, and

(3) before the time as of which the Secretary determined that the trust constitutes a qualified trust, the contributions to or for such trust were not used in a manner which would jeopardize the interests of its beneficiaries,

then such trust shall be considered as having constituted a qualified trust under subsection (a) and as having been exempt from taxation under section 501(a) for the period beginning on the date on which contributions were first made to or for such trust and ending on the date such trust first constituted (without regard to this subsection) a qualified trust under subsection (a).

[(j) **Repealed.** Pub.L. 97-248, Title II, § 238(b), Sept. 3, 1982, 96 Stat. 512]

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(k) Cash or deferred arrangements.--

(1) General rule.--A profit-sharing or stock bonus plan, a pre-ERISA money purchase plan, or a rural cooperative plan shall not be considered as not satisfying the requirements of subsection (a) merely because the plan includes a qualified cash or deferred arrangement.

(2) Qualified cash or deferred arrangement.--A qualified cash or deferred arrangement is any arrangement which is part of a profit-sharing or stock bonus plan, a pre-ERISA money purchase plan, or a rural cooperative plan which meets the requirements of subsection (a)--

(A) under which a covered employee may elect to have the employer make payments as contributions to a trust under the plan on behalf of the employee, or to the employee directly in cash;

(B) under which amounts held by the trust which are attributable to employer contributions made pursuant to the employee's election--

(i) may not be distributable to participants or other beneficiaries earlier than--

(I) severance from employment, death, or disability,

(II) an event described in paragraph (10),

(III) in the case of a profit-sharing or stock bonus plan, the attainment of age 59 ½,

(IV) in the case of contributions to a profit-sharing or stock bonus plan to which section 402(e)(3) applies, upon hardship of the employee, or

(V) in the case of a qualified reservist distribution (as defined in section 72(t)(2)(G)(iii)), the date on which a period referred to in subclause (III) of such section begins, and

(ii) will not be distributable merely by reason of the completion of a stated period of participation or the lapse of a fixed number of years;

(C) which provides that an employee's right to his accrued benefit derived from employer contributions made to the trust pursuant to his election is nonforfeitable, and

(D) which does not require, as a condition of participation in the arrangement, that an employee complete a period of service with the employer (or employers) maintaining the plan extending beyond the period permitted under section 410(a)(1) (determined without regard to subparagraph (B)(i) thereof).

(3) Application of participation and discrimination standards.--

(A) A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement unless--

(i) those employees eligible to benefit under the arrangement satisfy the provisions of section 410(b)(1), and

(ii) the actual deferral percentage for eligible highly compensated employees (as defined in paragraph (5)) for the plan year bears a relationship to the actual deferral percentage for all other eligible employees for the preceding plan year which meets either of the following tests:

(I) The actual deferral percentage for the group of eligible highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 1.25.

(II) The excess of the actual deferral percentage for the group of eligible highly compensated employees over that of all other eligible employees is not more than 2 percentage points, and the actual deferral percentage for the group of eligible highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 2.

If 2 or more plans which include cash or deferred arrangements are considered as 1 plan for purposes of section 401(a)(4) or 410(b), the cash or deferred arrangements included in such plans shall be treated as 1 arrangement for purposes of this subparagraph.

If any highly compensated employee is a participant under 2 or more cash or deferred arrangements of the employer, for purposes of determining the deferral percentage with respect to such employee, all such cash or deferred arrangements shall be treated as 1 cash or deferred arrangement. An arrangement may apply clause (ii) by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary.

(B) For purposes of subparagraph (A), the actual deferral percentage for a specified group of employees for a plan year shall be the average of the ratios (calculated separately for each employee in such group) of--

(i) the amount of employer contributions actually paid over to the trust on behalf of each such employee for such plan year, to

(ii) the employee's compensation for such plan year.

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(C) A cash or deferred arrangement shall be treated as meeting the requirements of subsection (a)(4) with respect to contributions if the requirements of subparagraph (A)(ii) are met.

(D) For purposes of subparagraph (B), the employer contributions on behalf of any employee--

(i) shall include any employer contributions made pursuant to the employee's election under paragraph (2), and

(ii) under such rules as the Secretary may prescribe, may, at the election of the employer, include--

(I) matching contributions (as defined in 401(m)(4)(A)) which meet the requirements of paragraph (2)(B) and (C), and

(II) qualified nonelective contributions (within the meaning of section 401(m)(4)(C)).

(E) For purposes of this paragraph, in the case of the first plan year of any plan (other than a successor plan), the amount taken into account as the actual deferral percentage of nonhighly compensated employees for the preceding plan year shall be--

(i) 3 percent, or

(ii) if the employer makes an election under this subclause, the actual deferral percentage of nonhighly compensated employees determined for such first plan year.

(F) Special rule for early participation.--If an employer elects to apply section 410(b)(4)(B) in determining whether a cash or deferred arrangement meets the requirements of subparagraph (A)(i), the employer may, in determining whether the arrangement meets the requirements of subparagraph (A)(ii), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).

(G) Governmental plan.--A governmental plan (within the meaning of section 414(d)) shall be treated as meeting the requirements of this paragraph.

(4) Other requirements.--

(A) Benefits (other than matching contributions) must not be contingent on election to defer.--A cash or deferred arrangement of any employer shall not be treated as a qualified cash or deferred arrangement if any other benefit is conditioned (directly or indirectly) on the employee electing to have the employer make or not make contributions under the arrangement in lieu of receiving cash. The preceding sentence shall not apply to any matching contribution (as defined in section 401(m)) made by reason of such an election.

(B) Eligibility of State and local governments and tax-exempt organizations.--

(i) Tax-exempts eligible.--Except as provided in clause (ii), any organization exempt from tax under this subtitle may include a qualified cash or deferred arrangement as part of a plan maintained by it.

(ii) Governments ineligible.--A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by a State or local government or political subdivision thereof, or any agency or instrumentality thereof. This clause shall not apply to a rural cooperative plan or to a plan of an employer described in clause (iii).

(iii) Treatment of Indian tribal governments.--An employer which is an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing may include a qualified cash or deferred arrangement as part of a plan maintained by the employer.

(C) Coordination with other plans.--Except as provided in section 401(m), any employer contribution made pursuant to an employee's election under a qualified cash or deferred arrangement shall not be taken into account for purposes of determining whether any other plan meets the requirements of section 401(a) or 410(b). This subparagraph shall not apply for purposes of determining whether a plan meets the average benefit requirement of section 410(b)(2)(A)(ii).

(5) Highly compensated employee.--For purposes of this subsection, the term "highly compensated employee" has the meaning given such term by section 414(q).

(6) Pre-ERISA money purchase plan.--For purposes of this subsection, the term "pre-ERISA money purchase plan" means a pension plan--

(A) which is a defined contribution plan (as defined in section 414(i)),

(B) which was in existence on June 27, 1974, and which, on such date, included a salary reduction arrangement, and

(C) under which neither the employee contributions nor the employer contributions may exceed the levels provided for by the contribution formula in effect under the plan on such date.

(7) Rural cooperative plan.--For purposes of this subsection--

(A) In general.--The term "rural cooperative plan" means any pension plan--

(i) which is a defined contribution plan (as defined in section 414(i)), and

(ii) which is established and maintained by a rural cooperative.

(B) Rural cooperative defined.--For purposes of subparagraph (A), the term "rural cooperative" means--

(i) any organization which--

(I) is engaged primarily in providing electric service on a mutual or cooperative basis, or

(II) is engaged primarily in providing electric service to the public in its area of service and which is exempt from tax under this subtitle or which is a State or local government (or an agency or instrumentality thereof), other than a municipality (or an agency or instrumentality thereof),

(ii) any organization described in paragraph (4) or (6) of section 501(c) and at least 80 percent of the members of which are organizations described in clause (i),

(iii) a cooperative telephone company described in section 501(c)(12),

(iv) any organization which--

(I) is a mutual irrigation or ditch company described in section 501(c)(12) (without regard to the 85 percent requirement thereof), or

(II) is a district organized under the laws of a State as a municipal corporation for the purpose of irrigation, water conservation, or drainage, and

(v) an organization which is a national association of organizations described in clause (i), (ii),, [5] (iii), or (iv).

(C) Special rule for certain distributions.--A rural cooperative plan which includes a qualified cash or deferred arrangement shall not be treated as violating the requirements of section 401(a) or of paragraph (2) merely by reason of a hardship distribution or a distribution to a participant after attainment of age 59 ½. For purposes of this section, the term "hardship distribution" means a distribution described in paragraph (2)(B)(i)(IV) (without regard to the limitation of its application to profit-sharing or stock bonus plans).

(8) Arrangement not disqualified if excess contributions distributed.--

(A) In general.--A cash or deferred arrangement shall not be treated as failing to meet the requirements of clause (ii) of paragraph (3)(A) for any plan year if, before the close of the following plan year--

(i) the amount of the excess contributions for such plan year (and any income allocable to such contributions through the end of such year) is distributed, or

(ii) to the extent provided in regulations, the employee elects to treat the amount of the excess contributions as an amount distributed to the employee and then contributed by the employee to the plan.

Any distribution of excess contributions (and income) may be made without regard to any other provision of law.

(B) Excess contributions.--For purposes of subparagraph (A), the term "excess contributions" means, with respect to any plan year, the excess of--

(i) the aggregate amount of employer contributions actually paid over to the trust on behalf of highly compensated employees for such plan year, over

(ii) the maximum amount of such contributions permitted under the limitations of clause (ii) of paragraph (3)(A) (determined by reducing contributions made on behalf of highly compensated employees in order of the actual deferral percentages beginning with the highest of such percentages).

(C) Method of distributing excess contributions.--Any distribution of the excess contributions for any plan year shall be made to highly compensated employees on the basis of the amount of contributions by, or on behalf of, each of such employees.

(D) Additional tax under section 72(t) not to apply.--No tax shall be imposed under section 72(t) on any amount required to be distributed under this paragraph.

(E) Treatment of matching contributions forfeited by reason of excess deferral or contribution or permissible withdrawal.--For purposes of paragraph (2)(C), a matching contribution (within the meaning of subsection (m)) shall not be treated as forfeitable merely because such contribution is forfeitable if the contribution to which the matching contribution relates is treated as an excess contribution under subparagraph (B), an excess deferral under section 402(g)(2)(A), a permissible withdrawal under section 414(w), or an excess aggregate contribution under section 401(m)(6)(B).

(F) Cross reference.--

For excise tax on certain excess contributions, see section 4979.

(9) Compensation.--For purposes of this subsection, the term "compensation" has the meaning given such term by section 414(s).

(10) Distributions upon termination of plan--

(A) In general.--An event described in this subparagraph is the termination of the plan without establishment or maintenance of another defined contribution plan (other than an employee stock ownership plan as defined in section 4975(e)(7)).

(B) Distributions must be lump sum distributions.--

(i) In general.--A termination shall not be treated as described in subparagraph (A) with respect to any employee unless the employee receives a lump sum distribution by reason of the termination.

(ii) Lump-sum distribution.--For purposes of this subparagraph, the term "lump-sum distribution" has the meaning given such term by section 402(e)(4)(D) (without regard to subclauses (I), (II), (III), and (IV) of clause (i) thereof). Such term includes a distribution of an annuity contract from--

(I) a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501(a), or

(II) an annuity plan described in section 403(a).

(11) Adoption of simple plan to meet nondiscrimination tests.--

(A) In general.--A cash or deferred arrangement maintained by an eligible employer shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement meets--

(i) the contribution requirements of subparagraph (B),

(ii) the exclusive plan requirements of subparagraph (C), and

(iii) the vesting requirements of section 408(p)(3).

(B) Contribution requirements.--

(i) In general.--The requirements of this subparagraph are met if, under the arrangement--

(I) an employee may elect to have the employer make elective contributions for the year on behalf of the employee to a trust under the plan in an amount which is expressed as a percentage of compensation of the employee but which in no event exceeds the amount in effect under section 408(p)(2)(A)(ii),

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(II) the employer is required to make a matching contribution to the trust for the year in an amount equal to so much of the amount the employee elects under subclause (I) as does not exceed 3 percent of compensation for the year, and

(III) no other contributions may be made other than contributions described in subclause (I) or (II).

(ii) Employer may elect 2-percent nonelective contribution.--An employer shall be treated as meeting the requirements of clause (i)(II) for any year if, in lieu of the contributions described in such clause, the employer elects (pursuant to the terms of the arrangement) to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 60th day before the beginning of such year.

(iii) Administrative requirements.--

(I) In general.--Rules similar to the rules of subparagraphs (B) and (C) of section 408(p)(5) shall apply for purposes of this subparagraph.

(II) Notice of election period.--The requirements of this subparagraph shall not be treated as met with respect to any year unless the employer notifies each employee eligible to participate, within a reasonable period of time before the 60th day before the beginning of such year (and, for the first year the employee is so eligible, the 60th day before the first day such employee is so eligible), of the rules similar to the rules of section 408(p)(5)(C) which apply by reason of subclause (I).

(C) Exclusive plan requirement.--The requirements of this subparagraph are met for any year to which this paragraph applies if no contributions were made, or benefits were accrued, for services during such year under any qualified plan of the employer on behalf of any employee eligible to participate in the cash or deferred arrangement, other than contributions described in subparagraph (B).

(D) Definitions and special rule.--

(i) Definitions.--For purposes of this paragraph, any term used in this paragraph which is also used in section 408(p) shall have the meaning given such term by such section.

(ii) Coordination with top-heavy rules.--A plan meeting the requirements of this paragraph for any year shall not be treated as a top-heavy plan under section 416 for such year if such plan allows only contributions required under this paragraph.

(12) Alternative methods of meeting nondiscrimination requirements.--

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(A) In general.--A cash or deferred arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement--

(i) meets the contribution requirements of subparagraph (B) or (C), and

(ii) meets the notice requirements of subparagraph (D).

(B) Matching contributions.--

(i) In general.--The requirements of this subparagraph are met if, under the arrangement, the employer makes matching contributions on behalf of each employee who is not a highly compensated employee in an amount equal to--

(I) 100 percent of the elective contributions of the employee to the extent such elective contributions do not exceed 3 percent of the employee's compensation, and

(II) 50 percent of the elective contributions of the employee to the extent that such elective contributions exceed 3 percent but do not exceed 5 percent of the employee's compensation.

(ii) Rate for highly compensated employees.--The requirements of this subparagraph are not met if, under the arrangement, the rate of matching contribution with respect to any elective contribution of a highly compensated employee at any rate of elective contribution is greater than that with respect to an employee who is not a highly compensated employee.

(iii) Alternative plan designs.--If the rate of any matching contribution with respect to any rate of elective contribution is not equal to the percentage required under clause (i), an arrangement shall not be treated as failing to meet the requirements of clause (i) if--

(I) the rate of an employer's matching contribution does not increase as an employee's rate of elective contributions increase, and

(II) the aggregate amount of matching contributions at such rate of elective contribution is at least equal to the aggregate amount of matching contributions which would be made if matching contributions were made on the basis of the percentages described in clause (i).

(C) Nonelective contributions.--The requirements of this subparagraph are met if, under the arrangement, the employer is required, without regard to whether the employee makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly compensated employee and who is eligible to participate in the arrangement in an amount equal to at least 3 percent of the employee's compensation.

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(D) Notice requirement.--An arrangement meets the requirements of this paragraph if, under the arrangement, each employee eligible to participate is, within a reasonable period before any year, given written notice of the employee's rights and obligations under the arrangement which--

(i) is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and

(ii) is written in a manner calculated to be understood by the average employee eligible to participate.

(E) Other requirements.--

(i) Withdrawal and vesting restrictions.--An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) of this paragraph unless the requirements of subparagraphs (B) and (C) of paragraph (2) are met with respect to all employer contributions (including matching contributions) taken into account in determining whether the requirements of subparagraphs (B) and (C) of this paragraph are met.

(ii) Social security and similar contributions not taken into account.--An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) unless such requirements are met without regard to subsection (l), and, for purposes of subsection (l), employer contributions under subparagraph (B) or (C) shall not be taken into account.

(F) Other plans.--An arrangement shall be treated as meeting the requirements under subparagraph (A)(i) if any other plan maintained by the employer meets such requirements with respect to employees eligible under the arrangement.

(13) Alternative method for automatic contribution arrangements to meet nondiscrimination requirements.--

(A) In general.--A qualified automatic contribution arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii).

(B) Qualified automatic contribution arrangement.--For purposes of this paragraph, the term "qualified automatic contribution arrangement" means any cash or deferred arrangement which meets the requirements of subparagraphs (C) through (E).

(C) Automatic deferral.--

(i) In general.--The requirements of this subparagraph are met if, under the arrangement, each employee eligible to participate in the arrangement is treated as having elected to have the employer make elective contributions in an amount equal to a qualified percentage of compensation.

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(ii) Election out.--The election treated as having been made under clause (i) shall cease to apply with respect to any employee if such employee makes an affirmative election--

(I) to not have such contributions made, or

(II) to make elective contributions at a level specified in such affirmative election.

(iii) Qualified percentage.--For purposes of this subparagraph, the term "qualified percentage" means, with respect to any employee, any percentage determined under the arrangement if such percentage is applied uniformly, does not exceed 10 percent, and is at least--

(I) 3 percent during the period ending on the last day of the first plan year which begins after the date on which the first elective contribution described in clause (i) is made with respect to such employee,

(II) 4 percent during the first plan year following the plan year described in subclause (I),

(III) 5 percent during the second plan year following the plan year described in subclause (I), and

(IV) 6 percent during any subsequent plan year.

(iv) Automatic deferral for current employees not required.--Clause (i) may be applied without taking into account any employee who--

(I) was eligible to participate in the arrangement (or a predecessor arrangement) immediately before the date on which such arrangement becomes a qualified automatic contribution arrangement (determined after application of this clause), and

(II) had an election in effect on such date either to participate in the arrangement or to not participate in the arrangement.

(D) Matching or nonelective contributions.--

(i) In general.--The requirements of this subparagraph are met if, under the arrangement, the employer--

(I) makes matching contributions on behalf of each employee who is not a highly compensated employee in an amount equal to the sum of 100 percent of the elective contributions of the employee to the extent that such contributions do not exceed 1 percent of compensation plus 50 percent of so much of such contributions as exceed 1 percent but do not exceed 6 percent of compensation, or

(II) is required, without regard to whether the employee makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly compensated employee and who is eligible to participate in the arrangement in an amount equal to at least 3 percent of the employee's compensation.

(ii) Application of rules for matching contributions.--The rules of clauses (ii) and (iii) of paragraph (12)(B) shall apply for purposes of clause (i)(I).

(iii) Withdrawal and vesting restrictions.--An arrangement shall not be treated as meeting the requirements of clause (i) unless, with respect to employer contributions (including matching contributions) taken into account in determining whether the requirements of clause (i) are met--

(I) any employee who has completed at least 2 years of service (within the meaning of section 411(a)) has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from such employer contributions, and

(II) the requirements of subparagraph (B) of paragraph (2) are met with respect to all such employer contributions.

(iv) Application of certain other rules.--The rules of subparagraphs (E) (ii) and (F) of paragraph (12) shall apply for purposes of subclauses (I) and (II) of clause (i).

(E) Notice requirements.--

(i) In general.--The requirements of this subparagraph are met if, within a reasonable period before each plan year, each employee eligible to participate in the arrangement for such year receives written notice of the employee's rights and obligations under the arrangement which--

(I) is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and

(II) is written in a manner calculated to be understood by the average employee to whom the arrangement applies.

(ii) Timing and content requirements.--A notice shall not be treated as meeting the requirements of clause (i) with respect to an employee unless--

(I) the notice explains the employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf (or to elect to have such contributions made at a different percentage),

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(II) in the case of an arrangement under which the employee may elect among 2 or more investment options, the notice explains how contributions made under the arrangement will be invested in the absence of any investment election by the employee, and

(III) the employee has a reasonable period of time after receipt of the notice described in subclauses (I) and (II) and before the first elective contribution is made to make either such election.

(l) Permitted disparity in plan contributions or benefits.--

(1) In general.--The requirements of this subsection are met with respect to a plan if--

(A) in the case of a defined contribution plan, the requirements of paragraph (2) are met, and

(B) in the case of a defined benefit plan, the requirements of paragraph (3) are met.

(2) Defined contribution plan.--

(A) In general.--A defined contribution plan meets the requirements of this paragraph if the excess contribution percentage does not exceed the base contribution percentage by more than the lesser of--

(i) the base contribution percentage, or

(ii) the greater of--

(I) 5.7 percentage points, or

(II) the percentage equal to the portion of the rate of tax under section 3111(a) (in effect as of the beginning of the year) which is attributable to old-age insurance.

(B) Contribution percentages.--For purposes of this paragraph--

(i) Excess contribution percentage.--The term "excess contribution percentage" means the percentage of compensation which is contributed by the employer under the plan with respect to that portion of each participant's compensation in excess of the integration level.

(ii) Base contribution percentage.--The term "base contribution percentage" means the percentage of compensation contributed by the employer under the plan with respect to that portion of each participant's compensation not in excess of the integration level.

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(3) Defined benefit plan.--A defined benefit plan meets the requirements of this paragraph if--

(A) Excess plans.--

(i) In general.--In the case of a plan other than an offset plan--

(I) the excess benefit percentage does not exceed the base benefit percentage by more than the maximum excess allowance,

(II) any optional form of benefit, preretirement benefit, actuarial factor, or other benefit or feature provided with respect to compensation in excess of the integration level is provided with respect to compensation not in excess of such level, and

(III) benefits are based on average annual compensation.

(ii) Benefit percentages.--For purposes of this subparagraph, the excess and base benefit percentages shall be computed in the same manner as the excess and base contribution percentages under paragraph (2)(B), except that such determination shall be made on the basis of benefits attributable to employer contributions rather than contributions.

(B) Offset plans.--In the case of an offset plan, the plan provides that--

(i) a participant's accrued benefit attributable to employer contributions (within the meaning of section 411(c)(1)) may not be reduced (by reason of the offset) by more than the maximum offset allowance, and

(ii) benefits are based on average annual compensation.

(4) Definitions relating to paragraph (3).--For purposes of paragraph (3)--

(A) Maximum excess allowance.--The maximum excess allowance is equal to--

(i) in the case of benefits attributable to any year of service with the employer taken into account under the plan, ¾ of a percentage point, and

(ii) in the case of total benefits, ¾ of a percentage point, multiplied by the participant's years of service (not in excess of 35) with the employer taken into account under the plan.

In no event shall the maximum excess allowance exceed the base benefit percentage.

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(B) Maximum offset allowance.--The maximum offset allowance is equal to--

(i) in the case of benefits attributable to any year of service with the employer taken into account under the plan, ¾ percent of the participant's final average compensation, and

(ii) in the case of total benefits, ¾ percent of the participant's final average compensation, multiplied by the participant's years of service (not in excess of 35) with the employer taken into account under the plan.

In no event shall the maximum offset allowance exceed 50 percent of the benefit which would have accrued without regard to the offset reduction.

(C) Reductions.--

(i) In general.--The Secretary shall prescribe regulations requiring the reduction of the ¾ percentage factor under subparagraph (A) or (B)--

(I) in the case of a plan other than an offset plan which has an integration level in excess of covered compensation, or

(II) with respect to any participant in an offset plan who has final average compensation in excess of covered compensation.

(ii) Basis of reductions.--Any reductions under clause (i) shall be based on the percentages of compensation replaced by the employer-derived portions of primary insurance amounts under the Social Security Act for participants with compensation in excess of covered compensation.

(D) Offset plan.--The term "offset plan" means any plan with respect to which the benefit attributable to employer contributions for each participant is reduced by an amount specified in the plan.

(5) Other definitions and special rules.--For purposes of this subsection--

(A) Integration level.--

(i) In general.--The term "integration level" means the amount of compensation specified under the plan (by dollar amount or formula) at or below which the rate at which contributions or benefits are provided (expressed as a percentage) is less than such rate above such amount.

(ii) Limitation.--The integration level for any year may not exceed the contribution and benefit base in effect under section 230 of the Social Security Act for such year.

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(iii) Level to apply to all participants.--A plan's integration level shall apply with respect to all participants in the plan.

(iv) Multiple integration levels.--Under rules prescribed by the Secretary, a defined benefit plan may specify multiple integration levels.

(B) Compensation.--The term "compensation" has the meaning given such term by section 414(s).

(C) Average annual compensation.--The term "average annual compensation" means the participant's highest average annual compensation for--

(i) any period of at least 3 consecutive years, or

(ii) if shorter, the participant's full period of service.

(D) Final average compensation.--

(i) In general.--The term "final average compensation" means the participant's average annual compensation for--

(I) the 3-consecutive year period ending with the current year, or

(II) if shorter, the participant's full period of service.

(ii) Limitation.--A participant's final average compensation shall be determined by not taking into account in any year compensation in excess of the contribution and benefit base in effect under section 230 of the Social Security Act for such year.

(E) Covered compensation.--

(i) In general.--The term "covered compensation" means, with respect to an employee, the average of the contribution and benefit bases in effect under section 230 of the Social Security Act for each year in the 35-year period ending with the year in which the employee attains the social security retirement age.

(ii) Computation for any year.--For purposes of clause (i), the determination for any year preceding the year in which the employee attains the social security retirement age shall be made by assuming that there is no increase in the bases described in clause (i) after the determination year and before the employee attains the social security retirement age.

(iii) Social security retirement age.--For purposes of this subparagraph, the term "social security retirement age" has the meaning given such term by section 415(b)(8).

(F) Regulations.--The Secretary shall prescribe such regulations as are necessary or appropriate to carry out the purposes of this subsection, including--

(i) in the case of a defined benefit plan which provides for unreduced benefits commencing before the social security retirement age (as defined in section 415(b)(8)), rules providing for the reduction of the maximum excess allowance and the maximum offset allowance, and

(ii) in the case of an employee covered by 2 or more plans of the employer which fail to meet the requirements of subsection (a)(4) (without regard to this subsection), rules preventing the multiple use of the disparity permitted under this subsection with respect to any employee.

For purposes of clause (i), unreduced benefits shall not include benefits for disability (within the meaning of section 223(d) of the Social Security Act).

(6) Special rule for plan maintained by railroads.--In determining whether a plan which includes employees of a railroad employer who are entitled to benefits under the Railroad Retirement Act of 1974 meets the requirements of this subsection, rules similar to the rules set forth in this subsection shall apply. Such rules shall take into account the employer-derived portion of the employees' tier 2 railroad retirement benefits and any supplemental annuity under the Railroad Retirement Act of 1974.

(m) Nondiscrimination test for matching contributions and employee contributions.--

(1) In general.--A defined contribution plan shall be treated as meeting the requirements of subsection (a)(4) with respect to the amount of any matching contribution or employee contribution for any plan year only if the contribution percentage requirement of paragraph (2) of this subsection is met for such plan year.

(2) Requirements.--

(A) Contribution percentage requirement.--A plan meets the contribution percentage requirement of this paragraph for any plan year only if the contribution percentage for eligible highly compensated employees for such plan year does not exceed the greater of--

(i) 125 percent of such percentage for all other eligible employees for the preceding plan year, or

(ii) the lesser of 200 percent of such percentage for all other eligible employees for the preceding plan year, or such percentage for all other eligible employees for the preceding plan year plus 2 percentage points.

This subparagraph may be applied by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary.

(B) Multiple plans treated as a single plan.--If two or more plans of an employer to which matching contributions, employee contributions, or elective deferrals are made are treated as one plan for purposes of section 410(b), such plans shall be treated as one plan for purposes of this subsection. If a highly compensated employee participates in two or more plans of an employer to which contributions to which this subsection applies are made, all such contributions shall be aggregated for purposes of this subsection.

(3) Contribution percentage.--For purposes of paragraph (2), the contribution percentage for a specified group of employees for a plan year shall be the average of the ratios (calculated separately for each employee in such group) of--

(A) the sum of the matching contributions and employee contributions paid under the plan on behalf of each such employee for such plan year, to

(B) the employee's compensation (within the meaning of section 414(s)) for such plan year.

Under regulations, an employer may elect to take into account (in computing the contribution percentage) elective deferrals and qualified nonelective contributions under the plan or any other plan of the employer. If matching contributions are taken into account for purposes of subsection (k)(3)(A)(ii) for any plan year, such contributions shall not be taken into account under subparagraph (A) for such year. Rules similar to the rules of subsection (k)(3)(E) shall apply for purposes of this subsection.

(4) Definitions.--For purposes of this subsection--

(A) Matching contribution.--The term "matching contribution" means--

(i) any employer contribution made to a defined contribution plan on behalf of an employee on account of an employee contribution made by such employee, and

(ii) any employer contribution made to a defined contribution plan on behalf of an employee on account of an employee's elective deferral.

(B) Elective deferral.--The term "elective deferral" means any employer contribution described in section 402(g)(3).

(C) Qualified nonelective contributions.--The term "qualified nonelective contribution" means any employer contribution (other than a matching contribution) with respect to which--

(i) the employee may not elect to have the contribution paid to the employee in cash instead of being contributed to the plan, and

(ii) the requirements of subparagraphs (B) and (C) of subsection (k)(2) are met.

(5) Employees taken into consideration.--

(A) In general.--Any employee who is eligible to make an employee contribution (or, if the employer takes elective contributions into account, elective contributions) or to receive a matching contribution under the plan being tested under paragraph (1) shall be considered an eligible employee for purposes of this subsection.

(B) Certain nonparticipants.--If an employee contribution is required as a condition of participation in the plan, any employee who would be a participant in the plan if such employee made such a contribution shall be treated as an eligible employee on behalf of whom no employer contributions are made.

(C) Special rule for early participation.--If an employer elects to apply section 410(b)(4)(B) in determining whether a plan meets the requirements of section 410(b), the employer may, in determining whether the plan meets the requirements of paragraph (2), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).

(6) Plan not disqualified if excess aggregate contributions distributed before end of following plan year.--

(A) In general.--A plan shall not be treated as failing to meet the requirements of paragraph (1) for any plan year if, before the close of the following plan year, the amount of the excess aggregate contributions for such plan year (and any income allocable to such contributions through the end of such year) is distributed (or, if forfeitable, is forfeited). Such contributions (and such income) may be distributed without regard to any other provision of law.

(B) Excess aggregate contributions.--For purposes of subparagraph (A), the term "excess aggregate contributions" means, with respect to any plan year, the excess of--

(i) the aggregate amount of the matching contributions and employee contributions (and any qualified nonelective contribution or elective contribution taken into account in computing the contribution percentage) actually made on behalf of highly compensated employees for such plan year, over

(ii) the maximum amount of such contributions permitted under the limitations of paragraph (2)(A) (determined by reducing contributions made on behalf of highly compensated employees in order of their contribution percentages beginning with the highest of such percentages).

(C) Method of distributing excess aggregate contributions.--Any distribution of the excess aggregate contributions for any plan year shall be made to highly compensated employees on the basis of the amount of contributions on behalf of, or by, each such employee. Forfeitures of excess aggregate contributions may not be allocated to participants whose contributions are reduced under this paragraph.

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(D) Coordination with subsection (k) and 402(g).--The determination of the amount of excess aggregate contributions with respect to a plan shall be made after--

(i) first determining the excess deferrals (within the meaning of section 402(g)), and

(ii) then determining the excess contributions under subsection (k).

(7) Treatment of distributions.--

(A) Additional tax of section 72(t) not applicable.--No tax shall be imposed under section 72(t) on any amount required to be distributed under paragraph (6).

(B) Exclusion of employee contributions.--Any distribution attributable to employee contributions shall not be included in gross income except to the extent attributable to income on such contributions.

(8) Highly compensated employee.--For purposes of this subsection, the term "highly compensated employee" has the meaning given to such term by section 414(q).

(9) Regulations.--The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection and subsection (k), including regulations permitting appropriate aggregation of plans and contributions.

(10) Alternative method of satisfying tests.--A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan--

(A) meets the contribution requirements of subparagraph (B) of subsection (k)(11),

(B) meets the exclusive plan requirements of subsection (k)(11)(C), and

(C) meets the vesting requirements of section 408(p)(3).

(11) Additional alternative method of satisfying tests.--

(A) In general.--A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan--

(i) meets the contribution requirements of subparagraph (B) or (C) of subsection (k)(12),

(ii) meets the notice requirements of subsection (k)(12)(D), and

(iii) meets the requirements of subparagraph (B).

(B) Limitation on matching contributions.--The requirements of this subparagraph are met if--

(i) matching contributions on behalf of any employee may not be made with respect to an employee's contributions or elective deferrals in excess of 6 percent of the employee's compensation,

(ii) the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increase, and

(iii) the matching contribution with respect to any highly compensated employee at any rate of an employee contribution or rate of elective deferral is not greater than that with respect to an employee who is not a highly compensated employee.

(12) Alternative method for automatic contribution arrangements.--A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan--

(A) is a qualified automatic contribution arrangement (as defined in subsection (k)(13)), and

(B) meets the requirements of paragraph (11)(B).

(13) Cross reference.--

For excise tax on certain excess contributions, see section 4979.

(n) Coordination with qualified domestic relations orders.--The Secretary shall prescribe such rules or regulations as may be necessary to coordinate the requirements of subsection (a)(13)(B) and section 414(p) (and the regulations issued by the Secretary of Labor thereunder) with the other provisions of this chapter.

(o) Cross reference.--

For exemption from tax of a trust qualified under this section, see section 501(a).

CREDIT(S)

(Aug. 16, 1954, c. 736, 68A Stat. 134; Oct. 10, 1962, Pub.L. 87-792, § 2, 76 Stat. 809; Oct. 23, 1962, Pub.L. 87-863, § 2(a), 76 Stat. 1141; Feb. 26, 1964, Pub.L. 88-272, Title II, § 219(a), 78 Stat. 57; July 30, 1965, Pub.L. 89-97, Title I, § 106(d)(4), 79 Stat. 337; Nov. 13, 1966, Pub.L. 89-809, Title II, §§ 204(b)(1), (c), 205(a), 80 Stat. 1577, 1578; Jan. 12, 1971, Pub.L. 91-691, § 1(a), 84 Stat. 2074; Sept. 2, 1974, Pub.L. 93-406, Title II, §§ 1012(b), 1016(a)(2), 1021, 1022(a) to (d), (f), 1023, 2001(c) to (e)(4), (h)(1), 2004(a)(1), 88 Stat. 913, 929, 935, 937 to 940, 943, 952 to 955, 957, 979; Apr. 15, 1976, Pub.L. 94-267, § 1(c)(1), (2), 90 Stat. 367; Oct. 4, 1976, Pub.L. 94-455, Title VIII, § 803(b)(2), Title XV, § 1505(b), Title XIX,

§§ 1901(a)(56), 1906(b)(13)(A), 90 Stat. 1584, 1738, 1773, 1834; Nov. 6, 1978, Pub.L. 95-600, Title I, §§ 135(a), 141(f)(3), 143(a), 152(e), 92 Stat. 2785, 2795, 2796, 2799; Apr. 1, 1980, Pub.L. 96-222, Title I, § 101(a)(7)(L)(i)(V), (9), (14)(E)(iii), 94 Stat. 199, 201, 205; Sept. 26, 1980, Pub.L. 96-364, Title II, § 208(a), (e), Title IV, § 410(b), 94 Stat. 1289, 1290, 1308; Dec. 28, 1980, Pub.L. 96-605, Title II, §§ 221(a), 225(b)(1), (2), 94 Stat. 3528, 3529; Aug. 13, 1981, Pub.L. 97-34, Title III, §§ 312(b)(1), (c)(2) to (4), (e)(2), 314(a)(1), 335, 338(a), 95 Stat. 283 to 286, 297, 298; Sept. 3, 1982, Pub.L. 97-248, Title II, §§ 237(a), (b), (e)(1), 238(b), (d)(1), (2), 240(b), 242(a), 249(a), 254(a), 96 Stat. 511 to 513, 520, 521, 527, 533; Jan. 12, 1983, Pub.L. 97-448, Title I, § 103(c)(10)(A), (d)(2), (g)(2)(A), Title III, § 306(a)(12), 96 Stat. 2377 to 2379, 2405; Apr. 20, 1983, Pub.L. 98-21, Title I, § 124(c)(4)(A), 97 Stat. 91; July 18, 1984, Pub.L. 98-369, Title II, § 211(b)(5), Title IV, §§ 474(r)(13), 491(e)(4), (5), Title V, §§ 521(a), 524(d)(1), 527(a), (b), 528(b), Title VII, § 713(c)(2)(A), (d)(3), 98 Stat. 754, 842, 853, 865, 872, 875, 876, 877, 957, 958; Aug. 23, 1984, Pub.L. 98-397, Title II, §§ 203(a), 204(a), Title III, § 301(b), 98 Stat. 1440, 1445, 1451; Oct. 22, 1986, Pub.L. 99-514, Title XI, §§ 1106(d)(1), 1111(a), (b), 1112(b), (d)(1), 1114(b)(7), 1116(a) to (e), 1117(a), 1119(a), 1121(b), 1136(a), 1143(a), 1145(a), 1171(b)(5), 1174(c)(2)(A), 1175(a)(1), 1176(a), Title XVIII, §§ 1848(b), 1852(a)(4)(A), (6), (b)(8), (g), (h)(1), 1879(g)(1), (2), 1898(b)(2)(A), (3)(A), (7)(A), (13)(A), (14)(A), (c)(3), 1899A(10), 100 Stat. 2423, 2435, 2439, 2444, 2445, 2451, 2454 to 2456, 2459, 2463, 2465, 2485, 2490, 2513, 2518, 2519, 2857, 2865 to 2869, 2906, 2907, 2945, 2948, 2950, 2953, 2958; Dec. 22, 1987, Pub.L. 100-203, Title IX, § 9341(a), 101 Stat. 1330-369; Nov. 10, 1988, Pub.L. 100-647, Title I, §§ 1011(c)(7)(A), (d)(4), (e)(3), (g)(1) to (3), (h)(3), (k)(1)(A), (B), (2) to (7), (9), (l)(1) to (5)(A), (6), (7), 1011A(j), (l), 1011B(j)(1), (2), (6), (k)(1), (2), Title VI, §§ 6053(a), 6055(a), 6071(a), (b), 102 Stat. 3458, 3459, 3460, 3463, 3464, 3468, 3469, 3470, 3483, 3492, 3493, 3696, 3697, 3705; Nov. 8, 1989, Pub.L. 101-140, Title II, § 203(a)(5), 103 Stat. 830; Dec. 19, 1989, Pub.L. 101-239, Title VII, §§ 7311(a), 7811(g)(1), (h)(3), 7816(l), 7881(i)(1)(A), (4)(A), 103 Stat. 2354, 2409, 2421, 2442; Nov. 5, 1990, Pub.L. 101-508, Title XI, § 12011(b), 104 Stat. 1388-571; July 3, 1992, Pub.L. 102-318, Title V, §§ 521(b)(5) to (8), 522(a)(1), 106 Stat. 310, 313; Aug. 10, 1993, Pub.L. 103-66, Title XIII, § 13212(a), 107 Stat. 471; Dec. 8, 1994, Pub.L. 103-465, Title VII, §§ 732(a), 751(a)(9)(C), 766(b), 776(d), 108 Stat. 5004, 5021, 5037, 5048; Aug. 20, 1996, Pub.L. 104-188, Title I, §§ 1401(b)(5), (6), 1404(a), 1422(a), (b), 1426(a), 1431(b)(2), (c)(1)(B), 1432(a), (b), 1433(a) to (e), 1441(a), 1443(a), (b), 1445(a), 1459(a), (b), 1704(a), (t)(67), 110 Stat. 1789, 1791, 1800, 1801, 1803 to 1809, 1811, 1820, 1878, 1890; Aug. 5, 1997, Pub.L. 105-34, Title XV, §§ 1502(b), 1505(a)(1), (2), (b), 1525(a), 1530(c)(1), Title XVI, § 1601(d)(2)(A), (B), (D), (3), 111 Stat. 1060, 1063, 1072, 1078, 1088, 1089; Dec. 21, 2000, Pub.L. 106-554, § 1(a)(7) [Title III, § 316(c)], 114 Stat. 2763, 2763A-644; June 7, 2001, Pub.L. 107-16, Title VI, §§ 611(c), (f)(3), (g)(1), 641(e)(3), 643(b), 646(a)(1), 657(a), 666(a), 115 Stat. 97, 99, 120, 122, 126, 135, 143; Mar. 9, 2002, Pub.L. 107-147, Title IV, § 411(o)(2), (q)(1), 116 Stat. 48, 51; Oct. 4, 2004, Pub.L. 108-311, Title IV, § 407(b), 118 Stat. 1190; Aug. 17, 2006, Pub.L. 109-280, Title I, § 114(a), Title VIII, §§ 827(b)(1), 861(a), (b), Title IX, §§ 901(a)(1), (2)(A), 902(a), (b), (d)(2)(C), (D), (e)(3)(B), 905(b), 120 Stat. 853, 1000, 1021, 1026, 1029, 1033, 1035, 1038, 1050; June 17, 2008, Pub.L. 110-245, Title I, § 104(a), 122 Stat. 1626; Dec. 23, 2008, Pub.L. 110-458, Title I, §§ 101(d)(2)(A), (B), (C), 109(a), (b)(1), (2), Title II, § 201(a), 122 Stat. 5099, 5111, 5116; Mar. 30, 2010, Pub.L. 111-152, Title I, § 1004(d)(5), 124 Stat. 1036; Pub.L. 113-97, Title II, § 202(c)(3)(A), (4), (5), Apr. 7, 2014, 128 Stat. 1136; Pub.L. 113-295, Div. A, Title II, § 221(a)(52), Dec. 19, 2014, 128 Stat. 4045.)

Notes of Decisions (178)

Footnotes

1 So in original. Period before semicolon probably should be a closing parenthesis.

2 So in original. Probably should be capitalized.

3 So in original.

4 So in original. Probably should be "section".

5 So in original.

26 U.S.C.A. § 401, 26 USCA § 401
Current through P.L. 114-248.

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United States Code Annotated
Title 29. Labor
Chapter 7. Labor-Management Relations (Refs & Annos)
Subchapter IV. Liabilities of and Restrictions on Labor and Management

29 U.S.C.A. § 186

§ 186. Restrictions on financial transactions

Currentness

(a) Payment or lending, etc., of money by employer or agent to employees, representatives, or labor organizations

It shall be unlawful for any employer or association of employers or any person who acts as a labor relations expert, adviser, or consultant to an employer or who acts in the interest of an employer to pay, lend, or deliver, or agree to pay, lend, or deliver, any money or other thing of value--

(1) to any representative of any of his employees who are employed in an industry affecting commerce; or

(2) to any labor organization, or any officer or employee thereof, which represents, seeks to represent, or would admit to membership, any of the employees of such employer who are employed in an industry affecting commerce; or

(3) to any employee or group or committee of employees of such employer employed in an industry affecting commerce in excess of their normal compensation for the purpose of causing such employee or group or committee directly or indirectly to influence any other employees in the exercise of the right to organize and bargain collectively through representatives of their own choosing; or

(4) to any officer or employee of a labor organization engaged in an industry affecting commerce with intent to influence him in respect to any of his actions, decisions, or duties as a representative of employees or as such officer or employee of such labor organization.

(b) Request, demand, etc., for money or other thing of value

(1) It shall be unlawful for any person to request, demand, receive, or accept, or agree to receive or accept, any payment, loan, or delivery of any money or other thing of value prohibited by subsection (a) of this section.

(2) It shall be unlawful for any labor organization, or for any person acting as an officer, agent, representative, or employee of such labor organization, to demand or accept from the operator of any motor vehicle (as defined in section 13102 of Title 49) employed in the transportation of property in commerce, or the employer of any such operator, any money or other thing of value payable to such organization or to an officer, agent, representative or employee thereof as a fee or charge for the unloading, or in connection with the unloading, of the cargo of such vehicle: *Provided,* That nothing in this paragraph shall be construed to make unlawful any payment by an employer to any of his employees as compensation for their services as employees.

(c) Exceptions

The provisions of this section shall not be applicable (1) in respect to any money or other thing of value payable by an employer to any of his employees whose established duties include acting openly for such employer in matters of labor relations or personnel administration or to any representative of his employees, or to any officer or employee of a labor organization, who is also an employee or former employee of such employer, as compensation for, or by reason of, his service as an employee of such employer; (2) with respect to the payment or delivery of any money or other thing of value in satisfaction of a judgment of any court or a decision or award of an arbitrator or impartial chairman or in compromise, adjustment, settlement, or release of any claim, complaint, grievance, or dispute in the absence of fraud or duress; (3) with respect to the sale or purchase of an article or commodity at the prevailing market price in the regular course of business; (4) with respect to money deducted from the wages of employees in payment of membership dues in a labor organization: *Provided,* That the employer has received from each employee, on whose account such deductions are made, a written assignment which shall not be irrevocable for a period of more than one year, or beyond the termination date of the applicable collective agreement, whichever occurs sooner; (5) with respect to money or other thing of value paid to a trust fund established by such representative, for the sole and exclusive benefit of the employees of such employer, and their families and dependents (or of such employees, families, and dependents jointly with the employees of other employers making similar payments, and their families and dependents): *Provided,* That (A) such payments are held in trust for the purpose of paying, either from principal or income or both, for the benefit of employees, their families and dependents, for medical or hospital care, pensions on retirement or death of employees, compensation for injuries or illness resulting from occupational activity or insurance to provide any of the foregoing, or unemployment benefits or life insurance, disability and sickness insurance, or accident insurance; (B) the detailed basis on which such payments are to be made is specified in a written agreement with the employer, and employees and employers are equally represented in the administration of such fund, together with such neutral persons as the representatives of the employers and the representatives of employees may agree upon and in the event the employer and employee groups deadlock on the administration of such fund and there are no neutral persons empowered to break such deadlock, such agreement provides that the two groups shall agree on an impartial umpire to decide such dispute, or in event of their failure to agree within a reasonable length of time, an impartial umpire to decide such dispute shall, on petition of either group, be appointed by the district court of the United States for the district where the trust fund has its principal office, and shall also contain provisions for an annual audit of the trust fund, a statement of the results of which shall be available for inspection by interested persons at the principal office of the trust fund and at such other places as may be designated in such written agreement; and (C) such payments as are intended to be used for the purpose of providing pensions or annuities for employees are made to a separate trust which provides that the funds held therein cannot be used for any purpose other than paying such pensions or annuities; (6) with respect to money or other thing of value paid by any employer to a trust fund established by such representative for the purpose of pooled vacation, holiday, severance or similar benefits, or defraying costs of apprenticeship or other training programs: *Provided,* That the requirements of clause (B) of the proviso to clause (5) of this subsection shall apply to such trust funds; (7) with respect to money or other thing of value paid by any employer to a pooled or individual trust fund established by such representative for the purpose of (A) scholarships for the benefit of employees, their families, and dependents for study at educational institutions, (B) child care centers for preschool and school age dependents of employees, or (C) financial assistance for employee housing: *Provided,* That no labor organization or employer shall be required to bargain on the establishment of any such trust fund, and refusal to do so shall not constitute an unfair labor practice: *Provided further,* That the requirements of clause (B) of the proviso to clause (5) of this subsection shall apply to such trust funds; (8) with respect to money or any other thing of value paid by any employer to a trust fund established by such representative for the purpose of defraying the costs of legal services for employees, their families, and dependents for counsel or plan of their choice: *Provided,* That the requirements of clause (B) of the proviso to clause (5) of this subsection shall apply to such trust funds: *Provided further,* That no such legal services shall be furnished: (A) to initiate any proceeding directed (i) against any such employer or its officers or agents except in workman's compensation cases, or (ii) against such labor organization, or its parent or subordinate bodies, or their officers or agents, or (iii) against any other employer or labor organization, or their

officers or agents, in any matter arising under subchapter II of this chapter or this chapter; and (B) in any proceeding where a labor organization would be prohibited from defraying the costs of legal services by the provisions of the Labor-Management Reporting and Disclosure Act of 1959 [29 U.S.C.A. § 401 et seq.]; or (9) with respect to money or other things of value paid by an employer to a plant, area or industrywide labor management committee established for one or more of the purposes set forth in section 5(b) of the Labor Management Cooperation Act of 1978.

