



Steps for terminating a defined benefit plan

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Terminating a defined benefit (DB) plan covered by Title IV of ERISA (i.e., a Pension Benefit Guaranty Corporation [PBGC] covered plan) is an involved, detailed, and time-consuming process. Many DB sponsors have already frozen their plans in anticipation of eventually terminating them, which many are expected to do beginning in 2012.

That's when provisions in the Pension Protection Act of 2006 (PPA) that affect interest rates for lump-sum payments will be fully phased in. These new rates will result in lower lump-sum values and, thus, a reduced termination liability for plans offering a lump-sum distribution option. In other words, it should be less expensive to terminate a plan beginning in 2012.

If plan assets are sufficient to pay all benefit liabilities, the sponsor can voluntarily begin the process to terminate the plan with PBGC as a "standard termination." Most sponsors will also submit a plan termination filing to the IRS, requesting a "favorable determination letter." Although not required, a favorable determination letter ensures that all qualification requirements have been met at the time of the plan termination. In addition, failure to apply for one may increase chances of a future IRS audit of the termination.

There are many issues that must be considered in a plan termination, including: developing a communication strategy, ensuring the accuracy of participant data, locating missing participants, and soliciting bids for group annuities. If the plan has not yet been frozen, then the plan sponsor needs to consider the impact on other parts of the retirement program (both qualified and nonqualified) and decide whether replacement benefits will be provided. As you might expect, the termination process requires ongoing, coordinated efforts involving the plan sponsor, actuary, legal counsel, investment committee, benefits department, and/or administrative service provider. The process requires meticulous attention to detail and can be expected to last between 12 and 24 months.

Key termination considerations

In anticipation of a plan termination, a plan sponsor should first address several key questions, including:

What will be the effective date of the termination (i.e., the plan termination date)?

- The plan termination date is the date chosen by the plan sponsor and represents the start of the plan termination process. The plan termination process will end when the last benefit is paid from the plan.

What lump-sum options will be available to participants as a result of the plan termination?

- Will a lump-sum option need to be added to the plan, or will the plan's current lump-sum option need to be modified?
- Will retirees currently receiving annuity payments have the option to elect a lump sum as a result of the plan termination or will they only be able to continue the annuity option elected at retirement?

What rollover choices will be available to participants who elect a lump-sum option and how will they be communicated?

What changes to the plan's investment portfolio need to be considered, given the shortened investment horizon?

Required by the PBGC

Several notices/forms—briefly described below—are required in completing a standard termination with the PBGC.

Notice of Intent to Terminate (NOIT). Must be issued to affected parties at least 60 days and not more than 90 days before the proposed termination date. Affected parties include participants, beneficiaries of deceased participants, alternate payees under qualified domestic relations orders (QDROs), and employee organizations representing participants.

Notice of Plan Benefits (NOPB). Must be issued to participants, beneficiaries of deceased participants, and alternate payees no later than the time the plan administrator files the Standard Termination Notice (PBGC Form 500) with the PBGC.

Standard Termination Notice (PBGC Form 500, including the Schedule EA-S). Must be filed with the PBGC on or before the 180th day after the proposed termination date. Note: The PBGC has 60 days after receiving a complete Form 500 to review the termination for compliance with the law and regulations.

Notice of Annuity Information. Must be provided to affected parties no later than 45 days before the distribution date if any benefits are to be distributed in an annuity form.

Schedule MP (including applicable attachments). Must be sent to the PBGC if the plan has Missing Participants; generally provided at the same time as the PBGC Form 501.

Notice of Annuity Contract. Must be provided to participants receiving their plan benefits in the form of an annuity no later than 30 days after the contract is available.

Post-Distribution Certification (PBGC Form 501). Must be filed with the PBGC no later than 30 days after all plan benefits are distributed. The PBGC will assess a penalty for late filings only to the extent the certification is filed more than 90 days after the distribution deadline.

Required by the IRS

Several notices/forms—briefly described below—are required if a sponsor decides to request a favorable determination letter from the IRS.

IRS Notice to Interested Parties. Informs affected parties of the sponsor's intention to file for a "favorable determination letter" with the IRS relative to the plan termination. Must be provided 10–24 days before filing with the IRS.

