

Retirement Plans: Workforce Reductions and Triggering Events Employers Should Keep in Mind

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As a result of the coronavirus pandemic, U.S. employers are shedding employees at rates that haven't been seen since the 2007-09 recession. This trend is expected to continue. The following is a high-level summary of several triggering events that employers who maintain qualified retirement plans should keep in mind when undertaking significant workforce reductions. *The rules surrounding workforce reductions and retirement plans are complex and include many nuances and exceptions. Please use this summary for general information purposes only and not legal advice. As always, please reach out with any specific questions or issues you have.*

1. Partial Terminations

- a. If a qualified retirement plan experiences a "partial termination," Section 411(d)(3) of the *Internal Revenue Code* provides that all "affected employees" (as described below) must become 100% vested in their accrued benefits (to the extent funded) or in the amounts credited to their plan account(s).
- b. Whether a partial termination has occurred is a facts-and-circumstances determination. One scenario that requires careful evaluation is a significant reduction in workforce. For example, the Internal Revenue Service (IRS) has found that a qualified retirement plan may have a partial termination if at least 20% of participating employees experienced an employer-initiated severance from employment with the employer(s) maintaining the plan in a given year. In making the 20% calculation, the IRS generally looks at the number of active participants reported on the plan's Form 5500 at the end of the previous year compared with the number of active participants at the end of the year in which the event occurred. However, court cases and other guidance may allow some employees to be excluded from the calculation, such as voluntary quits, scheduled retirements, or normal turnover. If there is a turnover rate of at least 20%, a rebuttal presumption of a partial plan termination is created.
- c. Partial terminations can occur in connection with a significant corporate event such as a closing of a plant or a division, or as a result of general employee turnover due to adverse economic conditions or other reasons that are not within the employer's control.
- d. An "affected employee" for this purpose is generally anyone who left employment for any reason during the year or period in which the partial termination occurred (e., both voluntary and involuntary terminations are included). For this reason, note that the definition of "affected employee" will likely encompass a larger group of employees than the group that is identified with an employer-initiated severance from employment for the 20% test described

above in determining if a partial termination has occurred. Affected employees who improperly incurred a forfeiture must be made whole.

2. Active Participant Reduction Reportable Event

- a. Section 4043(a) of the Employee Retirement Income Security Act (ERISA) requires that plan administrators and contributing sponsors of qualified defined benefit retirement plans (pension plans) notify the Pension Benefit Guaranty Corporation (PBGC) within 30 days after the occurrence of certain “reportable events.” Note that certain plan administrators and plan sponsors may be subject to advance reporting requirements.
- b. One such reportable event occurs when the number of active participants under a pension plan is reduced below 80% of the number of active participants at the beginning of the plan year because of a “single-cause event” or an “attrition event.”
- c. A “single-cause event” occurs when, as a result of a new single cause, the ratio of the aggregate number of individuals who ceased to be active participants because of that single cause, to the number of active participants at the beginning of the plan year, exceeds 20%. Single-cause events can include events such as the discontinuance of an operation or business, a natural disaster, a mass layoff, or an early retirement incentive program.
- d. An “attrition event” occurs on the last day of a plan year if the sum of the number of active participants covered by the plan at the end of the plan year (plus the number of individuals who ceased to be active participants during the same plan year that are reported to PBGC in a single-cause event, if any), is less than 80% of the number of active participants at the beginning of such plan year.
- e. PBGC regulations include important interpretive guidance, extensions, and waiver provisions that could apply depending on the situation.

3. 4062(e) Substantial Cessation of Operations at a Facility

- a. Section 4062(e) of ERISA and related rules require that administrators of pension plans notify the PBGC within 60 days after the occurrence of a substantial cessation of operations at a facility (a 4062(e) event).
- b. A 4062(e) event occurs when there is a permanent cessation of operations at a facility and that cessation results in a workforce reduction of more than 15% of the total number of “eligible employees.” “Eligible employees” include employees who participate in *any* retirement plan (e. any defined benefit plan or defined contribution plan) maintained by members of the plan sponsor’s controlled group. PBGC forms describe a variety of events as potential causes of a cessation of operations, including a facility shutdown, a facility sale, discontinued operations, the winding down of a company, or a reduction in force.
- c. If a 4062(e) event occurs, the employer is required to satisfy the resulting liability as calculated pursuant to PBGC regulations. The liability can generally be satisfied by an employer electing to make additional contributions to the pension plan. Depending on the circumstances, the PBGC and the employer may agree on alternative means of satisfying the 4062(e) liability.
- d. PBGC interpretive guidance describes important exceptions that could apply depending on the situation.

4. Complete or Partial Withdrawals from Multiemployer Pension Plans

- a. Although the complex rules related to withdrawal liability are outside the scope of this post, employers who participate in defined benefit pension plans maintained under one or more collective bargaining agreements (CBA) and to which multiple employers contribute (multiemployer plans) should be aware that significant liabilities can be triggered upon a complete or partial withdrawal from a multiemployer plan.
- b. In general, a complete withdrawal from a multiemployer plan occurs if a participating employer either permanently ceases to have an obligation to contribute to the multiemployer plan, or permanently ceases all covered operations under the multiemployer plan.
- c. A partial withdrawal from a multiemployer plan occurs if on the last day of the plan year there is a 70% contribution decline, or there is a partial cessation of the employer’s contribution obligation. A partial cessation arises if an

employer no longer has an obligation to contribute to the plan under one or more, but not all, CBAs, and continues to perform work in the jurisdiction of the type for which contributions were previously required or transfers such work to another location or to an entity or entities owned or controlled by the employer. It can also arise if the employer ceases to have an obligation to contribute with respect to work performed at one or more facilities, but continues to perform work at the facility of the type for which the obligation to contribute ceased.

d. PBGC guidance describes important exceptions that apply to particular industries and interpretive rules that could apply depending on the situation.

5. Other Considerations

- a. Nondiscrimination testing. If more non-highly compensated employees than highly compensated employees are laid off, employers should consider how the resulting demographic change may affect nondiscrimination testing of their plan.
- b. Special plan exceptions on eligibility for employer contributions. Some plans with year-end match or nonelective contribution formulas require employees to be employed on the last day of the plan year in order to receive a benefit. In some cases, that requirement may be waived in the plan's formula for employees who are involuntarily terminated. Plan sponsors should carefully review their benefit allocation formula when faced with a significant layoff or reduction in force.
- c. Non-qualified plan payments. If an employer is laying off a large portion of its workforce, including highly compensated employees, it may need to consider the cash-flow impact of many terminated employees looking for a cash payment from such plans after employment termination.

We would be happy to provide more detailed information or advice with respect to any of the foregoing, as well as information for your specific circumstances and facts. Please also let us know if you are not currently receiving Winston & Strawn client alerts, and we will make sure to have you included.

Please feel free to contact any of the individuals below or your usual Winston relationship attorney if you have any questions.

View all of our COVID-19 perspectives [here](#). Contact a member of our COVID-19 Legal Task Force [here](#).

Please click [here](#) to read about the Consolidated Appropriations Act, 2021, which includes limited relief for tax-qualified ERISA retirement plans with respect to partial plan terminations.

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