(d) Penalties for violations

(1) Any person who participates in a transaction involving a payment, loan, or delivery of money or other thing of value to a labor organization in payment of membership dues or to a joint labor-management trust fund as defined by clause (B) of the proviso to clause (5) of subsection (c) of this section or to a plant, area, or industry-wide labor-management committee that is received and used by such labor organization, trust fund, or committee, which transaction does not satisfy all the applicable requirements of subsections (c)(4) through (c)(9) of this section, and willfully and with intent to benefit himself or to benefit other persons he knows are not permitted to receive a payment, loan, money, or other thing of value under subsections (c)(4) through (c)(9) violates this subsection, shall, upon conviction thereof, be guilty of a felony and be subject to a fine of not more than $15,000, or imprisoned for not more than five years, or both; but if the value of the amount of money or thing of value involved in any violation of the provisions of this section does not exceed $1,000, such person shall be guilty of a misdemeanor and be subject to a fine of not more than $10,000, or imprisoned for not more than one year, or both.

(2) Except for violations involving transactions covered by subsection (d)(1) of this section, any person who willfully violates this section shall, upon conviction thereof, be guilty of a felony and be subject to a fine of not more than $15,000, or imprisoned for not more than five years, or both; but if the value of the amount of money or thing of value involved in any violation of the provisions of this section does not exceed $1,000, such person shall be guilty of a misdemeanor and be subject to a fine of not more than $10,000, or imprisoned for not more than one year, or both.

(e) Jurisdiction of courts

The district courts of the United States and the United States courts of the Territories and possessions shall have jurisdiction, for cause shown, and subject to the provisions of section 381 of Title 28 (relating to notice to opposite party) to restrain violations of this section, without regard to the provisions of section 17 of Title 15 and section 52 of this title, and the provisions of chapter 6 of this title.

(f) Effective date of provisions

This section shall not apply to any contract in force on June 23, 1947, until the expiration of such contract, or until July 1, 1948, whichever first occurs.

(g) Contributions to trust funds

Compliance with the restrictions contained in subsection (c)(5)(B) of this section upon contributions to trust funds, otherwise lawful, shall not be applicable to contributions to such trust funds established by collective agreement prior to January 1, 1946, nor shall subsection (c)(5)(A) of this section be construed as prohibiting contributions to such trust funds if prior to January 1, 1947, such funds contained provisions for pooled vacation benefits.

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(June 23, 1947, c. 120, Title III, § 302, 61 Stat. 157; Sept. 14, 1959, Pub.L. 86-257, Title V, § 505, 73 Stat. 537; Oct. 14, 1969, Pub.L. 91-86, 83 Stat. 133; Aug. 15, 1973, Pub.L. 93-95, 87 Stat. 314; Oct. 27, 1978, Pub.L. 95-524, § 6(d), 92 Stat. 2021; Oct. 12, 1984, Pub.L. 98-473, Title II, § 801, 98 Stat. 2131; Apr. 18, 1990, Pub.L. 101-273, § 1, 104 Stat. 138; Pub.L. 104-88, Title III, § 337, Dec. 29, 1995, 109 Stat. 954.)

Notes of Decisions (1708)

29 U.S.C.A. § 186, 29 USCA § 186
Current through P.L. 114-248.

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United States Code Annotated
Title 29. Labor
Chapter 18. Employee Retirement Income Security Program (Refs & Annos)
Subchapter I. Protection of Employee Benefit Rights (Refs & Annos)
Subtitle B. Regulatory Provisions
Part 2. Participation and Vesting (Refs & Annos)

29 U.S.C.A. § 1060

§ 1060. Multiple employer plans and other special rules

Currentness

(a) Plan maintained by more than one employer

Notwithstanding any other provision of this part or part 3, the following provisions of this subsection shall apply to a plan maintained by more than one employer:

(1) Section 1052 of this title shall be applied as if all employees of each of the employers were employed by a single employer.

(2) Sections 1053 and 1054 of this title shall be applied as if all such employers constituted a single employer, except that the application of any rules with respect to breaks in service shall be made under regulations prescribed by the Secretary.

(3) The minimum funding standard provided by section 1082 of this title shall be determined as if all participants in the plan were employed by a single employer.

(b) Maintenance of plan of predecessor employer

For purposes of this part and part 3--

(1) in any case in which the employer maintains a plan of a predecessor employer, service for such predecessor shall be treated as service for the employer, and

(2) in any case in which the employer maintains a plan which is not the plan maintained by a predecessor employer, service for such predecessor shall, to the extent provided in regulations prescribed by the Secretary of the Treasury, be treated as service for the employer.

(c) Plan maintained by controlled group of corporations

For purposes of sections 1052, 1053, and 1054 of this title, all employees of all corporations which are members of a controlled group of corporations (within the meaning of section 1563(a) of Title 26, determined without regard to section

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1563(a)(4) and (e)(3)(C) of Title 26) shall be treated as employed by a single employer. With respect to a plan adopted by more than one such corporation, the minimum funding standard of section 1082 of this title shall be determined as if all such employers were a single employer, and allocated to each employer in accordance with regulations prescribed by the Secretary of the Treasury.

(d) Plan of trades or businesses under common control

For purposes of sections 1052, 1053, and 1054 of this title, under regulations prescribed by the Secretary of the Treasury, all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer. The regulations prescribed under this subsection shall be based on principles similar to the principles which apply in the case of subsection (c) of this section.

(e) Special rules for eligible combined defined benefit plans and qualified cash or deferred arrangements

(1) General rule

Except as provided in this subsection, this chapter shall be applied to any defined benefit plan or applicable individual account plan which are [1] part of an eligible combined plan in the same manner as if each such plan were not a part of the eligible combined plan. In the case of a termination of the defined benefit plan and the applicable defined contribution plan forming part of an eligible combined plan, the plan administrator shall terminate each such plan separately.

(2) Eligible combined plan

For purposes of this subsection--

(A) In general

The term "eligible combined plan" means a plan--

(i) which is maintained by an employer which, at the time the plan is established, is a small employer,

(ii) which consists of a defined benefit plan and an applicable individual account plan each of which qualifies under section 401(a) of Title 26,

(iii) the assets of which are held in a single trust forming part of the plan and are clearly identified and allocated to the defined benefit plan and the applicable individual account plan to the extent necessary for the separate application of this chapter under paragraph (1), and

(iv) with respect to which the benefit, contribution, vesting, and nondiscrimination requirements of subparagraphs (B), (C), (D), (E), and (F) are met.

For purposes of this subparagraph, the term "small employer" has the meaning given such term by section 4980D(d)(2) of Title 26, except that such section shall be applied by substituting "500" for "50" each place it appears.

(B) Benefit requirements

(i) In general

The benefit requirements of this subparagraph are met with respect to the defined benefit plan forming part of the eligible combined plan if the accrued benefit of each participant derived from employer contributions, when expressed as an annual retirement benefit, is not less than the applicable percentage of the participant's final average pay. For purposes of this clause, final average pay shall be determined using the period of consecutive years (not exceeding 5) during which the participant had the greatest aggregate compensation from the employer.

(ii) Applicable percentage

For purposes of clause (i), the applicable percentage is the lesser of--

(I) 1 percent multiplied by the number of years of service with the employer, or

(II) 20 percent.

(iii) Special rule for applicable defined benefit plans

If the defined benefit plan under clause (i) is an applicable defined benefit plan as defined in section 1053(f)(3)(B) of this title which meets the interest credit requirements of section 1054(b)(5)(B)(i) of this title, the plan shall be treated as meeting the requirements of clause (i) with respect to any plan year if each participant receives pay credit for the year which is not less than the percentage of compensation determined in accordance with the following table:

If the participant's age as of the beginning of the year is--	The percentage is--
30 or less	2
Over 30 but less than 40	4
40 or over but less than 50	6
50 or over	8.

(iv) Years of service

For purposes of this subparagraph, years of service shall be determined under the rules of paragraphs (1), (2), and (3) of section 1053(b) of this title, except that the plan may not disregard any year of service because of a participant making, or failing to make, any elective deferral with respect to the qualified cash or deferred arrangement to which subparagraph (C) applies.

(C) Contribution requirements

(i) In general

The contribution requirements of this subparagraph with respect to any applicable individual account plan forming part of an eligible combined plan are met if--

(I) the qualified cash or deferred arrangement included in such plan constitutes an automatic contribution arrangement, and

(II) the employer is required to make matching contributions on behalf of each employee eligible to participate in the arrangement in an amount equal to 50 percent of the elective contributions of the employee to the extent such elective contributions do not exceed 4 percent of compensation.

Rules similar to the rules of clauses (ii) and (iii) of section 401(k)(12) (B) of Title 26 shall apply for purposes of this clause.

(ii) Nonelective contributions

An applicable individual account plan shall not be treated as failing to meet the requirements of clause (i) because the employer makes nonelective contributions under the plan but such contributions shall not be taken into account in determining whether the requirements of clause (i)(II) are met.

(D) Vesting requirements

The vesting requirements of this subparagraph are met if--

(i) in the case of a defined benefit plan forming part of an eligible combined plan an employee who has completed at least 3 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit under the plan derived from employer contributions, and

(ii) in the case of an applicable individual account plan forming part of eligible combined plan--

(I) an employee has a nonforfeitable right to any matching contribution made under the qualified cash or deferred arrangement included in such plan by an employer with respect to any elective contribution, including matching contributions in excess of the contributions required under subparagraph (C)(i)(II), and

(II) an employee who has completed at least 3 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit derived under the arrangement from nonelective contributions of the employer.

For purposes of this subparagraph, the rules of section 1053 of this title shall apply to the extent not inconsistent with this subparagraph.

(E) Uniform provision of contributions and benefits

In the case of a defined benefit plan or applicable individual account plan forming part of an eligible combined plan, the requirements of this subparagraph are met if all contributions and benefits under each such plan, and all rights and features under each such plan, must be provided uniformly to all participants.

(F) Requirements must be met without taking into account social security and similar contributions and benefits or other plans

(i) In general

The requirements of this subparagraph are met if the requirements of clauses (ii) and (iii) are met.

(ii) Social security and similar contributions

The requirements of this clause are met if--

(I) the requirements of subparagraphs (B) and (C) are met without regard to section 401(l) of Title 26, and

(II) the requirements of sections 401(a)(4) and 410(b) of Title 26 are met with respect to both the applicable defined contribution plan and defined benefit plan forming part of an eligible combined plan without regard to section 401(l) of Title 26.

(iii) Other plans and arrangements

The requirements of this clause are met if the applicable defined contribution plan and defined benefit plan forming part of an eligible combined plan meet the requirements of sections 401(a)(4) and 410(b) of Title 26 without being combined with any other plan.

(3) Automatic contribution arrangement

For purposes of this subsection--

(A) In general

A qualified cash or deferred arrangement shall be treated as an automatic contribution arrangement if the arrangement--

(i) provides that each employee eligible to participate in the arrangement is treated as having elected to have the employer make elective contributions in an amount equal to 4 percent of the employee's compensation unless

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the employee specifically elects not to have such contributions made or to have such contributions made at a different rate, and

(ii) meets the notice requirements under subparagraph (B).

(B) Notice requirements

(i) In general

The requirements of this subparagraph are met if the requirements of clauses (ii) and (iii) are met.

(ii) Reasonable period to make election

The requirements of this clause are met if each employee to whom subparagraph (A)(i) applies--

(I) receives a notice explaining the employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf or to have the contributions made at a different rate, and

(II) has a reasonable period of time after receipt of such notice and before the first elective contribution is made to make such election.

(iii) Annual notice of rights and obligations

The requirements of this clause are met if each employee eligible to participate in the arrangement is, within a reasonable period before any year, given notice of the employee's rights and obligations under the arrangement.

The requirements of this subparagraph shall not be treated as met unless the requirements of clauses (i) and (ii) of section 401(k)(12)(D) of Title 26 are met with respect to the notices described in clauses (ii) and (iii) of this subparagraph.

(4) Coordination with other requirements

(A) Treatment of separate plans

The except clause in section 1002(35) of this title shall not apply to an eligible combined plan.

(B) Reporting

An eligible combined plan shall be treated as a single plan for purposes of section 1023 of this title.

(5) Applicable individual account plan

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For purposes of this subsection--

(A) In general

The term "applicable individual account plan" means an individual account plan which includes a qualified cash or deferred arrangement.

(B) Qualified cash or deferred arrangement

The term "qualified cash or deferred arrangement" has the meaning given such term by section 401(k)(2) of Title 26.

(f) Cooperative and small employer charity pension plans

(1) In general

For purposes of this subchapter, except as provided in this subsection, a CSEC plan is an employee pension benefit plan (other than a multiemployer plan) that is a defined benefit plan--

(A) to which section 104 of the Pension Protection Act of 2006 applies, without regard to--

(i) section 104(a)(2) of such Act;

(ii) the amendments to such section 104 by section 202(b) of the Preservation of Access to Care for Medicare Beneficiaries and Pension Relief Act of 2010; and

(iii) paragraph (3)(B);

(B) that, as of June 25, 2010, was maintained by more than one employer and all of the employers were organizations described in section 501(c)(3) of Title 26; or

(C) that, as of June 25, 2010, was maintained by an employer--

(i) described in section 501(c)(3) of such Title,

(ii) chartered under part B of subtitle II of Title 36,

(iii) with employees in at least 40 States, and

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(iv) whose primary exempt purpose is to provide services with respect to children.

(2) Aggregation

All employers that are treated as a single employer under subsection (b) or (c) of section 414 of Title 26 shall be treated as a single employer for purposes of determining if a plan was maintained by more than one employer under subparagraph [2] (B) and (C) of paragraph (1).

(3) Election

(A) In general

If a plan falls within the definition of a CSEC plan under this subsection (without regard to this paragraph), such plan shall be a CSEC plan unless the plan sponsor elects not later than the close of the first plan year of the plan beginning after December 31, 2013, not to be treated as a CSEC plan. An election under the preceding sentence shall take effect for such plan year and, once made, may be revoked only with the consent of the Secretary of the Treasury.

(B) Special rule

If a plan described in subparagraph (A) is treated as a CSEC plan, section 104 of the Pension Protection Act of 2006, as amended by the Preservation of Access to Care for Medicare Beneficiaries and Pension Relief Act of 2010, shall cease to apply to such plan as of the first date as of which such plan is treated as a CSEC plan.

CREDIT(S)

(Pub.L. 93-406, Title I, § 210, Sept. 2, 1974, 88 Stat. 866; Pub.L. 101-239, Title VII, §§ 7891(a)(1), 7894(c)(10), Dec. 19, 1989, 103 Stat. 2445, 2449; Pub.L. 109-280, Title IX, § 903(b)(1), (2)(A), Aug. 17, 2006, 120 Stat. 1044, 1048; Pub.L. 110-458, Title I, § 109(c)(2), Dec. 23, 2008, 122 Stat. 5111; Pub.L. 113-97, Title I, §§ 101, 103(a), Apr. 7, 2014, 128 Stat. 1102, 1117; Pub.L. 113-235, Div. P, § 3(a), Dec. 16, 2014, 128 Stat. 2829.)

Notes of Decisions (3)

Footnotes

1 So in original. Probably should be "is".

2 So in original. Probably should be "subparagraphs".

29 U.S.C.A. § 1060, 29 USCA § 1060

Current through P.L. 114-248.

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United States Code Annotated
Title 29. Labor
Chapter 18. Employee Retirement Income Security Program (Refs & Annos)
Subchapter III. Plan Termination Insurance (Refs & Annos)
Subtitle D. Liability (Refs & Annos)

29 U.S.C.A. § 1361

§ 1361. Amounts payable by corporation

Currentness

The corporation shall pay benefits under a single-employer plan terminated under this subchapter subject to the limitations and requirements of subtitle B of this subchapter. The corporation shall provide financial assistance to pay benefits under a multiemployer plan which is insolvent under section 1426 or 1441(d)(2)(A) of this title, subject to the limitations and requirements of subtitles B, C, and E of this subchapter. Amounts guaranteed by the corporation under sections 1322 and 1322a of this title shall be paid by the corporation only out of the appropriate fund. The corporation shall make payments under the supplemental program to reimburse multiemployer plans for uncollectible withdrawal liability only out of the fund established under section 1305(e) of this title.

CREDIT(S)

(Pub.L. 93-406, Title IV, § 4061, Sept. 2, 1974, 88 Stat. 1029; Pub.L. 96-364, Title IV, § 403(f), Sept. 26, 1980, 94 Stat. 1301.)

29 U.S.C.A. § 1361, 29 USCA § 1361
Current through P.L. 114-248.

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United States Code Annotated
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Chapter 18. Employee Retirement Income Security Program (Refs & Annos)
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Subtitle D. Liability (Refs & Annos)

29 U.S.C.A. § 1368

§ 1368. Lien for liability

Currentness

(a) Creation of lien

If any person liable to the corporation under section 1362, 1363, or 1364 of this title neglects or refuses to pay, after demand, the amount of such liability (including interest), there shall be a lien in favor of the corporation in the amount of such liability (including interest) upon all property and rights to property, whether real or personal, belonging to such person, except that such lien may not be in an amount in excess of 30 percent of the collective net worth of all persons described in section 1362(a) of this title [1]

(b) Term of lien

The lien imposed by subsection (a) of this section arises on the date of termination of a plan, and continues until the liability imposed under section 1362, 1363, or 1364 of this title is satisfied or becomes unenforceable by reason of lapse of time.

(c) Priority

(1) Except as otherwise provided under this section, the priority of a lien imposed under subsection (a) of this section shall be determined in the same manner as under section 6323 of Title 26 (as in effect on April 7, 1986). Such section 6323 shall be applied for purposes of this section by disregarding subsection (g)(4) and by substituting--

(A) "lien imposed by section 4068 of the Employee Retirement Income Security Act of 1974 [29 U.S.C.A. § 1368]" for "lien imposed by section 6321" each place it appears in subsections (a), (b), (c)(1), (c)(4)(B), (d), (e), and (h)(5);

(B) "the corporation" for "the Secretary" in subsections (a) and (b)(9)(C);

(C) "the payment of the amount on which the section 4068(a) lien is based" for "the collection of any tax under this title" in subsection (b)(3);

(D) "a person whose property is subject to the lien" for "the taxpayer" in subsections (b)(8), (c)(2)(A)(i) (the first place it appears), (c)(2)(A)(ii), (c)(2)(B), (c)(4)(B), and (c)(4)(C) (in the matter preceding clause (i));

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(E) "such person" for "the taxpayer" in subsections (c)(2)(A)(i) (the second place it appears) and (c)(4)(C)(ii);

(F) "payment of the loan value of the amount on which the lien is based is made to the corporation" for "satisfaction of a levy pursuant to section 6332(b)" in subsection (b)(9)(C);

(G) "section 4068(a) lien" for "tax lien" each place it appears in subsections (c)(1), (c)(2)(A), (c)(2)(B), (c)(3)(B)(iii), (c)(4)(B), (d), and (h)(5); and

(H) "the date on which the lien is first filed" for "the date of the assessment of the tax" in subsection (g)(3)(A).

(2) In a case under Title 11 or in insolvency proceedings, the lien imposed under subsection (a) of this section shall be treated in the same manner as a tax due and owing to the United States for purposes of Title 11 or section 3713 of Title 31.

(3) For purposes of applying section 6323(a) of Title 26 to determine the priority between the lien imposed under subsection (a) of this section and a Federal tax lien, each lien shall be treated as a judgment lien arising as of the time notice of such lien is filed.

(4) For purposes of this subsection, notice of the lien imposed by subsection (a) of this section shall be filed in the same manner as under section 6323(f) and (g) of Title 26.

(d) Civil action; limitation period

(1) In any case where there has been a refusal or neglect to pay the liability imposed under section 1362, 1363, or 1364 of this title, the corporation may bring civil action in a district court of the United States to enforce the lien of the corporation under this section with respect to such liability or to subject any property, of whatever nature, of the liable person, or in which he has any right, title, or interest to the payment of such liability.

(2) The liability imposed by section 1362, 1363, or 1364 of this title may be collected by a proceeding in court if the proceeding is commenced within 6 years after the date upon which the plan was terminated or prior to the expiration of any period for collection agreed upon in writing by the corporation and the liable person before the expiration of such 6-year period. The period of limitations provided under this paragraph shall be suspended for the period the assets of the liable person are in the control or custody of any court of the United States, or of any State, or of the District of Columbia, and for 6 months thereafter, and for any period during which the liable person is outside the United States if such period of absence is for a continuous period of at least 6 months.

(e) Release or subordination

If the corporation determines that release of the lien or subordination of the lien to any other creditor of the liable person would not adversely affect the collection of the liability imposed under section 1362, 1363, or 1364 of this title, or that the amount realizable by the corporation from the property to which the lien attaches will ultimately be increased by such release or subordination, and that the ultimate collection of the liability will be facilitated by such release or

subordination, the corporation may issue a certificate of release or subordination of the lien with respect to such property, or any part thereof.

(f) Definitions

For purposes of this section--

(1) The collective net worth of persons subject to liability in connection with a plan termination shall be determined as provided in section 1362(d)(1) of this title.

(2) The term "pre-tax profits" has the meaning provided in section 1362(d)(2) of this title.

CREDIT(S)

(Pub.L. 93-406, Title IV, § 4068, Sept. 2, 1974, 88 Stat. 1032; Pub.L. 95-598, Title III, § 321(c), Nov. 6, 1978, 92 Stat. 2678; Pub.L. 99-272, Title XI, § 11016(a)(6)(B), (c)(14), Apr. 7, 1986, 100 Stat. 271, 275; Pub.L. 100-203, Title IX, § 9312(b)(2)(B), (C)(ii), Dec. 22, 1987, 101 Stat. 1330-361, 1330-362; Pub.L. 101-239, Title VII, §§ 7881(f)(3)(B), (10)(B), (C), (12), 7891(a)(1), 7894(g)(4)(A), Dec. 19, 1989, 103 Stat. 2440, 2441, 2445, 2451.)

Notes of Decisions (8)

Footnotes

1 So in original. Probably should be followed by a period.

29 U.S.C.A. § 1368, 29 USCA § 1368

Current through P.L. 114-248.

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United States Code Annotated
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Subchapter III. Plan Termination Insurance (Refs & Annos)
Subtitle E. Special Provisions for Multiemployer Plans (Refs & Annos)
Part 1. Employer Withdrawals (Refs & Annos)

29 U.S.C.A. § 1383

§ 1383. Complete withdrawal

Currentness

(a) Determinative factors

For purposes of this part, a complete withdrawal from a multiemployer plan occurs when an employer--

(1) permanently ceases to have an obligation to contribute under the plan, or

(2) permanently ceases all covered operations under the plan.

(b) Building and construction industry

(1) Notwithstanding subsection (a) of this section, in the case of an employer that has an obligation to contribute under a plan for work performed in the building and construction industry, a complete withdrawal occurs only as described in paragraph (2), if--

(A) substantially all the employees with respect to whom the employer has an obligation to contribute under the plan perform work in the building and construction industry, and

(B) the plan--

(i) primarily covers employees in the building and construction industry, or

(ii) is amended to provide that this subsection applies to employers described in this paragraph.

(2) A withdrawal occurs under this paragraph if--

(A) an employer ceases to have an obligation to contribute under the plan, and

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(B) the employer--

(i) continues to perform work in the jurisdiction of the collective bargaining agreement of the type for which contributions were previously required, or

(ii) resumes such work within 5 years after the date on which the obligation to contribute under the plan ceases, and does not renew the obligation at the time of the resumption.

(3) In the case of a plan terminated by mass withdrawal (within the meaning of section 1341a(a)(2) of this title), paragraph (2) shall be applied by substituting "3 years" for "5 years" in subparagraph (B)(ii).

(c) Entertainment industry

(1) Notwithstanding subsection (a) of this section, in the case of an employer that has an obligation to contribute under a plan for work performed in the entertainment industry, primarily on a temporary or project-by-project basis, if the plan primarily covers employees in the entertainment industry, a complete withdrawal occurs only as described in subsection (b)(2) of this section applied by substituting "plan" for "collective bargaining agreement" in subparagraph (B)(i) thereof.

(2) For purposes of this subsection, the term "entertainment industry" means--

(A) theater, motion picture (except to the extent provided in regulations prescribed by the corporation), radio, television, sound or visual recording, music, and dance, and

(B) such other entertainment activities as the corporation may determine to be appropriate.

(3) The corporation may by regulation exclude a group or class of employers described in the preceding sentence from the application of this subsection if the corporation determines that such exclusion is necessary--

(A) to protect the interest of the plan's participants and beneficiaries, or

(B) to prevent a significant risk of loss to the corporation with respect to the plan.

(4) A plan may be amended to provide that this subsection shall not apply to a group or class of employers under the plan.

(d) Other determinative factors

(1) Notwithstanding subsection (a) of this section, in the case of an employer who--

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(A) has an obligation to contribute under a plan described in paragraph (2) primarily for work described in such paragraph, and

(B) does not continue to perform work within the jurisdiction of the plan,

a complete withdrawal occurs only as described in paragraph (3).

(2) A plan is described in this paragraph if substantially all of the contributions required under the plan are made by employers primarily engaged in the long and short haul trucking industry, the household goods moving industry, or the public warehousing industry.

(3) A withdrawal occurs under this paragraph if--

(A) an employer permanently ceases to have an obligation to contribute under the plan or permanently ceases all covered operations under the plan, and

(B) either--

(i) the corporation determines that the plan has suffered substantial damage to its contribution base as a result of such cessation, or

(ii) the employer fails to furnish a bond issued by a corporate surety company that is an acceptable surety for purposes of section 1112 of this title, or an amount held in escrow by a bank or similar financial institution satisfactory to the plan, in an amount equal to 50 percent of the withdrawal liability of the employer.

(4) If, after an employer furnishes a bond or escrow to a plan under paragraph (3)(B)(ii), the corporation determines that the cessation of the employer's obligation to contribute under the plan (considered together with any cessations by other employers), or cessation of covered operations under the plan, has resulted in substantial damage to the contribution base of the plan, the employer shall be treated as having withdrawn from the plan on the date on which the obligation to contribute or covered operations ceased, and such bond or escrow shall be paid to the plan. The corporation shall not make a determination under this paragraph more than 60 months after the date on which such obligation to contribute or covered operations ceased.

(5) If the corporation determines that the employer has no further liability under the plan either--

(A) because it determines that the contribution base of the plan has not suffered substantial damage as a result of the cessation of the employer's obligation to contribute or cessation of covered operations (considered together with any cessation of contribution obligation, or of covered operations, with respect to other employers), or

(B) because it may not make a determination under paragraph (4) because of the last sentence thereof,

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then the bond shall be cancelled or the escrow refunded.

(6) Nothing in this subsection shall be construed as a limitation on the amount of the withdrawal liability of any employer.

(e) Date of complete withdrawal

For purposes of this part, the date of a complete withdrawal is the date of the cessation of the obligation to contribute or the cessation of covered operations.

(f) Special liability withdrawal rules for industries other than construction and entertainment industries; procedures applicable to amend plans

(1) The corporation may prescribe regulations under which plans in industries other than the construction or entertainment industries may be amended to provide for special withdrawal liability rules similar to the rules described in subsections (b) and (c) of this section.

(2) Regulations under paragraph (1) shall permit use of special withdrawal liability rules--

(A) only in industries (or portions thereof) in which, as determined by the corporation, the characteristics that would make use of such rules appropriate are clearly shown, and

(B) only if the corporation determines, in each instance in which special withdrawal liability rules are permitted, that use of such rules will not pose a significant risk to the corporation under this subchapter.

CREDIT(S)

(Pub.L. 93-406, Title IV, § 4203, as added Pub.L. 96-364, Title I, § 104(2), Sept. 26, 1980, 94 Stat. 1218.)

Notes of Decisions (50)

29 U.S.C.A. § 1383, 29 USCA § 1383
Current through P.L. 114-248.

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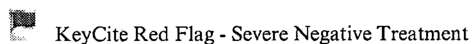
KeyCite Red Flag - Severe Negative Treatment
KeyCite Red Flag Negative Treatment§1422. Repealed. Pub.L. 113-235, Div. O, Title I, §108(a)(1), Dec. 16, 2014, 128 Stat. 2786

United States Code Annotated
Title 29. Labor
Chapter 18. Employee Retirement Income Security Program (Refs & Annos)
Subchapter III. Plan Termination Insurance (Refs & Annos)
Subtitle E. Special Provisions for Multiemployer Plans (Refs & Annos)
Part 3. Insolvent Plans (Refs & Annos)

29 U.S.C.A. § 1422

§ 1422. Repealed. Pub.L. 113-235, Div. O, Title I, § 108(a)(1), Dec. 16, 2014, 128 Stat. 2786

Effective: December 16, 2014
Currentness

29 U.S.C.A. § 1422, 29 USCA § 1422
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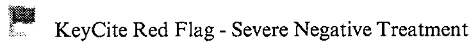

KeyCite Red Flag - Severe Negative Treatment

KeyCite Red Flag Negative Treatment§ 1423. Repealed. Pub.L. 113-235, Div. O, Title I, § 108(a)(1), Dec. 16, 2014, 128 Stat. 2786

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Subtitle E. Special Provisions for Multiemployer Plans (Refs & Annos)
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29 U.S.C.A. § 1423

§ 1423. Repealed. Pub.L. 113-235, Div. O, Title I, § 108(a)(1), Dec. 16, 2014, 128 Stat. 2786

Effective: December 16, 2014
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29 U.S.C.A. § 1423, 29 USCA § 1423
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Subtitle E. Special Provisions for Multiemployer Plans (Refs & Annos)
Part 3. Insolvent Plans (Refs & Annos)

29 U.S.C.A. § 1424

§ 1424. Repealed. Pub.L. 113-235, Div. O, Title I, § 108(a)(1), Dec. 16, 2014, 128 Stat. 2786

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29 U.S.C.A. § 1424, 29 USCA § 1424
Current through P.L. 114-248.

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KeyCite Red Flag - Severe Negative Treatment
KeyCite Red Flag Negative Treatment§1425. Repealed. Pub.L. 113-235, Div. O, Title I, §108(a)(1), Dec. 16, 2014, 128 Stat. 2786

United States Code Annotated
Title 29. Labor
Chapter 18. Employee Retirement Income Security Program (Refs & Annos)
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Subtitle E. Special Provisions for Multiemployer Plans (Refs & Annos)
Part 3. Insolvent Plans (Refs & Annos)

29 U.S.C.A. § 1425

§ 1425. Repealed. Pub.L. 113-235, Div. O, Title I, § 108(a)(1), Dec. 16, 2014, 128 Stat. 2786

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Currentness

29 U.S.C.A. § 1425, 29 USCA § 1425
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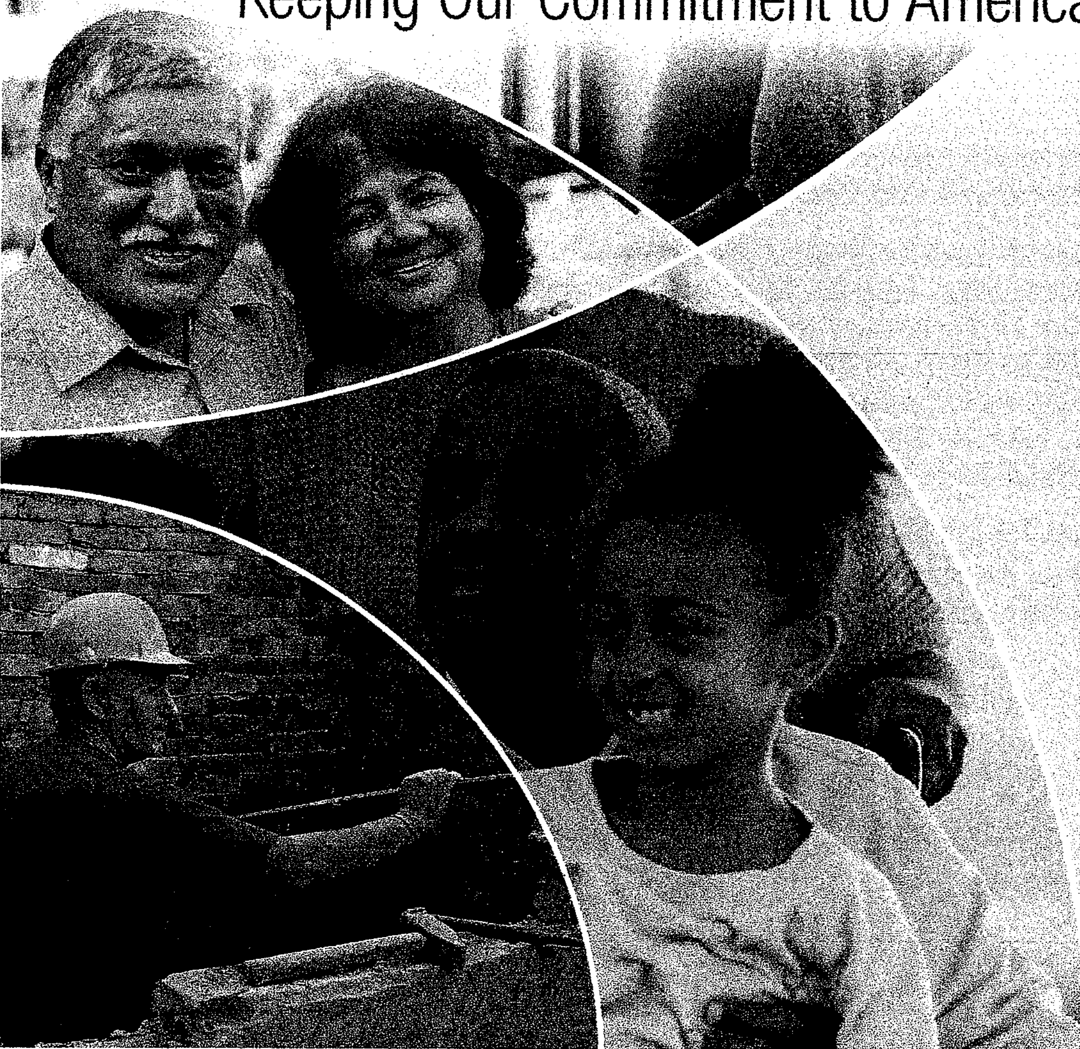
Annual Report 2016

Keeping Our Commitment to America's Workers



A MESSAGE FROM OUR CHAIR

Protecting retirement security for the middle class in our country remains a top priority of the Obama Administration. The Pension Benefit Guaranty Corporation (PBGC) has an important role in ensuring that workers have every opportunity to retire with dignity and financial stability. Today, hundreds of thousands of retirees currently receive $5.8 billion annually from the PBGC and nearly 40 million workers and retirees are in plans insured by the PBGC. The strength and future of the PBGC's insurance programs are vital to the retirement security of the millions of workers and retirees in defined benefit plans.

On behalf of the PBGC Board of Directors, I am pleased to present the PBGC's FY 2016 Annual Report, which provides important information about the PBGC's operations and finances. The report highlights many of PBGC's accomplishments over this past fiscal year to preserve plans and protect pensions, as well as the PBGC's future program challenges.

Two of PBGC's accomplishments this year, of which I am especially proud, are its continuing progress on implementing the Smaller Asset Managers Pilot Program and an enterprise risk management framework. The Smaller Asset Managers Pilot Program reduces barriers that smaller investment firms face when competing for the PBGC's business. We are pleased that, after extensive collaborative work with the PBGC Advisory Committee, PBGC made awards to five firms in June. In addition, the PBGC has made significant progress on enterprise risk management in evaluating the different entity-wide risks that the corporation might experience. These efforts help to foster a culture of risk awareness that is essential to good governance and stewardship.

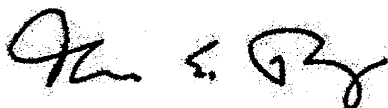
While I am pleased that given the recent trends in claims and premiums, the single-employer program is likely to continue to improve over the next decade, I remain concerned that the multiemployer plan program faces a growing deficit. The FY 2016 Annual Report shows that the multiemployer plan program deficit is at an all-time high and needs significant reform in order to remain viable.

Multiemployer defined benefit plans provide retirement security to more than 10 million participants and their beneficiaries. But PBGC estimates that plans covering about 10% to 15% of the 10 million multiemployer participants are at risk of running out of money over the next 20 years and that PBGC's multiemployer insurance program is likely to run out of money by the end of 2025. Insolvency of PBGC's multiemployer insurance program would devastate not only the retirement benefits of the 1 million to 1.5 million participants and their families in these at-risk plans but all the participants in multiemployer plans that are currently receiving financial assistance from PBGC as well.

We must address the challenges of the multiemployer insurance program before it is too late. The Multiemployer Pension Reform Act (MPRA) Report issued earlier this year showed that the longer we wait, the greater the premium increases needed to avoid insolvency, further straining a system that is already under great stress.

The PBGC multiemployer insurance program needs reform that addressees the problems affecting plans, and also strengthens the multiemployer fund so that workers, retirees, and plan sponsors can rely on it for years to come. The President's 2017 Budget proposed a structure for increased premiums under the multiemployer program at a level that would help alleviate some of the risk of the multiemployer program becoming insolvent within 20 years. Changes to the multiemployer insurance program such as this restructuring are urgently needed to protect the lifetime pensions of millions of America's workers and retirees.

The strength and future of the PBGC's insurance programs are vital to the retirement security of the millions of workers and retirees in defined benefit plans. My fellow Board members, Treasury Secretary Jack Lew and Commerce Secretary Penny Pritzker, and I are proud of the work PBGC has accomplished to provide a more secure future for America's workers and retirees. We are confident that under the continued leadership of Director Tom Reeder, the PBGC will continue to work toward financially sound insurance programs to protect the retirement savings of America's workers and retirees.



Thomas E. Perez
Secretary of Labor
Chair of the Board

A MESSAGE FROM THE DIRECTOR

The most important role we have at the Pension Benefit Guaranty Corporation is to protect the retirement security of nearly 40 million workers, retirees, and beneficiaries in traditional pension plans. These plans, and the guarantee provided by the PBGC, are important not only for the participants, but also their families and often the communities in which they live.

As many Americans continue to benefit from longer lifespans, the need for lifetime income is more important for current retirees and generations that follow. Nothing gives people more retirement security than a traditional pension that they can't outlive or outspend.

During this past year, I've been able to work with a talented group of professionals to make sure that when a plan can no longer fulfill its promises to participants and beneficiaries, PBGC will step in and pay the statutory guarantee.

Currently, we pay nearly 840,000 retirees and beneficiaries, and almost 560,000 workers are scheduled to receive benefits from PBGC when they retire. We are committed to getting timely and accurate payments to these people each month.

Preserving plans and protecting pensioners are two of our highest priorities. An important accomplishment this year was the restoration of two RG Steel pension plans to the Renco Group. This is the second time in our history that we have restored a plan back to the sponsor that made the commitment to its workers in the first place. This is an extraordinary outcome for the 1,350 people covered. Thanks to PBGC's efforts, they will receive the full benefits they've worked for.

We also strive to engage and collaborate with the stakeholder community, including participants, sponsors and service providers, to listen to their concerns and continue to work on ways to make it easier for plan sponsors to maintain traditional pension plans. This year, for example, PBGC issued a final rule that cuts penalties for late payment of premiums in half, which reduces the regulatory and financial burdens of sponsoring a pension plan.

Additionally, the scope of PBGC's mission is increasing by expanding our Missing Participants Program to include terminating defined contribution plans that are not covered by the existing program. We reached out to the community to see what was needed and got input on practical ways to do it. In September, we issued a proposed rule that would help find participants and connect them with their retirement savings.

PBGC's work on implementing the Multiemployer Pension Reform Act of 2014 is ongoing. We issued a proposed rule on facilitated mergers, a tool targeted to help troubled multiemployer plans improve their long-term health. PBGC continues to work with the Departments of Labor and Treasury to carry out the law.

PBGC continues to collaborate with stakeholders in the multiemployer system to find solutions to resolve its financial difficulties. At the same time, we must protect the benefits of those left behind in the existing defined benefit system, even as new plan models emerge.

We are working to remedy the financial troubles of PBGC's Multiemployer Program, which is expected to run out of money in the near future. It is in all stakeholders' interests -- workers, retirees, and plan sponsors -- that the PBGC is financially sound.

We continue to work with others in the administration on ways to improve the financial condition of the multiemployer program. There is still much work to be done to protect the retirement incomes of those who rely on us.

Providing excellent customer service is among our top priorities. We are proud that the retirees we serve have given us a score of 90 on the American Customer Satisfaction Index. This score is among the best in the public and private sectors. Everywhere I go, people make an effort to tell me about someone at PBGC who was very helpful to them. It reinforces what I already know – that the drivers of PBGC's hard work and accomplishments are the agency's professional staff who are dedicated and passionate about PBGC's mission. Together, we have a firm commitment to ensure that American workers have greater financial security in their retirement years.

I am grateful to the Board of Directors – Secretary of Labor Tom Perez, Secretary of the Treasury Jack Lew and Secretary of Commerce Penny Pritzker and their staff – for their support during my first year at PBGC. We thank them for their leadership and dedication to our mission.

W. Thomas Reeder
Director
November 15, 2016

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This annual report is prepared to meet applicable legal requirements and is in accordance with and pursuant to the provisions of: the Government Corporation Control Act, 31 U.S.C. Section 9106; Circular No. A-11, Revised, "Preparation, Submission and Execution of the Budget," Office of Management and Budget, July 1, 2016; and Circular No. A-136 Revised, "Financial Reporting Requirements," Office of Management and Budget, October, 7, 2016. Section 4008 of the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. Section 1308, also requires an actuarial report evaluating expected operations and claims that will be issued as soon as practicable.

ANNUAL PERFORMANCE REPORT

Established by Congress in 1974, the Pension Benefit Guaranty Corporation (PBGC and the Corporation) insures the defined benefit pensions of workers and retirees in private-sector pension plans. PBGC now protects the retirement security of nearly 40 million American workers and retirees in defined benefit pension plans. PBGC is responsible for benefit payments to more than 1.5 million people in failed plans who otherwise may have lost their pensions – earned for years of work for steel mills, auto parts suppliers, trucking companies, grocery and department stores, airlines and more. In doing so, the Corporation enhances the retirement security of workers and retirees, and their families across the country.

PBGC runs two programs to insure different types of defined benefit pension plans: single-employer plans and multiemployer plans. These two insurance programs are operated and financed separately. PBGC's mission is to enhance retirement security by preserving plans and protecting pensioners' benefits.

The Corporation strives for excellence in the following areas:

- Preserve plans and protect plan participants and their families.
- Pay benefits accurately and on time.
- Maintain high standards of stewardship and accountability.

This annual performance report outlines PBGC's operations, measures of success, and progress toward achieving our mission.

OPERATIONS IN BRIEF

PBGC strengthens retirement security by preserving plans and protecting plan participants and their families. The corporation guarantees payment of the defined benefit pension benefits, up to the legal limits, earned by nearly 40 million American workers and retirees in nearly 24,000 plans. Since 1974, PBGC has become responsible for more than 1.5 million people in over 4,800 failed single-employer and multiemployer plans. PBGC made benefit payments of $5.8 billion in FY 2016.

To preserve plans and protect plan participants in FY 2016, the Corporation:

- Helped to protect over 55,000 people by taking various actions in the bankruptcy process to encourage companies to keep their plans when they emerged from bankruptcy.
- Reached an agreement that returned two terminated pension plans to the sponsor, required the sponsor to restore full benefits to the plan's 1,350 steelworkers, and mandated back payments to retirees for benefits not guaranteed by PBGC.
- Paid $113 million in financial assistance to 65 insolvent multiemployer plans.
- Through the Early Warning Program, negotiated almost $3 billion in financial assurance to protect more than 367,000 people in plans at risk from corporate events and transactions. These agreements also avoid placing an unnecessary burden on premium payers.
- Conducted compliance reviews of plan sponsor calculations for plans that ended through standard terminations, resulting in almost 940 participants receiving corrected benefit amounts with a value of $4.5 million.

To pay timely and accurate benefits in FY 2016, the Corporation:

- Assumed responsibility for more than 46,000 people in 76 trusteed single-employer plans.
- Started paying benefits to almost 35,000 retirees in single-employer plans.
- Paid $5.7 billion to nearly 840,000 retirees from more than 4,700 failed single-employer plans.

To maintain high standards of stewardship and accountability in FY 2016, the Corporation:

- Achieved an unmodified financial statement audit opinion.
- Reduced the number of open audit recommendations from 163 to 86, a reduction of 47 percent.
- Continued to provide outstanding service to retirees, as demonstrated by a retiree customer satisfaction score of 90 that is among the best public and private sectors, according to the American Customer Satisfaction Index.

STRATEGIC GOALS AND RESULTS

This annual performance report provides information on PBGC's performance in achieving its mission as outlined in its three strategic goals. Performance results for FY 2016 are detailed below.

GOAL NO. 1: PRESERVING PLANS AND PROTECTING PENSIONERS

PBGC engages in activities to preserve plans and protect plan participants by administering two separate insurance programs. The multiemployer program protects over 10 million workers and retirees in about 1,400 pension plans. The single-employer program protects about 30 million workers and retirees in over 22,000 pension plans.

This year, the multiemployer program:

- Paid $113 million in financial assistance to 65 multiemployer pension plans covering the benefits of over 59,000 participants with an additional 27,000 people entitled to benefits once they retire. Ten of the 65 plans became insolvent during FY 2016. These 10 newly insolvent plans cover about 10,000 participants.
- Performed 16 multiemployer plan audits to protect the benefits of more than 14,000 people.

This year, the single-employer program:

- Monitored 1,500 companies for financial transactions that potentially posed risks to the financial viability of plans.
- Protected pensioners whose plan sponsors were in bankruptcy.
- Ensured that participants received the law's full protection in both underfunded and fully funded plan terminations.

MULTIEMPLOYER PROGRAM

A multiemployer plan is a pension plan created through a collective bargaining agreement between employers and a union. The employers are usually in the same or related industries. Multiemployer plans provide benefits for people in several industries, such as transportation, construction, mining, and hospitality. PBGC provides financial assistance to insolvent multiemployer plans, and offers technical assistance to multiemployer plan administrators, service providers and other stakeholders.

