Q&A with Groom Law Group

Addressing Alternative Assets in Defined Benefit Plan Terminations – The Legal Perspective

GROOM LAW GROUP

Groom Law Group, Chartered

Headquarters	Washington, DC
Year Founded	1975
Area of Focus	ERISA, Employee Benefits
Website	www.groom.com

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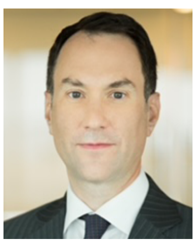

Co-Chair, Plan Sponsor Group

David co-chairs Groom Law Group, Chartered's Plan Sponsor Group. Groom is the largest employee benefits law firm in the United States with nearly ninety lawyers focusing on all aspects of benefits – from health and retirement plans, to IRAs, to litigation and policy involving these plans. David regularly focuses on fiduciary and practical compliance issues involving pension plans, including their wind-down and de-risking.

BCG: *Can you tell us a bit about Groom's work in terminating defined benefit plans and how it has evolved in recent years?*

Levine: Since its founding in 1975, Groom has long been a thought leader in guiding the creation, administration and maintenance, and preparation for and termination of defined benefit plans. In recent years, with a significant number of large corporate defined benefit plans being "frozen" to future benefit accruals, a significant focus of our defined benefit pension plan practice has shifted to de-risking, compliance (including significant Department of Labor investigations involving missing participants and cybersecurity), and implementing terminations (whether of fully funded or underfunded plans) of our clients' defined benefit plans through their post-termination PBGC audit phase.

BCG: *In November 2021, we published an article about Addressing Alternative Assets in Defined Benefit Plan Terminations – Considerations for Plan Sponsors[1]. As counsel to pension plans of all sizes – from smaller professional services companies to the largest of the Fortune 500 – do you see considerations relating to alternative assets in pension plans being a significant focus at this point?*

Levine: Absolutely. With the ever-increasing focus on defined benefit plan investigations and scrutiny of pension terminations, a lot of our focus is working collaboratively with advisors, consultants like BCG, actuaries, recordkeepers and internal benefits staff on preparing for termination. As plan fiduciaries prepare their pension plans for their final phases, a key discussion we regularly have is ensuring that plan assets are in a form that allows the implementation of the plans for their wind-down in a manner consistent with plan fiduciaries' duties under ERISA, the key law governing the operation and termination of pension plans. While the liquidity of pension plan assets to facilitate monthly and annual pension plan payments is a key concern for operational compliance under ERISA, this focus on alternative asset classes, if any, and their liquidity often increases as a plan approaches termination.

BCG: *Why is it that alternative assets are a particular focus for you as you advise clients with pension plans approaching the termination process?*

Levine: Put simply, under ERISA, plan fiduciaries have a duty to invest pension plan assets in a prudent manner that diversifies risk and ensures that a pension plan has assets sufficient to fund the benefits payable to participants and beneficiaries. Defined benefit pension plans of all sizes have long looked to alternative assets as a portfolio diversifying alternative to address their fiduciary duties under ERISA and many pension plans have benefited from investing in alternative assets. However, some alternative asset classes have liquidity "gates" or other restrictions that limit the ability to immediately liquidate these investments.

In an ongoing pension plan, the unique liquidity attributes of some alternative asset classes, such as the length of the "J curve" for private equity, is regularly managed as part of an ongoing fiduciary process that may be reflected in

1 *This Q&A is Part II of a two-part series. To read Part I, click here.*

a pension plan's investment policy statement. However, when a pension plan is terminated, all plan assets have to be distributed or annuitized and a pension plan alternative investment may not have time to complete its regular investment cycle.

BCG: *When do you encourage a client to focus on alternative assets in their pension portfolio and are there any general rules of thumb you can recommend for our readers?*

Levine: In most cases, the process of getting to the final termination of a pension plan, unless it is a distress termination in bankruptcy, follows a pretty consistent series of steps. Although not always the case, it is common that a plan is "frozen" to future accruals at some point which means that no further benefits under the plan are earned, or, in lawyer-speak, "accrued". After that point, it is common that the plan fiduciaries will, as a plan becomes better funded over time, attempt to "de-risk" investments so that there is less risk of a downside investment event dramatically increasing a pension plan's underfunding. Eventually this de-risking reaches a point where plan termination becomes feasible.

When a plan freezes or begins to de-risk, it can be a good time to flag any alternative investments to ensure that these investments have an investment horizon that will not exceed the expected life of the pension plan. In addition, we may at this point, working with other advisors as appropriate, begin discussions of paths to address potential liquidity issues to ensure alternative investments do not delay the future termination process.

BCG: *When a client is about to enter the formal pension termination process, are there additional items that become important to focus on?*

Levine: Yes. As the BCG team knows well, the pension termination process involves a significant number of steps and once the formal plan termination process is implemented, many deadlines are triggered. For example, while a cash balance pension plan may have always allowed for lump sum distributions for terminated employees, it is common practice for a plan that is terminated to allow for a one-time window during which all participants – even those who are still active employees of an employer – may elect to receive a lump sum. Depending on the demographics of a pension plan, this lump sum can cause a need to liquidate alternative assets earlier.

Further, there is always the basic question of "what can I do" with my alternative assets when a plan is in its final payout stage. Some alternative assets may have buyers on the secondary market, but not all do. At that point, we often have to explore more creative options involving in-kind transfers to insurance carriers or other parties. Layered into this discussion are ERISA's prohibited transactions rules that can limit some of the methods that can be utilized to make alternative assets liquid. As a result, depending on the structure of a pension plan's investments, early identification and proactive attention to this issue can help minimize the risk of a potential bad outcome – such as a need to "un-terminate" a pension plan.

BCG: *In closing, what do you see as distinguishing Groom from other law firms that advise on pension plan terminations?*

Levine: What distinguishes Groom is our level of expertise in this area. From our inception right after the enactment of ERISA in 1974, we have been involved in every key ERISA development. Because of our size, we provide what we consider to be a unique level of specific subject matter expertise that leverages our colleagues' expertise in working at agencies like the PBGC, a number of our colleagues' experience as actuaries and accountants, our industry-leading knowledge of ERISA and its prohibited transaction rules, and our experience with creating and investing in alternative investment products. In short, while there are always new developments, because of our industry leading knowledge base, we come equipped from the first moment to guide clients through the pension plan termination process and especially any challenges that emerge in this process.

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About BCG Pension Risk Consultants | BCG Penbridge ("BCG")

BCG specializes in assisting defined benefit plan sponsors with managing the costs and risks associated with their pension plans. Since 1983, BCG has successfully helped over 2,500 organizations achieve their pension de-risking goals.

Please visit our website bcgpension.com to learn more.