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PBGC Walks Back Early Warning Program Expansion

PBGC appears to be dialing back the guidance it issued late last year on the Early Warning Program, a risk mitigation program created pursuant to PBGC's authority to terminate a pension plan "whenever it determines that the possible long-run loss [to the PBGC] with respect to the plan may reasonably be expected to increase unreasonably if the plan is not terminated." 29 U.S.C. § 1342(a)(4).

Background

Historically, PBGC used the Early Warning Program to identify and investigate plan sponsors contemplating transactions that could increase the risk of loss to the pension plan or to PBGC as a contingent unsecured creditor of the sponsor, such as a large dividend to a shareholder, a spinoff, or taking on large amounts of secured debt. PBGC would analyze the transaction and, if appropriate, negotiate additional protection for the pension plan in the form of extra contributions, guarantees, or other forms of protection.

On December 21, 2016, PBGC released guidance on its website regarding the Early Warning Program. That guidance provided some clarity regarding the types of plans PBGC monitors, the information requested from a company if PBGC opens an Early Warning Program inquiry, and examples of negotiated protections. The December guidance also identified, for the first time, a company's credit deterioration or downward trend in a company's financial metrics as factors that might trigger an inquiry under the Early Warning Program. In other words, while historically PBGC focused on *transactions or events*, the December guidance included *trends* in the list of risk identification factors.

Plan sponsors and industry professionals were quick to cry foul. Plan sponsors have long protested that PBGC's procedures and analysis under the Early Warning Program lack transparency and, in many cases, that PBGC has prejudged a transaction before it receives any information from the company. Sponsors have also been frustrated by PBGC's apparent resistance at times to engage in meaningful settlement negotiations, forcing companies to negotiate against themselves to achieve a resolution. The apparent expansion of the Early Warning Program, suggested to plan sponsors that they could be subject to even more scrutiny by PBGC, regardless whether the company was contemplating a corporate transaction or just going about business as usual.

PBGC's updated guidance

In response to these industry concerns, on May 10, 2017, PBGC updated the guidance on its website regarding the Early Warning Program. PBGC removed credit deterioration and a downward trend in a company's financial metrics as risk identification factors, stating in an FAQ section that "[a] change in a plan sponsor's credit quality does not trigger an Early

Warning Program review." However, PBGC made clear that, in analyzing a transaction under the Early Warning Program, PBGC generally considers a company's credit quality in its analysis. If the plan sponsor has a high credit rating or a contemplated transaction will not result in a credit rating downgrade, it is less likely that PBGC will pursue an Early Warning Program investigation. By extension, then, if a sponsor has a low credit rating or a transaction will result in a credit downgrade, PBGC is more likely to take action.

PBGC clarified that the December guidance was not meant to expand the Early Warning Program and that PBGC has not "changed the monitoring criteria or the processes involved" in the program. Rather, PBGC stated that the December guidance was meant to increase transparency regarding the Early Warning Program process.
Like the December guidance, the new guidance reaffirms that PBGC focuses its monitoring efforts on plans with: (1) underfunding of $50 million or more, or (2) 5,000 or more participants, both determined on an aggregate controlled group basis. The guidance also provides examples of transactions or events that might trigger an Early Warning Program investigation, such as:

- A change in controlled group, such as a subsidiary spinoff,
- A major divestiture by an employer,
- A leveraged buyout, and
- Substitution of secured debt for unsecured debt.

The guidance further discusses the types of information PBGC typically requests in an Early Warning Program investigation and provides a sample information request. Finally, PBGC describes the types of protections it typically negotiates with plan sponsors in an Early Warning Program settlement, such as additional contributions to the plan, letters of credit, security interests or guarantees.

Observations

It should be encouraging to plan sponsors that PBGC disclaimed any prior expansion of the Early Warning Program and clarified that a company's credit deterioration or financial downturn alone will not trigger an Early Warning Program inquiry. However, PBGC still views the Early Warning Program as one of the most powerful tools in its arsenal for protecting single-employer defined benefit pension plans and the PBGC insurance fund that covers those plans, so sponsors should expect PBGC to continue to pursue Early Warning Program investigations in the context of corporate transactions, such as those identified above.

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