The multiemployer insurance program is likely to run out of money by the end of 2025. PBGC is taking steps to improve the financial status of its multiemployer program. For example, PBGC reviews plan termination filings and plan merger notices, and responds to requests for PBGC approval of various transactions under the multiemployer provisions of ERISA's Title IV. In addition, PBGC continues to implement changes mandated by the Multiemployer Pension Reform Act of 2014 (MPRA).

Protecting Pensioners in Multiemployer Plans

PBGC monitors all multiemployer plans that request or receive financial assistance. In FY 2016, the Corporation began providing financial assistance to 10 insolvent multiemployer plans covering about 10,000

participants. Additionally, the Corporation performed 16 audits of multiemployer plans that cover more than 14,000 people and identified 142 findings. The chief objectives of these audits are to ensure:

- Timely and accurate payment of benefits to all plan participants.
- Compliance with laws and regulations.
- Effective and efficient management of the assets remaining in terminated plans.

Multiemployer Plan Partitions and Applications for Benefit Suspensions

MPRA provides more options for sponsors of plans likely to become insolvent when facing funding issues. Certain critical and declining plans that are projected to run out of money, generally within 20 years, may ask PBGC to approve a partition. A partition will transfer responsibility for paying a portion of participants' and beneficiaries' monthly guaranteed benefit amounts to a successor plan that will receive financial assistance from PBGC, relieving the original plan of some of its financial obligations.

In order for a plan to be eligible for a partition, the plan sponsor must show that the plan has taken all reasonable measures to avoid insolvency, including maximum benefit suspensions under the law, and that partition is necessary for the plan to remain solvent. If partition is approved, the original plan will have an ongoing benefit payment obligation to preserve benefits for all participants at levels above PBGC guaranteed amounts over the long term.

Generally, applicants for partitions will also apply to the Treasury Department for a suspension of benefits to 110 percent of the PBGC-guaranteed level, except for age-protected and disability-protected benefits. PBGC plays a consultative role to the Treasury Department for the review of applications for benefit suspensions.

In FY 2016, PBGC received three applications for partition. Of those applications, one was denied and two are currently under review.

Multiemployer Plan Mergers and Transfers

Plan mergers can be a way to help protect people's benefits in multiemployer plans. In general, mergers can broaden a plan's contribution base, reduce administrative and investment expenses for small plans, and rescue troubled plans from projected insolvency. Similarly, transfers of assets and liabilities between plans, often accompanied by a plan merger, can have a healthy impact on all plans involved. Such transfers may result in steady or improved funding to help sustain the plans in the future. In FY 2016, PBGC processed six plan mergers and one transfer of plan assets and liabilities. These transactions were not related to provisions under MPRA.

In FY 2016, PBGC proposed a rule that would implement changes under MPRA and update the plan merger process in general. The proposed rules give PBGC the authority to facilitate plan mergers by providing technical assistance, or financial assistance if necessary, to avoid plan insolvency.

Assistance to Multiemployer Plan Sponsors

PBGC provides technical assistance to multiemployer plan professionals regarding difficult interpretation issues arising under Title IV of ERISA. In 2016, PBGC worked with plan sponsors on how to administer the

payment of Qualified Pre-Retirement Survivor Annuities (QPSA) under the revised rules pursuant to MPRA. That law made QPSA benefits payable to spouses of participants who were alive on the date of plan insolvency or termination. PBGC worked with terminated and insolvent multiemployer plans to ensure the successful payment of these benefits.

SINGLE-EMPLOYER PROGRAM

The single-employer program covers defined benefit pension plans that are sponsored by one employer. When an underfunded single-employer plan terminates, PBGC steps in to provide guaranteed benefits. This typically happens when the employer sponsoring an underfunded plan goes bankrupt or out of business, and can no longer afford to keep the plan going. In this type of termination, PBGC takes over the plan's assets, administration, and payment of plan benefits up to the legal limits. Single-employer plans can also end in a standard termination, provided the plan has enough money to pay all benefits owed to participants.

The single-employer program continues to have a deficit, but given the recent trends in claims and premiums, it is likely to improve over the next decade. Now and in the coming years, PBGC will continue its efforts to protect the interests of single-employer plan participants and beneficiaries.

Protecting Pensioners When Plans Are at Risk

Under the Early Warning Program, PBGC monitored more than 1,500 companies to identify transactions and events that potentially posed risk to the people covered under their pension plans. The Corporation reviewed more than 200 transactions and, where appropriate, arranged agreements for suitable protections to safeguard participant benefits in the following three cases:

- PBGC and Sears finalized an agreement to help protect the Sears pension plan and its nearly 200,000 participants. Sears will continue to protect the assets of certain special purpose subsidiaries, which hold real estate and/or intellectual property assets. The subsidiaries will grant springing liens of up to $2.7 billion on the protected assets in favor of PBGC. The liens will be triggered only by failure to make required contributions to the plan, by prohibited transfers of ownership interests in the subsidiaries, termination of the pension plan, or by bankruptcy of the company or certain subsidiaries.
- PBGC reached an agreement with Alcoa, Inc. in connection with the company's split into two businesses: the mining and commodities business and the value-added business that consists of the multimaterial products and solutions company. Alcoa will make cash contributions totaling $150 million over two years in addition to its required pension contributions. This agreement helps to protect more than 102,000 participants in the pension plans.
- PBGC reached an agreement with Computer Sciences Corporation (CSC) and CSRA Inc., to protect the benefits of more than 23,000 participants. PBGC acted prior to the separation of CSC's public sector consulting practice from its commercial practice, and the merger of the public sector practice with SRA International, Inc. Under the agreement, CSRA now sponsors all of CSC's pension plans. If CSRA's indebtedness does not decline to agreed-upon levels or the company does not achieve investment-grade ratings, CSRA will contribute $100 million to its largest pension plan.

Additionally, each year PBGC receives distress termination applications and identifies abandoned plans. These situations may signify a plan's financial difficulty and often result in plan terminations or settlement agreements.

Protecting Pensioners Whose Employers File for Bankruptcy

PBGC takes an active role in bankruptcies to protect the interests of employees and retirees in the plans. The Corporation works to prevent unnecessary terminations and to obtain the maximum possible financial recovery when a plan must terminate. Examples include:

- PBGC was prepared to terminate HOVENSA's pension plan after the company closed its oil refinery and filed for bankruptcy. However, PBGC worked closely with all stakeholders to reach a resolution that provided for assumption of the pension plan by Hess Corporation, HOVENSA's 50 percent joint-owner. As a result, the plan was not terminated, and its 1,610 participants can expect to receive their promised plan benefits.
- Alpha Natural Resources, Inc., a coal company, filed Chapter 11 bankruptcy on August 3, 2015, in the Eastern District of Virginia. At the time, Alpha sponsored three single-employer plans with a total of 14,794 participants and combined unfunded benefit liabilities of approximately $429 million. PBGC co-chaired the Committee of Unsecured Creditors. In the course of the bankruptcy, several of Alpha's mines were sold to its first-lien lenders and are operating as Contura Energy, Inc. Alpha emerged from bankruptcy on July 26, 2016, and continued sponsorship of its single-employer plans (though it withdrew from the multiemployer UMWA 1974 Pension Plan). Alpha agreed to make a total of $18 million in excess contributions to its single-employer plans, in two equal installments in 2017 and 2018. The excess contributions are part of the bankruptcy plan of reorganization.

Significant Litigation

PBGC protects participants in America's private-sector pensions through litigation in federal and state courts. In June 2016, PBGC restored the RG Steel pension plans to the sponsorship of The Renco Group, Inc. This marks only the second time in PBGC history that terminated plans were restored to an employer.

The restoration followed PBGC's lawsuit against Renco, in which PBGC alleged that Renco had entered into a financing transaction with a principal purpose of evading liability for RG Steel's pension plans. PBGC also alleged that Renco committed fraud against PBGC in connection with that transaction. Less than five months after the transaction, RG Steel liquidated in bankruptcy, and later its pension plans were terminated.

In December 2015, a trial was held, but PBGC and Renco negotiated a settlement prior to the court's decision. In the settlement, Renco agreed to assume the plans, to pay all future benefits promised under the plans, and to make back payments for benefits not guaranteed by PBGC. Renco also agreed to reimburse PBGC for $15 million in benefits paid after the termination, and to pay about $35 million in shutdown benefits to participants that would have gone unpaid absent the plan restoration. Shutdown benefits are early retirement benefits payable to certain participants when a company shuts down its operations.

Protecting Pensioners in Standard Terminations

A company can end a fully funded plan in a standard termination by paying all the benefits it owes. In FY 2016, almost 1,340 plans, covering approximately 193,000 participants, filed standard terminations. The number of standard terminations was consistent with past years and will have minimal effect on PBGC's premium income. Large plans that filed this year include CVS Health Corporation, Inova Health System, Community Hospitals of Indiana, Philips Electronics, Pfizer, Inc., and First American Financial Corporation. Philips Electronics also completed the standard termination process in FY 2016. Other large plans, such as NBC Universal, Acument Global Technologies, Fluor Corporation, Hannaford Brothers, and Fannie Mae, completed previously filed standard terminations. Approximately 1,225 plans with more than 209,000 participants completed standard terminations in FY 2016.

PBGC conducted 260 standard termination audits to verify that plan sponsors properly calculated participants' benefits due to the plan termination. As a result, almost 940 people in these plans received an additional $4.5 million in benefits.

GOAL NO. 2: PAYING TIMELY AND ACCURATE BENEFITS

Nearly 1.4 million current and future retirees in trusteed single-employer pension plans rely on PBGC for their benefits. The benefits administration team is committed to paying their benefits accurately and on time.

Benefit Administration

When a single-employer plan ends without enough money to cover all of its benefit promises, PBGC steps in to become trustee and pay benefits up to legal limits. In FY 2016, PBGC became responsible for more than 46,000 additional workers and retirees in 76 single-employer plans. Nearly 17,000 of these new participants are already retired and continue to receive their benefit every month.

The five largest plans that PBGC trusteed in FY 2016 were sponsored by the Great Atlantic & Pacific Tea Company Inc. (21,069 participants), Freedom Communications (5,214 participants), Southern Regional Health System Inc. (2,759 participants), Walter Energy Inc. (2,722 participants), and the Estate of Vincent Posner (2,101 participants).

PBGC paid $5.7 billion in benefits to almost 840,000 retirees in single-employer plans. In FY 2016, almost 35,000 new retirees applied to begin benefits. The benefit administration team processed over 87 percent of those applications in 45 days or less, an improvement over FY 2015's 80 percent.

The benefit administration team's highest priority is to ensure that existing retirees in newly trusteed plans continue to receive retirement benefits without interruption. In addition, the benefit administration team makes sure that newly eligible retirees who apply for benefits receive them promptly.

PBGC also works hard to make sure that benefits are accurate. Each month, almost 220,000 retirees whose final benefits are being calculated received an estimated benefit amount. Over the last six years, more than 95 percent of our estimated benefits have been within 10 percent of the final benefit amount.

After PBGC becomes trustee of a plan, the benefits administration team begins a complex, multiyear process of valuing the plan's assets, reviewing plan and participant data, and calculating final benefits. Only after this

process is finished can we tell individual participants the exact amount of their benefit. In FY 2016 the benefit administration team informed 67,318 people of their final benefit amounts, including 15,256 participants in the Delphi Salaried Plan and 19,741 in the Delphi Hourly Plan.

PBGC continues to work on calculating final benefits of its largest and oldest plans, including the Delphi plans. Delphi is PBGC's second largest case, and its pension plans present by far the most complex asset structure in the Corporation's history. Processing times have increased due to procedure changes and a reorganization for the Office of Benefits Administration designed to enhance the quality of work products and close audit findings. These improvements will reduce processing times beginning in FY 2018.

Reviews and Appeals

When participants in trusteed single-employer plans disagree with PBGC's determination of their benefit, they have the right to bring their concerns to the attention of the PBGC's Appeals Board. Employers may also appeal certain PBGC determinations. The Appeals Board independently reviews each appeal, and provides a detailed written explanation of its decisions. Historically, approximately 1 percent of benefit determinations are appealed. In FY 2016, the Appeals Board closed 351 appeals, with 217 still open at the end of the year. The Appeals Board statistics for the last ten fiscal years are on PBGC's website.[1]

[1] http://www.pbgc.gov/Documents/PBGC-appeals-datagov.pdf.

GOAL NO. 3: MAINTAINING HIGH STANDARDS OF STEWARDSHIP AND ACCOUNTABILITY

Participant and Plan Sponsor Advocate

The PBGC Participant and Plan Sponsor Advocate, selected by the PBGC Board of Directors, acts as a liaison between PBGC, sponsors of insured defined benefit plans, and participants in PBGC-trusteed plans. The duties of the position include advocating for the full attainment of the rights of participants in trusteed plans and assisting participants and plans sponsors in resolving disputes with the Corporation. The Advocate also identifies areas in which participants and plan sponsors have persistent problems in dealings with PBGC, and may propose changes in PBGC's administrative practices to mitigate problems. The Advocate summarizes requests for assistance and identifies persistent problems, as well as specific legislative and regulatory changes to address such problems, in an annual report to PBGC's congressional committees of jurisdiction, the PBGC Board of Directors, and PBGC's Director.

The Advocate issued her second annual report on December 31, 2015. The report noted progress in handling unusual benefits issues and PBGC's engagement with participant advocacy groups; and expressed optimism that changes in PBGC's leadership will lead to an improved relationship between the corporation and the sponsor community. The Advocate identified areas where improvement could be made, and also recommended the corporation take a fresh look at premium penalties.

Accountability: Measuring and Monitoring Performance

PBGC continuously monitors how well the Corporation does its job and serves customers using a wide range of performance measures. Among them are how quickly and seamlessly the Corporation pays retirees, how accurately PBGC calculates their benefits, and how well the Corporation invests assets. PBGC conducts surveys to help improve the coordination and cooperation essential to meet customer service goals.

Each quarter, PBGC leaders participate in data-driven discussions covering the Corporation's progress in pre- and post-trusteeship operations, stewardship and accountability, customer satisfaction, and building and maintaining a model workplace. The strategic use of performance data better informs planning and execution of operations, as well as corporate and program area decision-making.

TABLE 1: SUMMARY OF PBGC MEASURES AND ACTIVITIES

	Target	2016	2015
Preserve Plan and Protect Pensioners			
People Protected in Plans Emerging From Bankruptcy		55,000	16,000
Standard Termination Audits: Additional Payments		$4.5 M to 940 people	$5.8 M to 1,456 people
Pay Timely and Accurate Benefits			
People Receiving Benefits – Single-employer		840,000	826,000
People to Receive Benefits in Future – Single-employer		559,000	560,000
People Receiving Benefits in Plans Receiving Financial Assistance – Multiemployer		59,000	54,000
People to Receive Benefits in Future in Plans Receiving Financial Assistance – Multiemployer		27,000	25,000
New Retiree On-time Payments	100%	100%	100%
Estimated Benefits Within 10 percent of Final Calculation	95%	96%	96%
Average Time to Provide Benefit Determinations (years)	4.3	6.3	4.8
Improper Payment Rates within OMB Threshold[1]	<1.5%	Yes	Yes
Applications Processed in 45 Days	87%	87%	80%
Maintain High Standards of Stewardship and Accountability			
Retiree Satisfaction – ACSI[2]	90	90	91
Caller Satisfaction – ACSI	83	84	83
Premium Filer Satisfaction – ACSI	73	79	76
Overall Customer Satisfaction[3]	80	73	75
Contract Awards Fully Competed		75%	92%
Financial Surplus (Deficit) – Single-employer		($20.6B)	($24.1B)
Financial Surplus (Deficit) – Multiemployer		($58.8B)	($52.3B)
Unmodified Audit Opinion	Yes	Yes	Yes
Compliance with EEOC Management Directive 715	Yes	Yes	Yes

1 The OMB threshold for significant improper payment reporting is as follows: amounts that exceed (1) both 1.5 percent and $10 million in improper payments, or (2) $100 million in improper payments.
2 The American Customer Satisfaction Index (ACSI) uses a 0-100 scale; 80 or above is considered excellent.
3 Measures customer satisfaction with information and services provided by the corporation.

PBGC'S OWN FINANCES MUST BE SOUND

PBGC's operations are financed by insurance premiums set by Congress and paid by sponsors of defined benefit plans, along with investment income, assets from pension plans trusteed by PBGC, and recoveries from the companies formerly responsible for the plans. PBGC receives no funds from taxpayer dollars. The Corporation pays benefits based on federal law and the provisions of the plans trusteed by PBGC.

Fiscal Deficit

The net financial position remains in deficit for both the single-employer and multiemployer programs. The net financial position of the larger single-employer program is likely, but not guaranteed, to improve over the next decade. Current projections of the single-employer program show a surplus in 2025. The multiemployer insurance program is likely to run out of money by the end of 2025. The single-employer and multiemployer programs are operated and financed separately. Assets from one program cannot be used to support the other program.

Financial Soundness and Financial Integrity

PBGC is responsible for insuring the pensions of tens of millions of people, whose benefits are valued at hundreds of billions of dollars. In addition to collecting premiums, exercising care in the management of about $100 billion in total assets and attaining the 24th consecutive unmodified audit opinion on its financial statements, PBGC stayed focused on improving management in several areas.

Collecting Premiums

In FY 2016, combined premium cash receipts collected totaled $5.5 billion. Single-employer program premium cash receipts collected were $5.2 billion. Separately, multiemployer program premium cash receipts were around $300 million. Premium rates are generally indexed for inflation. In addition, the Bipartisan Budget Act of 2013, the Multiemployer Pension Reform Act of 2014, and the Bipartisan Budget Act of 2015 specify premium rates or premium increases for certain years. In FY 2016, PBGC published a final rule that reduces the late premium payment penalty rates for all plans and waives most of the penalty for plans with a good compliance record that pay promptly after notification of late payment.

Investing Prudently

PBGC investment assets are administered by private investment management firms, subject to PBGC's investment policies and oversight procedures. Procedures for internal controls, due diligence and risk management are subject to periodic review. Regular and detailed communication with management firms enables the Corporation to stay informed on matters affecting its investment program. The following table provides a comparison of PBGC investment performance relative to each composites' respective benchmark. For further information, refer to Section VII. Investment Activities.

TABLE 2: PBGC FY 2016 INVESTMENT RETURNS VERSUS BENCHMARKS

	1-Year Period	3-Year Period	5-Year Period
Total Fund Composite	**10.8%**	**6.2%**	**6.7%**
Total Fund Benchmark[1]	**10.4%**	**6.0%**	**6.4%**
ERISA/ PPA Portfolio Benchmark[2]	**11.2%**	**8.4%**	**11.1%**
Total Global Public Stock	13.5%	6.7%	12.1%
Total Public Stock Benchmark[3]	13.1%	6.4%	11.7%
Total Global Bonds	10.0%	6.3%	4.8%
Total Global Bonds Benchmark[4]	9.6%	6.2%	4.4%

[1] The Total Fund Benchmark is a dynamic weighted benchmark based upon the weights of the Total Global Public Stock Benchmark, the Total Global Bonds Benchmark and the Total Money Market Securities Benchmark. This benchmark is utilized to compare against the Total Fund Composite returns shown above.
[2] The ERISA/PPA Portfolio Benchmark is based upon a hypothetical portfolio with a 60% allocation to the Standard & Poor's 500 equity index and a 40% allocation to the Barclays Capital Aggregate fixed income index. See section VII Investment Activities (The Pension Protection Act of 2006 Reporting Requirement).
[3] The Total Global Public Stock Benchmark is a dynamic weighted benchmark based upon the weights of the U.S. Public Stock composite and the International Public Stock composite and the returns of their respective benchmarks.
[4] The Total Global Bonds Benchmark is a dynamic weighted benchmark based upon the weights of PBGC's fixed income managers and the returns of their respective benchmarks.

Smaller Asset Managers Pilot Program

PBGC implemented a Smaller Asset Managers Pilot Program that creates new opportunities for smaller asset managers to compete for the Corporation's business. Before the pilot program, these contracts were out of reach for smaller asset managers because the minimum required assets under management, often in the billions, was too large for small firms to qualify. In order for firms to be eligible for the pilot program, applicants were required to have a minimum of $250 million in assets under management and a five-year performance history. They also were required to undergo the same competitive evaluation as other PBGC money managers.

In FY 2016, five firms were selected to participate in the pilot program, and each firm will be responsible for investing $175 million in U.S. core fixed-income instruments. PBGC limited its allocations to no more than 20 percent of a firm's assets under management, which is in keeping with industry standards. The firms will be evaluated on their performance, after fees, against the portfolio benchmark over a full market cycle of highs and lows at an acceptable level of risk.

OUTREACH AND CUSTOMER SERVICE

Listening to Customers

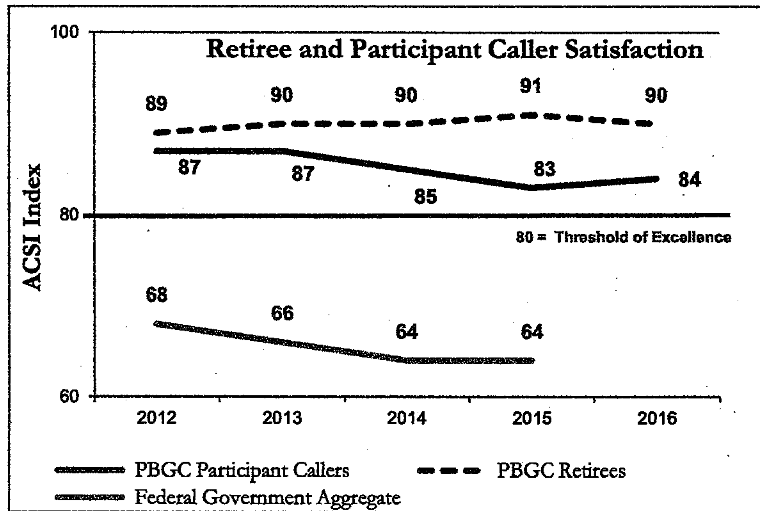
Our customers are at the center of PBGC's mission, and their interests are considered when decisions are made at every level of the organization. PBGC first identifies and prioritizes customer needs through the use

of surveys that assess major processes and communications. The Corporation then sets targets to promote continued improvement in the areas that matter most to our customers.

Telephone Surveys

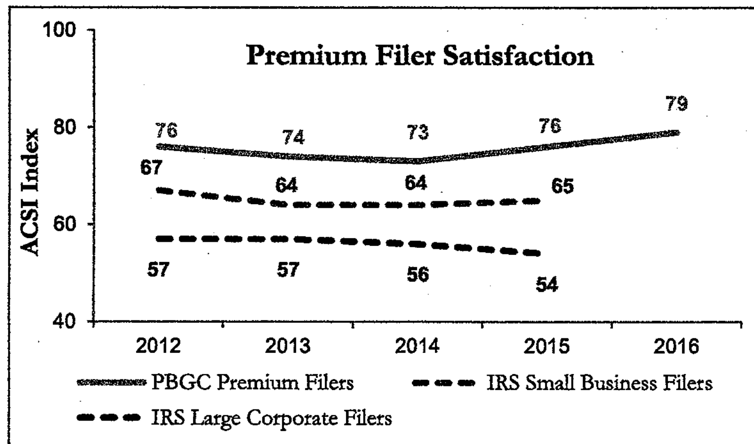
PBGC uses telephone surveys to get feedback from its customers, including retirees, premium filers, and callers to the Corporation's Customer Contact Center. The American Customer Satisfaction Index (ACSI) evaluates PBGC's services to this sector of customers. ACSI surveys use a proven statistical methodology to identify where improvements can be made.

The retiree survey measures satisfaction among retirees who receive monthly benefits from PBGC. This group rated the Corporation's satisfaction at 90 or above for four consecutive years, including a score of 90 in FY 2016. Survey respondents indicated an appreciation of PBGC's dependable and timely payment of their PBGC benefits. In the 2015 ACSI Federal Government Report, PBGC was recognized among government's "satisfaction success stories," with a score higher than the best among private-sector firms.



The participant caller survey measures the satisfaction of pension plan participants who call PBGC's toll-free number. Customers rate their overall experience, including the automated phone system, interactions with representatives, and resolution of their concerns. Other service aspects, such as written communication or the benefit application process, are also evaluated. PBGC exceeded its FY 2016 target of 83, scoring an 84.

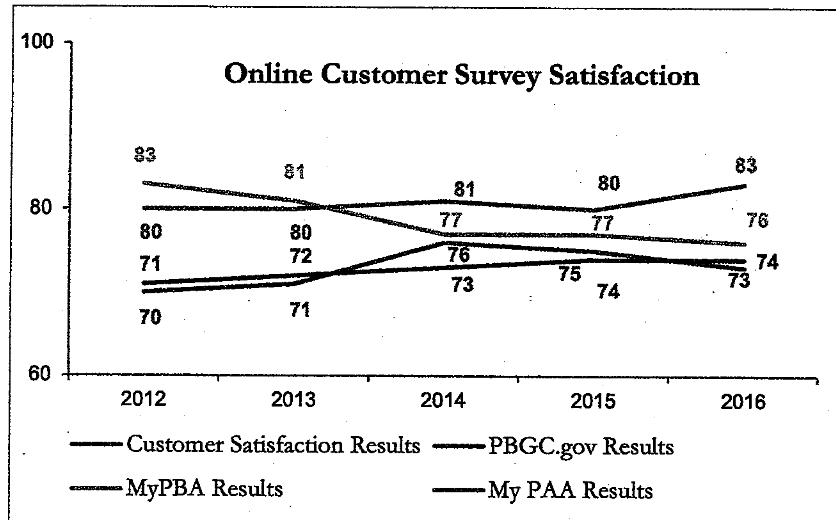
The premium filer survey measures satisfaction among plan sponsors and their representatives who file mandatory annual premiums with PBGC. For the second consecutive year, the premium filer score increased by three points over the previous year's score, achieving a 79 and surpassing the goal of 73. Streamlining of filing requirements in recent years improved the process.



Online Surveys

PBGC conducts four online surveys measuring user satisfaction. These cover:

- Online service for participants using My Pension Benefit Account (MyPBA);
- Online service for practitioners using My Plan Administration Account (My PAA);
- The PBGC.gov website; and
- Overall satisfaction of all customers.



These surveys provide valuable benchmarking insight and track trends in customer satisfaction. Online surveys collect feedback continuously, allowing PBGC to promptly address customer concerns.

Participants use MyPBA to conduct transactions with PBGC, such as applying for benefits, updating their address or banking information, specifying federal tax withholding, or requesting benefit estimates. The MyPBA survey measures satisfaction in areas, such as functionality, look and feel, and plain language. MyPBA incorporated two customer friendly upgrades designed to improve messaging and make it easier for participants to select benefit forms and to file their taxes. The MyPBA satisfaction score is 76, just below its target of 77.

Practitioners use My PAA to file premiums with PBGC. The My PAA survey measures satisfaction covering topics such as navigation and site performance. The satisfaction score is 83, exceeding the target of 79. My PAA implemented upgrades to simplify navigation, improve printing, increase validations that reduce filing errors, and make other usability improvements based on customer feedback.

The PBGC.gov survey measures satisfaction with PBGC's public website, in terms of content and plain language. The website satisfaction score was 74, meeting the target. PBGC is using this customer feedback for a site redesign slated to launch in FY 2017. More specifically, the new site will provide visitors simple search features and easier navigation as well as better visibility for the MyPBA application.

PBGC's customer satisfaction survey takes a broader perspective and measures customer views on how well the Corporation performs its mission. This year, PBGC attained a score of 73, below the target of 80. The Corporation continues to listen to its customers and strives to serve them better. The combination of improvements to the online service tools, the Corporation's website redesign and improved communications with future retirees is expected to have a positive impact on overall customer satisfaction.

Reaching Out to Customers and Stakeholders

PBGC continues to educate and reach out to stakeholders, constituents, and customers about the Corporation's ongoing activities. In FY 2016, PBGC representatives participated in 160 events with plans sponsors, service providers and participant groups. These events involved discussions on topics such as the multiemployer insurance program, actuarial matters and lifetime income.

PBGC holds regular meetings with organizations that represent the interests of pension plan participants such as AARP, the Pension Rights Center, the National Retiree Legislative Network, and various labor organizations. The Corporation regularly communicates with employer and practitioner groups such as the American Society of Pension Professionals and Actuaries, the ERISA Industry Committee, the American Benefits Council, the National Coordinating Committee for Multiemployer Plans, the U.S. Chamber of Commerce, the American Bar Association's Joint Committee on Employee Benefits, and several organizations representing the actuarial profession. These meetings strengthen PBGC's relationships with stakeholders and build on shared goals.

PBGC's blog – *Retirement Matters* – launched a new series titled *Director's Hub.* Written by Director Reeder, the series presents his take on PBGC's activities and his thoughts about preserving pension plans and protecting retirement security. With a 40 percent increase in page views over the prior year, *Retirement Matters* also brings to customers important stories about PBGC and pensions.

The Corporation expanded its online outreach materials on PBGC.gov to ensure that customers have easy access to information, including updated content on the Health Coverage Tax Credit, the Delphi Hourly and Salaried Pension Plans, and PBGC's multiemployer activities. In addition to informing the public through a variety of formats, including press releases and newsletters, PBGC sent over 2 million emails to keep customers and stakeholders informed about the latest developments on pensions and retirement security. All PBGC.gov content complements PBGC's social media outreach, which includes regular postings to Facebook and Twitter.

SUSTAINING THE PROGRAMS

PBGC continuously monitors and reports on its insurance programs and their effectiveness. The model used to accomplish this task is reviewed internally and by outside experts. The Corporation implements strategies to strengthen the programs' financial health and improve its ability to manage risk.

Research and Analysis Activities

PBGC serves as an expert and impartial source of information about pensions and retirement policy. The Policy Research and Analysis Department (PRAD) delivers timely and accurate analysis of PBGC programs and policy alternatives to policy-makers and external stakeholders.

Each year PRAD updates the Pension Insurance Data Book, a compendium of data regarding PBGC and its single-employer and multiemployer insurance programs. As part of its focus on the multiemployer insurance system, this year PBGC added a graphical supplement that illustrates aspects of the multiemployer program in greater detail. The supplement allows users to look at time-series data on the funding status of multiemployer plans as set forth in the Pension Protection Act of 2006. Additional studies on both the multiemployer and single-employer retirement systems are in progress.

Improvements to Pension Insurance Modeling System (PIMS) and Related Reports

PRAD's primary forecasting model is PIMS. In FY 2016, PRAD used the model to issue three major reports: the report due every five years under the Multiemployer Pension Plan Amendments Act of 1980; the annual Projections Report, which outlines the direction of PBGC's single-employer and multiemployer programs; and a special report, required by the Multiemployer Pension Reform Act of 2014 (MPRA), that estimates average premiums needed in order to maintain PBGC solvency for 10- and 20-year periods. Each of the reports, and the PIMS model, has a dedicated page on PBGC's website[1], and PRAD staff performs outreach to a variety of audiences to discuss the future outlook for PBGC's programs.

Outside experts review PIMS, and the model is periodically tested through a congressionally mandated peer review. Completed reviews are publicly available, and PBGC uses reviews to improve PIMS and the Corporation's reports. PBGC also uses PIMS to illustrate the effects of proposed changes to pension law and to provide other technical assistance.

Managing Enterprise Risk

In March 2016, PBGC established an Enterprise Risk Management Council to develop and implement an enterprise risk management framework for PBGC. The framework will help managers, leaders and the Board of Directors assess and mitigate the Corporation's risks. The council is responsible for integrating risk management into the culture and processes of the corporation, leveraging existing work where possible. It also works to develop the Corporation's risk profile and advises leadership on plans to deal with strategic risks. PBGC created and posted a vacancy for a Risk Management Officer and is interviewing applicants.

Regulatory Activities

PBGC continues to issue regulations to protect plan participants and minimize burdens on pension plans and plan sponsors. In FY 2016, PBGC published:

- A proposed rule to expand the Missing Participants Program to cover defined contribution plans. The Missing Participants Program helps plans by providing alternatives for dealing with the benefits of missing participants on plan termination, letting plans transfer the benefits to PBGC instead of establishing an individual retirement account at a financial institution for each missing participant account. The program helps participants who lose touch with their plans because PBGC will add the missing participant to its online searchable database – making it easier for people to find their accounts – and also will periodically search for the participant.
- A proposed rule to facilitate multiemployer plan mergers. This rule implements statutory procedures that give PBGC new authority to facilitate mergers among seriously underfunded plans. Such mergers can improve plans' ability to survive and continue paying benefits to participants.
- A final rule to reduce penalties for late payment of premiums. Smaller penalties reduce the cost of maintaining plans and encourage their continuance.

[1] http://www.pbgc.gov/about/projections-report/pension-insurance-modeling-system.html

- A final rule on annual reporting for controlled groups with serious plan underfunding. Under the rule, plans that seek a reporting waiver must determine their aggregate underfunding by using unstabilized interest rates that have not been adjusted to IRS-determined corridors. The rule adds new reporting waivers for smaller plans and for plans that must file solely because of large missed contributions or funding waiver applications previously reported to PBGC. It also provides alternative ways to report certain actuarial information.
- A final rule that makes minor changes to the interim final rule on multiemployer plan partitions that PBGC issued in FY 2015 to take account of public comments.

STRENGTHENING A DIVERSE WORKFORCE AND LEADERSHIP

In an effort to improve organizational performance and ensure proper alignment within the Corporation, PBGC successfully implemented the reorganizations of five mission critical departments and began preparing for a potential wave of retirements. With 36 percent of its workforce eligible to retire in the next five years, PBGC has increased succession planning efforts throughout the Corporation. PBGC began developing departmental succession plans that address not just mission critical positions, but also all key positions as identified by management, back-ups for key positions, roles and responsibilities of key positons, and knowledge transfer strategies to prevent a loss of institutional knowledge.

Federal Employee Viewpoint Survey

The Federal Employee Viewpoint Survey (FEVS) provides a confidential and voluntary method for PBGC federal employees to share honest and candid feedback about the Corporation's work environment, work-life balance programs, and other aspects of the Corporation. The survey also provides an opportunity for employees to influence positive change in their workplace. All federal employees are encouraged to take the survey and have their voice heard. In FY 2016, 65 percent of PBGC's federal employees participated in the survey. This rate of participation is significantly higher than the government-wide participation rate of 46 percent.

According to the survey results, PBGC has an engaged workforce. Our 2016 FEVS engagement score is 72 percent, the Corporation's highest score yet. The engagement score measures responses to questions on how well leaders lead, the interpersonal employee/supervisor relationship, and the level of employee motivation related to their role in the workplace. PBGC exceeded its engagement score target of 69 percent, as well as the government-wide target of 67 percent.

PBGC's leaders use the feedback from the FEVS to gain valuable insight into the concerns of PBGC's greatest asset, its workforce. Reviewing the survey results is one of the ways the Corporation's leaders identifies PBGC's strengths and challenges. This year's survey results can be found on PBGC.gov.

Diversity and Inclusion

According to FEVS, 63 percent of PBGC employees believe that the Corporation's policies and programs promote diversity in the workplace. In its second year, PBGC's Diversity and Inclusion Council is one of these programs that promotes dialogue across the Corporation on diversity and inclusion priorities. The council consists of senior-level management, affinity groups and the Independent Union of Pension

Employees for Democracy and Justice. The group met monthly to identify and promote diversity and inclusion practices in a variety of areas, including recruitment, communication, and employee engagement.

This year, the council partnered with Morgan State University's Summer Academy of Mathematics and Science Program to host a day-long event that introduced high school students to the field of actuarial science and PBGC. The students engaged in hands-on activities to learn more about PBGC as a career option and the career path needed for actuarial science. The council also expanded its employee engagement practices by participating in a community day where staff learned more about the Corporation's diverse affinity groups.

Management and Leadership Training

PBGC introduced a new service that offers a variety of assessments for individuals, teams and organizations. The assessments provide insight into such dimensions as leadership, conflict management, emotional intelligence, team functioning and organizational culture. This service provides opportunities for self-awareness and a better understanding of the impact on others – two main objectives for leadership development.

Records Management Training and Workshops

The National Archives and Records Administration (NARA) recognized PBGC as a leader in federal records management training. In November 2015, NARA reported that PBGC created online records management training and workshops that engage different areas of the Corporation in meeting records management requirements.

SAFEGUARDING CUSTOMER INTERESTS

Strengthening E-Government and Information Technology

While maintaining a sound security posture, PBGC continued to refine its strategy to modernize its information technology (IT) platform. PBGC updated its IT infrastructure program planning process to include procedures for end of serviceable life technology management and established a security requirements checklist utilized for all IT acquisitions. The procedures and checklist will ensure that acquired IT hardware, software, and professional services comply with PBGC and federal policy requirements. As a result of changes noted by the Inspector General's independent auditor in late 2015, two material weaknesses were downgraded to significant deficiencies – entity-wide security program planning and management, and access controls and configuration management. In addition, during FY 2016, PBGC's Office of Information Technology completed a vast number of initiatives, including:

- Enforcement of personal identification verification card usage for logical access for all users, expanded from just privileged users in the previous year.
- Acquisition of identity and access management services that will ultimately establish an enterprise identity management platform for the Corporation.
- Migration to Skype for Business on the Microsoft Office 365 cloud, migration of all electronic mail to the Microsoft Office 365, and migration of each individual's home directory content to the OneDrive for Business component of the Microsoft Office 365 cloud in response to the Cloud First initiative.

- Reduction of access to participant privacy data by masking sensitive data in development environments and test environments.
- Relocation of Service Desk staff to a facility in Colorado to improve service and efficiency.

Ensuring Ethical Practices

The U.S. Office of Government Ethics (OGE) conducted an inspection of PBGC's ethics program. The inspection's purpose was to collect and assess the program's compliance data and to identify and mitigate program vulnerabilities. OGE found that the program complied with its requirements and made only one recommendation for PBGC to ensure timely notification of financial disclosure report filing requirements for new entrant confidential reports. After conducting a follow-up review and determining that PBGC had taken sufficient action to resolve the concern underlying the one recommendation, OGE officially closed its review of the ethics program.

In FY 2016, PBGC continued to ensure that new employees received ethics training within 90 days of their date of hire. All financial-disclosure filers and agency-designated employees received annual ethics training by the end of the fiscal year. In advance of OGE requirements, the ethics program required all public financial disclosure report filers to use OGE's electronic filing system, *Integrity*, at the start of the fiscal year. PBGC also developed and provided agency-wide training on the Hatch Act, a federal statute that limits federal employee participation in partisan political activity.

Protecting Privacy Interests

Among PBGC's highest priorities is protecting the personal information of its participants, beneficiaries, employees and contractors. In FY 2016, the Corporation's privacy team reviewed PBGC systems to optimize the confidentiality, integrity, and availability of the information PBGC maintains. In addition to mandatory Privacy Awareness Training for new hires and annual refresher training for current employees and contractors, the privacy team hosted its sixth annual Privacy Week. This multi-day event offered training, information about hot topics in the privacy field, Q&A sessions, and a guest speaker. The privacy team also reached out to other work units within the Corporation to provide role-based training on handling personally identifiable information.

Strengthening Transparency and Disclosure

PBGC continues to promote compliance with the Freedom of Information Act (FOIA) and the Privacy Act through the efficient use of technology and human capital management. The Corporation ended FY 2016 with no backlog of FOIA requests. The disclosure team's compliance goal received support across the Corporation, resulting in streamlined processes and decreased processing times. The average processing time for all requests, including simple, complex and special project cases, is seven working days – 13 days less than the 20-day statutory time requirement.

INDEPENDENT EVALUATION OF PBGC PROGRAMS

PBGC programs are regularly subjected to independent evaluations that help the Corporation remain true to its mission and accountable for services provided to the public. PBGC continues to work to strengthen controls over operations, financial reporting, and compliance with laws and regulations.

Office of Inspector General (OIG)

PBGC places a strong emphasis on diligently addressing the OIG's audit recommendations. To facilitate timely completion and closure of such recommendations, regular status reports are issued to executive management to assist in monitoring corrective actions, particularly those relating to material weaknesses and significant deficiencies. Once work on recommendations is completed, evidence documenting the corrective actions taken is provided for OIG review.

PBGC is committed to addressing the related OIG recommendations in a timely manner. During FY 2016, PBGC reduced the number of open OIG recommendations from 163 to 86, representing a significant reduction from prior years. PBGC closed 16 recommendations related to the two material weaknesses, Entity Wide Security and Access Controls/Configuration Management. As a result, these material weaknesses were reduced to significant deficiencies. In addition, PBGC closed seven recommendations regarding the Present Value of Non-recoverable Future Financial Assistance significant deficiency.

PBGC's OIG oversaw the annual financial statement audit completed by an independent public accounting firm, CliftonLarsonAllen LLP. In addition, during FY 2016 the OIG performed other audits and evaluations, including the following:

- Audit of the Effectiveness of PBGC's Governance of Internal Control (AUD-2016-8): In this report the OIG made three recommendations regarding PBGC's Internal Control Committee activities, agency risk assessment processes, and documentation practices for assessments supporting assurance statements under the Federal Managers' Financial Integrity Act. PBGC management agreed to implement each of the OIG's recommendations.
- Audit of PBGC's Fiscal Year 2015 Compliance with Improper Payments Information Act Requirements (AUD-2016-09): For 2015, PBGC performed a risk assessment of the Benefit Payments and Premium Refunds Payment streams based on risk factors included in Appendix C of OMB Circular A-123. PBGC concluded that neither program was susceptible to significant improper payments. In FY 2016, the OIG confirmed that PBGC had complied with applicable improper payment reporting requirements.
- Fiscal Year 2015 Cybersecurity Act Evaluation (Eval-2016-10): The OIG performed an assessment analyzing PBGC's information security policies, practices and procedures governing computer systems that contain personally identifiable information (PII). The OIG did not identify any recommendations.

For more information about OIG's work in promoting accountability in PBGC operations, visit OIG.PBGC.gov.

Government Accountability Office (GAO)

PBGC's single-employer and multiemployer insurance programs remain on GAO's biennial "high-risk" list of 30 government programs most at risk due to vulnerabilities. This status is due to long-term structural

challenges relating to funding of defined benefit pension plans and the limited tools available to the Corporation to address PBGC's long-term financial stability.

PBGC also monitors progress in addressing GAO recommendations. As of September 30, 2016, PBGC had two open GAO recommendations relating to past reviews with one recommendation having been reported to GAO as being complete. PBGC is considering corrective actions to address the remaining recommendation.

For more information about GAO work on pensions and retirement security issues, visit GAO.gov.

FINANCES

FISCAL YEAR 2016 FINANCIAL STATEMENT HIGHLIGHTS

The Pension Benefit Guaranty Corporation (PBGC or the Corporation) is a federal corporation established under the Employee Retirement Income Security Act (ERISA) of 1974, as amended. It guarantees payment of basic pension benefits earned by nearly 40 million of America's workers and retirees participating in nearly 24,000 private-sector defined benefit pension plans. The Corporation receives no funds from general tax revenues. Operations are financed by insurance premiums set by Congress and paid by sponsors of defined benefit plans, investment income, assets from pension plans trusteed by PBGC, and recoveries from the companies formerly responsible for the plans.

FINANCIAL POSITION

PBGC Combined Financial Position

PBGC's combined net position decreased by $3,064 million, increasing the Corporation's combined deficit to $79,413 million as of September 30, 2016, a record loss, from $76,349 million as of September 30, 2015. This is largely due to pension liability valuation interest factors decreasing for both insurance programs, the select interest rate factor decreased by 53 basis points to 2.27% at September 30, 2016, from 2.80% at September 30, 2015, and the ultimate factor for both insurance programs decreased to 2.14% at September 30, 2016 (after the first 20 years) from 2.86% at September 30, 2015 (after the first 25 years). The overall FY 2016 impact of the change in interest factors was $12,542 million and consists of $6,141 million from multiemployer probable plans, $6,301 million from terminated single-employer plans, and $100 million from insolvent multiemployer plans. Another factor driving the combined loss is the addition of over $6,300 million for the 11 plans added to PBGC's inventory of multiemployer plans requiring financial assistance currently or in the future. Charges were partially offset by $8,791 million in investment income and $6,686 million in premium and other income.

Multiemployer Financial Position

- The multiemployer program's net position declined by $6,549 million, increasing its deficit to $58,833 million, an all-time high for the multiemployer program. PBGC's recently issued FY 2015 Projections Report indicates that the program's risk of insolvency rises over time, exceeding 50 percent in 2025. The risk of insolvency rises rapidly over the following 10 years, reaching over 90 percent by the end of FY 2035. When the program becomes insolvent, PBGC will be unable to provide financial assistance to pay the full level of guaranteed benefits in insolvent plans.
- The $6,549 million increase in the multiemployer program's deficit is primarily due to newly identified probable plans and decreases in interest factors offset by changes in assumptions regarding the percentage of benefits that would be guaranteed upon the insolvency of a plan. Losses from financial assistance in insolvent and probable plans were $6,768 million. The primary factors for this loss are the addition of 10 new probable plans with net claims of $6,332 million (which represent 10 of the 11 new additions to PBGC's multiemployer inventory), and charges resulting from the change in interest factors of $6,141 million for previously identified multiemployer probable plans, offset by gains due to change in the guaranteed factor of $4,051 million. Losses for insolvent plans (i.e., plans currently receiving financial assistance) included $100 million due to the change in interest factors and $56 million due to expected interest on accrued liabilities. Other factors that contributed to the multiemployer program's deficit are

charges of $39 million for administrative expenses and $11 million in actuarial adjustments, offset by $282 million in net premium income and $143 million in investment income.

Single-Employer Financial Position

- The single-employer program's net position increased by $3,485 million, decreasing the program's deficit to $20,580 million. The primary factors in the single-employer program's net gain of $3,485 million included $8,648 million in investment income, $6,404 million in net premium income and other income, and $417 million credit from completed and probable terminations. These factors were offset by charges of $6,301 million due to a reduction in interest factors, $2,929 million charge due to expected interest on accrued liabilities, $2,285 million from actuarial adjustments, and $469 million of administrative, investment, and other expenses.

INVESTMENTS

- PBGC's Total Fund Composite (excluding transition accounts) returned 10.8% in FY 2016, exceeding the Total Fund Benchmark return of 10.4%. FY 2016 investment returns contributed to a total PBGC combined investment income of $8,791 million.
- Due to higher fixed income returns in FY 2016 (10.0% return for Total Global Bonds versus 2.2% in FY 2015), global fixed income market returns generated a gain of $5,923 million from fixed income investments compared to a $1,113 million gain for FY 2015. Due to an increase in equity returns in FY 2016 (13.5% return for Total Global Public Stock versus a negative 3.6% in FY 2015), global equity market returns generated $2,768 million of investment income from equity investments compared to a loss of $1,231 million for FY 2015.