IRS Form 5310 ("Application for Determination for Terminating Plan"). Should be filed with the IRS before the date the Form 500 is filed with the PBGC. IRS Form 5310 provides the IRS with basic information relative to the plan, coverage information, the reason it's being terminated, and other details that will assist the IRS in making their determination.

In addition, an **ERISA §204(h) Notice** is required when "a plan amendment results in the significant reduction in the rate of future benefit accruals or eliminates or significantly reduces an early retirement benefit or retirement-type subsidy." Generally, this notice must be provided to affected parties no less than 45 days before the effective date of the reduction.

A termination timeline

As mentioned, the termination process requires meticulous attention to detail. A termination timeline is included in this package to help keep track of those details. It lists the steps and associated timing requirements, can assist in assigning responsibility for each step in the process, and could be used to monitor the progress through a long and arduous process. It's not uncommon for the PBGC to audit a plan termination at some point after all benefits have been distributed, which is why it's crucial that every step of the process be clearly documented.

The following is a broad, high-level overview of the standard termination process. Vanguard is available to discuss the process in greater detail and offer suggestions.

High-level plan termination steps/timing

Action	Timing	Who receives?
Draft board resolution to freeze (if plan is not already frozen) and terminate plan	Before issuing 204(h) notice and Notice of Intent to Terminate	NA
Plan amendments for termination	Finalize before plan termination date	NA
204(h) notice (notify participants of benefit freeze)	No less than 45 days before plan freeze date	Affected parties (participants, beneficiaries of deceased participants, etc.)
Notice of Intent to Terminate	No less than 60 days and no more than 90 days before plan termination	Affected parties (participants, beneficiaries of deceased participants, etc.)
Benefit freeze date	NA	NA
Plan termination date	NA	NA
Issue Notice to Interested Parties (i.e., notify participants of determination letter filing)	10–24 days before filing with the IRS to request a determination letter (i.e., Form 5310)	Affected parties (participants, beneficiaries of deceased participants, etc.)
Plan Termination Determination Letter Request (i.e., Form 5310)	Filing should be made before PBGC Form 500 is filed	IRS
Notice of Plan Benefits	Before filing PBGC Form 500	Affected parties (participants, beneficiaries of deceased participants, etc.)
Standard Termination Notice—PBGC Form 500 including Schedule EA-S submission	No later than 180 days after the plan termination date	PBGC
Expected approval from the PBGC	60 days following submission of Form 500	Plan sponsor
IRS approval of Determination Letter	Typically 9–12 months after submission	Plan sponsor
Distribution of benefit election forms	Can be sent with Notice of Plan Benefits but probably should wait until IRS approval of Determination Letter	Affected parties (participants, beneficiaries of deceased participants, etc.)
Notice of Annuity Information	At least 45 days before distributions	Affected parties (participants, beneficiaries of deceased participants, etc.)

Action	Timing	Who receives?
Distribute all assets	Pending IRS and PBGC approval— all assets must be distributed by the later of (a) 180 days after expiration of PBGC’s 60-day review period, or (b) 120 days after receipt of a favorable IRS determination letter, provided that a valid determination letter was filed before Form 500	Affected parties (participants, beneficiaries of deceased participants, etc.) and Annuity Provider
Notice of Annuity Contract	No later than 30 days after all plan benefits are distributed	Participants receiving an annuity
PBGC Form 501 Post-Distribution Certificate	No later than 30 days after all plan benefits are distributed (although the PBGC will not assess a fine until 90 days have passed)	PBGC
Schedule MP (for missing participants)	Generally at the same time as the PBGC Form 501	PBGC

Other actions for plan termination

- IRS Form 5500 and PBGC Premium filings.
- Coordinate/finalize the purchase of group annuities for those not taking a lump-sum distribution.
- Review trust requirements and investments.
- Ensure written commitment to contribute funds to the plan (if plan not fully funded).
- Close trust.
- Participate in PBGC audit, if applicable.

For more information, contact your Vanguard representative.

For additional information and one-stop access to other valuable resources, please visit Vanguard’s DC Resource Center at vanguard.com/dcresourcecenter or Vanguard’s DB Resource Center at vanguard.com/dbresourcecenter.



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