OPERATIONS

- PBGC's combined single-employer benefit payments and multiemployer financial assistance were $5,772 million in FY 2016 and $5,673 million in FY 2015. PBGC assumed responsibility for the benefit payments of an additional 46,000 workers and retirees in the 76 single-employer plans that were trusteed during FY 2016.
- FY 2016 combined net premium income increased by $2,311 million to $6,661 million compared to FY 2015 net premium income of $4,350 million. The primary components of the combined net premium income are: (a) variable-rate premium (VRP) generated income of $4,639 million, and: (b) flat-rate premium income of $2,026 million. Overall, this represented a 50% year-to-year increase in combined premium income and is largely due to the increase in premium rates and higher levels of plan underfunding.
- During FY 2016, PBGC assumed financial responsibility for 67 underfunded single-employer plans that were terminated. Some of these plans are pending the completion of a trusteeship agreement with PBGC as of year-end and are being administered by interim trustees. Because of PBGC's previous efforts to evaluate its exposure to probable terminations, $382 million of the net claims for these plans were already reflected in PBGC's FY 2015 results. These 67 terminated plans had an average funded ratio of about 58%, and these terminations resulted in an aggregate net loss to PBGC of $975 million (see Note 12).

- Three single-employer plans with underfunding of $249 million were newly classified as probable terminations in FY 2016 representing PBGC's total single-employer probable inventory. Probable terminations represent PBGC's best estimate of claims for plans that are likely to terminate in a future year.
- The present value of multiemployer nonrecoverable future financial assistance of $61,009 million consists of 65 insolvent plans ($2,139 million), 63 terminated plans not yet insolvent but probable ($1,986 million), and 40 ongoing plans which are projected to exhaust plan assets within 10 years and are classified as probable ($56,884 million) (see Note 7).

ESTIMATES OF REASONABLY POSSIBLE CONTINGENCIES

- At fiscal year-end, PBGC's estimate of its single-employer reasonably possible exposure increased to $223,275 million in FY 2016, a $5,576 million increase compared to $217,699 million into FY 2015. This increase is primarily due to an increase in the number of companies meeting the reasonably possible criteria.
- PBGC's estimate of its multiemployer reasonably possible exposure decreased to $19,485 million in FY 2016, a $472 million decrease from the $19,957 million in FY 2015. The primary reason for the decrease in liability was due to changes in the data and underlying assumptions.

(Dollars in millions)		FY 2016		FY 2015
Insurance Activity				
SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS COMBINED				
Single-employer Benefits Paid	$	**5,659**	$	5,570
Multiemployer Financial Assistance Paid	$	**113**	$	103
Retirees Receiving Benefits (at end of year)		**898,000**		880,000
Total Participants Receiving or Owed Benefits (at end of year)		**1,485,000**		1,473,000
New Underfunded Terminations		**67**		69
Terminated/Trusteed Plans (combined to date)		**4,779**		4,716
Plans That Have Received Financial Assistance		**65**		57
Summary of Operations				
SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS COMBINED				
Premium Income, Net	$	**6,661**	$	4,350
Losses (credits) From Completed and Probable Terminations	$	**(417)**	$	(780)
Losses From Financial Assistance	$	**6,768**	$	9,963
Investment Income	$	**8,791**	$	392
Actuarial Charges and Adjustments	$	**11,682**	$	9,639
Financial Position				
SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS COMBINED				
Total Assets	$	**99,546**	$	87,659
Total Liabilities	$	**178,959**	$	164,008
Net Income (Loss)	$	**(3,064)**	$	(14,577)
Net Position	$	**(79,413)**	$	(76,349)
SINGLE-EMPLOYER PROGRAM				
Total Assets	$	**97,342**	$	85,735
Total Liabilities	$	**117,922**	$	109,800
Net Income (Loss)	$	**3,485**	$	(4,727)
Net Position	$	**(20,580)**	$	(24,065)
MULTIEMPLOYER PROGRAM				
Total Assets	$	**2,204**	$	1,924
Total Liabilities	$	**61,037**	$	54,208
Net Income (Loss)	$	**(6,549)**	$	(9,850)
Net Position	$	**(58,833)**	$	(52,284)

FINANCIAL SUMMARY–SINGLE-EMPLOYER PROGRAM

(Dollars in millions)		Fiscal Year Ended September 30,								
	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Insurance Activity:										
Benefits paid	$ **5,659**	5,570	5,522	5,449	5,384	5,340	5,467	4,478	4,292	4,266
Participants receiving monthly benefits at end of year [1]	**838,493**	825,666	812,608	799,210	781,160	775,300	747,530	743,610	640,070	631,130
Plans trusteed and pending trusteeship by PBGC[2]	**4,769**	4,706	4,640	4,557	4,446	4,292	4,140	3,993	3,850	3,783
Summary of Operations:										
Premium income, net [3]	$ **6,379**	4,138	3,812	2,943	2,642	2,072	2,231	1,822	1,340	1,476
Other income	$ **25**	11	22	38	13	17	30	16	23	55
Investment income (loss)	$ **8,648**	324	6,439	2,741	8,792	3,446	7,594	6,330	(4,164)	4,737
Actuarial charges and adjustments (credits)	$ **11,515**	9,504	1,864	3,054	14,874	6,561	9,421	13,901	(4,813)	346
Losses (credits) from completed and probable terminations	$ **(417)**	(780)	(115)	468	2,006	201	509	4,234	(826)	399
Administrative and investment expenses	$ **465**	446	464	434	443	424	449	417	400	378
Other expenses	$ **4**	30	17	5	-	21	(7)	15	5	114
Net income (loss)	$ **3,485**	(4,727)	8,043	1,761	(5,876)	(1,672)	(517)	(10,399)	2,433	5,031
Summary of Financial Position:										
Cash and investments	$ **89,596**	80,090	81,215	77,881	76,941	71,292	69,150	62,062	51,722	61,122
Total assets	$ **97,342**	85,735	88,013	83,227	82,973	78,960	77,463	68,736	64,612	67,241
Present value of future benefits	$ **113,704**	106,926	102,774	105,018	105,635	92,953	90,022	83,035	59,996	69,235
Net position	$ **(20,580)**	(24,065)	(19,338)	(27,381)	(29,142)	(23,266)	(21,594)	(21,077)	(10,678)	(13,111)

1) This measure may differ from yearly performance numbers reported in PBGC's Annual Performance Report, which also include participants whose benefit payments ended during the year (for example, due to death or a final lump-sum payout).
2) These cumulative measures may differ due to plans that terminated in a prior year may have been removed from inventory in a subsequent year.
3) Beginning in FY 2009, PBGC started to reflect premium income net of bad debt expense for premium, interest and penalties.

As a general note, a dash "-" indicates no net activity to be reported.

FINANCIAL SUMMARY–MULTIEMPLOYER PROGRAM

(Dollars in millions)		Fiscal Year Ended September 30,									
		2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Insurance Activity:											
Financial assistance paid	$	**113**	**103**	97	89	95	115	97	86	85	71
Plans that have received financial assistance		**65**	**57**	53	44	49	49	50	43	42	36
Summary of Operations:											
Premium income, net [1]	$	**282**	**212**	122	110	92	92	93	95	90	81
Other income	$	**-**	**-**	-	-	-	-	-	2	-	-
Investment income (loss)	$	**143**	**68**	75	(96)	91	148	183	121	121	23
Actuarial charges and adjustments	$	**167**	**135**	95	41	164	99	-	-	(1)	-
Losses (gains) from insolvent and probable plans - financial	$	**6,768**	**9,963**	34,260	2,969	2,466	1,461	831	614	(271)	319
Administrative and investment expenses	$	**39**	32	18	25	20	14	12	-	-	-
Net income (loss)	$	**(6,549)**	(9,850)	(34,176)	(3,021)	(2,467)	(1,334)	(567)	(396)	482	(216)
Summary of Financial Position:											
Cash and investments	$	**2,037**	**1,768**	1,701	1,715	1,804	1,725	1,613	1,441	1,318	1,196
Total assets	$	**2,204**	**1,924**	1,769	1,719	1,807	1,739	1,628	1,459	1,327	1,197
Present value of future benefits	$	**-**	**-**	-	-	1	1	1	1	1	2
Nonrecoverable future financial assistance, present value	$	**61,009**	54,186	44,190	9,931	7,010	4,475	3,030	2,296	1,768	2,124
Net position	$	**(58,833)**	(52,284)	(42,434)	(8,258)	(5,237)	(2,770)	(1,436)	(869)	(473)	(955)

1) Beginning in FY 2009, PBGC started to reflect premium income net of bad debt expense for premium, interest and penalties.

As a general note, a dash "-" indicates no net activity to be reported.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL POSITION

I. INTRODUCTION

PBGC management believes its discussion and analysis of its financial statements and other statistical data will help all interested parties and readers better understand PBGC's financial condition and results of operations. Readers should consider this material in conjunction with the Annual Performance Report starting on page 1, the financial statements beginning on page 54, and the accompanying notes beginning on page 58.

II. FINANCIAL AND PROGRAM RISKS

As of September 30, 2016, the single-employer and multiemployer programs reported deficits of $20,580 million and $58,833 million, respectively. The multiemployer program's net position declined by $6,549 million, increasing its deficit to $58,833 million, a record high for the multiemployer program. Notwithstanding these deficits, the Corporation has about $97,342 million in single-employer assets and $2,204 million in multiemployer assets and will be able to meet its obligations for a number of years. However, it is not certain that either program at present has the resources to fully satisfy PBGC's long-term obligations. For example, the multiemployer program is projected to likely exhaust its assets by 2025 (Please refer to Section V Overall Capital and Liquidity).

In FY 2017, significant factors beyond PBGC's control (including the performance of financial markets, changes in interest rates, plan contributions made by sponsors, and recently enacted statutory and regulatory changes) will continue to influence PBGC's underwriting income and investment gains or losses. PBGC's best estimate of FY 2017 premium receipts ranges between $7,100 million and $7,400 million. No reasonable estimate can be made of FY 2017 terminations, effects of changes in interest rates, or investment income.

PBGC's operating results can change markedly from year to year depending on the severity of losses from plan terminations, investment performance, changes in the interest factors used to discount future benefit payments, general economic conditions, changes in law, and other factors. PBGC's operating results may vary more than those of most private insurers, in part because PBGC must insure against catastrophic risk without all the tools private insurers use to address risk. Most private insurers can diversify or reinsure their catastrophic risks or apply traditional insurance underwriting methods to these risks. Unlike private insurers, the Corporation cannot decline insurance coverage regardless of the potential risk posed by an insured. Private insurers can also adjust premiums in response to risk. PBGC cannot. PBGC's premiums are defined by statute and Congress must approve any premium changes.

Claims against PBGC's insurance programs vary greatly from year to year. A single large pension plan termination or insolvency may result in a larger claim against the Corporation than the termination or insolvency of many smaller plans. So, future claims will continue to depend largely on the rare and unpredictable failures of a few very large plans. Additionally, PBGC's risks are concentrated in certain industries. Finally, PBGC's financial condition is also sensitive to market risk. Interest rates and equity returns affect not only PBGC's own assets and liabilities but also those of PBGC-insured plans.

III. LEGISLATIVE AND REGULATORY DEVELOPMENTS

BIPARTISAN BUDGET ACT OF 2015

Premiums The Bipartisan Budget Act of 2015 (P.L. 114-74), signed into law on November 2, 2015, increases PBGC single-employer premiums beginning with the 2017 plan year and accelerates the premium due date for the 2025 plan year. PBGC posts premium rates on its website.

- The single-employer annual flat-rate premium replaces increases for inflation with specific dollar amounts for 2017-2019. These amounts increase the 2016 premium of $64 per participant to $69 for 2017, $74 for 2018, and $80 for 2019. Subsequently, the amount will be indexed for inflation.
- The variable-rate premium, which is $30 per $1,000 of unfunded vested benefits for 2016, will continue to be indexed for inflation, plus increase by an additional $3 for 2017, $4 for 2018, and $4 for 2019.
- The premium due date for the 2025 plan year for single-employer and multiemployer plans is accelerated by one month for most plans. For example, the due date for calendar-year plans will be September 15, 2025, rather than October 15.

Minimum Funding. The new law extends for three years temporary provisions of current law that constrain interest rates used to value liabilities for purposes of calculating minimum required contributions. The 10 percent corridor around the 25-year average segment rates will remain in effect through 2020 (three additional years) and then will widen in 5 percent increments — to 15% for 2021, 20% for 2022, 25% for 2023, and 30% for 2024 and later plan years. The law also modifies the provision that allows plans to replace standard mortality assumptions for plan funding when the plans are large enough to have credible mortality experience. Smaller plans would be allowed to adjust the standard mortality tables to the extent they have credible mortality experience.

REGULATORY REVIEW AND REFORM

In 2011, the President issued Executive Order 13563, "Improving Regulation and Regulatory Review," for agencies to consider the benefits and costs of regulations. In response, PBGC continues to focus on making regulations work better to protect plan participants and reduce burdens on pension plans and plan sponsors.

Fiscal year 2016 saw PBGC take an important step toward both these goals with the publication of a proposed rule on missing participants in response to congressional authorization to expand PBGC's existing Missing Participants Program to cover terminated individual account plans (such as "401(k) plans"). The expanded program will offer such plans the opportunity to provide their missing participants protections like those already afforded to missing participants in terminated PBGC-insured plans — a listing of missing participants on PBGC's website and no annual fees to eat away at benefit values. In addition, the proposal simplifies benefit valuation procedures for terminated insured plans with missing participants. PBGC is seeking public comment on its proposal and plans to have the expanded program operational in 2018. The program is designed to cover terminated small professional service pension plans and multiemployer plans as well.

On the multiemployer plan front, PBGC in FY 2016 issued a final rule to fine-tune the interim final rule on multiemployer plan partitions that it issued in FY 2015, and a proposed rule to facilitate multiemployer plan

mergers. PBGC is now considering the comments received on its merger proposal. These complementary regulations (on dividing and combining plans) implement MPRA, enacted in FY 2015. Together they seek to improve plans' ability to survive and continue paying participants' benefits.

PBGC took the initiative in FY 2016 to re-examine the penalties it charges for the late payment of premiums, and the result was a final rule providing substantial penalty relief. Premium penalties are tied to the amount of premium paid late, and Congress has raised premiums significantly over the years. As a result, penalties have grown proportionally. PBGC reviewed its experience with premium penalties and concluded that it could reduce penalties and still reasonably expect a satisfactory level of compliance. Accordingly, PBGC changed its premium payment regulation to cut late payment penalties in half. PBGC went further and established a new 80-percent penalty waiver for plans with good premium compliance histories that correct underpayments promptly after notification by PBGC.

Also in fiscal year 2016, PBGC issued a final rule on annual reporting for controlled groups with serious plan underfunding. Under the rule, a determination of whether aggregate plan underfunding is low enough to qualify for a reporting waiver must be made using recent market interest rates rather than rates used under minimum funding rules which reference long-term averages. The rule also adds new reporting waivers for smaller plans and for plans that must file solely because of large missed contributions or funding waiver applications previously reported to PBGC. It also provides alternative ways to report certain actuarial information.

IV. DISCUSSION OF INSURANCE PROGRAMS

PBGC operates two separate insurance programs for defined benefit plans. PBGC's single-employer program guarantees basic pension benefits when underfunded plans terminate. By contrast, in the multiemployer program, the insured event is plan insolvency. PBGC's multiemployer program financially assists insolvent covered plans to pay benefits at the level the law guarantees.

By law, the two programs are funded and administered separately and their financial conditions, results of operations, and cash flows are reported separately. The accompanying financial statements for both programs, which appear on pages 54-57, have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). Please refer to Note 2: "Significant Accounting Policies" for further detail, including a description of PBGC's valuation method used in determining benefit liabilities.

IV.A SINGLE-EMPLOYER PROGRAM RESULTS OF ACTIVITIES AND TRENDS

The single-employer program covers about 28.4 million people (excluding those in plans that PBGC has trusteed), down from the 29.8 million people PBGC covered in 2015. The number of covered ongoing plans increased from about 22,200 in 2015 to about 22,300 in 2016.

Plans that were terminated in a standard termination had sufficient funding to cover future benefits and distributed all plan benefits as insurance company annuities or lump sums pursuant to the standard termination rules of ERISA. In these cases, PBGC's activities are limited to ensuring compliance with standard termination regulations.

In contrast, PBGC becomes trustee when a covered underfunded plan terminates. PBGC applies legal limits to payouts and pays the benefits. To determine the amount to pay each person, PBGC takes into account (a) the benefit that the participant had accrued in the terminated plan, (b) the availability of assets from the terminated plan to cover benefits, (c) how much PBGC recovers from employers for plan underfunding, and (d) the limits on guaranteed benefits provided under ERISA. The guarantee limits are indexed (i.e., they increase in proportion to increases in a specified Social Security wage index) and vary based on the participant's age and elected form of payment.

Because of indexing, the guarantee limits for plans that fail in calendar year 2017 will be 7.1% higher than the limits that applied for 2015 and 2016 as shown below for sample ages:

Maximum Guaranteed Annual Benefit Payable as a Single Life Annuity

Age	Plans Terminating in 2015 and 2016	Plans Terminating in 2017
70	$99,826	$106,957
65	$60,136	$64,432
60	$39,089	$41,881
55	$27,061	$28,994

The guarantee limit is a cap on what PBGC guarantees, not on what PBGC pays. In some cases, PBGC pays benefits above the guarantee limit.

The applicable maximum guarantee is determined by the year the retiree's plan terminated (or, if the plan terminated during the plan sponsor's bankruptcy, the year the sponsor entered bankruptcy), even if the retiree does not begin collecting benefits until a future year.

Net income for the single-employer program was $3,485 million in FY 2016. The primary drivers included the following: investment income of $8,648 million, net premium income and other income of $6,404 million, and a credit due to completed and probable terminations of $417 million. This was offset by a charge of $6,301 million due to a decrease in interest factors (which has the effect of increasing benefit liabilities and actuarial charges), a $2,929 million actuarial charge due to expected interest on accrued liabilities, a charge for actuarial adjustments of $2,285 million, a charge of $366 million in administrative and other expenses, and investment expenses of $103 million.

PBGC's single-employer program realized net income of $3,485 million compared with a net loss in FY 2015 of $4,727 million. This favorable $8,212 million change was primarily attributable to:

(1) an increase in investment income of $8,324 million (a gain of $8,648 million compared to a gain of $324 million in FY 2015),
(2) an increase in net premium and other income of $2,255 million,
(3) a decrease in charges due to expected interest of $410 million,
(4) a decrease in administrative, investment, and other expenses of $7 million,

(5) an increase in charges for underwriting actuarial adjustments of $1,971 million,
(6) an increase in actuarial charges due to change in interest factors of $450 million; and
(7) a decrease in credits from completed and probable terminations of $363 million.

Actuarial charges and adjustments arise from changes from mortality and retirement assumptions, changes in interest factors and expected interest. Expected interest refers to the interest that PBGC expects to accrue during the current fiscal year based on PBGC's liability and interest factors at the end of the prior year, with adjustments made for new plans and benefit payments made during the year.

SINGLE-EMPLOYER UNDERWRITING ACTIVITY

PBGC's single-employer program realized a net underwriting gain of $4,170 million in FY 2016, $61 million less than the FY 2015 gain of $4,231 million. This $61 million decrease from the previous year was primarily due to the $1,971 million increase in charges for underwriting actuarial adjustments and a decrease of $363 million in credits from completed and probable terminations, partially offset by a $2,241 million increase in single-employer net premium income.

Premium and other income from underwriting activity increased (from $4,149 million in FY 2015 to $6,404 million in FY 2016), largely due to an increase in net premium income from plan sponsors (from $4,138 million in FY 2015 to $6,379 million in FY 2016). The increase in net premium income was primarily due to the increase in the variable rate premium for plan years beginning in 2016, given the combined effect of the variable rate increases and higher levels of underfunding. Other income, consisting of interest on recoveries from sponsors, increased from $11 million in FY 2015 to $25 million in FY 2016.

Annual variable rate premium income, paid by underfunded single-employer plans, increased by $2,074 million to a total of $4,639 million. The prior year's VRP rate of $24 per $1,000 of underfunding increased to $30 per $1,000 of underfunding for plan years beginning in 2016. Annual flat rate premiums for the single-employer program increased from $57 to $64 per participant in FY 2016, contributing to an increase in the flat rate premium income of $186 million to a total of $1,742 million.

Beginning with calendar year 2008 plans, the Pension Protection Act (PPA) eliminated the full-funding VRP exemption and changed the interest rate rules for determining a plan's present value of vested benefits for VRP purposes. Under PPA, the present value is determined using three "segment" rates. The first of these applies to benefits expected to be paid within five years of the first day of the plan year, the second applies to the following 15 years, and the third applies to benefits expected to be paid after that.

The Treasury determines each segment rate monthly using the portion of a corporate bond yield curve that is based on corporate bonds maturing during that segment rate period. The corporate bond yield curve is also prescribed every month by the Treasury. It reflects the yields for the previous month on investment-grade corporate bonds with varying maturities that are in the top three quality levels. The January 2016 segment rates for calendar-year plans were 1.82%, 4.12% and 5.01% for the first, second, and third segments, respectively.

The Corporation's credits from completed and probable plan terminations decreased from a credit of $780 million in FY 2015 to a credit of $417 million in FY 2016. The $417 million FY 2016 credit is due to a credit of $1,183 million from revaluations of plans that had terminated in prior years and a $209 million decrease in

probable claims, offset by $975 million for charges related to new plan terminations (see "Subtotal terminated plans" in Note 12).

The net claim for single-employer probable terminations as of September 30, 2016, was $376 million, while the net claim as of September 30, 2015, was $585 million. This $209 million decrease is due primarily to the transfer of $382 million of previously accrued claims to a termination status, the deletion of one plan with a net claim of $40 million, and a favorable decrease in the reserve for small unidentified probables of $36 million. These factors were offset by the addition of three new probables with net claims of $249 million (see Note 6).

Single-employer administrative expenses increased $8 million from $354 million in FY 2015 to $362 million in FY 2016.

In summary, the following key metrics describe the components of PBGC's single-employer present value of future benefits liability:

- $113,011 million – trusteed plans (4,738 plans)
- $296 million – plans pending termination and trusteeship (31 plans)
- $376 million – three probable plans and a reserve for small plans
- During FY 2016, PBGC terminated 67 underfunded single-employer plans with a net claim of $975 million, with $382 million already accrued as probable.

SINGLE-EMPLOYER FINANCIAL ACTIVITY

In FY 2016, single-employer financial net loss decreased from a loss of $8,958 million in FY 2015 to a loss of $685 million. This is due to an increase of $8,324 million in investment income ($8,648 million in FY 2016 compared with $324 million in FY 2015), offset by an increase of $40 million in actuarial charges and an increase of $11 million in investment expense. PBGC marks its assets to market, which is consistent with the Financial Accounting Standards Board (FASB) Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures* (see Note 5).

Actuarial charges under financial activity represent the effects of changes in interest rates and the expected interest accrued on the present value of future benefits. The interest rate in effect at the beginning of FY 2016 (2.80%) decreased compared to the rate at the beginning of FY 2015 (3.35%). A charge to the single-employer interest factor occurred in both FY 2015 and FY 2016 due to a decrease in the interest factors from the previous year (the interest factor charge was $5,851 million in FY 2015 and $6,301 million in FY 2016). The expected interest refers to the interest that PBGC expects to accrue during the fiscal year on PBGC's liability at the end of the prior year. Charges to the single-employer expected interest decreased in FY 2016 (the expected interest charge was $3,339 million in FY 2015 and $2,929 million in FY 2016).

PBGC discounts its liabilities for future benefits with interest factors[1] that, together with the mortality table used by PBGC, approximate the price in the private-sector annuity market at which a plan sponsor or PBGC could settle its obligations. In FY 2016 PBGC's select interest factor decreased to 2.27% (for the first 20 years after the valuation date) at September 30, 2016, from 2.80% (for the first 25 years) at September 30, 2015. The ultimate factor decreased to 2.14% at September 30, 2016 (after the first 20 years) from 2.86% at September 30, 2015 (after the first 25 years).

PBGC's single-employer Present Value of Future Benefits (PVFB) increased from $106,926 million at September 30, 2015, to $113,704 million at September 30, 2016. PVFB comprises the majority of PBGC's combined total liabilities of $178,959 million on its Statements of Financial Position.

IV.B MULTIEMPLOYER PROGRAM RESULTS OF ACTIVITIES AND TRENDS

During FY 2016, PBGC's obligations for future financial assistance to multiemployer plans increased from $54,186 million at September 30, 2015, to $61,009 million at September 30, 2016, an increase of $6,823 million (13%).

There were three key drivers for change in our reported multiemployer liabilities that are included in the losses from insolvent and probable plans-financial assistance amount of $6,768 million as of September 30, 2016. A significant driver of the change is the net addition of 11 new plans added to the multiemployer inventory (includes 10 multiemployer probable plans as well as 1 new insolvent plan) in FY 2016. These additional plans accounted for $6,347 million in additional guaranteed liabilities reported by PBGC at September 30, 2016. Of this $6,347 million amount, multiemployer plans classified as probable accounted for $6,332 million.

Another key actuarial driver increasing the liabilities in FY 2016 was the decrease in the pension liability valuation interest factors. The select interest rate factor decreased by 53 basis points to 2.27% at September 30, 2016, from 2.80% at September 30, 2015. This decrease in interest factor accounted for over $6.2 billion in additional guaranteed liabilities.

Finally, another key actuarial driver (partially offsetting the above increases) for the change in estimated multiemployer liabilities is updated actuarial assumptions. The most important of these is a change in the estimated guarantee factor that PBGC uses in determining PBGC-guaranteed liabilities for multiemployer plans. The change reflects a revised procedure for determining the guaranteed benefit reduction factor, based on an assumption that both retirees and terminated vested participants have lower average years of service compared to estimates used prior to September 30, 2016. In FY 2016, PBGC hired an actuarial firm to conduct a study of PBGC's actual guarantee factor experience for multiemployer plans. This comprehensive study looked at all plans in the PBGC multiemployer probable plan universe where guarantee benefit data were available. This study found that the PBGC guarantees a smaller percentage of the multiemployer plan liabilities than previously estimated. As a result, PBGC updated the assumption to reflect the lower

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[1] PBGC surveys life insurance industry annuity prices through the American Council of Life Insurers (ACLI) to obtain input needed to determine interest factors and then derives interest factors that will best match the private-sector prices from the surveys. The interest factors are often referred to as select and ultimate interest factors. Any pair of interest factors will generate liability amounts that differ from the survey prices, which cover 14 different ages or benefit timings. The PBGC process derives the interest factor pair that differs least over the range of prices in the survey.

guarantee. This change in the guaranteed factor assumption accounted for nearly a $4,051 million reduction in the estimated guaranteed liabilities.

PBGC paid $113 million in financial assistance to 65 insolvent plans that cover over 59,000 retirees.

PBGC's multiemployer program covers about 10.6 million participants (an increase from 10.3 million participants in FY 2015) in about 1,400 insured plans. The multiemployer flat rate premium increased from $26 per participant in 2015 to $27 for 2016. This upward movement contributed to an increase in flat rate premium income of $72 million to a total of $284 million.

A multiemployer plan is a pension plan maintained by two or more unrelated employers under collective bargaining agreements with one or more unions. Multiemployer plans cover most unionized workers in the trucking, retail food, construction, mining and garment industries. A person doing work for any employer contributing to the plan is usually eligible for benefits. Workers accrue pension credits in the plan even when they change employment from one contributing employer to another.

Multiemployer plans are typically governed by a board of trustees appointed in equal numbers by labor and management. Under ERISA, the trustees have a fiduciary duty to act solely in the interest of participants and beneficiaries. Multiemployer plans are subject to ERISA minimum funding requirements. Although bargaining parties negotiate over plan contributions, they usually delegate plan design to the trustees.

Most collective bargaining agreements that cover multiemployer plans provide for contributions based on time worked in a covered job. Some plans base contributions on "units of production," such as number of items produced or gross sales achieved. In some plans, benefits depend on the level of contributions that employers make to the plan for the participants' work.

Contributions are held in a trust fund that is managed and invested by the board of trustees in accordance with ERISA's fiduciary standards. All plan assets in the trust are available to pay all benefit claims. Assets do not revert to contributing employers.

Employers in multiemployer plans generally remain in the plan unless they go out of business, bargain out of the plan, or move their business out of the plan coverage area. If an employer withdraws from the plan, it may be assessed withdrawal liability. Withdrawal liability is generally based on the plan's unfunded vested benefits and the employer's share of contributions to the plan made by all contributing employers. In some instances, the employer may be assessed partial withdrawal liability.

PBGC does not trustee multiemployer plans. In the multiemployer program, the event triggering PBGC's guarantee is plan insolvency – the inability to pay guaranteed benefits when due.

Insolvency usually occurs after all contributing employers have withdrawn from the plan, and the plan has spent almost all of its assets, leaving the plan without a source of income. PBGC provides insolvent multiemployer plans with financial assistance in the statutorily required form of loans, sufficient to pay PBGC-guaranteed benefits and reasonable administrative expenses. These loans generally continue until the plan no longer needs assistance or has paid all promised benefits at the guaranteed level. These loans are rarely repaid (and for that reason are fully reserved).

Benefits under the multiemployer program are calculated based on (a) the benefit a participant would have received under the insolvent plan, subject to (b) the legal multiemployer guarantee under ERISA. The guaranteed amount depends on the participant's years of service and the level of the benefit accruals. Monthly benefit accrual rates per year of service up to $11 are fully guaranteed; the portion of monthly benefit accrual rates between $11 and $44 is 75% guaranteed; monthly benefit accrual rates in excess of $44 are not guaranteed. For example, for a participant with 20 years of service, PBGC's guarantee would cover 100% of annual amounts up to $2,640 and partially cover amounts in excess of that not to exceed a total of $8,580 per year. Similarly, for a participant with 35 years of service, PBGC's guarantee would cover 100% of annual amounts up to $4,620 and partially cover amounts in excess of that not to exceed a total of $15,015 per year. The multiemployer guarantee limit has been in place since 2001.

The multiemployer program reported a net loss of $6,549 million in FY 2016 compared with a net loss of $9,850 million in FY 2015. This resulted in a negative net position of $58,833 million in FY 2016 compared with a negative net position of $52,284 million in FY 2015. The FY 2016 deficit is an all-time high for the multiemployer program.

The year-to-year decrease in net loss of $3,301 million was primarily due to the decrease in financial assistance losses from insolvent and probable plans of $3,195 million, an increase in investment income of $75 million, and an increase in premium income of $70 million, offset by an unfavorable impact from the change in interest factors of $23 million, an increase in administrative expenses of $7 million, an increase in charges due to expected interest of $5 million, and an increase in charges to actuarial adjustments of $4 million. Multiemployer program investments originate mainly from the cash receipts for premiums due from insured plans. PBGC is required to invest these premiums in obligations issued or guaranteed by the United States government.

V. OVERALL CAPITAL AND LIQUIDITY

PBGC's obligations include monthly payments to participants and beneficiaries in terminated defined benefit plans, financial assistance to multiemployer plans and PBGC's operating expenses. The financial resources available to pay these obligations are underwriting income received from insured plan sponsors (largely premiums), the income earned on PBGC's investments and the assets taken over from failed plans.

The Corporation has sufficient liquidity to meet its obligations for a number of years; however, barring changes, neither program will, with certainty be able to fully satisfy PBGC's long-term obligations to plan participants. For example, the FY 2015 Projections Report shows that the risk of multiemployer program insolvency rises rapidly, exceeding 50 percent in 2025 and reaching over 90 percent by the end of 2035. On the other hand, FY 2015 single-employer scenarios simulated over the 10 year projection period indicated that none would result in PBGC assets being completely exhausted.

FY 2016 combined premium cash receipts totaled $5,520 million, an increase of $1,824 million from $3,696 million in FY 2015, due primarily to the increase in variable rate premiums. Net cash flow used by investment activities decreased to $490 million used versus $712 million used in FY 2015. In FY 2016, PBGC's cash receipts of $7,482 million from operating activities of the single-employer program were sufficient to cover its operating cash obligations of $6,341 million. This resulted in net cash provided by operating activities of $1,141 million (as compared to net cash used of $136 million in FY 2015). When the

single-employer cash used through investing activities of about $412 million is added to this net cash provided, the single-employer program in the aggregate experienced a net cash increase of $729 million.

In the multiemployer program, cash receipts of $316 million from operating activities were sufficient to cover its operating cash obligations of $147 million, resulting in net cash provided by operations of $169 million. When this net cash provided is added to net cash used through investing activities of $78 million, the multiemployer program in the aggregate experienced an overall net cash increase of $91 million.

During FY 2016, PBGC recovered $88 million through agreements with sponsors of terminated plans for unpaid contributions and unfunded benefits. A portion of those recovered funds are paid out as additional benefits to plan participants with nonguaranteed benefits according to statutory priorities.

In FY 2016, PBGC's combined net increase in cash and cash equivalents amounted to $820 million, arising from an increase of $729 million for the single-employer program and an increase of $91 million for the multiemployer program.

VI. SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAM EXPOSURE

PBGC estimates its single-employer loss exposure to reasonably possible terminations (e.g., underfunded plans sponsored by companies with credit ratings below investment grade) of $223,275 million at September 30, 2016, and $217,699 million at September 30, 2015. PBGC's exposure to loss may be less than these amounts because of the statutory guarantee limits on insured pensions, but PBGC is unable to estimate prospectively the extent and effect of the guarantee limitations. These estimates are measured as of December 31 of the previous year (see Note 9). For FY 2016, this exposure was concentrated in the following sectors: manufacturing (primarily automobile/auto parts and fabricated metals), transportation (primarily airlines)/communications/utilities and services.

PBGC estimates that, as of September 30, 2016, it is reasonably possible that multiemployer plans may require future financial assistance of $19,485 million, compared to $19,957 million at September 30, 2015. The decrease in FY 2016 from FY 2015 is primarily due to changes in the data and underlying assumptions. The change in data was a result of updated plan asset and liability information. The changes in assumptions include the reduction in discount factors, an update to the small plan bulk reserve process, and the revised procedure for determining the guaranteed benefit reduction factor (an assumption that both retirees and terminated vested participants have smaller guaranteed benefits compared to that of a higher assumption that was used prior to September 30, 2016).

The significant volatility in plan underfunding and sponsor credit quality over time makes long-term estimates of PBGC's expected claims uncertain. This volatility, along with the concentration of claims in a relatively small number of terminated plans, has characterized PBGC's experience to date and will likely continue. Factors such as economic conditions affecting interest rates, financial markets and the rate of business failures will also influence PBGC's claims going forward.

PBGC's sources of information on plan underfunding are the most recent Section 4010 and PBGC premium filings, Form 5500 and other submissions to the Corporation. PBGC publishes Table S-49, "Various Measures of Underfunding in PBGC-Insured Plans," in its *Pension Insurance Data Book*. In that table the limitations of the estimates are fully and appropriately described.

In FY 2016, 1,338 plans filed standard terminations. The number of filings is consistent with that in the previous five years (ranging from 1,350 to 1,450 each year). Even though the total number of filings remains steady, there is a noticeable increase in larger plan standard terminations. Some of the large plans that terminated were those sponsored by CVS Health Corporation, Inova Health System, Community Hospitals of Indiana, Philips Electronics, Pfizer, Inc. and First American Financial Corporation. Philips Electronics also completed the standard termination process in FY 2016. Other large plans such as NBC Universal, Acument Global Technologies, Fluor Corporation, Hannaford Brothers and Fannie Mae completed previously filed standard terminations.

As in previous years, the majority of the plans that filed standard terminations were small plans with 300 or fewer participants.

The short-term projection shows that while the number of standard terminations is expected to stay steady over the next five years, the number of large plans terminating is expected to increase. The Internal Revenue Service (IRS) plans to issue regulations implementing new mortality tables in 2017, which will make lump sums more expensive. The volume of standard terminations is, therefore, expected to be high in 2017 as PBGC expects employers to pay out lump sums associated with a standard termination before the new IRS mortality tables go into effect. After the new mortality tables are adopted, the number of terminations may possibly be lower as long as interest rates do not rise. However, if low interest rates rise and lower the lump sum value of benefits, this would partially offset the decrease in standard terminations (as a result of the new mortality table). While the number of terminations may remain at current levels, terminations of larger plans will significantly increase the workload associated with standard terminations.

VII. INVESTMENT ACTIVITIES

PBGC uses institutional investment management firms to invest its assets, subject to PBGC's oversight and consistent with the investment policy statement approved by our Board. PBGC does not determine the specific investments to be made, but instead relies on PBGC's investment managers' discretion in executing investments appropriate for their assigned investment mandates. PBGC does ensure that each investment manager adheres to PBGC's prescribed investment guidelines associated with each investment mandate and measures each investment manager's performance in comparison with agreed-upon benchmarks.

PBGC's investment assets consist of premium revenues, which are accounted for in the revolving fund, and assets from trusteed plans and their sponsors, which are accounted for in the trust fund. By law, PBGC is required to invest certain revolving funds (i.e., Funds 1 and 2) in obligations issued or guaranteed by the United States government. Portions of the other revolving fund (i.e., Fund 7) can be invested in other debt obligations, but under PBGC's current investment policy these revolving funds are invested solely in Treasury securities (PBGC has never established funds 3, 4, 5 or 6, which ERISA authorized for special discretionary purposes). As required under MPRA, PBGC holds certain multiemployer premium amounts in non-interest-bearing accounts.

Total revolving fund investments, including cash and investment income, on September 30, 2016, were $26,013 million ($1,490 million for Fund 1, $2,036 million for Fund 2, and $22,487 million for Fund 7). Trust fund investments totaled $65,620 million as of September 30, 2016. At the end of FY 2016, PBGC's total

investments consisting of cash and cash equivalents, investments, and investment income receivable as shown on the Statements of Financial Position were $91,633 million.

The objective of PBGC's investment policy is to maximize funded status within a prudent risk framework that is informed by PBGC's fixed obligations and asset composition of potential trusteed plans. The investment policy establishes a 30 percent target asset allocation for equities and other non-fixed income assets, and a 70 percent asset allocation for fixed income.

PBGC's investment program had assets under performance management of $89,500 million as of September 30, 2016. Of the $2,100 million difference between the September 30, 2016, assets reported on the Statements of Financial Position and the assets within PBGC's investment performance portfolio, $900 million represent net unsettled purchases, $500 million for funds available for the following month's benefit payments, $400 million are newly trusteed assets that have not yet been commingled, and $300 million represent custodial bank holding accounts. Asset allocation percentages refer to the investments within PBGC's investment program that are subject to the Corporation's investment policy, as described below.

Cash and fixed income securities totaled about 70 percent of total assets under performance management invested at the end of FY 2016, compared with approximately 68 percent for FY 2015. Equity securities (i.e., public equities) represented about 29 percent of total assets under performance management invested at the end of FY 2016, compared with approximately 31 percent for FY 2015. The Total Fund Composite return (excluding private market assets and transition accounts) for FY 2016 was 10.8% compared with 0.1% in FY 2015. The returns reflect stronger capital markets performance during the period. A small percentage of PBGC's investments (1.3 percent of total investment assets at FY 2016, compared with 0.1 percent at FY 2015) predominantly represent assets that are in the process of moving out of one of the manager portfolios either for liquidation or for transfer to another manager. The return of the Total Fund Composite including these transition accounts was 10.7% in FY 2016, compared to 0.1% in FY 2015. Private markets assets, comprised largely of private equity, private debt, and private real estate that are currently part of the investment portfolio, represented about 1.2% of total investments at the end of FY 2016, compared with 1.7% of total investments at the end of FY 2015.

Due to the cyclical nature of capital markets, PBGC also reports five-year returns for its investment program. For the five-year period ending September 30, 2016, PBGC's return on total invested funds excluding transition accounts was 6.7% compared with a total fund benchmark return of 6.4% — a benchmark based on the relative weights of the underlying managed accounts. Including the transition accounts, the five-year annualized return was 6.7%. Separately, the ERISA/PPA hypothetical portfolio benchmark return for the five-year period ending September 30, 2016, was 11.1%. (See section VII Investment Activities (The Pension Protection Act of 2006 Reporting Requirement).

The table below summarizes the performance of PBGC's investment program.

INVESTMENT PERFORMANCE

(Annual Rates of Return)

	September 30,		Three and Five Years Ended September 30, 2016	
	2016	2015	3 yrs	5 yrs
Total Fund Composite	**10.8%**	0.1%	6.2%	6.7%
Total Fund Benchmark[1]	**10.4**	(0.1)	6.0	6.4
ERISA/PPA Portfolio Benchmark[2]	**11.2**	1.0	8.4	11.1
Total Global Public Stock	**13.5**	(3.6)	6.7	12.1
Total Global Public Stock Benchmark[3]	**13.1**	(4.3)	6.4	11.7
Total Global Bonds	**10.0**	2.2	6.3	4.8
Total Global Bonds Benchmark[4]	**9.6**	2.2	6.2	4.4
Smaller Asset Managers Pilot Program[5]	**n/a**	n/a	n/a	n/a
Trust Funds	**12.0**	(1.0)	6.6	8.1
Revolving Funds	**7.1**	3.4	5.0	2.9
Indices				
Russell 3000 Index	**15.0**	(0.5)	10.4	16.4
MSCI ACWI ex-U.S. IMI Index	**9.8**	(11.4)	0.6	6.4
Dow Jones U.S. Select Real Estate Securities Index	**17.7**	11.8	14.2	15.6
Barclays Capital Treasury Index	**4.1**	3.8	3.4	2.2
Barclays Capital Aggregate Bond Index	**5.2**	2.9	4.0	3.1
Barclays Capital Global Aggregate ex-US Index, Hedged	**7.5**	3.4	5.8	5.0

[1] The Total Fund Benchmark is a dynamic weighted benchmark based upon the weights of the Total Global Public Stock Benchmark, the Total Global Bonds Benchmark and the Total Money Market Securities Benchmark. This benchmark is utilized to compare against the Total Fund Composite returns shown above.
[2] The ERISA/PPA Portfolio Benchmark is based upon a hypothetical portfolio with a 60% allocation to the Standard & Poor's 500 equity index and a 40% allocation to the Barclays Capital Aggregate fixed income index. See section VII Investment Activities (The Pension Protection Act of 2006 Reporting Requirement).
[3] The Total Global Public Stock Benchmark is a dynamic weighted benchmark based upon the weights of the U.S. Public Stock composite and the International Public Stock composite and the returns of their respective benchmarks.
[4] The Total Global Bonds Benchmark is a dynamic weighted benchmark based upon the weights of PBGC's fixed income managers and the returns of their respective benchmarks.
[5] The performance inception date for the Smaller Asset Managers Pilot Program is August 2016. As such, one year of performance is not yet available.

FIXED INCOME

As described below, PBGC fixed income investment managers use a number of different benchmarks. Where applicable, the relative percentage that each index or benchmark represents for its respective asset class is provided. The percentage invested under each benchmark(s), in aggregate, for each asset class relative to the overall PBGC investment program as of September 30, 2016, is also provided below.

The Total Global Bonds Benchmark is a dynamic weighted benchmark based on the weights of the underlying fixed income managers and the returns of their respective benchmarks. As of September 30, 2016, the weighted benchmark encompasses the Revolving Fund Treasuries Custom Benchmark (30.3%), the Barclays Capital U.S. TIPS index (11.8%), the Total Long Duration Bonds Benchmark (24.0%), the Barclays Capital Aggregate Bond index (8.7%), the Total Developed Market Bonds Benchmark (10.4%), the Total High Yield Bonds Benchmark (5.6%), and the Total Emerging Market Bonds Benchmark (9.2%). The overall Total Global Bonds composite equals 65.6 percent of the total PBGC portfolio.

Treasuries: This category includes investments in United States Dollar (USD) denominated fixed income securities managed by outside professional asset managers and it applies to 19.9 percent of PBGC's investment program assets at year-end. The Revolving Fund Treasuries Custom Benchmark encompasses the Barclays Capital US Treasury 7+ index (65.0%) and the Barclays Capital US Treasury Intermediate index (35.0%). The Revolving Fund Treasuries Custom Benchmark is a customized index made up of U.S. Treasury notes and bonds. While PBGC is able to redeem composite assets upon request, the composite assets are part of the Revolving Fund and can only be redeemed to meet pension benefit obligations and administrative expenses.

U.S. Treasury Inflation Protected Securities (TIPS): This category includes investments in USD denominated fixed income securities managed by outside professional asset managers, and it applies to 7.8 percent of PBGC's investment program assets at year-end. The TIPS Benchmark is the Barclays Capital U.S. TIPS index. While PBGC is able to redeem composite assets upon request, the composite assets are part of the Revolving Fund and can only be redeemed to meet pension benefit obligations and administrative expenses.

Long Duration: This category includes investments mainly in USD-denominated fixed income securities managed by outside professional asset managers, and applies to 15.7 percent of PBGC's investment program assets at year-end. The Total Long Duration Bonds Benchmark is a dynamic weighted benchmark based on the weights of the underlying Trust Fund long-duration fixed income managers and the returns of their respective benchmarks. As of September 30, 2016, the Total Long Duration Bonds Benchmark encompasses the Barclays Capital Long U.S. Government/Credit index (47.2%), Barclays U.S. Long Credit Index (3.9%), and Custom Benchmarks (48.9%). The Barclays Capital Long U.S. Government/Credit index includes both government and credit securities. The government component includes public obligations of the U.S. Treasury that have remaining maturities of more than one year and publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government. The credit component of the index includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality (investment grade) requirements. The Barclays Capital U.S. Long Credit index includes investment-grade corporate debt and sovereign, supranational, local authority and non-U.S. agency bonds that are dollar denominated and have a remaining maturity of greater

than or equal to 10 years. The custom benchmarks include similar securities and are weighted combinations of sub-sector benchmarks. PBGC is able to redeem composite assets upon request.

Core: This category includes investments primarily in USD-denominated fixed income securities managed by outside professional asset managers. It applies to 5.7 percent of PBGC's investment program assets at year-end. The Core Fixed Income Benchmark is the Barclays Capital Aggregate Bond index. The Barclays Capital Aggregate Bond index includes securities that are registered with the Securities and Exchange Commission (SEC) and are taxable and dollar-denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, asset-backed securities, and foreign securities. PBGC is able to redeem composite assets upon request.

Developed Markets: This category includes investments in USD-denominated fixed income securities and fixed income securities denominated in other foreign currencies managed by outside professional asset managers. It applies to 6.8 percent of PBGC's investment program assets at year-end. The Total Developed Market Bonds Benchmark is a dynamic weighted benchmark based on the weights of all developed market bond managers and the returns of their respective benchmarks. As of September 30, 2016, the weighted benchmark encompasses the Barclays Capital Global Aggregate index hedged (52.5%) and the Barclays Capital Global Aggregate ex-USD index hedged (47.5%). The Barclays Capital Global Aggregate index provides a broad-based measure of the global investment-grade fixed income markets. The three major components of this index are the U.S. Aggregate, the Pan-European Aggregate, and the Asian-Pacific Aggregate Indices. The index also includes Eurodollar and Euro-Yen corporate bonds, Canadian government, agency and corporate securities, and USD-denominated investment grade 144A securities. The hedged index negates exposure to foreign currencies by hedging currency exposure back to the U.S. dollar. The ex-USD index excludes USD denominated securities and provides a broad-based measure of international investment-grade fixed income markets. PBGC is able to redeem composite assets upon request.

High Yield: This category includes investments primarily in USD-denominated fixed income securities managed by outside professional asset managers. It applies to 3.7 percent of PBGC's investment program assets at year-end. The Total High Yield Bonds Benchmark is a dynamic weighted benchmark based on the weights of all high yield bond managers and the returns of their respective benchmarks. As of September 30, 2016, the weighted benchmark encompasses the Barclays Capital US High Yield Ba/B 1% Capped index (55.1%), the Barclays Capital US High Yield 2% Issuer Capped index (29.1%) and the Barclays Capital US High Yield Ba/B 2% Capped index (15.8%). The Barclays Capital U.S. High Yield Ba/B 1% Issuer Capped index includes the universe of fixed rate, non-investment grade debt securities rated Ba or B. The index also includes Canadian and global bonds (SEC registered) of issuers in non-Emerging Market countries. The index limits the size of an individual issuer to 1% of the index. The Barclays Capital U.S. High Yield 2% Issuer Capped index includes the universe of fixed rate, non-investment grade debt securities rated Ba-D. The index also includes Canadian and global bonds (SEC-registered) of issuers in non-Emerging Market countries. The index limits the size of an individual issuer to 2% of the index. The Barclays Capital U.S. High Yield Ba/B 2% Issuer Capped index is identical to the Barclays Capital U.S. High Yield Ba/B 1% Issuer Capped index, except it limits the size of an individual issuer to 2% of the index instead of 1% of the index. PBGC is able to redeem composite assets upon request.

Emerging Market Bonds: This category includes fixed income securities denominated in either U.S. dollars or foreign currencies, and managed by outside professional asset managers. It comprises 6.0 percent of PBGC's investment program assets at year-end. The Total Emerging Market Bonds Benchmark is a dynamic weighted benchmark based on the weights of all emerging market bond managers and the returns of their respective benchmarks. As of September 30, 2016, the weighted benchmark encompasses the JP Morgan EMBIG Diversified index (50.8%) and Custom Benchmarks (49.2%). The custom benchmarks are weighted combinations of the JP Morgan EMBIG Diversified and the JP Morgan GBI EM Global Diversified indices. The JP Morgan EMBIG Diversified index includes USD-denominated debt instruments issued by Emerging Market countries. The index also includes USD-denominated Brady bonds, Eurobonds, and traded loans issued by sovereign and quasi-sovereign entities. The JP Morgan GBI EM Global Diversified index includes local currency or non-U.S. dollar-denominated debt instruments issued by Emerging Market countries. PBGC is able to redeem composite assets upon request.

MONEY MARKET SECURITIES

This category includes investments in money market instruments managed by an outside professional asset manager who invests in a diversified portfolio of short-term obligations and deposits, including, but not limited to, Treasury and agency obligations, certificates of deposits, commercial paper, and repurchase agreements (Trust Fund Cash). In addition, the category includes overnight investments in Treasury securities held at Treasury (Revolving Fund Cash). The Total Money Market Securities Benchmark is a dynamic weighted benchmark based on the weights of the Trust Fund Cash and the Revolving Fund Cash and the returns of their respective benchmarks. As of September 30, 2016, the weighted benchmark encompasses the 3-month Treasury bill (52.8%) and the 4-week Treasury bill (47.2%). The cash composite represents 3.0 percent of PBGC's investment program as of September 30, 2016. PBGC is able to redeem money market securities upon request.

GLOBAL PUBLIC STOCK

This category includes investments in the U.S. Public Stock composite and the International Public Stock composite, and applies to 27.9 percent of PBGC's investment program assets at fiscal year-end. The Total Global Public Stock Benchmark is a dynamic weighted benchmark based upon the weights of the U.S. Public Stock composite and the International Public Stock composite as well as on the returns of their respective benchmarks. PBGC is able to redeem composite assets upon request.

As of September 30, 2016, the Total Global Public Stock Benchmark comprises the Total U.S. Public Stock Benchmark (51.2%), and the Total International Public Stock Benchmark (48.8%).

U.S. Public Stock: This category includes investments in U.S. publicly traded equity securities and U.S. publicly traded real estate investment trusts (REITs) managed by outside professional asset managers. It applies to 14.3 percent of PBGC's investment program assets at year-end. The Total U.S. Public Stock Benchmark is a dynamic weighted benchmark based upon the weights of the U.S. Public Stock composite and the returns of their respective benchmarks. As of September 30, 2016, the weighted benchmark comprises the Russell 3000 index (88.1%) and the Dow Jones U.S. Select Real Estate Securities index (11.9%). PBGC is able to redeem composite assets upon request.

International Public Stock: This category includes investments in International Equity securities managed by outside professional asset managers. It applies to 13.6 percent of PBGC's investment program assets at year-end. The Total International Public Stock Benchmark is a dynamic weighted benchmark based upon the weights of all of the international funds and the returns of their respective benchmarks. As of September 30, 2016, the weighted benchmark encompasses the MSCI EAFE index (60.6%), the MSCI EAFE Small Cap index (9.8%), the MSCI Emerging Markets index (22.7%), and the MSCI Canada index (6.9%). The MSCI EAFE index (Europe, Australasia and Far East) is designed to measure the equity market performance of developed markets, excluding the U.S. and Canada. The MSCI EAFE Small Cap index is designed to measure the developed markets small capitalization equity performance, excluding the U.S. and Canada. The MSCI Emerging Markets index is designed to measure equity market performance of emerging markets and the MSCI Canada index is designed to measure the equity market performance of Canada. PBGC is able to redeem composite assets upon request.

Smaller Asset Managers Pilot Program: PBGC implemented the Smaller Asset Managers Pilot Program, which creates new opportunities for smaller asset managers, who wish to compete for the agency's business. Five investment management firms were selected to participate in the pilot program and were funded in fiscal year 2016. This category includes investments primarily in USD-denominated fixed income securities managed by outside professional asset managers. It applies to 1.0 percent of PBGC's investment program assets at fiscal year-end. The Smaller Asset Managers Pilot Program Benchmark is the Barclays Capital Aggregate Bond index. The Barclays Capital Aggregate Bond index includes securities that are SEC-registered, taxable, and dollar-denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, asset-backed securities, and foreign securities. PBGC is able to redeem composite assets upon request.

PRIVATE MARKETS

This category includes private equity, private debt, and private real estate funds that invest mainly in buyouts, venture capital, distressed debt, and commercial real estate. It applies to 1.2 percent of PBGC's investment program assets at year-end. Private investments are difficult to benchmark due to their illiquid nature. Typical benchmarks utilized for private equity include universe comparisons, where funds that have the same original investment date are compared against the performance of a similar fund. For direct private real estate investments, many institutions use the National Council of Real Estate Investment Funds (NCREIF) index, which includes U.S. commercial real estate properties acquired in the private market for investment purposes. For investments in private equity real estate, peer universe comparisons based on similar funds with the same original investment date are often utilized. Private market investments typically do not have redemption provisions; instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the funds. It is estimated that the majority of the underlying assets of the funds will be liquidated over the next five years. The fair values of the investments in this category have been estimated using the net asset value of PBGC's ownership interest in partners' capital.

THE PENSION PROTECTION ACT OF 2006 REPORTING REQUIREMENT

The Pension Protection Act of 2006 requires PBGC to estimate the effect of an asset allocation based on a combination of two commonly used market benchmarks. This hypothetical portfolio (used as a benchmark for a typical pension plan, rather than an insurer), with a 60 percent allocation to the Standard & Poor's 500

equity index and a 40 percent allocation to the Barclays Capital Aggregate Bond index, would have increased the assets of the Corporation by about $0.5 billion (11.4% return compared with PBGC's Total Fund Composite return including transition accounts of 10.7%) for the one-year period ending September 30, 2016, and increased the assets of the Corporation by about $20.2 billion (11.1% return compared with PBGC's Total Fund Composite return including transition accounts of 6.7%) over the five-year period ending September 30, 2016. For further analysis of PBGC's Investment Activities please refer to the MD&A of Results of Operations and Financial Position. As reported in last year's FY 2015 Annual Report, the same "60/40 portfolio" would have increased the assets of the Corporation by about $0.7 billion (1.0% return compared with PBGC's Total Fund Composite return including transition accounts of 0.1%) for the one-year period ending September 30, 2015, and increased the assets of the Corporation by about $16.1 billion (9.5% return compared with PBGC's Total Fund Composite return including transition accounts of 5.6%) for the five-year period ending September 30, 2015.

These results are summarized in the following table.

INVESTMENT PORTFOLIO ANALYSIS

60/40 Hypothetical Portfolio Analysis Versus PBGC Fiscal Year Actual Return
(60/40 comprises S&P 500 Index/Barclays Capital Aggregate Bond Index)

	1-Year Period Ending			5-Year Period Ending		
Fiscal Year	60/40 Incremental $ Billions	60/40 % Return	PBGC Actual Return[1]	60/40 Incremental $ Billions	60/40 % Return	PBGC Actual Return[1]
9/30/2015	$0.7	1.0%	0.1%	$16.1	9.5%	5.6%
9/30/2016	$0.5	11.4%	10.7%	$20.2	11.1%	6.7%

[1] PBGC actual return is the PBGC's Total Fund Composite return including transition accounts.

ANALYSIS OF ENTITY'S SYSTEMS, CONTROLS AND LEGAL COMPLIANCE

PBGC maintains an Internal Controls Program designed to support compliance with the *Federal Managers' Financial Integrity Act* (FMFIA) and Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control.* PBGC has begun implementation of the new requirements specified in the July 2016 revision to OMB Circular A-123 and, as described below, performs a number of activities that serve to undergird the FMFIA Statement of Assurance. For FY 2016, PBGC provided an unmodified FMFIA Statement of Assurance and also highlighted a compliance matter regarding a reported instance of noncompliance with the voluntary service provision of the Antideficiency Act.

INTERNAL CONTROL COMMITTEE

The PBGC Internal Control Committee (ICC) provides corporate oversight and accountability regarding internal controls over PBGC's operations, reporting, and compliance with laws and regulations. Chaired by the Chief Financial Officer, the committee includes members from each major area of the agency, including a representative of the OIG as a non-voting member. The ICC approves major changes to key financial reporting and entity-wide controls and PBGC systems, monitors the status of internal control deficiencies and related corrective actions, and considers other matters, including controls designed to prevent or detect fraud. The ICC charter was updated to reflect coordination with a newly established Risk Management Council (RMC), especially when risks that require new or updated controls as part of a risk remediation strategy are identified. In addition, the ICC will be increasing its focus on controls over operations, nonfinancial reporting, and compliance with laws and regulations, based on the updated OMB Circular A-123 requirements.

DOCUMENTATION AND TESTING OF CONTROLS

As part of the Internal Controls Program, controls are evaluated, on a test basis, to assess the adequacy of control design and the extent to which they are operating effectively. Reports regarding results of the testing are provided to stakeholders within the agency and corrective actions are recommended, where appropriate. Areas of focus include:

Standards for Internal Control in the Federal Government (Green Book): These standards, published by the GAO, represent guidance to be used by federal agencies in implementing effective internal control systems. FY 2016 was the first year of their applicability, and PBGC completed an initial assessment of activities and controls supporting the Green Book's five internal control components and the 17 underlying control principles. A number of recommendations were identified to enhance existing practices.

Financial Reporting Controls: Cycle memorandums documenting financial reporting controls within the following 12 major business process cycles were updated and approved during the fiscal year: Benefit Payments, Benefit Determinations, Budget, Financial Reporting, Human Resources/Payroll, Investments, Losses on Completed and Probable Terminations, Non-Recoverable Future Financial Assistance, Payables, Premiums, Single-Employer Contingent Liability, and Present Value of Future Benefits. The ICC has designated certain controls as key internal controls over financial reporting within each of these cycles, and

employees responsible for performance of these controls are required to provide quarterly representations regarding the performance of those controls and to maintain evidence documenting control execution.

Entity-Wide Controls: These controls are overarching controls that support the overall effectiveness of PBGC's internal control environment. The ICC has designated certain controls as key entity-wide controls within the following six categories: control environment, risk assessment, control activities, information and communication, monitoring and anti-fraud. With regard to anti-fraud efforts, PBGC conducted an initial fraud assessment during FY 2016 as part of a continuing effort to fully implement GAO's Framework for Managing Fraud Risks in Federal Programs. This framework is focused on identifying and responding to fraud risks and developing control activities to prevent and detect fraud. The use of this framework is required under the Fraud Reduction and Data Analytics Act and OMB Circular A-123.

Information Technology Controls: In order to protect the confidentiality, integrity, and availability of PBGC information systems and the information processed and stored by those systems, PBGC implements the controls included in the National Institute of Standards and Technology's Special Publication No. 800-53, *Security and Privacy Controls for Federal Information Systems and Organizations.* These controls are documented as part of System Security Plans which are maintained within the Cyber Security Assessment and Management (CSAM) tool managed by the Office of Technology's Enterprise Cybersecurity Division.

ASSESSMENT OF IMPROPER PAYMENT RISK

Based on the requirements of OMB Circular A-123, Appendix C, *Requirements for Effective Measurement and Remediation of Improper Payments*, and related improper payment legislation, PBGC performed risk assessments of two payment streams for FY 2016: 1) financial assistance payments to insolvent multiemployer plans that are unable to pay benefits when due under the requirements of Title IV of ERISA (Financial Assistance Payments); and 2) payments to contractors for goods and services, including government credit card transactions (Payments to Contractors). Please refer to the Improper Payment Assessment section of this report for additional information.

AUDIT COORDINATION AND FOLLOW-UP PROGRAM

In implementing OMB Circular A-50, PBGC has established its *Audit Coordination and Follow-up Directive.* It is PBGC policy to fully cooperate with audits of PBGC operations and ensure the efficient tracking, resolution, and implementation of agreed-upon audit recommendations contained in audit reports issued by OIG and the GAO. PBGC has dedicated staff to coordinate with OIG and GAO audit representatives in providing access to records and information needed to complete audits and ensure that management responses to draft reports are provided in a timely manner. To facilitate timely completion and closure of audit recommendations, staff regularly monitors implementation efforts, including regular distribution of audit follow-up status reports to executive management via a corporate-wide portal and formal submission of documentation evidencing completion of required corrective actions. Status reports are used to document planned corrective actions and estimated completion dates; they also indicate those recommendations for which work has been completed and reported as such to the OIG and to GAO. In addition, PBGC prepares a management report in response to the Semiannual Report to Congress (SARC) issued by the OIG, which addresses the status of agreed-upon OIG recommendations and provides other information required under the Inspector General Act of 1978, as amended.

COMPLIANCE WITH LAWS, REGULATIONS, AND OTHER REQUIREMENTS

To foster an environment that promotes compliance with laws and regulations, PBGC maintains two legal compendia: the *Compendium of Laws* lists statutes that may have a significant impact on PBGC's financial statements or PBGC operations, and the *Compendium of Executive Orders and OMB Requirements* lists other requirements applicable to PBGC. These documents provide brief descriptions of each applicable requirement and identify the PBGC department or other component with primary compliance responsibility. PBGC updates and maintains these lists to help ensure compliance with applicable laws, regulations, and other requirements.

RISK MANAGEMENT ACTIVITIES

PBGC established a Risk Management Council during FY 2016. PBGC has appointed an acting Risk Management Officer (RMO) and is actively recruiting to fill the position on a permanent basis. The RMO serves as RMC Chair and reports directly to the PBGC Director. The RMC has established a charter and is taking the lead in implementing enterprise risk management (ERM). This implementation will support integration and coordination of risk and control activities throughout the agency. PBGC has completed an assessment of entity-wide risks, and certain departments have initiated or completed risk assessments at the departmental level. The RMC is in the process of developing guidance supporting the completion and coordination of additional risk assessments across the agency. These efforts will support the preparation of a corporate risk profile as required by OMB Circular A-123.

FMFIA ASSURANCE STATEMENT PROCESS

The heads of departments, offices and selected other work units within PBGC performed assessments of internal controls over operations, reporting (financial and nonfinancial), and compliance with laws and regulations. These assessments addressed several different considerations affecting internal controls, such as existence of policies and procedures, extent of management oversight, performance of internal compliance reviews, results of external reviews (e.g., OIG, GAO, or other reviews), and evaluation of known internal control deficiencies. In addition, the ICC was presented with the results of the PBGC's initial Green Book assessment and prepared a list of cross-cutting control issues for consideration by members of PBGC's executive management. Further, the corrective actions taken in response to the two FMFIA material weaknesses that were reported in FY 2015 (System Security and IT Operational Effectiveness and Corrective Action Plans, and Operational Processes and Records Management) were evaluated for adequacy to ensure that these matters no longer represented material weaknesses. Based on the results of the completed assessments and other relevant factors, PBGC's executive management recommended, and the Director approved, the FY 2016 FMFIA Statement of Assurance included below:

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT STATEMENT OF ASSURANCE

PBGC's management is responsible for managing risks and maintaining effective internal control to meet the objectives of Sections 2 and 4 of the Federal Managers' Financial Integrity Act. PBGC conducted its assessment of risk and internal control in accordance with OMB Circular No. A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*. Based on the results of the assessment, PBGC

can provide reasonable assurance that internal controls over operations, reporting, and compliance were operating effectively as of September 30, 2016.

PBGC's management is also responsible for managing risks and maintaining effective internal control over financial reporting in accordance with Appendix A of OMB Circular A-123. PBGC conducted an assessment of internal controls over financial reporting. The results of that assessment provide reasonable assurance that internal controls over financial reporting were operating effectively as of September 30, 2016.

PBGC was not in compliance with law and regulation due to a violation of the voluntary services provision of the Antideficiency Act, which was duly reported externally, as required. PBGC is developing corrective actions to help prevent such a violation from occurring in the future, and has provided training on the Antideficiency Act requirements.

MANAGEMENT REPRESENTATION

PBGC's management is responsible for the accompanying Statements of Financial Position of the Single-Employer and Multiemployer Funds as of September 30, 2016, and September 30, 2015, the related Statements of Operations and Changes in Net Position, and the Statements of Cash Flows for the years then ended. PBGC's management is also responsible for establishing and maintaining systems of internal accounting and administrative controls that provide reasonable assurance that the control objectives (i.e., preparing reliable financial statements, safeguarding assets, and complying with laws and regulations) are achieved.

PBGC management believes the financial statements of the Single-Employer and Multiemployer Program Funds present fairly the financial position of PBGC as of September 30, 2016, and September 30, 2015, and the results of its operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) and actuarial standards applied on a consistent basis. As noted in the FMFIA Statement of Assurance above, PBGC provides reasonable assurance that its internal controls are effective.

Estimates of probable terminations, nonrecoverable future financial assistance, amounts due from employers, and the present value of future benefits have a material effect on the financial results being reported. Litigation has been disclosed and reported in accordance with U.S. GAAP.

As a result of the aforementioned, PBGC has based these statements, in part, upon informed judgments and estimates for those transactions not yet complete or for which the ultimate effects cannot be precisely measured, or for those that are subject to the effects of any pending litigation.

The Inspector General engaged CliftonLarsonAllen LLP to conduct the audit of the Corporation's fiscal years 2016 and 2015 financial statements, and CliftonLarsonAllen LLP issued an unmodified opinion on those financial statements.

W. Thomas Reeder
Director

Patricia Kelly
Chief Financial Officer

November 15, 2016

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF FINANCIAL POSITION

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	September 30,		September 30,		September 30,	
(Dollars in Millions)	**2016**	2015	**2016**	2015	**2016**	2015
ASSETS						
Cash and cash equivalents	**$4,423**	$ 3,694	**$102**	$ 11	**$4,525**	$ 3,705
Securities lending collateral (Notes 3 and 5)	**1,910**	1,245	**-**	-	**1,910**	1,245
Investments, at market (Notes 3 and 5):						
Fixed maturity securities	**57,292**	49,778	**1,925**	1,749	**59,217**	51,527
Equity securities	**23,684**	22,466	**-**	-	**23,684**	22,466
Private equity	**721**	895	**-**	-	**721**	895
Real estate and real estate investment trusts	**2,963**	2,855	**-**	-	**2,963**	2,855
Other	**72**	10	**-**	-	**72**	10
Total investments	**84,732**	76,004	**1,925**	1,749	**86,657**	77,753
Receivables, net:						
Sponsors of terminated plans	**55**	46	**-**	-	**55**	46
Premiums (Note 11)	**4,534**	3,375	**165**	154	**4,699**	3,529
Sale of securities	**1,080**	559	**-**	-	**1,080**	559
Derivative contracts (Note 4)	**124**	374	**-**	-	**124**	374
Investment income	**441**	392	**10**	8	**451**	400
Other	**6**	5	**-**	-	**6**	5
Total receivables	**6,240**	4,751	**175**	162	**6,415**	4,913
Capitalized assets, net	**37**	41	**2**	2	**39**	43
Total assets	**$97,342**	$85,735	**$2,204**	$1,924	**$99,546**	$87,659

The accompanying notes are an integral part of these financial statements.

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF FINANCIAL POSITION

(Dollars in Millions)	Single-Employer Program September 30, 2016	2015	Multiemployer Program September 30, 2016	2015	Memorandum Total September 30, 2016	2015
LIABILITIES						
Present value of future benefits, net (Note 6):						
Trusted plans	**$113,011**	$ 105,932	-	-	**$113,011**	$ 105,932
Plans pending termination and trusteeship	**296**	383	-	-	**296**	383
Settlements and judgments	**21**	26	-	-	**21**	26
Claims for probable terminations	**376**	585	-	-	**376**	585
Total present value of future benefits, net	**113,704**	106,926	-	-	**113,704**	106,926
Present value of nonrecoverable future financial assistance (Note 7)						
Insolvent plans	-	-	**2,139**	1,627	**2,139**	1,627
Probable insolvent plans	-	-	**58,870**	52,559	**58,870**	52,559
Total present value of nonrecoverable future financial assistance	-	-	**61,009**	54,186	**61,009**	54,186
Payables, net:						
Derivative contracts (Note 4)	**49**	334	-	-	**49**	334
Due for purchases of securities	**2,037**	1,100	-	-	**2,037**	1,100
Payable upon return of securities loaned	**1,910**	1,245	-	-	**1,910**	1,245
Unearned premiums	**167**	138	**7**	8	**174**	146
Accounts payable and accrued expenses (Note 8)	**55**	57	**21**	14	**76**	71
Total payables	**4,218**	2,874	**28**	22	**4,246**	2,896
Total liabilities	**117,922**	109,800	**61,037**	54,208	**178,959**	164,008
Net position	**(20,580)**	(24,065)	**(58,833)**	(52,284)	**(79,413)**	(76,349)
Total liabilities and net position	**$97,342**	$ 85,735	**$2,204**	$1,924	**$99,546**	$ 87,659

The accompanying notes are an integral part of these financial statements.

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION

(Dollars in Millions)	Single-Employer Program For the Years Ended September 30, 2016	2015	Multiemployer Program For the Years Ended September 30, 2016	2015	Memorandum Total For the Years Ended September 30, 2016	2015
UNDERWRITING:						
Income:						
Premium, net (Note 11)	**$6,379**	$ 4,138	**$282**	$ 212	**$6,661**	$ 4,350
Other	**25**	11	**-**	-	**25**	11
Total	**6,404**	4,149	**282**	212	**6,686**	4,361
Expenses:						
Administrative	**362**	354	**39**	32	**401**	386
Other	**4**	30	**-**	-	**4**	30
Total	**366**	384	**39**	32	**405**	416
Other underwriting activity:						
Losses (credits) from completed and probable terminations (Note 12)	**(417)**	(780)	**-**	-	**(417)**	(780)
Losses from insolvent and probable plans-financial assistance (Note 7)	**-**	-	**6,768**	9,963	**6,768**	9,963
Actuarial adjustments (credits) (Note 6)	**2,285**	314	**11**	7	**2,296**	321
Total	**1,868**	(466)	**6,779**	9,970	**8,647**	9,504
Underwriting gain (loss)	**4,170**	4,231	**(6,536)**	(9,790)	**(2,366)**	(5,559)
FINANCIAL:						
Investment income (loss) (Note 13):						
Fixed	**5,780**	1,045	**143**	68	**5,923**	1,113
Equity	**2,768**	(1,231)	**-**	-	**2,768**	(1,231)
Private equity	**81**	125	**-**	-	**81**	125
Real estate	**7**	379	**-**	-	**7**	379
Other	**12**	6	**-**	-	**12**	6
Total	**8,648**	324	**143**	68	**8,791**	392
Expenses:						
Investment	**103**	92	**-**	-	**103**	92
Actuarial charges (Note 6):						
Due to expected interest	**2,929**	3,339	**56**	51	**2,985**	3,390
Due to change in interest factors	**6,301**	5,851	**100**	77	**6,401**	5,928
Total	**9,333**	9,282	**156**	128	**9,489**	9,410
Financial gain (loss)	**(685)**	(8,958)	**(13)**	(60)	**(698)**	(9,018)
Net income (loss)	**3,485**	(4,727)	**(6,549)**	(9,850)	**(3,064)**	(14,577)
Net position, beginning of year	**(24,065)**	(19,338)	**(52,284)**	(42,434)	**(76,349)**	(61,772)
Net position, end of year	**($20,580)**	$ (24,065)	**($58,833)**	$ (52,284)	**($79,413)**	$ (76,349)

The accompanying notes are an integral part of these financial statements.

PENSION BENEFIT GUARANTY CORPORATION

STATEMENTS OF CASH FLOWS

(Dollars in millions)	Single-Employer Program For the Years Ended September 30, 2016	2015	Multiemployer Program For the Years Ended September 30, 2016	2015	Memorandum Total For the Years Ended September 30, 2016	2015
OPERATING ACTIVITIES:						
Premium receipts	**$ 5,250**	$ 3,571	**$ 270**	$ 125	**$ 5,520**	$ 3,696
Interest and dividends received	**2,107**	2,341	**46**	49	**2,153**	2,390
Cash received from plans upon trusteeship	**25**	22	**-**	-	**25**	22
Receipts from sponsors/non-sponsors	**88**	123	**-**	-	**88**	123
Receipts from the missing participant program	**6**	6	**-**	-	**6**	6
Other receipts	**6**	-	**-**	-	**6**	-
Benefit payments – trusteed plans	**(5,592)**	(5,525)	**-**	-	**(5,592)**	(5,525)
Financial assistance payments	**-**	-	**(113)**	(103)	**(113)**	(103)
Settlements and judgments	**(11)**	(6)	**-**	-	**(11)**	(6)
Payments for administrative and other expenses	**(454)**	(441)	**(28)**	(28)	**(482)**	(469)
Accrued interest paid on securities purchased	**(284)**	(227)	**(6)**	(6)	**(290)**	(233)
Net cash provided (used) by operating activities (Note 15)	**1,141**	(136)	**169**	37	**1,310**	(99)
INVESTING ACTIVITIES:						
Proceeds from sales of investments	**82,406**	70,708	**1,384**	2,770	**83,790**	73,478
Payments for purchases of investments	**(82,818)**	(71,385)	**(1,462)**	(2,805)	**(84,280)**	(74,190)
Net change in investment of securities lending collateral	**665**	(1,623)	**-**	-	**665**	(1,623)
Net change in securities lending payable	**(665)**	1,623	**-**	-	**(665)**	1,623
Net cash provided (used) by investing activities	**(412)**	(677)	**(78)**	(35)	**(490)**	(712)
Net increase (decrease) in cash and cash equivalents	**729**	(813)	**91**	2	**820**	(811)
Cash and cash equivalents, beginning of year	**3,694**	4,507	**11**	9	**3,705**	4,516
Cash and cash equivalents, end of year	**$ 4,423**	$ 3,694	**$ 102**	$ 11	**$ 4,525**	$ 3,705

The above cash flows are for trusteed plans and do not include non-trusteed plans.
The accompanying notes are an integral part of these financial statements

NOTES TO FINANCIAL STATEMENTS

September 30, 2016 and 2015

NOTE 1: ORGANIZATION AND PURPOSE

The Pension Benefit Guaranty Corporation (PBGC or the Corporation) is a federal corporation created by Title IV of the Employee Retirement Income Security Act of 1974 (ERISA) and is subject to the provisions of the Government Corporation Control Act. Its activities are defined by ERISA, as that act has been amended over the years. The Corporation insures the pension benefits, within statutory limits, of participants in covered single-employer and multiemployer defined benefit pension plans.

ERISA requires that PBGC programs be self-financing. ERISA provides that the U.S. Government is not liable for any obligation or liability incurred by PBGC.

For financial statement purposes, PBGC divides its business activity into two broad areas — "Underwriting Activity" and "Financial Activity" — covering both single-employer and multiemployer program segments. PBGC's Underwriting Activity provides financial guaranty insurance in return for insurance premiums (whether actually paid or not). Actual and expected probable losses that result from the termination of underfunded pension plans are included in this category, as are actuarial adjustments based on changes in actuarial assumptions, such as mortality. Financial Activity consists of the performance of PBGC's assets and liabilities. PBGC's assets consist of premiums collected from defined benefit plan sponsors, assets from distress or involuntarily terminated plans that PBGC has insured, and recoveries from the former sponsors of those terminated plans. PBGC's future benefit liabilities consist of those future benefits, under statutory limits, that PBGC has assumed following distress or involuntary terminations. Gains and losses on PBGC's investments and changes in the value of PBGC's future benefit liabilities (e.g., actuarial charges such as changes in interest factors and expected interest) are included in this area.

As of September 30, 2016, the single-employer and multiemployer programs reported net positions of $(20,580) million and $(58,833) million, respectively. The single-employer program had assets of $97,342 million offset by total liabilities of $117,922 million, which include a total present value of future benefits (PVFB) of $113,704 million. As of September 30, 2016, the multiemployer program had assets of $2,204 million offset by $61,009 million in present value of nonrecoverable future financial assistance. Notwithstanding these deficits, the Corporation has sufficient liquidity to meet its obligations (liabilities) for a significant number of years; however, neither program at present has the resources to fully satisfy PBGC's long-term obligations to plan participants.

PBGC's $91,633 million of total investments (including cash and investment income receivable) represents the largest component of PBGC's Statements of Financial Position combined assets of $99,546 million at September 30, 2016. This amount of $91,633 million (as compared to investments under management of $89,492 million, as reported in section VII Investment Activities) reflects the fact that PBGC experiences a recurring inflow of trusteed plan assets that have not yet been incorporated into the PBGC investment program. For total investments (i.e., not the investment program), cash and fixed-income securities ($64,187 million) represent 70 percent of the total investments, while equity securities ($23,690 million) represent 26 percent of total investments. Private market assets, real estate, and other investments ($3,756 million), represent 4 percent of the total investments.

SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAM EXPOSURE

PBGC's estimate of the total underfunding in single-employer plans was $223,275 million for those sponsored by companies that have credit ratings below investment grade and that PBGC classified as reasonably possible of termination, as of September 30, 2016. This is an increase of $5,576 million from the

reasonably possible exposure of $217,699 million in FY 2015. This increase is primarily due to the growth in the number of companies meeting the reasonably possible criteria. These estimates are measured as of December 31 of the previous year (see Note 9). For FY 2016, this exposure is concentrated in the following sectors: manufacturing (primarily automobile/auto parts and fabricated metals), transportation (primarily airlines)/communications/utilities, and services.

PBGC estimates that as of September 30, 2016, it is reasonably possible that multiemployer plans may require future financial assistance in the amount of $19,485 million (see Note 9). This is a decrease of $472 million from the reasonably possible exposure of $19,957 million in FY 2015. The primary reason for the decrease in liability was due to changes in the data and underlying assumptions. The change in data was a result of updated plan asset and liability information. The changes in assumptions include the reduction in discount factors, an update to the small plan bulk reserve process, and the revised procedure for determining the guaranteed benefit reduction factor (an assumption that both retirees and terminated vested participants have smaller guaranteed benefits compared to that of a higher assumption that was used prior to September 30, 2016).

There is significant volatility in plan underfunding and sponsor credit quality over time, which makes long-term estimation of PBGC's expected claims difficult. This volatility, along with the concentration of claims in a relatively small number of terminated plans, has characterized PBGC's experience to date and will likely continue. Among the factors that will influence PBGC's claims going forward are economic conditions affecting interest rates, financial markets, and the rate of business failures.

PBGC's sources of information on plan underfunding are the most recent Section 4010 and PBGC premium filings, and other submissions to the Corporation. PBGC publishes Table S-49, "Various Measures of Underfunding in PBGC-Insured Plans," in its Pension Insurance Data Tables where the limitations of the estimates are fully and appropriately described.

Under the single-employer program, PBGC is liable for the payment of guaranteed benefits with respect only to underfunded terminated plans. An underfunded plan may terminate only if PBGC or a bankruptcy court finds that one of the four conditions for a distress termination, as defined in ERISA, is met or if PBGC involuntarily terminates a plan under one of five specified statutory tests. The net liability assumed by PBGC is generally equal to the present value of the future benefits payable by PBGC less amounts provided by the plan's assets and amounts recoverable by PBGC from the plan sponsor and members of the plan sponsor's controlled group, as defined by ERISA.

Under the multiemployer program, if a plan becomes insolvent, it receives financial assistance from PBGC to allow the plan to continue to pay participants their guaranteed benefits. PBGC recognizes assistance as a loss to the extent that the plan is not expected to be able to repay these amounts from future plan contributions, employer withdrawal liability or investment earnings. Since multiemployer plans do not receive PBGC assistance until fully insolvent, financial assistance is almost never repaid; for this reason, such assistance is fully reserved.

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). The preparation of the financial statements, in conformity with U.S. GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

Estimates and assumptions may change over time as new information is obtained or subsequent developments occur. Actual results could differ from those estimates.

RECENT ACCOUNTING DEVELOPMENTS

In May 2015, the FASB issued Update No. 2015-07, "Fair Value Measurement (Topic 820, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)," which removes investments from the fair value hierarchy for which the practical expedient is used to measure fair value at net asset value (NAV). Instead, an entity is required to include those investments as a reconciling line item so that the total fair value amount of investments in the disclosure is consistent with the amount on the balance sheet. The amendment is effective beginning October 1, 2017. Adoption of this amendment is not expected to have a material effect on our financial statements.

In April 2015, the FASB issued Update No. 2015-05, "Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40; Customer's Accounting for Fees Paid in a Cloud Computing Arrangement)," which provides guidance in evaluating the accounting for fees paid by a customer in a cloud computing arrangement. The amendment, which allows for early adoption, is effective beginning October 1, 2016. Adoption of this update will not affect PBGC's financial statements.

In February 2015, the FASB issued an amendment to U.S. GAAP to remove the concept of "extraordinary items," which are defined as items that are unusual and infrequent in nature. The amendment, which allows for early adoption, is effective beginning on October 1, 2016. Adoption of this amendment is not expected to have an impact on our financial statements.

VALUATION METHOD

A primary objective of PBGC's financial statements is to provide information that is useful in assessing PBGC's present and future ability to ensure that its plan beneficiaries receive benefits when due. Accordingly, PBGC values its financial assets at estimated fair value, consistent with the standards for pension plans contained in the FASB Accounting Standards Codification Section 960, Defined Benefit Pension Plans. PBGC values its liabilities for the present value of future benefits and present value of nonrecoverable future financial assistance using assumptions derived from market-based (fair value) annuity prices from insurance companies, as described in the Statement of Actuarial Opinion. As described in Section 960, the assumptions are "those assumptions that are inherent in the estimated cost at the (valuation) date to obtain a contract with an insurance company to provide participants with their accumulated plan benefits." Also, in accordance with Section 960, PBGC selects assumptions for expected retirement ages and the cost of administrative expenses in accordance with its best estimate of anticipated experience.

The FASB Accounting Standards Codification Section 820, "Fair Value Measurements and Disclosures," defines fair value, establishes a framework for measuring fair value in U.S. GAAP, and expands disclosures about fair value measurements. Section 820 applies to accounting pronouncements that require or permit fair value measurements.

REVOLVING AND TRUST FUNDS

PBGC accounts for its single-employer and multiemployer programs' revolving and trust funds on an accrual basis. Each fund is charged its portion of the benefits paid each year. PBGC includes totals for the revolving and trust funds for presentation purposes in the financial statements; however, the single-employer and multiemployer programs are separate programs by law and, therefore, PBGC also reports them separately.

ERISA provides for the establishment of the revolving fund where premiums are collected and held. The assets in the revolving fund are used to cover deficits incurred by plans trusteed and to provide funds for

financial assistance. The Pension Protection Act of 1987 created a single-employer revolving fund (Fund 7) that is credited with all premiums in excess of $8.50 per participant, including all penalties and interest charged on these amounts, and its share of earnings from investments. This fund may not be used to pay PBGC's administrative costs or the benefits of any plan terminated prior to October 1, 1988, unless no other amounts are available.

The trust funds include assets (e.g., pension plan investments) PBGC assumes (or expects to assume) once a terminated plan has been trusteed, and related investment income. These assets generally are held by custodian banks. The trust funds support the operational functions of PBGC.

The trust funds reflect accounting activity associated with:

1) Trusteed plans (plans for which PBGC has legal responsibility). The assets and liabilities are reflected separately on PBGC's Statements of Financial Position, the income and expenses are included in the Statements of Operations and Changes in Net Position, and the cash flows from these plans are included in the Statements of Cash Flows.

2) Plans pending termination and trusteeship (plans for which PBGC has begun the process for termination and trusteeship by fiscal year-end). The assets and liabilities for these plans are reported as a net amount on the liability side of the Statements of Financial Position under "Present value of future benefits, net." For these plans, the income and expenses are included in the Statements of Operations and Changes in Net Position, but the cash flows are not included in the Statements of Cash Flows.

3) Probable terminations (plans that PBGC determines are likely to terminate and be trusteed by PBGC). The assets and liabilities for these plans are reported as a net amount on the liability side of the Statements of Financial Position under "Present value of future benefits, net." The accrued loss from these plans is included in the Statements of Operations and Changes in Net Position as part of "Losses from completed and probable terminations." The cash flows from these plans are not included in the Statements of Cash Flows. PBGC cannot exercise legal control over a plan's assets until it becomes the trustee.

ALLOCATION OF REVOLVING AND TRUST FUNDS

PBGC allocates assets, liabilities, income, and expenses to the single-employer and multiemployer programs' revolving and trust funds to the extent that such amounts are not directly attributable to a specific fund. Revolving fund investment income is allocated on the basis of each program's average cash and investments available during the year, while the expenses are allocated on the basis of each program's number of ongoing plans. Revolving fund assets and liabilities are allocated according to the year-end equity of each program's revolving funds. Plan assets acquired by PBGC and commingled at PBGC's custodian bank are credited directly to the appropriate fund, while the earnings and expenses on the commingled assets are allocated to each program's trust funds on the basis of each trust fund's value, relative to the total value of the commingled fund.

CASH AND CASH EQUIVALENTS

"Cash" includes cash on hand and demand deposits. "Cash equivalents" are investments with original maturities of one business day or highly liquid investments that are readily convertible into cash within one business day.

SECURITIES LENDING COLLATERAL

PBGC participates in a securities lending program administered by its custodian bank. The custodian bank requires collateral that equals 102 to 105 percent of the securities lent. The collateral is held by the custodian bank. The custodian bank either receives cash or non-cash as collateral or returns collateral to cover mark-to-market changes. Any cash collateral received is invested by PBGC's investment agent. In addition to the lending program managed by the custodian bank, some of PBGC's investment managers are authorized to invest in securities purchased under resale agreements (an agreement with a commitment by the seller to buy a security back from the purchaser at a specified price at a designated future date), and securities sold under repurchase agreements.

INVESTMENT VALUATION AND INCOME

PBGC bases market values on the last sale of a listed security, on the mean of the "bid-and-ask" for nonlisted securities, or on a valuation model in the case of fixed income securities that are not actively traded. These valuations are determined as of the end of each fiscal year. Purchases and sales of securities are recorded on the trade date. In addition, PBGC invests in and discloses its derivative investments in accordance with the guidance contained in the FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*. Investment income is accrued as earned. Dividend income is recorded on the ex-dividend date. Realized gains and losses on sales of investments are calculated using first-in, first-out for the revolving fund and weighted average cost for the trust fund. PBGC marks the plan's assets to market, and any increase or decrease in the market value of a plan's assets occurring after the date on which the plan is terminated must, by law, be credited to or suffered by PBGC.

SECURITIES PURCHASED UNDER REPURCHASE AGREEMENTS

PBGC's investment managers purchase securities under repurchase agreements, whereby the seller will buy the security back at a pre-agreed price and date. Those greater than one day are reported under "Fixed maturity securities" as "Securities purchased under repurchase agreements" in the Note 3 table entitled "Investments of Single-Employer Revolving Funds and Single-Employer Trusteed Plans,". Repurchase agreements that mature in one day are included in "Cash and cash equivalents," which are reported on the Statements of Financial Position. Refer to Note 3 for further information regarding repurchase agreements.

SPONSORS OF TERMINATED PLANS

The amounts due from sponsors of terminated plans or members of their controlled group represent the settled, but uncollected, claims for employer liability (underfunding as of date of plan termination) and for contributions due their plan less an allowance for estimated uncollectible amounts. PBGC discounts any amounts expected to be received beyond one year for time and risk factors. Some agreements between PBGC and plan sponsors provide for contingent payments based on future profits of the sponsors. The Corporation will report any such future amounts in the period they are realizable. Income and expenses related to amounts due from sponsors are reported in the underwriting section of the Statements of Operations and Changes in Net Position. Interest earned on settled claims for employer liability and due and unpaid employer contributions (DUEC) is reported as "Income: Other." The change in the allowances for uncollectible employer liability and DUEC is reported as "Expenses: Other."

PREMIUMS

Premiums receivable represent the plan reported premiums owed, and the PBGC estimated amounts on filings not yet submitted, for plans that have a plan year commencing before the end of PBGC's fiscal year

and past due premiums deemed collectible, including penalties and interest. The liability for unearned premiums represents annual premium fees that have been received in advance of the period in which they will be earned by PBGC. They remain as liabilities until such time as they are ratably earned over the period of time to which the premium applies. "Premium income, net" represents actual and estimated revenue generated from defined benefit pension plan premium filings as required by Title IV of ERISA less bad debt expense for premiums, interest and penalties (see Note 11).

CAPITALIZED ASSETS

Capitalized assets include furniture and fixtures, electronic processing equipment and internal-use software. This includes costs for internally developed software incurred during the application development stage (system design including software configuration and software interface, coding, and testing including parallel the processing phase). These costs are shown net of accumulated depreciation and amortization.

PRESENT VALUE OF FUTURE BENEFITS (PVFB)

The PVFB is the estimated liability for future pension benefits that PBGC is or will be obligated to pay the participants of trusteed plans and the net liability for plans pending termination and trusteeship. The PVFB liability (including trusteed plans and plans pending termination and trusteeship) is stated as the actuarial present value of estimated future benefits less the present value of estimated recoveries from sponsors and members of their controlled group and the assets of plans pending termination and trusteeship as of the date of the financial statements. PBGC also includes the estimated liabilities attributable to plans classified as probable terminations as a separate line item in the PVFB (net of estimated recoveries and plan assets). PBGC uses assumptions to adjust the value of those future payments to reflect the time value of money (by discounting) and the probability of payment (by means of decrements, such as for death or retirement). PBGC also includes anticipated expenses to settle the benefit obligation in the determination of the PVFB. PBGC's benefit payments to participants reduce the PVFB liability.

The values of the PVFB are particularly sensitive to changes in underlying estimates and assumptions. These estimates and assumptions could change and the impact of these changes may be material to PBGC's financial statements (see Note 6).

(1) Trusteed Plans: Represents the present value of future benefit payments less the present value of expected recoveries (for which a settlement agreement has not been reached with sponsors and members of their controlled group) for plans that have terminated and been trusteed by PBGC prior to fiscal year-end. Assets are shown separately from liabilities for trusteed plans.

(2) Pending Termination and Trusteeship: Represents the present value of future benefit payments less the plans' net assets (at fair value) anticipated to be received and the present value of expected recoveries (for which a settlement agreement has not been reached with sponsors and members of their controlled group) for plans for which termination action has been initiated and/or completed prior to fiscal year-end. Unlike trusteed plans, the liability for plans pending termination and trusteeship is shown net of plan assets.

(3) Settlements and Judgments: Represents estimated liabilities related to settled litigation (see Note 6).

(4) Net Claims for Probable Terminations: In accordance with the FASB Accounting Standards Codification Section 450, *Contingencies*, PBGC recognizes net claims for probable terminations which represent PBGC's best estimate of the losses, net of plan assets, and the present value of expected recoveries (from sponsors and members of their controlled group) for plans that are likely to terminate in the future. Under a specific identification process, PBGC evaluates each controlled group having $50 million or more of underfunding and recognizes a contingent loss for the estimated net claim of those plans meeting the probable termination criteria. These estimated losses are based on conditions that existed as of PBGC's fiscal year-end.

Management believes it is likely that one or more events subsequent to PBGC's fiscal year-end will occur, confirming the loss.

Criteria used for classifying a specific single-employer plan as a probable termination include, but are not limited to, one or more of the following conditions: the plan sponsor is in liquidation or comparable state insolvency proceeding with no known solvent controlled group member; sponsor has filed or intends to file for distress plan termination and the criteria will likely be met; or PBGC is considering the plan for involuntary termination. In addition, management takes into account other economic events and factors in making judgments regarding the classification of a plan as a probable termination. These events and factors may include, but are not limited to, the following: the plan sponsor is in bankruptcy or has indicated that a bankruptcy filing is imminent; the plan sponsor has stated that plan termination is likely; the plan sponsor has received a going concern opinion from its independent auditors; or the plan sponsor is in default under existing credit agreement(s).

In addition, a reserve for small unidentified probable losses is recorded for the estimated future contingent losses stemming from insured single-employer plans with an aggregate underfunding of less than $50 million. The reserve is based on the historic three-year rolling average of actual plan terminations (with an aggregate underfunding of less than $50 million) and indexed to the S&P 500 to reflect changes in economic conditions. (See Note 6 for further information on Net Claims for Probable Terminations).

(5) PBGC identifies certain plans as high-risk if the plan sponsor is in Chapter 11 proceedings or the sponsor's senior unsecured debt is rated CCC+/Caa1 or lower by S&P or Moody's, respectively. PBGC specifically reviews each plan identified as high-risk and classifies those plans as probable if, based on available evidence, PBGC concludes that plan termination is likely (based on criteria described in (4) above). Otherwise, high-risk plans are classified as reasonably possible.

(6) In accordance with the FASB Accounting Standards Codification Section 450, PBGC's exposure to losses from plans of companies that are classified as reasonably possible is disclosed in the footnotes. In order for a plan sponsor to be specifically classified as reasonably possible, it must first have $50 million or more of underfunding, as well as meet additional criteria. Criteria used for classifying a company as reasonably possible include, but are not limited to, one or more of the following conditions: the plan sponsor is in Chapter 11 reorganization; a funding waiver is pending or outstanding with the Internal Revenue Service; the sponsor missed a minimum funding contribution; the sponsor's bond rating is below investment-grade for Standard & Poor's (BB+) or Moody's (Ba1); or the sponsor has no bond rating but the Dun & Bradstreet Financial Stress Score is below the threshold considered to be investment grade (see Note 9).

PRESENT VALUE OF NONRECOVERABLE FUTURE FINANCIAL ASSISTANCE

In accordance with Title IV of ERISA, PBGC provides financial assistance to multiemployer plans, in the form of loans, to enable the plans to pay guaranteed benefits to participants and reasonable administrative expenses. These loans, issued in exchange for interest-bearing promissory notes, constitute an obligation of each plan.

The present value of nonrecoverable future financial assistance represents the estimated nonrecoverable payments to be provided by PBGC in the future to multiemployer plans that will not be able to meet their benefit obligations. The present value of nonrecoverable future financial assistance is based on the difference between the present value of future guaranteed benefits and expenses and the market value of plan assets, including the present value of future amounts expected to be paid by employers, for those plans that are expected to require future assistance. The amount reflects the rates at which, in the opinion of management, these liabilities (net of expenses) could be settled in the market for single-premium nonparticipating group annuities issued by private insurers (see Note 7).

A liability for a particular plan is included in the "Present Value of Nonrecoverable Future Financial Assistance" when it is determined that the plan is currently, or will likely become in the future, insolvent and will require assistance to pay the participants their guaranteed benefit. In accordance with the FASB Accounting Standards Codification Section 450, *Contingencies*, PBGC recognizes net claims for probable insolvencies for plans that are likely to become insolvent and may require future financial assistance. Projecting a future insolvency requires considering several complex factors, such as an estimate of future cash flows, future mortality rates, and age of participants not in pay status.

Each year, PBGC analyzes insured multiemployer plans to identify those plans that are at risk of becoming claims on the insurance program. Regulatory filings with PBGC and the other ERISA agencies are important to this analysis and determination of risk. In general, if a terminated plan's assets are less than the present value of its liabilities, PBGC considers the plan a probable risk of requiring financial assistance in the future.

PBGC also analyzes ongoing multiemployer plans (i.e., plans that continue to have employers making regular contributions for covered work) to determine whether any such plans may be probable or possible claims on the insurance program. In conducting this analysis each year, PBGC examines plans that are chronically underfunded, have poor cash flow trends, that have a falling contribution base, and that may lack a sufficient asset cushion to weather income losses. A combination of these factors, or any one factor that is of sufficient concern, leads to a more detailed analysis of the plan's funding and the likelihood that the contributing employers will be willing and able to maintain the plan.

PBGC uses specific criteria for classifying as insolvent (PBGC's insurable event for multiemployer plans), probable, and reasonably possible multiemployer plans. The criteria are as follows:

- Any multiemployer plans currently receiving financial assistance are classified as insolvent.
- Terminated, underfunded multiemployer plans (i.e., "wasting trusts") are classified as probable.
- Ongoing multiemployer plans projected to become insolvent:
    - Within 10 years are classified as probable.
    - From 10 to 20 years are classified as reasonably possible.

In addition, for small plans (fewer than 2,500 participants), the estimated probable and reasonably possible losses are accrued for the estimated future contingent losses stemming from the multiemployer program. This small plan bulk reserve uses an aggregate method to estimate liability and exposure, rather than reviewing each plan individually, based on the use of seven years of plan termination history to project the current probable liability. The small plan probables are calculated using a seven-year ratio of new plan terminations or insolvencies to the total unfunded liability in a given year. This ratio is applied to the current unfunded liability for small plans to calculate the probable exposure.

In general, the date of insolvency is estimated by projecting plan cash flows using PBGC's actuarial assumptions for terminated plans, but also considered are projections based on other assumptions, such as those used by the plan actuary.

MPRA provides that certain plans may apply to the Department of the Treasury to suspend benefits, and provides for a participant vote on the benefit suspension. These plans also may apply to PBGC for financial assistance: either for a facilitated merger or for a partition. Application for partition generally will occur in conjunction with an application to Treasury for benefit suspension. These actions are not considered in the determination of whether nonrecoverable future financial assistance is probable until the approval has been granted and the changes in benefit payments have commenced.

The present value of nonrecoverable future financial assistance is presented in the Liability section of the Statements of Financial Position (see Note 7).

ADMINISTRATIVE EXPENSES

These operating expenses (for either the single-employer or multiemployer insurance programs) are amounts paid and accrued for services rendered or while carrying out other activities that constitute PBGC's ongoing operations (e.g., payroll, contractual services, office space, materials and supplies). An expense allocation methodology is used to fully capture the administrative expenses attributable to either the single-employer or multiemployer insurance programs. All indirect administrative expenses associated with the single-employer and multiemployer programs are being allocated using the number of ongoing plans in each program.

OTHER EXPENSES

These expenses represent an estimate of the net amount of receivables deemed uncollectible during the period. The estimate is based on the most recent status of the debtor (e.g., sponsor), the age of the receivables and other factors that indicate the element of uncollectibility in the receivables outstanding.

LOSSES FROM COMPLETED AND PROBABLE TERMINATIONS

Amounts reported as losses from completed and probable terminations represent the difference as of the actual or expected date of plan termination (DOPT) between the present value of future benefits (including amounts owed under Section 4022(c) of ERISA) assumed, or expected to be assumed, by PBGC, less related plan assets, and the present value of expected recoveries from sponsors and members of their controlled group (see Note 12). When a plan terminates, the previously recorded probable net claim is reversed and newly estimated DOPT plan assets, recoveries and PVFB are netted and reported on the line "PVFB - Plans pending termination and trusteeship" (this value is usually different from the amount previously reported), with any change in the estimate being recorded in the Statements of Operations and Changes in Net Position. In addition, the plan's net income from DOPT to the beginning of PBGC's fiscal year is included as a component of losses from completed and probable terminations for plans with termination dates prior to the year in which they were added to PBGC's inventory of terminated plans.

ACTUARIAL ADJUSTMENTS AND CHARGES (CREDITS)

PBGC classifies actuarial adjustments related to insurance-based changes in method and the effect of experience as underwriting activity; actuarial adjustments are the result of the movement of plans from one valuation methodology to another, (e.g., nonseriatim), (calculating the liability for the group) to seriatim (calculating separate liability for each person), and of new updated data (e.g., deaths, revised participant data). Actuarial charges (credits) are related to changes in interest factors, and expected interest is classified as financial activity. These adjustments and charges (credits) represent the change in the PVFB that results from applying actuarial assumptions in the calculation of future benefit liabilities (see Note 6).

DEPRECIATION AND AMORTIZATION

PBGC calculates depreciation on the straight-line basis over estimated useful lives of five years for equipment and 10 years for furniture and fixtures. PBGC calculates amortization for capitalized software, which includes certain costs incurred for purchasing and developing software for internal use, on the straight-line basis over estimated useful lives not to exceed five years, commencing on the date that the Corporation determines that the internal-use software is implemented. Routine maintenance and leasehold improvements (the amounts of which are not material) are charged to operations as incurred. Capitalization of software cost occurs during the development stage, and costs incurred during the preliminary project and post-implementation stages are expensed as incurred.

NOTE 3: INVESTMENTS

Premium receipts are invested through the revolving fund in U.S. Treasury securities. The trust funds include assets that PBGC assumes or expects to assume with respect to terminated plans (e.g., recoveries from sponsors) and investment income thereon. These assets generally are held by custodian banks. The basis and market value of the investments by type are detailed below, as well as related investment profile data. The basis indicated is the cost of the asset if assumed after the date of plan termination or the market value at date of plan termination if the asset was assumed as a result of a plan's termination. PBGC marks the plan's assets to market, and any increase or decrease in the market value of a plan's assets occurring after the date on which the plan is terminated must, by law, be credited to or suffered by PBGC. Investment securities denominated in foreign currency are translated into U.S. dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income, and expenses are translated into U.S. dollars at the prevailing exchange rates on the respective dates of the transactions. The portfolio does not isolate that portion of the results of operations resulting from changes in foreign exchange rates of investments from the fluctuations arising from changes in market prices of securities held. Such fluctuations are included with the net realized and unrealized gain or loss on investments. For PBGC's securities, unrealized holding gains and losses are both recognized by including them in earnings. Unrealized holding gains and losses measure the total change in fair value — consisting of unpaid interest income earned or unpaid accrued dividend and the remaining change in fair value from holding the security.

To Be Announced (TBA) and Bond Forward transactions are recorded as regular buys and sells of investments and not as derivatives. TBA is a contract for the purchase or sale of mortgage-backed securities to be delivered on a future date. The term TBA is derived from the fact that the actual mortgage-backed security that will be delivered to fulfill a TBA trade is not designated at the time the trade is made. The securities are to be announced 48 hours prior to the established trade settlement date. TBAs are issued by the Federal Home Loan Mortgage Corporation (FHLMC), the Federal National Mortgage Association (FNMA), and Government National Mortgage Association (GNMA). In accordance with FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*, TBA and Bond Forward contracts are deemed regular way trades as they are completed within the time frame generally established by regulations and conventions in the market place or by the exchange on which they are executed. Thus, recording of TBA and Bond Forward contracts recognizes the acquisition or disposition of the securities at the full contract amounts on day one of the trade.

Bond Forwards and TBAs are reported to "Receivables, net – Sale of securities" and "Due for purchases of securities" from derivative contracts receivables and payables. As of September 30, 2016, TBA receivables were $498 million and no Bond Forward receivables were reported. In addition, as of September 30, 2016, TBA payables were $1,214 million and no Bond Forward payables were reported.

INVESTMENTS OF SINGLE-EMPLOYER REVOLVING FUNDS AND SINGLE-EMPLOYER TRUSTEED PLANS

	September 30, 2016		September 30, 2015	
(Dollars in millions)	Basis	Market Value	Basis	Market Value
Fixed maturity securities:				
U.S. Government securities	$25,460	$27,070	$21,106	$21,807
Commercial paper/securities purchased under repurchase agreements	128	128	162	162
Asset backed securities	3,815	3,889	3,456	3,502
Pooled funds				
Domestic	1,876	1,827	1,969	1,822
International	213	252	1,144	1,261
Global/other	-	-	-	-
Corporate bonds and other	11,783	12,537	11,247	11,174
International securities	11,311	11,589	10,805	10,050
Subtotal	54,586	57,292	49,889	49,778
Equity securities:				
Domestic	142	162	1,379	1,662
International	769	794	770	736
Pooled funds				
Domestic	10,357	11,424	9,173	9,877
International	8,038	11,300	7,252	10,189
Global/other	4	4	2	2
Subtotal	19,310	23,684	18,576	22,466
Private equity	1,290	721	1,284	895
Real estate and real estate investment trusts	2,613	2,963	2,443	2,855
Insurance contracts and other investments	72	72	9	10
Total(1)	$77,871	$84,732 (2)	$72,201	$76,004

(1) Total includes securities on loan at September 30, 2016, and September 30, 2015, with a market value of $3,037 million and $1,894 million, respectively.

(2) This total of $84,732 million of investments at market value represents the single-employer assets only.

INVESTMENTS OF MULTIEMPLOYER REVOLVING FUNDS AND MULTIEMPLOYER TRUSTEED PLANS

	September 30, 2016		September 30, 2015	
(Dollars in millions)	Basis	Market Value	Basis	Market Value
Investment securities:				
Fixed U.S. Government securities	$1,811	$1,925	$1,696	$1,749
Equity securities	-	-	-	-
Total	$1,811	$1,925	$1,696	$1,749

INVESTMENT PROFILE

	September 30,	
	2016	2015
Fixed Income Assets		
Average Quality	**A**	A
Average Maturity (years)	**13.2**	12.5
Duration (years)	**9.4**	8.4
Yield to Maturity (%)	**2.9**	3.0
Equity Assets		
Average Price/Earnings Ratio	**21.8**	19.7
Dividend Yield (%)	**2.5**	2.7
Beta	**1.0**	1.0

DERIVATIVE INSTRUMENTS

PBGC assigns investment discretion and grants specific authority to all of its investment managers to invest according to specific portfolio investment guidelines the Corporation has established. PBGC further limits the use of derivatives by investment managers through tailored provisions in the investment guidelines with investment managers consistent with PBGC's investment policy statement and overall risk tolerance. These investment managers, who act as fiduciaries to PBGC, determine when it may or may not be appropriate to utilize derivatives in the portfolio(s) for which they are responsible. Investments in derivatives carry many of the same risks of the underlying instruments and carry additional risks that are not associated with direct investments in the securities underlying the derivatives.

Risks may arise from the potential inability to terminate or sell derivative positions, although derivative instruments are generally more liquid than physical market instruments. A liquid secondary market may not always exist for certain derivative positions. Over-the-counter derivative instruments also involve counterparty risk that the other party to the derivative instrument will not meet its obligations.

The use of derivatives by PBGC investment managers is restricted in so far as portfolios cannot use derivatives to create leverage in the portfolios for which they are responsible. Thus, the portfolios shall not utilize derivatives to leverage the portfolio beyond the maximum risk level associated with a fully invested portfolio of physical securities.

Derivative instruments are used to mitigate risk (e.g., adjust duration or currency exposures), enhance investment returns, and/or as liquid and cost-efficient substitutes for positions in physical securities. These derivative instruments are not designated as accounting hedges consistent with FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*, which requires an active designation as a prerequisite for any hedge accounting. PBGC uses a no hedging designation, which results in the gain or loss on a derivative instrument to be recognized currently in earnings. Derivatives are accounted for at fair value in accordance with the FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*. Derivatives are marked to market with changes in value reported as a component of financial income on the Statements of Operations and Changes in Net Position. PBGC presents all derivatives at fair value on the Statements of Financial Position.

During fiscal years 2016 and 2015, PBGC, through its investment managers, invested in investment products that used various U.S. and non-U.S. derivative instruments. Those products included, but are not limited to: index futures, options, money market futures, government bond futures, interest rate, credit default and total return swaps and swaption (an option on a swap) contracts, stock warrants and rights, debt option contracts,

and foreign currency forward and option contracts. Some of these derivatives are traded on organized exchanges and thus bear minimal counterparty risk. The counterparties to PBGC's non-exchange-traded derivative contracts are major financial institutions subject to ISDA (International Swaps and Derivatives Association, Inc.) master agreements and minimum credit ratings. PBGC monitors PBGC's counterparty risk and exchanges collateral under most contracts to further support performance by counterparties. Some of PBGC's non-exchange traded derivative contracts are centrally cleared through a Commodity Futures Trading Commission (CFTC)-recognized clearinghouse and the required margin (collateral) is maintained by the clearinghouse to support the performance by counterparties, which are members of the clearinghouse. A clearinghouse reduces the settlement risks by netting offsetting transactions between multiple counterparties, by requiring higher levels of collateral deposits or margin requirements compared to bilateral arrangements. Settlement risks are also reduced by the clearinghouse providing independent valuation of trades and margin, monitoring the credit worthiness of the clearing firms, and providing a guarantee fund, which could be used to cover losses that exceed a defaulting clearing firm's margin on deposit.

A futures contract is an agreement between a buyer or seller and an established futures exchange clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date) in the future. The futures exchanges and clearinghouses clear, settle, and guarantee transactions occurring through their facilities. Upon entering into a futures contract, an "initial margin" amount (in cash or liquid securities) of generally 1 to 6 percent of the face value indicated in the futures contract is required to be deposited with the broker. Open futures positions are marked to market daily. Subsequent payments known as "variation margin" are made or received by the portfolio dependent upon the daily fluctuations in value of the underlying contract. PBGC maintains adequate liquidity in its portfolio to meet these margin calls.

PBGC also invests in forward contracts. A forward foreign currency contract is a commitment to purchase or sell a foreign currency at the settlement date (in the future) at a negotiated rate. Foreign currency forward, futures, and option contracts may be used as a substitute for cash currency holdings. This is in order to minimize currency risk exposure to changes in foreign currency exchange rates and to adjust overall currency exposure to reflect the investment views of the fixed income and equity portfolio managers regarding relationships between currencies.

A swap is an agreement between two parties to exchange different financial returns on a notional investment amount. The major forms of swaps traded are interest rate swaps, credit default swaps, and total return swaps. These swaps are netted for reporting purposes. PBGC uses swap and swaption contracts to adjust exposure to interest rates, fixed income securities exposure, credit exposure, and equity exposure, and to generate income based on the investment views of the portfolio managers regarding interest rates, indices, and individual issues.

Interest rate swaps involve exchanges of fixed rate and floating rate interest. Interest rate swaps are often used to alter exposure to interest rate fluctuations by swapping fixed rate obligations for floating rate obligations, or vice versa. The counterparties to the swap agree to exchange interest payments on specific dates, according to a predetermined formula. The payment flows are usually netted against each other, with one party paying the difference to the other.

A credit default swap is a contract between a buyer and seller of protection against pre-defined credit events. PBGC may buy or sell credit default swap contracts to seek to increase the portfolio's income or to mitigate the risk of default on portfolio securities.

A total return swap is a contract between a buyer and seller of exposures to certain asset classes, such as equities. PBGC may buy or sell total return contracts to seek to increase or reduce the portfolio's exposure to certain asset classes.

An option contract is a contract in which the writer of the option grants the buyer of the option the right to purchase from (call option) or sell to (put option) the writer a designated instrument at a specified price within a specified period of time.

Stock warrants and rights allow PBGC to purchase securities at a stipulated price within a specified time limit.

For the fiscal years ended September 30, 2016 and 2015, gains and losses from settled margin calls are reported in "Investment income" on the Statements of Operations and Changes in Net Position. Securities and cash are pledged as collateral for derivative contracts (e.g., futures and swaps) and are recorded as a receivable or payable.

Pursuant to the provisions of the FASB Accounting Standards Codification Section 815, *Derivatives and Hedging*, this standard requires the disclosure of fair values of derivative instruments and their gains and losses in its financial statements of both the derivative positions existing at period end and the effect of using derivatives during the reporting period.

The following three key tables present PBGC's use of derivative instruments and its impact on PBGC's financial statements:

- Fair Values of Derivative Instruments – Identifies the location of derivative fair values on the Statements of Financial Position, as well as the notional amounts.
- Offsetting of Derivative Assets – Presents the impact of legally enforceable master netting agreements on derivative assets.
- Offsetting of Derivative Liabilities – Presents the impact of legally enforceable master netting agreements on derivative liabilities.

FAIR VALUES OF DERIVATIVE INSTRUMENTS

	Asset Derivative					
	September 30, 2016			September 30, 2015		
(Dollars in millions)	Statements of Financial Position Location	Notional	FMV	Statements of Financial Position Location	Notional	FMV
Futures	Derivative Contracts	$3,421	$2	Derivative Contracts	$3,453	$13
Swap contracts						
Interest rate swaps	Investments-Fixed	2,866	(14)	Investments-Fixed	4,301	22
Other derivative swaps	Investments-Fixed	1,683	(19)	Investments-Fixed	1,365	(19)
Option contracts	Investments-Fixed	220	2	Investments-Fixed	48	1
Forwards - foreign exchange	Investments-Fixed	13,815	2	Investments-Fixed	9,166	15
	Investments-Equity	-	-	Investments-Equity	-	-

	Liability Derivative					
	September 30, 2016			September 30, 2015		
(Dollars in millions)	Statements of Financial Position Location	Notional	FMV	Statements of Financial Position Location	Notional	FMV
Futures	Derivative Contracts	$2,392	$ (22)	Derivative Contracts	$1,788	$ (11)
Option contracts	Derivative Contracts	352	(5)	Derivative Contracts	167	(1)

Additional information specific to derivative instruments is disclosed in Note 4 – Derivative Contracts, and Note 5 – Fair Value Measurements.

PBGC uses a net presentation on the Statements of Financial Position for those derivative financial instruments entered into with counterparties under legally enforceable master netting agreements. Derivative receivables and derivative payables are netted on the Statements of Financial Position with the same counterparty and the related cash collateral receivables and payables when a legally enforceable master netting agreement exists (i.e., for over-the-counter derivatives). Master netting agreements are used to mitigate counterparty credit risk in certain transactions, including derivatives transactions, repurchase agreements and reverse repurchase agreements. The master netting agreement also may require the exchange of cash or marketable securities to collateralize either party's net position. Any cash collateral exchanged with counterparties under these master netting agreements is also netted against the applicable derivative fair values on the Statements of Financial Position.

OFFSETTING OF DERIVATIVE ASSETS FAIR VALUE

(Dollars in millions)	September 30, 2016			September 30, 2015		
	Gross Amount of Recognized Assets	**Gross Amounts Offset in Statements of Financial Position**	**Net Amounts of Assets Presented in Statements of Financial Position**	Gross Amount of Recognized Assets	Gross Amounts Offset in Statements of Financial Position	Net Amounts of Assets Presented in Statements of Financial Position
Derivatives						
Interest-rate contracts	**$ 3**	**$ (1)**	**$ 2**	$ 105	$ (83)	$ 22
Foreign exchange contracts	**58**	**(34)**	**24**	26	(11)	15
Other derivative contracts[1]	**6**	**(4)**	**2**	3	(3)	-
Cash collateral nettings	**-**	**(4)**	**(4)**	-	(1)	(1)
Total Derivatives	**$ 67**	**$ (43)**	**$ 24**	$ 134	$ (98)	$ 36
Other financial instruments[2]						
Repurchase agreements	**$ 100**	**$ -**	**$ 100**	$ 156	$ -	$ 156
Securities lending collateral	**1,910**	**-**	**1,910**	1,245	-	1,245
Total derivatives and other financial instruments	**$ 2,077**	**$ (43)**	**$ 2,034**	$ 1,535	$ (98)	$ 1,437

(Dollars in millions)	September 30, 2016 Gross Amounts Not Offset in Statements of Financial Position			September 30, 2015 Gross Amounts Not Offset in Statements of Financial Position		
	Net Amount of Assets Presented in Statements of Financial Position	**Collateral Received**	**Net Amount**	Net Amount of Assets Presented in Statements of Financial Position	Collateral Received	Net Amount
Repurchase agreements	**100**	**-**	**100**	156	-	156
Security lending collateral	**1,910**	**(1,910)**	**-**	1,245	(1,245)	-
Total	**$ 2,010**	**$ (1,910)**	**$ 100**	$ 1,401	$ (1,245)	$ 156

(1) Other derivative contracts include total return swaps, currency swaps, and credit default swaps.
(2) Under subheading "Other financial instruments", repurchase agreements and securities lending collateral are presented on a gross basis within the table and on the Statements of Financial Position.

OFFSETTING OF DERIVATIVE LIABILITIES FAIR VALUE

	September 30, 2016			September 30, 2015		
(Dollars in millions)	Gross Amount of Recognized Liabilities	Gross Amounts Offset in Statements of Financial Position	Net Amounts of Assets Presented in Statements of Financial Position	Gross Amount of Recognized Liabilities	Gross Amounts Offset in Statements of Financial Position	Net Amounts of Assets Presented in Statements of Financial Position
Derivatives						
Interest-rate contracts	$ 2	$ (1)	$ 1	$ 83	$ (83)	$ -
Foreign exchange contracts	55	(34)	21	11	(11)	-
Other derivative contracts[1]	26	(4)	22	22	(3)	19
Cash collateral nettings	-	-	-	-	-	-
Total Derivatives	$ 83	$ (39)	$ 44	$ 116	$ (97)	$ 19
Other financial instruments[2]						
Resale agreements	$ -	$ -	$ -	$ -	$ -	$ -
Securities lending collateral	1,910	-	1,910	1,245	-	1,245
Total derivatives and other financial instruments	$ 1,993	$ (39)	$ 1,954	$ 1,361	$ (97)	$ 1,264

(Dollars in millions)	September 30, 2016 Gross Amounts Not Offset in Statements of Financial Position			September 30, 2015 Gross Amounts Not Offset in Statements of Financial Position		
	Net Amount of Liabilities Presented in Statements of Financial Position	**Collateral Received**	**Net Amount**	Net Amount of Liabilities Presented in Statements of Financial Position	Collateral Received	Net Amount
Resale agreements	-	-	-	-	-	-
Security lending collateral	1,910	(1,910)	-	1,245	(1,245)	-
Total	$ 1,910	$ (1,910)	$ -	$ 1,245	$ (1,245)	$ -

[1] Other derivative contracts include total return swaps, currency swaps, and credit default swaps.
[2] Under subheading "Other financial instruments", repurchase agreements and securities lending collateral are presented on a gross basis within the table and on the Statements of Financial Position.

The following table identifies the location of derivative gains and losses on the Statements of Operations and Changes in Net Position as of September 30, 2016, and September 30, 2015.

EFFECT OF DERIVATIVE CONTRACTS ON THE STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION

(Dollars in millions)	Location of Gain or (Loss) Recognized in Income on Derivatives	Amount of Gain or (Loss) Recognized in Income on Derivatives Sept. 30, 2016	Sept. 30, 2015
Futures			
Contracts in a receivable position	Investment Income-Fixed	**($107)**	($69)
Contracts in a receivable position	Investment Income-Equity	**-**	-
Contracts in a payable position	Investment Income-Fixed	**239**	138
Contracts in a payable position	Investment Income-Equity	**-**	-
Swap agreements			
Interest rate swaps	Investment Income-Fixed	**(13)**	(18)
Other derivative swaps	Investment Income-Fixed	**(6)**	(5)
Option contracts			
Options purchased (long)	Investment Income-Fixed	**1**	(1)
Options purchased (long)	Investment Income-Equity	**-**	-
Options written (sold short)	Investment Income-Fixed	**3**	7
Options written (sold short)	Investment Income-Equity	**-**	-
Forward contracts			
Forwards - foreign exchange	Investment Income-Fixed	**(75)**	419
	Investment Income-Equity	**0** *	0 *

* Less than $500,000.

Additional information specific to derivative instruments is disclosed in Note 4 - Derivative Contracts, and Note 5 - Fair Value Measurements.

SECURITIES LENDING

PBGC participates in a securities lending program administered by its custodian bank. The custodian bank requires initial collateral that equals 102 to 105 percent of the securities lent. The collateral is held by the custodian bank or its agent. The custodian bank either receives cash or non-cash as collateral or returns collateral to cover mark-to-market changes. Any cash collateral received is invested by PBGC's investment agent. In addition to the lending program managed by the custodian bank, some of PBGC's investment managers are authorized to invest in securities purchased under resale agreements (an agreement with a commitment by the seller to buy a security back from the purchaser at a specified price at a designated future date).

The average value of securities on loan through September 30, 2016, and through September 30, 2015, was $2,170 million and $2,443 million, respectively. The average value of lendable securities was $24,770 million through September 30, 2016, and $26,099 million through September 30, 2015. The ratio of the average value of securities on loan and the average value of lendable securities is the average utilization rate. This average utilization rate for the fiscal year ending September 30, 2016, was 9%, unchanged from the average utilization rate for the fiscal year ending September 30, 2015.

The average value of U.S. Corporate Bonds and Equity securities on loan through September 30, 2016, was $1,301 million, as compared to $1,456 million through September 30, 2015. The average value of U.S. Corporate Bonds and Equity securities on loan is 60% of the $2,170 million average value of securities on loan through September 30, 2016, as compared to 60% of the $2,443 million average value of securities on loan through September 30, 2015. The average value of lendable U.S. Corporate Bonds and Equity securities was $14,618 million through September 30, 2016, or 59 percent of PBGC's overall average value of lendable securities; while the average value of lendable U.S. Corporate Bonds and Equity securities was $15,876 million through September 30, 2015, or 61 percent of PBGC's overall average value of lendable securities. The average utilization of U.S. Corporate Bonds and Equity securities for fiscal year ending September 30, 2016, was 9%, unchanged from the average utilization rate for the fiscal year ending September 30, 2015.

The average value of U.S. Government securities on loan through September 30, 2016, was $750 million, as compared to $786 million through September 30, 2015. The average value of U.S. Government securities on loan was 35% of the $2,170 million average value of securities on loan through September 30, 2016, as compared to 32% of the $2,443 million average value of securities on loan through September 30, 2015. The average value of lendable U.S. Government securities through September 30, 2016, was $4,674 million, or 19 percent of PBGC's overall average value of lendable securities; whereas the average value of lendable U.S. Government securities through September 30, 2015, was $4,833 million, or 19 percent of PBGC's overall average value of lendable securities. The average utilization of U.S. Government securities for fiscal year ending September 30, 2016, was 16%, unchanged from the average utilization rate for the fiscal year ending September 30, 2015.

The following table presents utilization rates of investment securities in the Security Lending Collateral Program.

UTILIZATION RATES OF SECURITY LENDING COLLATERAL

	Daily Utilization Rates at Sept. 30, 2016	Sept. 30, 2016 Average Utilization Rates	Sept. 30, 2015 Average Utilization Rates
U.S. Corporate Bond & Equity	10%	9%	9%
U.S. Government Securities	24%	16%	16%
Non-U.S. Corporate Bond & Equity	5%	4%	2%
Non- U.S. Fixed Income	1%	2%	4%
Total PBGC Program	11%	9%	9%

The amount of cash collateral received for securities on loan at September 30, 2016, and September 30, 2015, was $1,910 million and $1,245 million, respectively. These amounts are recorded as assets and are offset with a corresponding liability. For lending agreements collateralized by securities, no accompanying asset or liability is recorded, as PBGC does not sell or re-pledge the associated collateral. For those securities lending activities that PBGC directs through its custodian manager, the corporation chooses to invest proceeds from securities lending in the Quality A cash collateral pool. PBGC earned $12 million from its agency securities lending programs as of September 30, 2016. Also contributing to PBGC's securities lending income is its participation in certain pooled index funds. Net income from securities lending is included in "Investment income – Fixed" on the Statements of Operations and Changes in Net Position.

PBGC does not have the right by contract or custom to sell or re-pledge non-cash collateral, and therefore it is not reported on the Statements of Financial Position. Non-cash collateral, which consists of highly rated debt instruments, has increased year over year. This is caused by regulatory changes affecting the brokers who borrow securities that have made the use of cash collateral less attractive and non-cash collateral somewhat more attractive than in prior periods.

REPURCHASE AGREEMENTS

PBGC's repurchase agreements entitle and obligate the Corporation to repurchase or redeem the same or substantially the same securities that were previously transferred as collateralized securities. In addition, repurchase agreements require the Corporation to redeem the collateralized securities, before maturity at a fixed determinable price.

As of September 30, 2016, PBGC had $100 million in repurchase agreements. This amount represents maturities of one day and is reported as an asset and included in the "Cash and cash equivalents" balance. There was no

associated liability for these secured borrowings reported as "Securities sold under repurchase agreements." PBGC has no restrictions placed on the cash received for all of its outstanding repurchase agreements as of September 30, 2016.

NOTE 4: DERIVATIVE CONTRACTS

PBGC's derivative financial instruments are recorded at fair value and are included on the Statements of Financial Position as investments and derivative contracts. Foreign exchange forwards are included in "Fixed maturity securities." Swaps are netted for the individual contracts as "Receivables, net – Derivative contracts" and "Derivative contracts" (liabilities). Bond forwards and TBAs are reclassified as "Receivables, net – Sale of securities" and "Due for purchases of securities" from derivative contracts receivables and payables. The amounts subject to credit risk related to derivative instruments are generally limited to the amounts, if any, by which the counterparty's obligations exceed our obligations with that counterparty. PBGC considers this risk remote and does not expect the settlement of these transactions to have a material effect in the Statements of Operations or Changes in Net Position and Statements of Financial Position.

Amounts in the table below represent the derivative contracts in a receivable position at financial statement date. Collateral deposits of $103 million, which represent cash paid as collateral on certain derivative contracts, are shown below.

DERIVATIVE CONTRACTS

(Dollars in millions)	September 30, 2016	September 30, 2015
Open receivable trades on derivatives:		
Collateral deposits	**$103** [1]	$100 [2]
Futures contracts	**2**	13
Interest rate swaps	**9**	111
Other derivative swaps	**10**	150
Total	**$124**	$374

* Less than $500,000

[1] Where a legally enforceable master netting agreement exists, collateral deposits receivable for derivative contracts will include counterparty netting. Collateral deposits receivable of $103 million are the result of $135 million gross collateral deposits receivable less $32 million collateral deposits receivable netted for swap derivative counterparties.

[2] For fiscal year 2015, where a legally enforceable master netting agreement exists, collateral deposits receivable for derivative contracts will include counterparty netting. Collateral deposits receivable of $100 million are the result of $122 million gross collateral deposits receivable less $22 million collateral deposits receivable netted for swap derivative counterparties.

Amounts in the Derivative Contracts table below represent derivative contracts in a payable position at financial statement date, which PBGC reflects as a liability. Collateral deposits of $4 million, which represent cash received as collateral on certain derivative contracts, are included.

DERIVATIVE CONTRACTS

(Dollars in millions)	September 30, 2016	September 30, 2015
Open payable trades on derivatives:		
Collateral deposits	$4 [1]	$59 [2]
Futures contracts	22	11
Interest rate swaps	8	113
Other derivative swaps	10	150
Options-fixed income	5	1
Total	$49	$334

[1] Where a legally enforceable master netting agreement exists, collateral deposits payable for derivative contracts will include counterparty netting. Collateral deposits payable of $4 million are the result of $36 million gross collateral deposits payable less $32 million collateral deposits receivable netted for swap derivative counterparties.

[2] For fiscal year 2015, where a legally enforceable master netting agreement exists, collateral deposits payable for derivative contracts will include counterparty netting. Collateral deposits payable of $59 million are the result of $81 million gross collateral deposits payable less $22 million collateral deposits receivable netted for swap derivative counterparties.

NOTE 5: FAIR VALUE MEASUREMENTS

Pursuant to the provisions of the FASB Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures*, the standard provides a consistent definition of fair value and establishes a framework for measuring fair value in accordance with U.S. GAAP. It does not require the measurement of financial assets and liabilities at fair value. The standard is intended to increase consistency and comparability in, and disclosures about, fair value measurements by giving users better information about how extensively PBGC uses fair value to measure financial assets and liabilities, the inputs PBGC used to develop those measurements and the effect of the measurements, if any, on the financial condition, results of operations, liquidity and capital.

Section 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an "exit price") in the principal or most advantageous market for an asset or liability in an orderly transaction between market participants on the measurement date. When PBGC measures fair value for its financial assets and liabilities, PBGC considers the principal or most advantageous market in which the Corporation would transact. PBGC also considers assumptions that market participants would use when pricing the asset or liability. When possible, PBGC looks to active and observable markets to measure the fair value of identical, or similar, financial assets or liabilities. When identical financial assets and liabilities are not traded in active markets, PBGC looks to market observable data for similar assets and liabilities. In some instances, certain assets and liabilities are not actively traded in observable markets, and as a result PBGC uses alternative valuation techniques to measure their fair value.

In addition, Section 820 establishes a hierarchy for measuring fair value. That hierarchy is based on the observability of inputs to the valuation of a financial asset or liability as of the measurement date. The standard also requires the recognition of trading gains or losses related to certain derivative transactions whose fair value has been determined using unobservable market inputs.

PBGC believes that its valuation techniques and underlying assumptions used to measure fair value conform to the provisions of Section 820. PBGC has categorized the financial assets and liabilities that PBGC carries at fair value in the Statements of Financial Position based upon the standard's valuation hierarchy. The hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level

1), the next highest priority to pricing methods with significant observable market inputs (Level 2), and the lowest priority to significant unobservable valuation inputs (Level 3).

If the inputs used to measure a financial asset or liability cross different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement. Management's assessment of the significance of a particular input to the overall fair value measurement of a financial asset or liability requires judgment, and considers factors specific to that asset or liability, as follows:

Level 1 - Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market. PBGC's Level 1 investments primarily included are exchange-traded equity securities and certain U.S. Government securities.

Level 2 - Financial assets and liabilities whose values are based on quoted prices for similar assets and liabilities in active markets. PBGC also considers inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability. Level 2 inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets. This includes cash equivalents, securities lending collateral, U.S. Government securities, asset backed securities, fixed foreign investments, corporate bonds, repos, bond forwards, and swaps.
- Quoted prices for identical or similar assets or liabilities in non-active markets. This includes corporate stock, pooled funds fixed income, pooled funds equity, and foreign investments equity.
- Pricing models whose inputs are observable for substantially the full term of the asset or liability — included are insurance contracts and bank loans.
- Pricing models whose inputs are derived principally from or are corroborated by observable market information through correlation or other means for substantially the full term of the asset or liability.

Level 3 - Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable in the market and significant to the overall fair value measurement. These inputs reflect PBGC's judgment about the assumptions that a market participant would use in pricing the asset or liability and based on the best available information. The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. PBGC includes instruments whose values are based on a single source such as a broker, pricing service, or dealer, which cannot be corroborated by recent market transactions. These include fixed maturity securities such as corporate bonds that are comprised of securities that are no longer traded on the active market and/or not managed by any asset manager. Equity securities such as corporate stocks are also included, comprised of securities that are no longer traded on the active market and/or not managed by any asset manager. Real estate funds that invest primarily in U.S. commercial real estate are valued based on each underlying investment within the fund/account; they incorporate valuations that consider the evaluation of financing and sale transactions with third parties, expected cash flows and market-based information, including comparable transactions, and performance multiples, among other factors.

The assets and liabilities that PBGC carries at fair value are summarized by the three levels required by Section 820 in the following table. The fair value of the asset or liability represents the "exit price" – the price that would be received to sell the asset or paid to transfer the liability.

FAIR VALUE MEASUREMENTS ON A RECURRING BASIS AS OF SEPTEMBER 30, 2016

(Dollars in millions)	Quoted Market Prices in Active Markets (Level 1)	Pricing Methods with Significant Observable Market Inputs (Level 2)	Pricing Methods with Significant Unobservable Market Inputs (Level 3)	Total Net Carrying Value in Statements of Financial Position
Assets				
Cash and cash equivalents	$ 482	$ 4,043	-	$ 4,525
Securities lending collateral	-	1,910	-	1,910
Investments:				
Fixed maturity securities				
U.S. Government securities	-	28,995	-	
Commercial paper/securities purchased under repurchase agreements	-	128	-	
Asset backed/Mortgage backed securities	-	3,889	-	
Pooled funds				
Domestic	1	1,720	106	
International	-	252	-	
Global/other	-	-	-	
Corporate bonds and other	2	12,535	-	
International securities	2	11,587		
Total fixed maturity securities	5	59,106	106	59,217
Equity securities:				
Domestic	118	44	0*	
International	788	6	0*	
Pooled funds				
Domestic	0*	11,424	-	
International	-	11,300	-	
Global/other	4			
Total equity securities	910	22,774	0*	23,684
Private equity			721	721
Real estate and real estate investment trusts	1,104	1,538	321	2,963
Insurance contracts and other Investments	-	50	22	72
Receivables: (1)				
Derivative contracts(2)	2	122	-	124
Liabilities				
Payables: (1)				
Derivative contracts(3)	27	22	-	49

* Less than $500,000.

(1) Where a legally enforceable master netting agreement exists, amounts for "Receivables: Derivative contracts" and "Payables: Derivative contracts" will include counterparty netting against Level 2 financial assets and liabilities. The Collateral deposits associated with these related open receivables are $103 million ($135 million gross collateral deposits receivable less $32 million collateral deposits receivable to derivative counterparties). The Collateral deposits associated with the related open payables are $4 million ($36 million gross collateral deposits payable less $32 million collateral deposits receivable from derivative counterparties).

(2) Derivative contracts receivables are comprised of open receivable trades on futures, swaps, and collateral deposits. See the Derivative Contracts table under Note 4.

(3) Derivative contracts payables are comprised of open payable trades on futures, swaps, options, and collateral deposits. See the Derivative Contracts table under Note 4.

As of September 30, 2016, there were no significant transfers between Level 1 and Level 2. The end of the reporting period is the date used to recognize transfers between levels.

CHANGES IN LEVEL 3 ASSETS AND LIABILITIES MEASURED AT FAIR VALUE ON A RECURRING BASIS FOR THE YEAR ENDED SEPTEMBER 30, 2016

(Dollars in millions)	Fair Value at September 30, 2015	Total Realized and Unrealized Gains (Losses) included in Income	Purchases	Sales	Transfers Into Level 3	Transfers Out of Level 3	Fair Value at September 30, 2016	Change in Unrealized Gains (Losses) Related to Financial Instruments held at September 30, 2016(2)
Assets:								
Pooled funds (fixed)	$143	(37)	-	-	-	-	$106	$ (37)
Corporate bonds and other	$ -	-	-	-	-	-	$ -	$ -
Domestic/Int'l equity (1)	$ 0*	0*	0*	(1)	1	-	$ 0*	$ 0*
Private equity	$895	(187)	213	(200)	-	-	$721	$(180)
Real estate & real estate investment trusts	$339	(57)	42	(3)	-	-	$321	$ (57)
Other	$ 9	0*	21	(8)	-	-	$ 22	$ 0*

* Less than $500,000.

(1) Assets which are not actively traded in the market place.
(2) Amounts included in this column solely represent unrealized gains and losses and cannot be derived from other columns from this table.

Pursuant to FASB Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures – Investments in Certain Entities That Calculate Net Asset Value per Share*; additional disclosures for investments priced at net asset value are discussed below.

INVESTMENTS IN CERTAIN ENTITIES THAT CALCULATE NET ASSET VALUE PER SHARE (OR ITS EQUIVALENT) FOR THE YEAR ENDED SEPTEMBER 30, 2016

	Fair Value (in millions)	Unfunded Commitments [1]	Redemption Frequency (If Currently Eligible)	Redemption Notice Period
Real estate (a)	$ 2,963	$ 68	n/a	n/a
Private equity (b)	721	121	n/a	n/a
Pooled funds (c)	24,807	-	n/a	n/a
Total	$ 28,491	$189		

[1] Unfunded amounts include recallable distributions. A substantial portion of the unfunded commitments is unlikely to be called.

a. This class includes 138 real estate investments that invest primarily in U.S. commercial real estate, and to a lesser extent, U.S. residential real estate. The fair value of each individual investment in this class has been estimated using the net asset value of PBGC's ownership interest in partners' capital. Generally, these investments do not have redemption provisions. Distributions from each fund will be received as the underlying assets of the fund will be liquidated over the next 10 years or so. In addition, distributions will also include any periodic income distributions received. No fund investments in this class are planned to be sold. Individual portfolio investments will be sold over time, however, those have not yet been determined.

b. This class includes 569 private market investments that invest primarily in U.S. buyout and U.S. venture capital funds. A small number of those focus on natural resources. These investments do not have redemption provisions. Instead, the nature of the investments in this class is that distributions are received through the liquidation of the underlying assets of the funds. If these investments were held, it is estimated that the underlying assets of the fund would be liquidated over the next 12 years. However, the individual investments that will be sold have not yet been determined. The fair value of each individual investment has been estimated using the net asset value of PBGC's ownership interest in partners' capital.

c. This class includes investments in unit trusts that are intended to match returns of domestic and international indices. Units reflect a pro-rata share of the fund's investments. The per unit net asset value is determined each business day based on the fair value of the fund's investments. Issuances and redemptions are possible daily when a per unit value is determined and are based upon the closing per unit net asset value.

PBGC uses recent prices of group annuities to derive the interest factors used to calculate the present value of future benefit-payment obligations. PBGC determines the interest-factor set that, when combined with a specified mortality table, produces present values that approximate the prices private insurers would charge to annuitize the same benefit-payment obligations.

Based on this valuation and in accordance with the provisions of the FASB Accounting Standards Codification Section 820, *Fair Value Measurements and Disclosures*, the significant unobservable inputs for the liability is the interest rate risk for Level 3 fair value measurements. A change in interest factors has an impact to the calculation of PBGC's PVFB, and the impact will be reflected in the "Due to change in interest factors." The table below summarizes the hypothetical results of using a 100 basis point difference causing the PVFB liability to increase (decrease) with a corresponding decrease (increase) in the interest rates. Furthermore, any such hypothetical change in the PVFB liability would have a corresponding effect on "Due to change in interest factors" expense.

HYPOTHETICAL AND ACTUAL INTEREST RATE SENSITIVITY CALCULATIONS OF PVFB SINGLE-EMPLOYER TRUSTEED PLANS AND THE MULTIEMPLOYER PROGRAM(1)

September 30, 2016 *(Dollars in millions)*	Hypothetical Rates 1.27% for 20 years, 1.14% thereafter	Actual Rates(2) 2.27% for 20 years, 2.14% thereafter	Hypothetical Rates 3.27% for 20 years, 3.14% thereafter
Single-Employer Program	$127,672	**$113,580**	$ 102,002
Multiemployer Program	73,674	**61,009**	50,845
Total	$201,346	**$174,589**	$152,847

(1) Level 3 Fair Value Measurements.
(2) Actual rates and PVFB amounts calculated for September 30, 2016, fiscal year-end financial statements.

NOTE 6: PRESENT VALUE OF FUTURE BENEFITS

The PVFB is the estimated liability for future pension benefits that PBGC is or will be obligated to pay for trusteed plans and plans pending termination and trusteeship. For financial statement purposes, the net assets of plans pending termination and trusteeship (including estimated recoveries, assets, and miscellaneous liabilities) are included in the line item "Plans Pending Termination and Trusteeship." The estimated losses on probable future plan terminations are also included in the PVFB. The PVFB liability is stated as the actuarial present value of estimated future benefit payments.

For FY 2016, PBGC used a 20-year select interest factor of 2.27% followed by an ultimate factor of 2.14% thereafter. In FY 2015, PBGC used a 25-year select interest factor of 2.80% followed by an ultimate factor of 2.86% for the remaining years. These factors were determined to be those needed (given the mortality assumptions), to continue to match the survey of annuity prices provided by the American Council of Life Insurers (ACLI). Both the interest factor and the length of the select period may vary to produce the best fit with these prices. The prices reflect rates at which, in PBGC's opinion, the liabilities (net of administrative expenses) could be settled in the market at September 30, for the respective year, for single-premium nonparticipating group annuities issued by private insurers. Many factors including Federal Reserve policy, changing expectations about longevity risk, and competitive market conditions may affect these rates.

For FY 2016, PBGC used the Retirement Plan 2014 Healthy Male mortality table times 1.09 and the Retirement Plan Healthy Female mortality table times 0.99, each with adjustments before age 50, and projected to 2029 using the MP-2015 scale. For September 30, 2015, PBGC used the Retirement Plan-2000 Combined Healthy (RP-2000 CH) Male and Female Tables, each projected 28 years to 2028 using Scale AA

and set back one year. The number of years that PBGC projects the mortality table reflects the number of years from the base year (2014 in FY 2016 and 2000 in FY 2015) of the table to the end of the fiscal year (2 years in FY 2016, 15 years in FY 2015), plus PBGC's calculated duration of its liabilities (13 years in FY 2015 and FY 2014, respectively).

PBGC utilized the results of its recently completed 2016 mortality study. The study removes the margins used in previous studies and provides the most current mortality tables which best matched PBGC's seriatim population experience. Therefore, PBGC adopted a base mortality table (i.e., RP-2014 as adjusted instead of RP-2000 set back one year) that better reflects actual PBGC mortality experience. The ACLI survey of annuity prices, when combined with the mortality table, provides the basis for determining the interest factors used in calculating the PVFB. The insurance company prices, when combined with the stronger mortality table, results in a higher interest factor.

The expense reserve factor for administrative expenses beginning with the FY 2007 valuation is 1.37 percent plus additional reserves for cases in which plan asset determinations, participant database audits, and actuarial valuations were not yet complete. In addition to the completion of these milestones, PBGC continues to base the reserve on case size, number of participants, and time since trusteeship.

PBGC has in place a policy that allows the Corporation to not decrease a final benefit determination that is overstated by $5 or less. The effect of this policy is carried through to the calculation of the PVFB liability.

The PVFB for trusteed multiemployer plans for FY 2016 and FY 2015 reflect the payment of benefits and the changes in interest and mortality assumptions, expected interest, and the effect of experience.

The resulting liability represents PBGC's best estimate of the measure of anticipated experience under these programs.

The table on the following page summarizes the actuarial adjustments, charges, and credits that explain how the Corporation's single-employer program liability for the PVFB changed for the years ended September 30, 2016, and for the fiscal year ended September 30, 2015.

RECONCILIATION OF THE PRESENT VALUE OF FUTURE BENEFITS
FOR THE YEARS ENDED SEPTEMBER 30, 2016 AND 2015

(Dollars in millions)	September 30, 2016		2015	
Present value of future benefits, at beginning of year -- Single-Employer, net		$106,926		$102,774
Estimated recoveries, prior year		475		56
Assets of terminated plans pending trusteeship, net, prior year		447		226
Present value of future benefits at beginning of year, gross		107,848		103,056
Settlements and judgments, prior year		(26)		(62)
Net claims for probable terminations, prior year		(585)		(401)
Actuarial adjustments -- underwriting:				
Changes in method and assumptions	$2,598		$ 603	
Effect of experience	(313)		(289)	
Total actuarial adjustments -- underwriting	2,285		314	
Actuarial charges -- financial:				
Expected interest	2,929		3,339	
Change in interest factors	6,301		5,851	
Total actuarial charges -- financial	9,230		9,190	
Total actuarial charges, current year		11,515		9,504
Terminations:				
Current year	2,307		1,912	
Changes in prior year	(1,246)		(1,202)	
Total terminations		1,061		710
Benefit payments, current year[1]		(5,659)		(5,570)
Estimated recoveries, current year		(568)		(475)
Assets of terminated plans pending trusteeship, net, current year		(279)		(447)
Settlements and judgments, current year [2]		21		26
Net claims for probable terminations:				
Future benefits[3]	653		1,226	
Estimated plan assets and recoveries from sponsors	(277)		(641)	
Total net claims, current year		376		585
Present value of future benefits, at end of year -- Single-Employer, net		113,704		106,926
Present value of future benefits, at end of year -- Multiemployer		0*		0*
Total present value of future benefits, at end of year, net		$113,704		$106,926

* Less than $500,000 (actual amount is $199,930 and $266,702 for the 10 Pre-MPPA trusteed multiemployer plans at September 30, 2016, and September 30, 2015, respectively).

(1) The benefit payments of $5,659 million at September 30, 2016, and $5,570 million at September 30, 2015, include $67 million in FY 2016 and $45 million in FY 2015, respectively, for benefits paid from plan assets prior to trusteeship.

(2) PBGC determined it is highly unlikely that more than half of the total potential future Page/Collins settlement liability will be paid. Accordingly, PBGC estimates that PBGC's future Page/Collins settlement liability amount is $21 million at September 30, 2016, as compared to $26 million at September 30, 2015.

(3) The future benefits for probable terminations of $653 million and $1,226 million for the periods ending September 30, 2016, and September 30, 2015, include $127 million and $163 million, respectively, for probable terminations not specifically identified, and $526 million and $422 million, respectively, for specifically identified probables.

The following table details the assets that make up single-employer terminated plans pending termination and trusteeship:

ASSETS OF SINGLE-EMPLOYER PLANS PENDING TERMINATION AND TRUSTEESHIP, NET

	September 30, 2016		September 30, 2015	
(Dollars in millions)	**Basis**	**Market Value**	Basis	Market Value
U.S. Government securities	**$ -**	**$ -**	$ -	$ -
Corporate and other bonds	**156**	**156**	284	280
Equity securities	**168**	**168**	170	169
Private equity	**-**	**-**	0 *	0 *
Insurance contracts	**0 ***	**0 ***	0 *	0 *
Other	**(45)**	**(45)**	1	(2)
Total, net	**$ 279**	**$279**	$ 455	$ 447

* Less than $500,000

NET CLAIMS FOR PROBABLE TERMINATIONS

Factors that at present are not fully determinable may be responsible for why these claim estimates differ from actual experience. Included in net claims for probable terminations is a provision for future benefit liabilities for plans not specifically identified. This reserve for small unidentified probable losses is recorded for the estimated future contingent losses stemming from insured single-employer plans with an aggregate underfunding of less than $50 million. The reserve is based on the historic three-year rolling average of actual plan terminations (with an aggregate underfunding of less than $50 million) and indexed to the S&P 500 to reflect changes in economic conditions. The September 30, 2016, Net Claims for Probable Terminations is $376 million, of which $127 million is from the small unidentified probable losses and $249 million is from a specific identification process.

The values recorded in the following reconciliation table have been adjusted to the expected dates of termination.

RECONCILIATION OF NET CLAIMS FOR PROBABLE TERMINATIONS

	September 30,			
(Dollars in millions)	**2016**		2015	
Net claims for probable terminations, at beginning of year		**$ 585**		$ 401
New claims	**$ 249**		$ 422	
Actual terminations	**(382)**		(175)	
Deleted probables	**(40)**		-	
Change in benefit liabilities	**(36)**		(63)	
Change in plan assets	**-**		-	
Loss (credit) on probables		**(209)**		184
Net claims for probable terminations, at end of year		**$ 376**		$ 585

The following table itemizes the single-employer probable exposure by industry:

PROBABLES EXPOSURE BY INDUSTRY (PRINCIPAL CATEGORIES)

(Dollars in millions)	FY 2016	FY 2015
Manufacturing	$ 249	$ -
Retail	-	344
Health Care	-	78
Total	$249	$422

For further detail regarding single-employer probables, see Note 2 under Present Value of Future Benefits (PVFB) subpoint (4).

The following table shows what has happened to plans classified as probables. This table does not capture or include those plans that were not previously classified as probable before they terminated.

ACTUAL PROBABLES EXPERIENCE

As Initially Recorded Beginning in 1987

(Dollars in millions)	Status of Probables from 1987-2015 at September 30, 2016			
Beginning in 1987, number of plans reported as Probable:	Number of Plans	Percent of Plans	Net Claim	Percent of Net Claim
Probables terminated	377	79%	$30,220	72%
Probables not yet terminated or deleted	-	-	-	-
Probables deleted	102	21	12,014	28
Total	479	100%	$42,234	100%

NOTE 7: MULTIEMPLOYER FINANCIAL ASSISTANCE

PBGC provides financial assistance to multiemployer defined benefit pension plans in the form of loans. Since these loans are not generally repaid, an allowance is set up to the extent that repayment of these loans is not expected.

NOTES RECEIVABLE MULTIEMPLOYER FINANCIAL ASSISTANCE

(Dollars in millions)	September 30, 2016	September 30, 2015
Gross balance at beginning of year	$923	$880
Financial assistance payments - current year	113	103
Write-offs related to settlement agreements	0 *	(60)
Subtotal	1,036	923
Allowance for uncollectible amounts	(1,036)	(923)
Net balance at end of year	$ -	$ -

* Less than $500,000

Losses from financial assistance and probable financial assistance are reflected in the Statements of Operations and Changes in Net Position and include period changes in the estimated present value of nonrecoverable future financial assistance. Fiscal year changes are also attributable to the implementation of the revised procedure for determining the guaranteed benefit reduction factor. Losses from financial assistance are presented as actuarial charges, credits, and adjustments for plans that are known to be insolvent

as of the valuation date and/or have or are about to begin receiving financial assistance. In addition, a change in the valuation of the liability due to new data received (e.g., new plan expenses, more recent valuation liabilities, and new withdrawal payment schedules) is included as financial assistance from insolvent and probable plans on the Statements of Operations and Changes in Net Position. This valuation data change is a separate line item from actuarial adjustments and actuarial charges.

To determine the probable liability, ongoing plans are divided into segments based on the number of plan participants with different processes by plan size. The reserve for small ongoing plans (fewer than 2,500 participants) with probable losses not individually identified uses an aggregate method to estimate liability and exposure, rather than reviewing each plan individually, based on the use of seven years of plan termination history to project the current probable liability. For mid-sized plans (2,500 to 35,000 participants), risk-based rules are applied using a cash-flow model. For large plans (more than 35,000 participants), PBGC identifies ongoing high risk plans for a projection of the date of insolvency to measure the probable liability.

MPRA provides that certain plans may apply to the Department of the Treasury to suspend benefits, and provides for a participant vote on the benefit suspension. These plans also may apply to PBGC for financial assistance: either for a facilitated merger or a partition. Application for partition generally will occur in conjunction with an application to Treasury for benefit suspension. These actions are not considered in the determination of whether nonrecoverable future financial assistance is probable until the approval has been granted and the changes in benefit payments have commenced.

As of September 30, 2016, the Corporation expects 168 individually identified multiemployer plans will exhaust plan assets and need financial assistance from PBGC to pay guaranteed benefits and plan administrative expenses. The present value of nonrecoverable future financial assistance for these 168 plans is $61,009 million (inclusive of the reserve for small ongoing plan losses not individually identified). The 168 plans fall into three categories: (1) plans currently receiving financial assistance; (2) plans that have terminated but have not yet started receiving financial assistance from PBGC; and (3) ongoing plans (not terminated) that the Corporation expects will require financial assistance in the future. The latter two categories comprise multiemployer probables as defined by the following classification criteria:

- Probable insolvent plan-terminated future probables: A plan that may still have assets but the combination of plan assets and collectible payments of withdrawal liability are projected to be insufficient to cover plan benefits plus expenses.

- Probable insolvent plan-ongoing future probables: An ongoing plan with a projected date of insolvency within 10 years.

MULTIEMPLOYER FINANCIAL ASSISTANCE

(Dollars in millions)	September 30, 2016		September 30, 2015	
	Number of Plans	Net Liability	Number of Plans	Net Liability
Plans currently receiving financial assistance	**65**	**$2,139**	55	$1,627
Plans that have terminated but have not yet started receiving financial assistance (classified as probable)	**63**	**1,986**	67	2,110
Ongoing plans (not terminated) that the Corporation expects will require financial assistance in the future (classified as probable)	**40**	**56,884** [1]	38	50,449 [1]
Total	**168**	**$61,009**	160	$54,186

[1] Ongoing plans include a small probable bulk reserve of $1,011 million and $1,431 million for September 30, 2016, and September 30, 2015, respectively.

Of the 168 plans:

1) 65 have exhausted plan assets and are currently receiving financial assistance payments from PBGC. The present value of future financial assistance payments for these insolvent 65 plans is $2,139 million.

2) 63 plans have terminated but have not yet started receiving financial assistance payments from PBGC. Terminated multiemployer plans no longer have employers making regular contributions for covered work, though some plans continue to receive withdrawal liability payments from withdrawn employers. In general, PBGC records a loss for future financial assistance for any underfunded multiemployer plan that has terminated. The present value of future financial assistance payments for these 63 terminated plans is $1,986 million.

3) 40 plans are ongoing (i.e., have not terminated), but PBGC expects they will exhaust plan assets and need financial assistance within 10 years. In this analysis, PBGC takes into account the current plan assets, future income to the plan, the statutory funding rules, and the possibility for future increases in contributions. The present value of future financial assistance payments for these 40 ongoing plans is $56,884 million.

PRESENT VALUE OF NONRECOVERABLE FUTURE FINANCIAL ASSISTANCE AND LOSSES FROM FINANCIAL ASSISTANCE

(Dollars in millions)	September 30, 2016	September 30, 2015
Balance at beginning of year	**$54,186**	$44,190
Changes in allowance:		
Losses from insolvent and probable plans - financial assistance	**6,768**	9,963
Actuarial adjustments	**11**	7
Actuarial charges (credits) - Insolvent plans:		
Due to expected interest	**56**	52
Due to change in interest factors	**101**	77
Financial assistance granted (previously accrued)	**(113)**	(103)
Balance at end of period	**$61,009**	$54,186

In the table above, actuarial charges are reported separately from "Losses from insolvent and probable plans-financial assistance." As a result, the table includes the following lines: Actuarial adjustments, Due to expected interest, and Due to change in interest factors. Insolvent plans are presented within these three actuarial charges (credits) lines. "Losses from insolvent and probable plans-financial assistance" include plans that terminated but have not yet received financial assistance, ongoing plans that PBGC expects will require financial assistance in the future, and those insolvent plans that have a change in liability due to new plan data included in the valuation.

NOTE 8: ACCOUNTS PAYABLE AND ACCRUED EXPENSES

The following table itemizes accounts payable and accrued expenses reported in the Statements of Financial Position:

ACCOUNTS PAYABLE AND ACCRUED EXPENSES

(Dollars in millions)	September 30, 2016	September 30, 2015
Annual leave	**$10**	$ 9
Other payables and accrued expenses	**66**	62
Accounts payable and accrued expenses	**$76**	$ 71

NOTE 9: REASONABLY POSSIBLE CONTINGENCIES

SINGLE-EMPLOYER PLANS

Single-employer plans, sponsored by companies whose credit quality is below investment grade pose a greater risk of being terminated. The estimated unfunded vested benefits exposure amounts disclosed represent PBGC's estimates of the reasonably possible exposure to loss given the inherent uncertainties about these plans. In rare circumstances for certain large companies, the reasonably possible exposure calculation reflects the estimated unfunded guaranteed benefit determination rather than the estimated unfunded vested benefit determination.

In accordance with the FASB Accounting Standards Codification Section 450, *Contingencies*, PBGC classified a number of these companies that sponsor plans with total unfunded vested benefits greater than $50 million as reasonably possible rather than probable terminations, reflecting the sponsors' financial condition and other factors that did not indicate termination of their plans was likely. This classification was done based upon information about the companies as of September 30, 2016. PBGC criteria for a single-employer plan sponsor to be classified as Reasonably Possible are:

a. The sponsor(s) or significant member(s) of its controlled group (e.g., a parent or major subsidiary) is in reorganization under Title 11 of the United States Code.

b. An application for a funding waiver is pending or outstanding with the IRS.

c. A minimum funding contribution has been missed.

d. The sponsor(s) has an S&P senior unsecured credit rating or an issuer credit rating less two notches of BB+ or below, or a Moody's senior unsecured credit rating or a corporate family rating less one notch of Ba1 or below. If the controlled group is not rated by Moody's and S&P, PBGC will use the Dun & Bradstreet Financial Stress Score (if available) to classify the controlled group as Reasonably Possible or Remote.

e. The sponsor(s) has no bond rating, but analysis indicates that its unsecured debt would be below investment grade.

f. The sponsor(s) meet at least one of the PBGC "high risk" criteria.

g. Other (detailed explanation must be provided and be approved by PBGC's Contingency Working Group).

A reserve for the small unidentified reasonably possible exposure (companies that sponsor plans with less than $50 million in unfunded vested benefits) is calculated using an aggregate method to estimate liability and exposure, rather than reviewing each company individually.

The estimate of the reasonably possible exposure to loss for the single-employer plans of these companies was measured as of December 31, 2015. The reasonably possible exposure to loss was $223,275 million for FY 2016. This is an increase of $5,576 million from the reasonably possible exposure of $217,699 million in FY 2015. This increase is primarily due to the growth in the number of companies meeting the reasonably possible criteria.

Except in the rare circumstances indicated earlier in this note, the estimate of unfunded vested benefits exposure to loss is not generally based on PBGC-guaranteed benefit levels, since data is not available to determine an estimate at this level of precision. PBGC calculated this estimate, as in previous years, by using the most recent data available from filings and submissions to the Corporation for plan years ended on or after December 31, 2014. PBGC adjusted the value reported for liabilities to December 31, 2015, using a select rate of 2.74% for the first 20 years and 2.86% thereafter and applying the expense load as defined in 29 CFR Part 4044, Appendix C. The rates were derived in conjunction with the 1994 Group Annuity Mortality Static Table (with margins) projected to 2025 using Scale AA to approximate annuity prices as of December 31, 2015. The underfunding associated with these plans could be substantially different at September 30, 2016, because of the economic conditions that changed between December 31, 2015 and September 30, 2016. PBGC did not adjust the estimate for events that occurred between December 31, 2015, and September 30, 2016.

The following table by industry itemizes the single-employer reasonably possible exposure to loss:

REASONABLY POSSIBLE EXPOSURE TO LOSS BY INDUSTRY
(PRINCIPAL CATEGORIES)

(Dollars in millions)	FY 2016	FY 2015
Manufacturing [1]	$85,798	$84,108
Transportation, Communication and Utilities [2]	56,961	57,771
Services	36,066	32,887
Finance, Insurance, and Real Estate	12,782	12,624
Wholesale and Retail Trade	12,141	13,485
Health Care	11,450	12,895
Agriculture, Mining, and Construction	8,077	3,929
Total	$223,275	$217,699

[1] Primarily automobile/auto parts and fabricated metals.

[2] Primarily airlines.

MULTIEMPLOYER PLANS

There are some multiemployer plans that may require future financial assistance. PBGC included amounts in the liability for the present value of nonrecoverable future financial assistance (see Note 7) for multiemployer plans that PBGC estimated may require future financial assistance. In addition, PBGC estimated as of September 30, 2016, that it is reasonably possible that other multiemployer plans may require future financial assistance in the amount of $19,485 million.

PBGC calculated the future financial assistance liability for each multiemployer plan identified as probable (see Note 7), or reasonably possible. PBGC used a formula taking the present value of guaranteed future benefits and expense payments net of any future contributions or withdrawal liability payments. These amounts were as of the latter of September 30, 2016, or the projected (or actual, if known) date of plan insolvency, discounted back to September 30, 2016. PBGC's identification of plans that are likely to require such assistance and estimation of related amounts required consideration of many complex factors, including estimating future cash flows, future mortality rates, and age of participants not in pay status. These factors are affected by future events, including actions by plans and their sponsors, most of which are beyond PBGC's control. Reasonably possible multiemployer classification is defined as an ongoing plan with a projected insolvency date between 10 and 20 years from the valuation date.

To determine the probable liability, ongoing plans are divided into segments based on the number of plan participants with different processes by plan size (see Note 7). The reserve for small unidentified probable losses (fewer than 2,500 participants) uses an aggregate method to estimate liability and exposure, rather than reviewing each plan individually, based on the use of seven years of plan termination history to project the current probable liability. The reasonably possible exposure is derived from the total exposure for high risk plans by subtracting the probable liability for small plans. For mid-sized plans (2,500 to 35,000 participants), risk-based rules are applied using a cash-flow model. For large plans (more than 35,000 participants), PBGC identifies ongoing high risk plans for a projection of the date of insolvency to measure the reasonably possible exposure.

NOTE 10: COMMITMENTS

PBGC leases its office facility under a commitment that began on January 1, 2005, and expires December 10, 2018. This lease provides for periodic rate increases based on increases in operating costs and real estate taxes over a base amount. In addition, PBGC is leasing space for field benefit administrators. These leases began in 1996 and expire in 2021. The minimum future lease payments for office facilities having noncancellable terms in excess of one year as of September 30, 2016, are:

COMMITMENTS: FUTURE LEASE PAYMENTS

(Dollars in millions) Years Ending September 30,	Operating Leases
2017	$ 20.7
2018	19.5
2019	4.9
2020	0.4
2021	0.3
Minimum lease payments	$ 45.8

In addition to the committed minimum operating lease payments of $45.8 million as noted in the table above, PBGC has estimated future uncommitted operating leases of approximately $72 million.

Negotiations are currently underway for an extension of PBGC's current leases to bridge the period between the expiration of the current leases in FY 2019 to the beginning of PBGC's new leases.

Lease expenses were $19.9 million in FY 2016 and FY 2015.

NOTE 11: PREMIUMS

For both the single-employer and multiemployer programs, ERISA provides that PBGC shall continue to guarantee basic benefits despite the failure of a plan administrator to pay premiums when due. PBGC assesses interest and penalties on the late or unpaid portion of premiums. Interest continues to accrue until the premium and the interest due are paid. See Note 2, *Premiums* for PBGC's premium revenue accounting policy. For plan years beginning in 2016, the per-participant flat-rate premium was $64 for single-employer pension plans, $27 for multiemployer plans. For plan years 2015 and 2014, the per-participant flat-rate premiums for single-employer pension plans were $57 and $49, respectively, and for multiemployer plans, $26 and $12, respectively.

Single-employer plans also owe a variable-rate premium (VRP) tied to the amount of underfunding. For plans years beginning in 2016, the VRP rate was $30 per $1,000 of unfunded vested benefits subject to an overall cap of $500 per participant. For plan years 2015 and 2014, the VRP rates were $24 and $14 respectively. Applicable caps for those plan years are shown in a table below.

The termination premium applies to certain plan terminations occurring after 2005. If a pension plan terminates in a distress termination pursuant to ERISA section 4041(c)(2)(B)(ii) or (iii), or in a PBGC-initiated termination under ERISA section 4042, the plan sponsor and its controlled group are liable to PBGC for a termination premium at the rate of $1,250 per plan participant per year for three years.

Net premium income for FY 2016 was $6,661 million and consisted of $4,639 million in variable-rate premiums, $2,026 million in flat-rate premiums, $9 million interest and penalty income, and $5 million in termination premiums, offset by a bad debt expense of $18 million. Bad debt expenses include a reserve for uncollectible premium receivables (including flat, variable, and termination premiums), interest, and penalties.

Net premium income for FY 2015 was $4,350 million and consisted of $2,565 million in variable-rate premiums, $1,768 million in flat-rate premiums, $19 million in termination premiums, and $5 million interest and penalty income, offset by a bad debt expense of $7 million. Bad debt expenses include a reserve for uncollectible premium receivables (including flat, variable, and termination premiums), interest, and penalties.

Illustrated in the table below, on a plan year basis, is the flat-rate and variable-rate premium information for the single-employer and multiemployer programs:

	Single-Employer Plans			Multiemployer Plans
	Flat-Rate Premium	Variable-Rate Premium		
Plan Years Beginning on or after January 1	Rate Per Participant	Rate per $1,000 UVBs	Per Participant Cap	Flat-Rate Premium Rate Per Participant
2016	$64	$30	$500	$27
2015	$57	$24	$418	$26
2014	$49	$14	$412	$12

Premium income is accrued for months in which a plan year overlaps the fiscal year. Because of this rule, premiums for 2014, 2015, and 2016 plan years are accrued in FY 2016, and premium rates change each calendar year, so three sets of premium rates were used to calculate FY 2016 premium revenue.

For example, consider a plan with a September 1 to August 31 plan year. Only the first month of the plan year beginning 09/01/2016 occurs during FY 2016, so 1/12 of the plan's premium for this plan year is accrued in FY 2016 (along with 11/12 of its prior year's premium). Similarly, for a plan with a December 1 to November 30 plan year, the last two months of the plan year beginning 12/01/2014 plan year occur during FY 2016, so 2/12 of this plan's 2014 premium income is accrued in FY 2016 (along with 10/12 of its 2015 premium income).

The following tables present a year-to-year comparison of key premium receivable information.

Net Premiums Receivable

	Single-Employer		Multiemployer		Memorandum Total	
(Dollars in Million)	**Sept. 30, 2016**	Sept. 30, 2015	**Sept. 30, 2016**	Sept. 30, 2015	**Sept. 30, 2016**	Sept. 30, 2015
Premiums Not Yet Due:						
Estimated Flat-Rate Premiums	**$1,035**	$1,015	**$155**	$145	**$1,190**	$1,160
Estimated Variable-Rate Premiums	**3,154**	2,182	**-**	-	**3,154**	2,182
Total Net Premiums Not Yet Due	**4,189**	3,197	**155**	145	**4,344**	3,342
Premiums Past Due:						
Flat-Rate Premiums	**136**	66	**10**	9	**146**	75
Allowance for Bad Debt-Flat-Rate	**(7)**	(3)	**0 ***	0 *	**(7)**	(3)
Variable-Rate Premiums	**207**	103	**-**	-	**207**	103
Allowance for Bad Debt-Variable-Rate	**(10)**	(4)	**-**	-	**(10)**	(4)
Total Net Premiums Past Due	**326**	162	**10**	9	**336**	171
Termination Premiums:[1]						
Termination Premiums	**249**	244	**-**	-	**249**	244
Allowance for Bad Debt-Termination	**(234)**	(229)	**-**	-	**(234)**	(229)
	15	15	**-**	-	**15**	15
Interest and Penalty:						
Interest and Penalty Due	**5**	2	**0 ***	0 *	**5**	2
Allowance for Bad Debt-Int/Penalty	**(1)**	(1)	**0 ***	0 *	**(1)**	(1)
Total Net Interest and Penalty Due	**4**	1	**0 ***	0 *	**4**	1
Grand Total Net Premiums Receivable	**$4,534**	$3,375	**$165**	$154	**$4,699**	$3,529

* Less than $500,000

(1) All termination premiums are due from plan sponsors that are either in distress or under Chapter 11 reorganization. In these cases, PBGC files claims in accordance with bankruptcy law along with all other creditors and is entitled only to a pro-rata share of any remaining assets. Depending on the circumstances of the bankruptcy proceedings, it can be years before PBGC receives its pro-rata distribution from the bankruptcy estate. In most cases, PBGC ultimately receives either nothing or only a very small fraction of its total claims filed.

The following tables presents a year-to-year comparison of key premium income information.

PREMIUM INCOME BY PREMIUM TYPE

(Dollars in Million)	September 30, 2016	September 30, 2015
Flat-Rate Premium:		
Single-Employer	**$1,742**	$1,556
Multiemployer	**284**	212
Total Flat-Rate Premium	**2,026**	1,768
Variable-Rate Premiums	**4,639**	2,565
Interest and Penalty Income	**9**	5
Termination Premium	**5**	19
Less Bad Debts for Interest, Penalties, and Premiums	**(18)**	(7)
Total Net Premiums	**$6,661**	$4,350

PREMIUM INCOME BY PROGRAM

(Dollars in Million)	September 30, 2016	September 30, 2015
Single-Employer:		
Flat-Rate and Variable-Rate Premiums	**$6,381**	$4,121
Interest and Penalty Income	**9**	5
Termination Premiums	**5**	19
Less Bad Debts for Interest, Penalties, and Premiums	**(16)**	(7)
Total Single-Employer	**6,379**	4,138
Multiemployer:		
Flat-Rate Premiums	**284**	212
Interest and Penalty Income	**0** *	0 *
Less Bad Debts for Interest, Penalties, and Premiums	**(2)**	0 *
Total Multiemployer	**282**	212
Total Net Premiums	**$6,661**	$4,350

* Less than $500,000

NOTE 12: LOSSES FROM COMPLETED AND PROBABLE TERMINATIONS

Amounts reported as losses are the present value of future benefits less related plan assets and the present value of expected recoveries from sponsors. The following table details the components that make up the losses:

LOSSES FROM COMPLETED AND PROBABLE TERMINATIONS
SINGLE-EMPLOYER PROGRAM

	For the Years Ended September 30,					
	2016			2015		
(Dollars in millions)	New Terminations	Changes in Prior Years' Terminations[5]	Total	New Terminations	Changes in Prior Years' Terminations[5]	Total
Present value of future benefits	$2,307	$(1,246)	$1,061	$1,912	$(1,202)	$ 710
Less plan assets	1,332	(27)	1,305	1,132	86	1,218
Plan asset insufficiency	975	(1,219)	(244)	780	(1,288)	(508)
Less estimated recoveries	-	(30)	(30)	-	428	428
Subtotal	975[1]	(1,189)	(214)	780[1]	(1,716)	(936)
Settlements and judgments		6[6]	6[6]		(29)[6]	(29)[6]
Loss (credit) on probables	(382)[2]	173[3]	(209)[4]	(175)[2]	360[3]	185[4]
Total	$ 593	$ (1,010)	$(417)	$ 605	$ (1,385)	$(780)

[1] Gross amounts for plans terminated during the period (67 plans at September 30, 2016 and 69 plans at September 30, 2015), including plans previously recorded as probables.

[2] Net claims for plans previously recorded as probables that terminated.

[3] Includes deleted probables and changes to old and new probables.

[4] See Note 6 - includes $382 million at September 30, 2016, and $175 million at September 30, 2015, previously recorded relating to plans that terminated during the period ("Actual terminations").

[5] Changes in prior years' terminations result from revaluations of DOPT assets (e.g., as identified in the plan asset reconciliation process), changes in plan recoveries at DOPT (e.g., from an estimated recovery amount to an expected recovery amount), and changes in DOPT PVFB (e.g., new liability data) for plans with termination dates prior to the current fiscal year in which they were added to PBGC's inventory of terminated plans.

[6] PBGC determined that it is highly unlikely more than half of the total potential future Page/Collins settlement liability will be paid. Accordingly, PBGC estimates that the PBGC's future Page/Collins settlement liability is $21 million at September 30, 2016, as compared to $26 million at September 30, 2015.

NOTE 13: FINANCIAL INCOME

The following table details the combined financial income by type of investment for both the single-employer and multiemployer programs:

INVESTMENT INCOME SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS						
(Dollars in millions)	**Single-Employer Program Sept. 30, 2016**	**Multiemployer Program Sept. 30, 2016**	**Memorandum Total Sept. 30, 2016**	Single-Employer Program Sept. 30, 2015	Multiemployer Program Sept. 30, 2015	Memorandum Total Sept. 30, 2015
Fixed maturity securities:						
Interest earned	**$1,739**	**$38**	**$1,777**	$1,642	$33	$1,675
Realized gain (loss)	**1,204**	**32**	**1,236**	757	24	781
Unrealized gain (loss)	**2,837**	**73**	**2,910**	(1,354)	11	(1,343)
Total fixed maturity securities	**5,780**	**143**	**5,923**	1,045	68	1,113
Equity securities:						
Dividends earned	**47**	**-**	**47**	66	-	66
Realized gain (loss)	**2,213**	**-**	**2,213**	861	-	861
Unrealized gain (loss)	**508**	**-**	**508**	(2,158)	-	(2,158)
Total equity securities	**2,768**	**-**	**2,768**	(1,231)	-	(1,231)
Private equity:						
Distributions earned	**6**	**-**	**6**	9	-	9
Realized gain (loss)	**255**	**-**	**255**	265	-	265
Unrealized gain (loss)	**(180)**	**-**	**(180)**	(149)	-	(149)
Total private equity	**81**	**-**	**81**	125	-	125
Real estate:						
Distributions earned	**-**	**-**	**-**	-	-	-
Realized gain (loss)	**67**	**-**	**67**	161	-	161
Unrealized gain (loss)	**(60)**	**-**	**(60)**	218	-	218
Total real estate	**7**	**-**	**7**	379	-	379
Other income:						
Distributions earned	**12**	**-**	**12**	6	-	6
Realized gain (loss)	**-**	**-**	**-**	(3)	-	(3)
Unrealized gain (loss)	**-**	**-**	**-**	3	-	3
Total other income	**12**	**-**	**12**	6	-	6
Total investment income	**$8,648**	**$143**	**$8,791**	$324	$68	$392

NOTE 14: EMPLOYEE BENEFIT PLANS

All of PBGC's permanent full-time and part-time employees are covered by the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Full-time and part-time employees with less than five years of service under CSRS and hired after December 31, 1983, are automatically covered by both Social Security and FERS. Employees hired before January 1, 1984, participate in CSRS unless they elected and qualified to transfer to FERS. Employees hired during the 2013 calendar year or rehired with less than five years of civilian service that is potentially creditable under FERS participate in FERS-Revised Annuity Employees (FERS-RAE). These employees are still generally considered part of the same pension system but are uniquely identified in human resources and payroll systems to annotate their higher contribution rate. Additionally, under the Bipartisan Budget Act of 2013, a new category of FERS employees was created: FERS-Further Revised Annuity Employees or FERS-FRAE. This pension system is again generally the same, only the contribution rate is changed. As with FERS-RAE employees, human resources and payroll systems use unique identifiers to annotate this higher contribution rate.

PBGC's contribution to the CSRS plan for both FY 2016 and FY 2015 was 7.0 percent of base pay for those employees covered by that system. For those employees covered by FERS, the Corporation's contribution was 13.7 percent of base pay for FY 2016. For employees covered by FERS-RAE, the Corporation's contribution was 11.9 percent of base pay for FY 2016. For employees covered by FERS-FRAE, the Corporation's contribution was 11.9 percent of base pay for FY 2016. In addition, for FERS-covered employees, FERS-RAE covered employees, and FERS-FRAE covered employees, PBGC automatically contributes 1 percent of base pay to the employee's Thrift Savings account, matches the first 3 percent contributed by the employee and matches one-half of the next 2 percent contributed by the employee. Total retirement plan expenses amounted to $24 million in FY 2016, an increase of $1million from FY 2015. These financial statements do not reflect CSRS or FERS assets or accumulated plan benefits applicable to PBGC's employees. These amounts are reported by the U.S. Office of Personnel Management (OPM) and are not allocated to the individual employers. OPM accounts for federal health and life insurance programs for those eligible retired PBGC employees who had selected federal government-sponsored plans. PBGC does not offer other supplemental health and life insurance benefits to its employees.

NOTE 15: CASH FLOWS

The following table consists of detailed cash flows from the sales and purchases of investment activity. Sales and purchases of investments are driven by the level of newly trusteed plans, the unique investment strategies implemented by PBGC's investment managers, and the varying capital market conditions in which they invest during the year. These cash flow numbers can vary significantly from year to year based on the fluctuation in these three variables.

INVESTING ACTIVITIES (SINGLE-EMPLOYER AND MULTIEMPLOYER PROGRAMS COMBINED)

(Dollars in millions)	September 30, 2016	2015
Proceeds from sales of investments:		
Fixed maturity securities	**$69,594**	$66,330
Equity securities	**10,908**	4,281
Other/uncategorized	**3,288**	2,867
Memorandum total	**$83,790**	$73,478
Payments for purchases of investments:		
Fixed maturity securities	**$(74,671)**	$(67,477)
Equity securities	**(7,719)**	(4,281)
Other/uncategorized	**(1,890)**	(2,432)
Memorandum total	**$(84,280)**	$(74,190)

The following is a reconciliation between the net income as reported in the Statements of Operations and Changes in Net Position and net cash provided by operating activities as reported in the Statements of Cash Flows.

RECONCILIATION OF NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	September 30,		September 30,		September 30,	
(Dollars in millions)	2016	2015	2016	2015	2016	2015
Net income (loss)	**3,485**	(4,727)	**(6,549)**	(9,850)	**(3,064)**	(14,577)
Adjustments to reconcile net income to net cash provided by operating activities:						
Net (appreciation) decline in fair value of investments	**(6,758)**	1,550	**(91)**	(39)	**(6,849)**	1,511
Net gain (loss) of plans pending termination and trusteeship	**(21)**	2	**-**	-	**(21)**	2
Losses (credits) on completed and probable terminations	**(417)**	(780)	**-**	-	**(417)**	(780)
Actuarial charges (credits)	**11,515**	9,504	**-**	-	**11,515**	9,504
Benefit payments - trusteed plans	**(5,592)**	(5,525)	**-**	-	**(5,592)**	(5,525)
Settlements and judgments	**(11)**	(6)	**-**	-	**(11)**	(6)
Cash received from plans upon trusteeship	**25**	22	**-**	-	**25**	22
Receipts from sponsors/non-sponsors	**88**	123	**-**	-	**88**	123
EL/DUEC Trusteeship interest (non-cash)	**62**	111	**-**	-	**62**	111
Cash receipts timing from Trust to Revolving	**6**	-	**-**	-	**6**	-
Amortization of discounts/premiums	**(76)**	108	**(7)**	11	**(83)**	119
Amortization and Depreciation expense	**13**	13	**-**	-	**13**	13
Bad debt expense/Write-offs (net)	**4**	30	**-**	-	**4**	30
Changes in assets and liabilities, net of effects of trusteed and pending plans:						
(Increase) decrease in receivables	**(1,209)**	(583)	**(13)**	(90)	**(1,222)**	(673)
Increase in present value of nonrecoverable future financial assistance	**-**	-	**6,823**	9,996	**6,823**	9,996
Increase in unearned premiums	**29**	44	**(1)**	1	**28**	45
Increase (decrease) in accounts payable	**(2)**	(22)	**7**	8	**5**	(14)
Net cash provided (used) by operating activities	**1,141**	(136)	**169**	37	**1,310**	(99)

NOTE 16: LITIGATION

Legal challenges to PBGC's policies and positions continued in FY 2016. At the end of the fiscal year, PBGC had 25 active cases in state and federal courts and 207 bankruptcy and state receivership cases.

PBGC records as a liability on its financial statements an estimated cost for unresolved litigation to the extent that losses in such cases are probable and estimable in amount. PBGC cannot estimate with any degree of certainty the possible losses it could incur in the event it does not prevail in these matters.

NOTE 17: SUBSEQUENT EVENTS

Management evaluated subsequent events through publication on November 15, 2016, the date the financial statements were available to be issued. Events or transactions for either the single-employer or multiemployer program, occurring after September 30, 2016, and before the financial statements were available to be issued, that provided additional evidence about conditions that existed at September 30, 2016, have been recognized in the financial statements.

For the fiscal year ended September 30, 2016, there were no nonrecognized subsequent events or transactions to report for both the single-employer and multiemployer programs that provided evidence about conditions that did not exist on September 30, 2016, and which arose before the financial statements were available to be issued.

IMPROPER PAYMENT REPORTING

INTRODUCTION

OMB Circular A-123, Appendix C, *Requirements for Effective Measurement and Remediation of Improper Payments* and related improper payment statutes[1] require federal agencies to conduct improper payment risk assessments. In compliance with Executive Order 13520, the PBGC Director serves as the agency official accountable for improper payment reporting purposes.

OMB's Memorandum No. M-15-02, dated October 24, 2014, specifies that in performing a Step 1 risk assessment of improper payments, agencies must institute a systematic method of reviewing all programs or payment streams and identifying those that may be susceptible to significant risk of improper payments.

PBGC performs risk assessments of its payment streams using a rotational strategy based on a three-year cycle. PBGC's payment streams include the following: 1) benefit payments to participants in "final pay" status for plans trusteed by PBGC under Title IV of ERISA (Benefit Payments); 2) payments to contractors for goods and services, including government credit card transactions (Payments to Contractors); 3) payments made to federal employees, including payroll and travel reimbursements (Payments to Federal Employees); 4) financial assistance payments to insolvent multiemployer plans that are unable to pay benefits when due under the requirements of Title IV of ERISA (Financial Assistance Payments); and 5) refunds of previously-paid premiums (Premium Refunds).

None of PBGC's payment streams have been previously determined to be susceptible to significant risk of improper payments as defined by OMB.

RESULTS OF THE FY 2016 IMPROPER PAYMENT RISK ASSESSMENT

With the support of a public accounting and consulting firm, PBGC performed Step 1 risk assessments of the following two payment streams: Payments to Contractors and Financial Assistance Payments. In performing the risk assessments, PBGC considered factors specified in OMB guidance, including the complexity of the payment stream; the volume of payments; recent major changes in program funding, authorities, practices, or procedures; the level, experience, and quality of training for personnel responsible for making program eligibility determinations or certifying that payments are accurate; inherent risks of improper payments due to the nature of agency programs or operations; and any significant deficiencies in the audit reports issued by the PBGC Office of Inspector General (OIG) and the Government Accountability Office (GAO), and the results from prior risk assessments.

To be considered susceptible to significant risk of improper payments, OMB guidance specifies that gross annual improper payments (i.e., the total amount of overpayments plus underpayments) within a payment stream would have to exceed (1) both 1.5 percent of program outlays and $10,000,000 of payments made

[1] This references the Improper Payments Information Act of 2002 (IPIA), the Improper Payments Elimination and Recovery Act of 2010 (IPERA), and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA).

during the reporting period or (2) $100,000,000 (regardless of the improper payment percentage of total program outlays). Based on the results of the Step 1 risk assessments, PBGC determined that the Payments to Contractors and Financial Assistance Payments streams were not susceptible to significant risk of improper payments as defined by OMB.

Statistical Sampling and Testing Methodology

To supplement its risk assessment of Payments to Contractors and Financial Assistance Payments, PBGC performed optional statistical sampling of payments issued to contractors and eligible multiemployer plans. Payments selected as part of a statistical sample were drawn from the period October 1, 2014, through September 30, 2015. During this period, nearly 4,000 payments were made totaling nearly $329 million as part of Payments to Contractors, and 184 payments were made totaling nearly $103 million as part of Financial Assistance Payments.

In designing the sampling plan, PBGC followed OMB statistical sampling guidance regarding minimum sample sizes and took steps to ensure that the resulting sample would be representative of the payment population being tested, including the use of random selection and sample stratification techniques.

For Payments to Contractors, testing of a sample of 63 payments, totaling $32,201,631, was performed. The purpose of this testing was to assess whether payments complied with the improper payment definitions applicable to this payment stream. For example, we tested whether PBGC officials approved the payment, whether there was documentation supporting that goods or services were received or performed, and whether billed amounts were consistent with contractual terms, including whether unallowable costs, as defined in the Federal Acquisition Regulation (FAR), were excluded.

For Financial Assistance Payments, testing of a sample of 30 payments, totaling $35,211,862, was performed. The purpose of this testing was to assess whether the payments complied with the improper payment definition applicable to this payment stream. For example, we tested whether PBGC officials approved the payment, whether there was documentation supporting the insolvency of the multiemployer plan, whether administrative expenses of the plan were valid, whether active participants were receiving monthly benefits, whether active participants were eligible to receive monthly benefits, and whether deceased participants were removed from pay status and appropriately reflected in payment reconciliations.

Results of Testing of Payments to Contractors

Of the $32,201,631 tested for Contractor Payments, a total of $21,940 of actual improper payments were identified. The issues noted primarily related to minor unapplied withholding and ineligible goods and services issues. Based on statistical projections, the estimated gross improper payment (IP) rate is 0.21 percent with the projected value of estimated improper payments totaling $675,709. These amounts are below OMB thresholds for improper payment reporting. In addition, the achieved precision or accuracy levels were within the levels specified by OMB in its statistical sampling guidance.

Additional details relating to the testing of Payment to Contractors are presented in the following four tables: a) projection of gross improper payments (over-payments and under-payments added together), b) projection of net improper payments (under-payments subtracted from over-payments), c) improper payments by OMB error type, and d) matrix of improper payment categories.

Projection of Gross Improper Payments						
Sample Universe	IP %	IP $	Over-payments %	Over-payments IP $	Under-payments %	Under-payments IP $
$ 328,866,887	0.21	$ 675,709	0.21	$ 675,709	0.00	$ 0

Projection of Net Improper Payments		
Sample Universe	IP %	IP $
$ 328,866,887	0.21	$ 675,709

Improper Payments by OMB Error Type				
Type of Error	Sample Universe	Actual Gross Improper Payments $	Projected Gross Improper Payment %	Projected Improper Payment $
Unapplied Credit or Discounts	$ 328,866,887	$ 21,940	0.21	$ 675,709
All Issues Noted		$ 21,940	0.21	$ 675,709

Matrix of OMB Improper Payment Categories				
Reason for Improper Payment		Type of Improper Payment		
		Overpayments	Underpayments	
Program Design or Structural Issue		-	-	1
Inability to Authenticate Eligibility		-	-	2
Failure to Verify:	Death Data	-	-	3
	Financial Data	-	-	4
	Excluded Party Data	-	-	5
	Prisoner Data	-	-	6
	Other Eligibility Data	-	-	7
Administrative or Process Error Made by:	Federal Agency	$ 21,940	-	8
	State or Local Agency	-	-	9
	Other Party	-	-	10
Medical Necessity		-	-	11
Insufficient Documentation to Determine		-	-	12
Other Reason		-	-	13
		A	B	

Results of Testing Financial Assistance Payments

Of the $35,211,862 tested for Financial Assistance Payments, a total of $50,688 of gross improper payments were identified. The issues noted primarily related to minor payment errors, documentation, and participant eligibility issues. Based on statistical projections, the estimated gross improper payment (IP) rate for this payment stream is 0.44 percent with the projected value of estimated improper payments totaling $450,812. These amounts are below OMB thresholds for improper payment reporting. In addition, the achieved precision or accuracy levels were within the levels specified by OMB in its statistical sampling guidance.

Additional details relating to the testing of Financial Assistance Payments are presented in the following four tables: a) projection of gross improper payments (over-payments and under-payments added together), b) projection of net improper payments (under-payments subtracted from over-payments), c) improper payments by OMB error type, and d) matrix of improper payment categories.

Projection of Net Improper Payments						
Sample Universe	IP %	IP $	Over-payments %	Over-payments IP $	Under-payments %	Under-payments IP $
$ 102,640,002	0.44	$ 450,812	0.42	$ 428,245	0.02	$ 22,567

Projection of Net Improper Payments		
Sample Universe	IP %	IP $
$ 102,640,002	0.40	$ 405,678

Improper Payments by OMB Error Type				
Type of Error	Sample Universe	Actual Gross Improper Payments $	Projected Gross Improper Payment %	Projected Improper Payment $
Incorrect Amount	$ 102,640,002	$ 41,983	0.40	$ 407,087
Ineligible Recipient		$ 5,195	0.02	$ 21,158
Lack of Documentation		$ 3,510	0.02	$ 22,567
All Issues Noted		$ 50,688	0.44	$ 450,812

Matrix of OMB Improper Payment Categories				
Reason for Improper Payment		Type of Improper Payment		
		Overpayments	Underpayments	
Program Design or Structural Issue		-	-	1
Inability to Authenticate Eligibility		-	-	2
Failure to Verify:	Death Data	-	-	3
	Financial Data	-	-	4
	Excluded Party Data	-	-	5
	Prisoner Data	-	-	6
	Other Eligibility Data	$ 5,195	-	7
Administrative or Process Error Made by:	Federal Agency	$ 41,983	-	8
	State or Local Agency	-	-	9
	Other Party	-	-	10
Medical Necessity		-	-	11
Insufficient Documentation to Determine		-	$ 3,510	12
Other Reason		-	-	13
		A	B	

FOLLOW-UP ON CORRECTIVE ACTIONS RELATING TO PRIOR RISK ASSESSMENTS

PBGC continues to follow-up on issues identified in connection with prior year risk assessments. The following two payment streams have corrective action plans that remain in progress. Progress updates are shown below:

- Benefit Payments: The Office of Benefit Administration (OBA) has worked to implement corrective actions and take other steps to address legacy documentation issues associated with trusteed pension plans that were identified when PBGC conducted a pilot improper payment assessment in FY 2011. At that time, OMB advised that PBGC should focus its improper payment testing on payment accuracy and to implement strategies to improve pension-related documentation over time. OBA was formed as a result of a reorganization that was completed in FY 2016, and its new structure supports centralized documentation maintenance responsibilities and practices. Data collection and analysis is now centralized within its Data Management Division. To gain a fuller understanding of improper payment risks, OBA also completed an improper payment risk assessment and documented its risk responses. OBA has established monitoring and enforcement procedures to ensure documentation is imaged, archived and stored appropriately and compliance reviews are performed on a regular basis. In addition, OBA has taken steps to ensure that the source data used to support benefit calculations is clearly identified and maintained, has updated its policies to require explanations where data is found to be missing or unavailable, and has expanded its efforts to securely archive electronic data. OBA also provides training on the importance of document retention, archiving and imaging. Prior year improper payment assessments have found the Benefit Payment to be not susceptible to significant risk of improper payments and did not identify significant benefit calculation errors, and during FY 2016, OBA formally documented a risk acceptance policy associated with legacy documentation issues.

- Financial Assistance Payments: During FY 2016, the Multiemployer Program Division (MEPD) within PBGC implemented an automated system by which applicable multiemployer plans submit requests for financial assistance payments and related supporting documentation to MEPD for

review. This new process increases efficiency and reduces the potential for errors. As part of its oversight efforts, MEPD continues to work with applicable multiemployer plans to ensure that participant listings are consistently provided and maintained.

PREVENTING AND DETECTING IMPROPER PAYMENTS

In addition to its periodic improper payment testing and in support of the administration's Do Not Pay Initiative, PBGC employs a variety of means to prevent and detect improper payments on an ongoing basis:

- For all of its payment streams, PBGC has established controls to help ensure that payments are accurate and approved. For instance, pre-payment checks include ensuring that documentation for the payment is available for review by the approving official. On a post-payment basis, payment reconciliations are performed to help ensure completeness of payment processing and to identify errors. In addition, payments are subject to periodic compliance reviews.

- PBGC regularly performs electronic data analysis of payment transactions associated with Benefit Payments and Payments to Contractors – the two largest payment streams. This process helps to identify potential duplicate payments, other overpayments, and payment anomalies. When warranted, selected payments are subjected to additional research and analysis.

- For Benefit Payments, the largest payment stream, PBGC checks its participant database against the Social Security Administration's Death Master File (DMF) to help prevent sending out checks or automated deposits to payees who are deceased and should no longer be receiving benefits. Performing this check on a regular basis avoids costs associated with PBGC seeking payments from the estates of deceased participants. This helps avoid the potential for checks to be stolen or for automated deposits to be fraudulently withdrawn from the accounts of deceased participants. The following table presents the results of DMF matching for FY 2016:

Use of the Death Match File To Prevent Improper Payments			
Number of Payments Reviewed	Dollar Value of Payments Reviewed	Number of Payments Stopped	Dollar Value of Payments Stopped
9.8 million	$5.6 billion	16,213	$6,093,215

- PBGC participates in the Department of Treasury's Do Not Pay (DNP) program. For example, under the Payments to Contractors stream, payments are screened on a post-payment basis to assess whether companies receiving payments for work performed under PBGC contracts were properly registered in the General Service Administration's System for Award Management (SAM), have not been debarred or suspended from contracting in the federal sector, and do not have federal debts that have been referred to the Department of Treasury for collection. For FY 2016, PBGC did not identify any improper payments using the DNP process for the Payment to Contractors payment stream.

RECAPTURING IMPROPER PAYMENTS

Potential improper payments are subjected to further analysis based on the amount of the payment, the nature of the potential error, and other risk factors to determine whether amounts are due to PBGC. For Benefit Payments, PBGC has established procedures to recapture overpayments through recovery payments, installment repayment agreements, offsets against other continuing benefits to recoup amounts owed by the participant, or referrals to the Department of Treasury's Centralized Receivables Service. In some cases, recapture of payments may not be sought based on demonstration that a participant is experiencing financial hardship or other reasons. Other PBGC payment streams also have procedures in place to collect overpayments.

During FY 2016, some improper payments associated with the Benefit Payments stream were identified using electronic data analysis. For example, annuity payments that were being made to a beneficiary were terminated, after it was determined that the PBGC inadvertently continued to process payments associated with a certain and continuous benefit for a longer period than allowed. This instance was classified as a high dollar improper payment. PBGC is taking steps to help prevent the reoccurrence of such payments and will continue to proactively seek to identify overpayments.

Additionally during FY 2016, on two separate occasions, participant address and payment locations were not captured, updated, and transmitted to PBGC's paying agent in a timely way, resulting in payments going to a prior location. We classified the related payments as improper payments. PBGC has resolved the open issues resulting from these events and is working to prevent and minimize any impact in the future.

When it is suspected that PBGC payments were issued, misdirected, or obtained in a fraudulent manner, PBGC works closely with PBGC's Office of Inspector General (OIG). The OIG performs investigations of suspect transactions and, when appropriate, refers matters to the Department of Justice to determine whether there is a sufficient basis to initiate a civil or criminal prosecution.

2016 ACTUARIAL VALUATION

PBGC calculated and validated the present value of future PBGC-payable benefits (PVFB) for both the single-employer and multiemployer programs and of nonrecoverable future financial assistance (NRFFA) under the multiemployer program. Generally, we used the same methods and procedures as in 2015 for the Single-Employer and Multiemployer Programs.

PRESENT VALUE OF FUTURE BENEFITS AND NONRECOVERABLE FINANCIAL ASSISTANCE – 2016

	Number of Plans	Number of Participants (in thousands)	Liability (in millions)
I. SINGLE-EMPLOYER PROGRAM			
A. Terminated Plans			
1. Seriatim at fiscal year-end (FYE)	4,259	1,022	$ 78,966
2. Seriatim at DOPT, adjusted to FYE	81	161	22,601
3. Nonserieatim[1]	429	192	12,542
4. Missing Participants Program (seriatim)[2]	-	24	67
Subtotal	4,769	1,399	$ 114,176
B. Probable terminations (nonseriatim)[3]	3	4	653
	4,772	1,403	$ 114,829
II. MULTIEMPLOYER PROGRAM			
A. Pre-MPPAA terminations (seriatim)	10	0*	$ 0**
B. Pre-MPPAA liability (net of plan assets)			
1. Currently Receiving Assistance	65	86	2,139
2. Probable for Assistance	103	1,078	58,870
Total	178	1,164	$ 61,009

* Fewer than 500 participants

**Less than $500,000

Notes:

1) The liability for terminated plans has been increased by $21 million for settlements.
2) The Missing Participants Program refers to a liability that PBGC assumed for unlocated participants in standard plan terminations.
3) The net claims for probable plans reported in the financial statements include $127 million for not-yet-identified probable terminations. The assets for the probable plans, including the expected value of recoveries on employer liability and due-and-unpaid employer contributions claims, are $277 million. Thus, the net claims for probable terminations as reported in the financial statements are $653 million less $277 million, or $376 million.
4) The PVFB in the financial statements ($113,704 million) is net of estimated plan assets and recoveries on probable terminations ($277 million), estimated recoveries on terminated plans ($569 million), and estimated assets for plans pending trusteeship ($279 million), or, $114,829 million less $277 million less $569 million less $279 million = $113,704 million.

Single-Employer Program

PBGC calculated the single-employer program's liability for benefits in the terminated plans and probable terminations, as defined in Note 2 to the financial statements, using a combination of two methods: seriatim and nonseriatim. For 4,259 plans, representing about 89 percent of the total number of single-employer terminated plans (73 percent of the total participants in single-employer terminated plans), PBGC had sufficiently accurate data to calculate the liability separately for each participant's benefit (seriatim method). This was an increase of 37 plans over the 4,222 plans valued seriatim last year. For 81 plans whose data were

not yet fully automated, PBGC calculated the benefits and liability seriatim as of the date of plan termination (DOPT) and brought the total amounts forward to the end of fiscal year 2016 on a nonseriatim basis.

For 429 other terminated plans, PBGC did not have sufficiently accurate or complete data to value individual benefits. Instead, the Corporation used a "nonseriatim" method that brought the plan liabilities from the plan's most recent actuarial valuation forward to the end of fiscal year 2016 using certain assumptions and adjustment factors.

For the actuarial valuation, PBGC used a select and ultimate interest rate assumption of 2.27% for the first 20 years after the valuation date and 2.14% thereafter. The mortality tables used for valuing healthy lives were the adjusted RP-2014 Healthy Male and Female Tables, each projected to 2029 using Scale MP-2015. The projection period is determined as the sum of the elapsed time from the date of the table (2014) to the valuation date plus the period of time from the valuation date to the average date of payment of future benefits. In fiscal year 2015, the mortality table used for valuing healthy lives were the RP-2000 Combined Healthy Male and Female Tables, each projected 28 years to 2028 using Scale AA and set back one year.

For non-pay-status participants, PBGC used expected retirement ages, as explained in subpart B of the Allocation of Assets in Single-Employer Plans regulation. PBGC assumed that participants who had attained their expected retirement age were in pay status. In seriatim plans, for participants who were older than age 65, were not in pay status, and were unlocated at the valuation date, PBGC reduced the value of their future benefits to zero over the three years succeeding age 65 to reflect the lower likelihood of payment. Similarly, for located participants over age 70 and not in pay status, PBGC reduced the value of their future benefits to zero. For deferred participants who were older than age 70 in the Missing Participant Program, PBGC reduced the value of their future benefits to zero over the ten years succeeding age 70 to reflect the lower likelihood of payment.

Multiemployer Program

PBGC calculated the liability for the 10 pre-MPPAA terminations using the same assumptions and methods applied to the single-employer program.

PBGC based its valuation of the post-MPPAA liability for nonrecoverable future financial assistance on the most recent available actuarial reports, Form 5500 Schedule B or Schedule MB, as applicable, and information provided by representatives of the affected plans. The Corporation expected 168 plans to need financial assistance because severe industrial declines have left them with inadequate contribution bases and they had insufficient assets for current payments or were expected to run out of assets in the foreseeable future.

Statement of Actuarial Opinion

This valuation has been prepared in accordance with generally accepted actuarial principles and practices and, to the best of my knowledge, fairly reflects the actuarial present value of the Corporation's liabilities for the single-employer and multiemployer plan insurance programs as of September 30, 2016.

In preparing this valuation, I have relied upon information provided to me regarding plan provisions, plan participants, plan assets, and other matters, some of which are detailed in a complete Actuarial Report available from PBGC.

In my opinion, (1) the techniques and methodology used for valuing these liabilities are generally acceptable within the actuarial profession; (2) the assumptions used are appropriate for the purposes of this statement and are individually my best estimate of expected future experience, discounted using current settlement rates from insurance companies as determined by PBGC's Policy Research and Analysis Department; and (3) the resulting total liability represents my best estimate of anticipated experience under these programs.

I, Scott Young, am the Chief Valuation Actuary of the PBGC. I am a Member of the American Academy of Actuaries, a Fellow of the Society of Actuaries and an Enrolled Actuary. I meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained in this report.

Scott G. Young

Scott G. Young, FSA, EA, MAAA
Fellow of the Society of Actuaries
Enrolled Actuary
Member of the American Academy of Actuaries
Chief Valuation Actuary
Director, Actuarial Services and Technology Department
Office of Benefits Administration
Pension Benefit Guaranty Corporation

INDEPENDENT AUDIT AND MANAGEMENT'S RESPONSE

Office of Inspector General
Pension Benefit Guaranty Corporation

November 15, 2016

To the Board of Directors
Pension Benefit Guaranty Corporation

The Office of Inspector General contracted with CliftonLarsonAllen LLP, an independent certified public accounting firm, to audit the financial statements of the Single-Employer and Multiemployer Program Funds administered by the Pension Benefit Guaranty Corporation as of and for the years ended September 30, 2016 and 2015. CLA conducted the audit in accordance with the following auditing standards: *Government Auditing Standards* issued by the Comptroller General of the United States, attestation standards established by the American Institute of Certified Public Accountants, and the Office of Management and Budget's *Audit Requirements for Federal Financial Statements.*

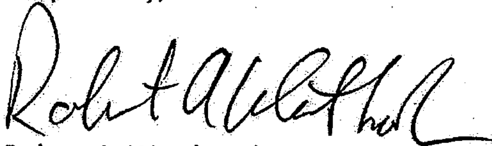
In their audit, CliftonLarsonAllen found:

- The financial statements present fairly, in all material respects, the financial position of the Single-Employer and Multiemployer Program Funds administered by the PBGC as of September 30, 2016 and 2015, and the results of their operations and cash flows for the years then ended, in accordance with accounting principles generally accepted in the U.S. This is the 24th consecutive unmodified financial statement audit opinion.
- PBGC maintained, in all material respects, effective internal control over financial reporting as of September 30, 2016, based on criteria established under 31 U.S.C. 3512 (c), (d), commonly known as the Federal Managers' Financial Integrity Act of 1982 (FMFIA) and OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control* (OMB Circular A-123). Serious internal control weaknesses in PBGC's programs and operations include four significant deficiencies (Controls over the Present Value of Future Benefit Liability, Present Value of Nonrecoverable Future Financial Assistance, Entity-Wide Security Program Planning and Management, and Access Controls and Configuration Management).
- Instances of noncompliance or other matters that are required to be reported in accordance with *Government Auditing Standards.*

- o Antideficiency Violation: On August 23, 2016, PBGC reported a violation of 31 U.S.C, 1342 in connection with voluntary services of an independent subcontractor.
- o Potential Antideficiency Violation: PBGC maintains operating leases for all office locations and its Continuity of Operations Plan (COOP) site. However, PBGC did not record its full contractual obligation under its current multiyear lease arrangements.

CliftonLarsonAllen is responsible for the accompanying auditor's report dated November 15, 2016 and the conclusions expressed in the report. We do not express opinions on PBGC's financial statements or internal control, nor do we draw conclusions on compliance with laws and regulations. The financial statement audit report (AUD-2017-2 / FA-16-110-1) is also available on our website at oig.pbgc.gov.

Respectfully,



Robert A. Westbrooks
Inspector General

cc: Thomas Reeder
Patricia Kelly
Alice Maroni
Cathleen Kronopolus
Ann Orr
Karen Morris
Michael Rae
Robert Scherer
Judith Starr
Theodore Winter
Marty Boehm

CliftonLarsonAllen

CliftonLarsonAllen LLP
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INDEPENDENT AUDITORS' REPORT

To the Board of Directors, Management
and the Inspector General of the
Pension Benefit Guaranty Corporation

Report on the Financial Statements

We have audited the accompanying financial statements of the Pension Benefit Guaranty Corporation (PBGC), which comprise the statements of financial position as of September 30, 2016 and 2015, and the related statements of operations, net position and cash flows of the Single-Employer and Multiemployer Program Funds administered by the PBGC for the years then ended, and the related notes to the financial statements (financial statements).

Management's Responsibility for the Financial Statements

PBGC management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America (U.S.); this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibilities

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of the financial statements in accordance with auditing standards generally accepted in the U.S.; the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, *Audit Requirements for Federal Financial Statements* (OMB Bulletin 15-02). Those standards and OMB Bulletin 15-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Single-Employer and Multiemployer Program Funds administered by the PBGC as of September 30, 2016 and 2015, and the results of their operations and cash flows for the years then ended, in accordance with accounting principles generally accepted in the U.S.

Emphasis of Matter

By law, PBGC's Single-Employer and Multiemployer Program Funds must be self-sustaining. As of September 30, 2016, PBGC reported in its financial statements net deficit positions (liabilities in excess of assets) in the Single-Employer and Multiemployer Program Funds of approximately $21 billion and $59 billion, respectively. As discussed in Note 9 to the financial statements, the potential losses from Single-Employer and Multiemployer plans whose termination is reasonably possible as a result of unfunded vested benefits are estimated to be approximately $223 billion and $19 billion, respectively. Management calculated the potential losses from single employer plans whose termination is reasonably possible based on the most recent data available from filings and submissions for plan years ended on or after December 31, 2014, and adjusted the value reported for liabilities to the estimated balance as of December 31, 2015, using actuarial assumptions. PBGC did not adjust the estimate for economic conditions that occurred between December 31, 2015 and September 30, 2016, and as a result, the actual loss for the Single-Employer Program as of September 30, 2016, could be substantially different. In addition, PBGC's net deficit and long-term viability could be further impacted by losses from plans classified as reasonably possible (or from other plans not yet identified as potential losses) as a result of deteriorating economic conditions, the insolvency of a large plan sponsor, or other factors. PBGC has been able to meet its short-term benefit obligations; however, as discussed in Note 1 to the financial statements, management believes that neither program at present has the resources to fully satisfy PBGC's long-term obligations to plan participants. Our opinion is not modified with respect to this matter.

Other Information

The Message from Our Chair, Message from the Director, Annual Performance Report, Operations in Brief, Strategic Goals and Results, Independent Evaluation of PBGC Programs, Fiscal Year (FY) 2016 Financial Statement Highlights, Management's Discussion and Analysis, Analysis of Entity's Systems, Control and Legal Compliance, Management Representation, Improper Payment Reporting, FY 2016 Actuarial Valuation, Letter of the Inspector General, and Management's Response to the Report of Independent Auditor and Organization contains a wide range of information, some of which is not directly related to the financial statements. This information is presented for purposes of additional analysis and is not a required part of the financial statements. This information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Report on Internal Control over Financial Reporting

We have audited PBGC's internal control over financial reporting as of September 30, 2016, based on criteria established under 31 U.S.C. 3512 (c), (d), commonly known as the Federal Managers' Financial Integrity Act of 1982 (FMFIA) and OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control* (OMB Circular A-123).

Management's Responsibility for Internal Control

PBGC management is responsible for maintaining effective internal control over financial reporting, evaluating the effectiveness of internal control over financial reporting based on the criteria described above, and for its statement of assurance of the effectiveness of internal control over financial reporting, included in the Annual Report.

Auditors' Responsibilities

Our responsibility is to express an opinion on PBGC's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with attestation standards established by the American Institute of Certified Public Accountants and the attestation standards contained in *Government Auditing Standards*.

An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and evaluating the design, and testing the operating effectiveness of internal control over financial reporting based on the assessed risk. Our audit of internal control also considered the entity's process for evaluating and reporting on internal control over financial reporting based on the criteria described above. Our audit also included performing such other procedures as we considered necessary in the circumstances.

We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing performance information and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Our internal control testing was for the purpose of expressing an opinion on whether effective internal control over financial reporting was maintained, in all material respects. Consequently, our audit may not identify all deficiencies in internal control over financial reporting that are less severe than a material weakness.

Definitions and Inherent Limitations of Internal Control over Financial Reporting

An entity's internal control over financial reporting is a process effected by those charged with governance, management and other personnel, designed to provide reasonable assurance that (1) transactions are properly recorded, processed and summarized to permit the preparation of financial statements in accordance with accounting principles generally accepted in the U.S.; (2) assets are safeguarded against loss from unauthorized acquisition, use or disposition; and (3) transactions are executed in accordance with laws governing the use of budget authority and other applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error. We also caution that projecting our audit results to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate.

Opinion on Internal Control over Financial Reporting

In our opinion, PBGC maintained, in all material respects, effective internal control over financial reporting as of September 30, 2016, based on criteria established under FMFIA and OMB Circular A-123.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the PBGC's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiencies, which are described in Exhibit I, to be significant deficiencies:

1. Controls over the Present Value of Future Benefit Liability
2. Present Value of Nonrecoverable Future Financial Assistance
3. Entity-wide Security Program Planning and Management
4. Access Controls and Configuration Management

Report on Compliance Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

As part of obtaining reasonable assurance about whether PBGC's financial statements are free from material misstatement, we performed tests of the PBGC's compliance with certain provisions of laws, regulations, contracts, and grant agreements noncompliance with which could have a direct effect on the determination of material financial statement amounts and disclosures.

The results of our tests disclosed instances of noncompliance or other matters, described below and in Exhibit II, that are required to be reported in accordance with *Government Auditing Standards*.

- Antideficiency Violation: On August 23, 2016, PBGC reported a violation of United States Code (U.S.C.), Title 31, Section 1342, in connection with voluntary services of an independent subcontractor.

- Potential Antideficiency Violation: PBGC maintains operating leases for all office site locations and its Continuity of Operations Plan (COOP) site. However, PBGC did not record its full contractual obligation under its current multiyear lease arrangements.

Management's Responsibility for Compliance

Management is responsible for complying with applicable laws, regulations, contracts, and grant agreements.

Auditors' Responsibilities

We are responsible for testing compliance with certain provisions of laws, regulations, contracts and grant agreements.

We did not test compliance with all laws, regulations, contracts, and grant agreements applicable to PBGC. We limited our tests to certain provisions of laws, regulations, contracts, and grant agreements noncompliance with which could have a direct effect on the determination of material financial statement amounts and disclosures. However, providing an opinion on compliance with those provisions was not an objective of our audits, and accordingly, we do not express such an opinion. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

Purpose of the Report on Compliance

The purpose of the Report on Compliance is solely to describe the scope of our testing of compliance and the result of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering PBGC's compliance. Accordingly, this report is not suitable for any other purpose.

Management's Response to Findings

Management's response to the findings identified in our report is presented in Exhibit IV. We did not audit PBGC's response and, accordingly, we express no opinion on it.

Status of Prior Year's Control Deficiencies and Noncompliance Issues

We have reviewed the status of PBGC's corrective actions with respect to the findings included in the prior year's Independent Auditors' Report, dated November 13, 2015. The status of prior year findings is presented in Exhibit III.

CliftonLarsonAllen LLP

Calverton, Maryland
November 15, 2016

EXHIBIT I

PENSION BENEFIT GUARANTY CORPORATION
INTERNAL CONTROL DEFICIENCIES
September 30, 2016

BACKGROUND

PBGC protects the pensions of nearly 40 million workers and retirees in nearly 24 thousand private defined benefit pension plans. Under Title IV of the Employee Retirement Income Security Act of 1974 (ERISA), PBGC insures, subject to statutory limits, pension benefits of participants in covered private defined benefit pension plans in the U.S. The establishment of a robust internal control framework and the implementation of the appropriate internal control activities are essential to PBGC operations. OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control,* requires agencies to integrate risk management and internal control functions. The Circular also requires management perform an assessment of its internal control based on GAO's *Standards for Internal Control in the Federal Government* (known as the Green Book). The Green Book defines internal control as a process used by management to help an entity achieve its objectives.

During FY 2016, we observed improvements to the internal controls within PBGC operations that impacted long-standing control deficiencies reported in previous years. These improvements led to a change in classification of a previously reported material weakness in controls over the PVFB liability to a significant deficiency. However, management is continuing its corrective actions related to certain findings as discussed below.

The following provides an overview of the significant deficiencies identified in our audit:

1. Controls over the Present Value of Future Benefit (PVFB) Liability

The Office of Benefits Administration (OBA) continues to make progress in their remediation efforts to correct long-standing deficiencies related to controls over the PVFB liability. The PVFB liability represents the estimated liability for future benefits that PBGC is, or will be, obligated to pay participants of covered Single-Employer and certain Multiemployer pension plans. Some of these efforts included refining OBA's organizational structure and the senior leadership team, updating and implementing specific plan asset valuation policies and procedures, and enlisting subject matter experts to perform key functions. Management performed a more in-depth risk assessment analysis of OBA's operations, to determine root causes of long-standing issues and procedures to mitigate such risks. Further, management's effort has led to the closure of several recommendations, previously identified by the Office of Inspector General and CliftonLarsonAllen LLP, resulting in the resolution of a long standing deficiency regarding the Corporation's valuation of plan assets and benefits.

However, the results of our FY 2016 procedures reveal certain controls over the calculation of the PVFB liability require management's continued focus.

PENSION BENEFIT GUARANTY CORPORATION
INTERNAL CONTROL DEFICIENCIES
September 30, 2016

Calculation of the Present Value of Future Benefit Liability

We continued to identify errors in the calculation of participant benefits and the related PVFB liability similar to those identified in prior audits. During our testing of the PVFB liability reported at June 30 and September 30, we identified:

- Errors caused by system limitations or programming flaws
- Data entry errors and inaccurate use of plan data provisions

Although the Corporation continues to refine its business processes related to the calculation of Individual Participant Valuation benefit liabilities, these control deficiencies impede the Corporation's ability to accurately calculate valuations for some participant's benefits and properly estimate and report related future liabilities.

Recommendations:

We continue to recommend that PBGC management:

- Develop and/or implement improvements to OBA systems used to calculate benefits and liabilities (Spectrum and the Integrated Present Value of Futures Benefit Systems).
- Perform risk assessment to identify primary cause of data entry and inaccurate use of plan data provision errors.
- Implement corrective action to address root cause of data entry and inaccurate use of plan data provisions.

2. Present Value of Nonrecoverable Future Financial Assistance (PV NRFFA)

The PV NRFFA represents the estimated nonrecoverable payments PBGC will make to certain multiemployer plans that will not be able to meet their benefit obligations to plan participants. Further, the classification of the future multiemployer liability is determined based on the projected date of insolvency. A cash flow model is updated by actuaries using various assumptions to calculate the PV NRFFA at September 30.

The lack of a quality control review process contributed to control deficiencies we found during testing of the PV NRFFA liability at September 30. Specifically, we identified the following:

- Failure to use the most current and relevant data to update the actuarial assumptions needed to calculate the PV NRFFA
- Errors in the data inputs used to calculate PV NRFFA

The Multiemployer Working Group Procedures for 2016, Appendix D states that "PBGC will use the most recently available data." In addition, "Actuarial Services and Technology Department (ASTD) will follow its existing controls for review and sign off on data entry and computations."

PENSION BENEFIT GUARANTY CORPORATION
INTERNAL CONTROL DEFICIENCIES
September 30, 2016

***Recommendations*:**

We recommend that PBGC management:

- Prepare separate annual assumption memos for the multiemployer and single-employer programs, with each assumption memo incorporating more refined key assumptions applicable to each program.
- Consider methods of calculating, reviewing, and documenting plan level adjustments to the IPVFB inputs in order to take individual plan conditions into account.
- Refine current quality control review procedures to effectively minimize data input errors.

3. Entity-wide Security Program Planning and Management

While PBGC continued to make progress in addressing the Corporation's entity-wide security program planning and management control deficiencies, these efforts have not resulted in a fully implemented effective entity-wide information security program as required under OMB and the National Institute of Standards and Technology (NIST) guidance.

In FY 2016, PBGC developed and published the PBGC Risk Management Framework (RMF) Process to transition to, and fully implement, an entity-wide information security risk management program. In addition, PBGC has developed and is implementing a plan to be fully compliant with OMB Circular A-130, *Managing Information as a Strategic Resource*, issued on July 28, 2016. PBGC, however, has not fully implemented components of its entity-wide information security risk management program. Some components not fully implemented include the following:

- Completion of the implementation of PBGC's RMF entity-wide security program and management, which supports PBGC organizational, mission and information system objectives by addressing each of the six RMF phases: categorize, select, implement, assess, authorize, and monitor.
- Full implementation of a continuous monitoring program.
- Common controls compliance with NIST SP 800-53, Revision 4, *Security and Privacy Controls for Federal Information Systems and Organizations* requirements.
- Completion of the transition to NIST 800-53, Revision 4 security controls.
- Full implementation of common controls and remediation of common control weaknesses.
- Availability of common controls to system owners for appropriate inclusion in system security plans.

PBGC implementation of NIST's RMF will establish an integrated enterprise-wide decision structure for cybersecurity risk management that includes and integrates PBGC mission and information system objectives, which will transition PBGC's entity-wide security program to near real-time risk management. This Framework will also address common controls weaknesses and full implementation of continuous monitoring controls.

Recommendations:

We recommend that PBGC management:

- Complete the PBGC RMF transition, fully implement the entity-wide information security risk management program, and provide periodic updates to stakeholders.
- Complete the migration to NIST SP 800-53, Revision 4, *Security and Privacy Controls for Federal Information Systems and Organizations* and provide periodic updates to stakeholders.
- Complete the implementation of NIST SP 800-53, Revision 4 controls for common controls, remediation of common controls weaknesses, and make available to system owners in Cyber Security Assessment and Management for appropriate inclusion in their system security plans.

4. Access Controls and Configuration Management

While PBGC made progress in addressing access controls and configuration management deficiencies identified in previous years, this progress did not fully resolve some security weaknesses. Weaknesses in the PBGC IT environment continue to contribute to deficiencies in system configuration, segregation of duties and role-based access controls based on least privilege.

In FY 2016, PBGC continued to implement various tools and processes to establish a more coherent environment for access controls and configuration management security controls.

Access controls and configuration management controls are an integral part of an effective information security management program. Access controls limit or detect inappropriate access to systems, protecting the data from unauthorized modification, loss or disclosure. Agencies should have formal policies and procedures and related control activities should be properly implemented and monitored. Configuration management ensures changes to systems are tested and approved and systems are configured securely in accordance with policy.

An information system is comprised of many components[1] that can be interconnected in a multitude of arrangements to meet a variety of business, mission and information security needs. How these information system components are networked, configured and managed is critical in providing adequate information security and supporting an organization's risk management process.

[1] Information system components include, for example, mainframes, workstations, servers (e.g., database, electronic mail, authentication, Web, proxy, file, domain name), network components (e.g., firewalls, routers, gateways, voice and data switches, wireless access points, network appliances, sensors), operating systems, middleware, and applications.

EXHIBIT I

PENSION BENEFIT GUARANTY CORPORATION
INTERNAL CONTROL DEFICIENCIES
September 30, 2016

PBGC has not fully addressed access controls and configuration management weaknesses, including:

- Implementation of controls to remedy vulnerabilities identified in key databases and applications, such as weaknesses in configuration, roles, privileges, auditing, file permission, and operating system access
- Development and implementation of an account management monitoring program that ensures that accounts are constantly maintained in accordance with PBGC account management standards and that reduces the dependency on recertification
- Development and implementation of processes and procedures for determining and documenting defined security configuration checklists for database applications
- Implementation of requirements for the disposition of dormant accounts for all PBGC systems
- Full implementation of controls to remove separated users from systems and applications
- Removal and decommission of systems and databases that have reached their end of service life
- Development and implementation of a plan of action to address known security weaknesses in accordance with PBGC's timeline for corrective action

Recommendations:

We continue to recommend that PBGC management:

- Develop and implement the following:
  - Controls to remedy vulnerabilities identified noted in key databases and applications such as weaknesses in configuration, roles, privileges, auditing, file permissions and operating system access.
  - An account management monitoring program that ensures that accounts are constantly maintained in accordance with PBGC account management standards and that reduces the dependency on recertification.
  - Development and implementation of processes and procedures for determining and documenting defined security configuration checklists for database applications.
  - Requirements for the disposition of dormant accounts for all PBGC systems.
  - Effective controls to remove separated users from systems and applications.
  - Removal and decommission of systems and databases that have reached their end of service life.
  - A plan of action to address known security weaknesses in accordance with PBGC's timeline for corrective actions.

EXHIBIT II

PENSION BENEFIT GUARANTY CORPORATION
NONCOMPLIANCE WITH LAWS AND REGULATIONS
September 30, 2016

NONCOMPLIANCE WITH THE ANTIDEFICIENCY ACT

Voluntary Services

During FY 2016, PBGC identified and reported an Antideficiency violation to the President, President of the Senate, Speaker of the House of Representatives, OMB Director and the Comptroller General. This noncompliance was due to an override of management controls. A Department Director, who is not a Contracting Officer, acted outside of his or her authority and allowed an independent subcontractor to continue performing work, without compensation, after the contract funding was exhausted.

U.S.C. Title 31, Section 1342, Limitations on voluntary services, states: "an officer or employee of the United States Government or of the District of Columbia government may not accept voluntary services for either government or employ personal services exceeding that authorized by law except for emergencies involving the safety of human life or the protection of property".

We recommend that management:

- Develop and implement a training program that includes specific guidance on Antideficiency responsibilities and procurement practices, for Senior Staff, Department Directors, Contracting Officers, Contracting Officer's Representatives, and other supervisory employees that have the authority to make management or contracting decisions.

Potential Noncompliance

Leases

The Corporation provided its FMFIA's assurance documentation in October 2016. During our review, we discovered that in FY 2015 PBGC's Office of General Counsel (OGC) undertook a review of its operating leases to examine the current lease obligation authority in light of a GAO ruling on multiyear lease authority and the Antideficiency Act. In FY 2015, OGC requested a legal opinion from the U.S. Department of Justice - Office of Legal Counsel (OLC) on its lease obligation authority including funding requirements. In a memorandum dated September 30, 2015 to PBGC OGC, OLC concluded that PBGC has the authority to enter into multiyear leases. However, it does not have the authority to fund multiyear leases longer than five years on an incremental basis and must recognize and record in full, all contractual obligations incurred in connection with the lease agreements. Additionally, OLC concluded that nothing in PBGC's organic statute provides a basis for incremental funding of lease obligations. The remaining life of PBGC's three headquarters leases expire in two years. The OGC "does not believe that, based on the current status of these leases, PBGC has an Antideficiency Act issue with the headquarters leases". Also, PBGC maintains a COOP lease and five federal benefit administration office site leases. It is OGC's opinion that "none of these six leases implicate Antideficiency concerns". Further, the OGC concluded that they have sufficient funds

PENSION BENEFIT GUARANTY CORPORATION
NONCOMPLIANCE WITH LAWS AND REGULATIONS
September 30, 2016

to cover their current obligations although these funds have not been obligated in full. Additional work is needed to determine if the Corporation is in violation of the Antideficiency Act.

U.S.C. Title 31, Section 1501(a)(1), requires an agency to record the full amount of its contractual liability against funds available at the time the contract was executed. U.S.C Title 31 Section 1341(a)(1)(A), prohibits a federal employee from making or authorizing an expenditure from, or creating or authorizing an obligation under, any appropriation or fund in excess of the amount available in the appropriation or fund unless authorized by law.

EXHIBIT III

PENSION BENEFIT GUARANTY CORPORATION
STATUS OF PRIOR YEAR'S FINDINGS

Prior Year Condition	Status as Reported at September 30, 2015[2]	Status as of September 30, 2016
1. Controls over PVFB Liability	***Material Weakness:*** PBGC had weaknesses in the following: • Calculation of the PVFB Liability • Valuation of Plan Assets • Documentation to Support Benefit Calculation	Partially resolved and downgraded to significant deficiency number 1 and included in Exhibit I.
2. Entity-wide Security Program Planning and Management	***Significant Deficiency:*** PBGC had weaknesses in the following: • PBGC had not completed security assessments and authorizations for its major applications • Weaknesses in PBGC's infrastructure design and deployment strategy for systems and applications adversely affected its ability to effectively implement common security controls across its systems and applications	Partially resolved and classified as significant deficiency number 3 and included in Exhibit I.
3. Access Controls and Configuration Management	***Significant Deficiency:*** Weaknesses in the IT environment contributed to deficiencies in system configuration, segregation of duties, role-based access controls, and monitoring.	Partially resolved and classified as significant deficiency number 4 and included in Exhibit I.
4. Controls over Premium Income	***Significant Deficiency:*** PBGC has control deficiencies in the following: • Recording of premium income • System requirements and system design documentation • Comparison match of 5500 and Comprehensive Premium Filings	Partially resolved and included in the Management Letter.

[2] Report on Internal Control Related to Pension Benefit Guaranty Corporation's Fiscal Year 2015 and 2014 Financial Statements Audit: http://oig.pbgc.gov/pdfs/FA-15-108-3.pdf

EXHIBIT III

PENSION BENEFIT GUARANTY CORPORATION
STATUS OF PRIOR YEAR'S FINDINGS

Compliance and Other Matters		
Noncompliance with Title 29 of the *Code of Federal Regulation (C.F.R.)*, Part 4044.41, Subpart (b), General valuation rules	Plan assets shall be based on the method of valuation that most accurately reflects such fair market value.	Resolved

EXHIBIT IV

PENSION BENEFIT GUARANTY CORPORATION
MANAGEMENTS RESPONSE FY2016
INDEPENDENT AUDITOR REPORT
SEPTEMBER 30, 2016

Pension Benefit Guaranty Corporation
1200 K Street, N.W., Washington, D.C. 20005-4026

Office of the Director

MEMORANDUM

NOV 15 2017

To: Robert Westbrooks
Inspector General

From: W. Thomas Reeder
Director

Subject: Response to the Independent Auditor's Combined Audit Report for the FY 2016 Financial Statement Audit

Thank you for the opportunity to comment on the Office of Inspector General's FY 2016 audit results regarding the agency's financial statements, internal controls, and compliance with laws and regulations. PBGC protects the pensions of millions of Americans, so it is especially noteworthy that our financial statements have once again received an unmodified opinion.

Over all, we agree with your opinion on internal controls, and are fully committed to addressing the issues in this year's report. We especially appreciate your attention to reviewing our corrective actions, resulting in the lowest number of open recommendations in many years. Please rest assured that we will continue working to address the remaining control weaknesses as we continue to implement Enterprise Risk Management throughout PBGC.

We sincerely appreciate your report's notice of PBGC's progress, as much staff work has gone into improving controls and implementing audit recommendations. Work remains to be done, and as management completes it, we will certainly keep your office informed.

cc: Patricia Kelly
Cathleen Kronopolus
Alice Maroni
Karen Morris
Ann Orr
Michael Rae
Robert Scherer
Judith Starr
Martin O. Boehm
Theodore J. Winter

ORGANIZATION

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Secretary of Labor

Jacob J. Lew
Secretary of the Treasury

Penny Pritzker
Secretary of Commerce

Executive Management

W. Thomas Reeder
Director

Patricia Kelly
Chief Financial Officer

Cathleen Kronopolus
Chief of Benefits Administration

Alice Maroni
Chief Management Officer

Ann Orr
Chief of Staff

Michael Rae
Deputy Chief Policy Officer

Karen Morris
Chief of Negotiations and Restructuring

Robert Scherer
Chief Information Officer

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Director
Office of Equal Employment Opportunity

Theodore J. Winter, Jr.
Director
Financial Operations Department

Scott G. Young
Director
Actuarial Services and Technology Department

Christopher Bone
Acting
Risk Management Officer

The PBGC Advisory Committee

Representing the Interests of Employee Organizations

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Hoboken, New Jersey

Representing the Interests of the General Public

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Robin Diamonte
Middletown, Connecticut

Henry C. Eickelberg
Lighthouse Point, Florida

Participant and Plan Sponsor Advocate

Constance A. Donovan

Pension Benefit Guaranty Corporation

OPINION 97-1

May 5, 1997

REFERENCE:
[*1] 4001(b)(1)4001 Definitions
4201(a)4201 Withdrawal Liability Established
29 CFR 4001.3>4001.3>

OPINION:

This responds to your request for the opinion of the Pension Benefit Guaranty Corporation ("PBGC") concerning the application of the employer liability provisions of the Employee Retirement Income Security Act of 1974 ("ERISA") to members of controlled groups located outside the United States.

Your request makes the following representations of fact. Company A is a privately-owned domestic holding corporation whose assets are its equity interests in several operating subsidiaries located throughout the world, including Company B, a domestic corporation. In September 1993, Company A and Company B (collectively, the "Debtors") petitioned for reorganization under Chapter 11 of the Bankruptcy Code.

Company B was obligated to contribute to the Plan, a "multiemployer plan" within the meaning of section 4001(a)(3) of ERISA. On January 1, 1994, Company B permanently ceased all covered operations or to have an obligation to contribute under the Plan within the meaning of ERISA § 4203(a). Subsequently, the Plan underwent a "mass withdrawal" within the meaning of 29 C.F.R. § 4001.2. The Plan [*2] filed bankruptcy claims against the Debtors for withdrawal liability, including liability allocable as a result of the mass withdrawal. The Debtors and the Plan entered into a settlement agreement that provided that the Plan would have an allowed general unsecured claim against Company B. The settlement agreement released certain entities that are under "common control" with Company B within the meaning of ERISA § 4001(b)(1). The settlement agreement expressly provided, however, that the release does not apply to eight wholly-owned subsidiaries of Company A that are incorporated and operate in the United Kingdom (collectively, the "UK Entities"). We assume that the settlement agreement was duly approved by the bankruptcy court.

You ask (i) whether the UK Entities constitute a "single employer" with the Debtors within the meaning of ERISA § 4001(b)(1), and if so (ii) whether the UK Entities' location outside the United States affects the principle that all controlled group members are jointly and severally liable for withdrawal liability.

As you know, section 4221 of ERISA provides that disputes between a plan sponsor and an employer on issues concerning withdrawal and withdrawal [*3] liability are to be resolved through arbitration. PBGC does not involve itself in such proceedings. However, PBGC will continue its practice of answering general questions of interpretation under Title IV of ERISA.

Section 4201(a) of ERISA provides that "if an employer withdraws from a multiemployer plan[,] . . . then the employer is liable to the plan in the amount determined under [part 1 of subtitle E of Title IV of ERISA] to be its withdrawal liability." Section 4001(b)(1) provides that for purposes of Title IV,

> under regulations prescribed by [PBGC], all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer and all such trades or businesses as a single employer. The regulations prescribed under the preceding sentence shall be consistent and coextensive with regulations prescribed for similar purposes by the Secretary of the Treasury under section 414(c) of the Internal Revenue Code of 1986 [("IRC")].

This principle of treating commonly controlled businesses as a single employer was subsequently reaffirmed during debates on the Multiemployer Pension Plan Amendments Act of 1980 ("MPPAA"). [*4] As the Senate floor sponsor stated:

Under current law, a group of trades or businesses under common control, whether or not incorporated, is treated as a single employer for purposes of employer liability under Title IV. Thus, if a terminating single employer plan is maintained by one or more members of a controlled group, the entire group is the "employer" and is responsible for any employer liability. The leading case in this area is Pension Benefit Guaranty Corporation v. Ouimet Corp., 470 F. Supp. 945 (D. Mass. 1979), [aff'd, 630 F.2d 4 (1st Cir. 1980), cert. denied, 450 U.S. 914 (1981),] in which the court held that all members of a controlled group are jointly and severally liable for employer liability imposed under section 4062 of ERISA. The bill does not modify the definition of "employer" in any way, and the Ouimet decision remains good law.

126 Cong. Rec. 23,287 (1980) (statement of Sen. Williams). In the years since MPPAA was enacted, the principle that withdrawal liability is a joint and several obligation of all controlled group members has become well settled. [*5] Your question concerns the application of this principle to foreign controlled group members.

Because it appears from your inquiry that Company A has a "controlling interest" in the UK Entities within the meaning of the section 414(c) regulations, the UK Entities would be under "common control" with the Debtors within the meaning of section 4001(b)(1) of ERISA and therefore treated with the Debtors as a single employer for purposes of section 4201(a). See 26 C.F.R. § 1.414(c)-2(a), (b)(1), (2)(A). It is our opinion that, as such, they would be jointly and severally liable for withdrawal liability.

In our view, your inquiry does not implicate extraterritorial application of ERISA. The Plan and its related trust are established and administered in the United States (see ERISA § 4021(a); IRC § 401(a)). The events that triggered liability under ERISA took place in the United States and involved the cessation of the contribution obligation or covered operations, under the Plan, of one or more United States entities. Thus, the liability in question represents the domestic application of United States law. The fact that this liability may ultimately include within its scope certain [*6] foreign affiliates does not compel a different conclusion, as by statute such affiliates are part of a "single employer." As the courts have correctly noted, Title IV's controlled group principle is intended to prevent business owners from avoiding liability by fractionalizing their business operations, and from juggling their activities to eviscerate the liability provisions of ERISA. These purposes would be ill-served by a controlled group principle that did not apply to *all* entities under common control.

Even if the question involved extraterritorial application of ERISA, we would reach the same conclusion. It is well settled that Congress has the power to enact laws that have extraterritorial application, but is presumed not to have exercised that power unless its intent to do so is clear from the statute. We think controlled group liability under ERISA was intended to have extraterritorial application, and that this is clear from the relevant statutes.

In original section 4001(b) of ERISA (now section 4001(b)(1)), Congress authorized PBGC to promulgate regulations governing the treatment of entities under common control. Those regulations are to be "consistent and coextensive" [*7] with certain Treasury regulations. Accordingly, when PBGC adopted regulations in 1976 to implement section 4001(b), it incorporated those Treasury regulations by reference. A few years later, in enacting MPPAA, Congress carried forward the controlled group principle for purposes of the new withdrawal liability rules. It did so again in 1986 when it enacted section 4001(a)(14) and amended section 4062(a) to codify the principle of controlled group liability in the context of termination of a single-employer plan, using slightly different terminology to describe the "employer." None of these legislative actions indicated any Congressional intent that controlled group liability be limited to domestic entities.

The PBGC regulations provide that two or more trades or businesses will be considered under common control (and hence a single employer) for purposes of Title IV of ERISA if they are "'under common control,' as defined in regulations prescribed under section 414(c) of the [IRC]." 29 C.F.R. § 4001.3(a)(1), (2). Section 414(c) of the IRC authorizes the Secretary of the Treasury to prescribe regulations based on "principles similar to the principles which apply in the case [*8] of subsection (b) [of section 414]."

Under section 414(b) of the IRC, employees of corporations that are "members of a controlled group of corporations (within the meaning of section 1563(a), determined without regard to section 1563(a)(4) and (e)(3)(C)) shall be treated as employed by a single employer." The Treasury Regulations under section 414(b) provide, in pertinent part, that

the term "members of a controlled group" means two or more corporations connected through stock ownership described in section 1563(a)(1), (2), or (3), whether or not such corporations are "component members of a controlled group"

within the meaning of section 1563(b).

26 C.F.R. § 1.414(b)-1(a). Thus, the governing Treasury regulation under section 414(b) does not incorporate the "foreign corporation" exclusion of section 1563(b)(2)(C). (That subsection excludes certain foreign entities from controlled group membership for purposes of filing consolidated tax returns.)

It follows that one of the "principles which apply in the case of subsection (b) [of section 414]" is that corporations connected through stock ownership under section 1563(a) shall be treated as a single employer, even if they might [*9] otherwise be excluded from the group under section 1563(b). And, true to Congress's mandate that the regulations under IRC § 414(c) be based on principles similar to those that apply under IRC § 414(b), the stock ownership tests set forth at 26 C.F.R. § 1.414(c)-1 et seq. substantially reflect the stock ownership tests of IRC § 1563(a), with no express exclusion of foreign entities.

Other sections of the IRC amply demonstrate that Congress knew how to specify a subgroup of corporations, such as "foreign corporations" or "domestic corporations," when that was its intent. See, for example, section 861(a)(1) (referring to "domestic corporations"); sections 881-84 (dealing with taxation of "foreign corporations"); and section 864(b) (providing rules for whether a "foreign corporation" is engaged in trade or business within the United States). Clearly, if Congress had intended to except foreign entities from the ambit of relevant controlled group provisions such as sections 414 and 1563(a) of the IRC or section 4001(b) of ERISA, it would have done so expressly. Instead, as noted above, the exclusion of foreign entities in section 1563(b) is to be disregarded when determining [*10] the membership of a "controlled group of corporations" under IRC § 414(b). This principle of expansive controlled group membership, which serves to effectuate the prophylactic purposes of controlled group liability, is embodied in the section 414(c) regulations as well. In sum, we think that section 4001(b)(1) of ERISA ultimately incorporates IRC provisions that generally apply to all corporations under common control, including foreign corporations. Accordingly, it would be our opinion that Congress intended for the controlled group principle under Title IV of ERISA to have extraterritorial application on the facts you have given.

The opinions stated herein are limited to Title IV of ERISA, and we express no view regarding jurisdictional issues relating to suits against foreign situs entities.

We hope the foregoing response is helpful. If you have any questions, please feel free to call Nathaniel Rayle of this Office at 202.326.4020, ext. 3886.

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