Protecting America's Pensions

OFFICE OF INSPECTOR GENERAL

REPORT

Risk Assessment of PBGC's Implementation of Special Financial Assistance

Report No. SR-2022-09
March 17, 2022

March 17, 2022

MEMORANDUM

TO: Gordon Hartogensis
Director

FROM: Nicholas Novak
Inspector General
Nicholas J. Novak

SUBJECT: Risk Assessment of PBGC's Implementation of Special Financial Assistance (SR-2022-09)

I am pleased to transmit the attached report resulting from the Risk Assessment (Assessment) of the Pension Benefit Guaranty Corporation's Implementation of Special Financial Assistance (SR-2022-09/SR-21-160).

We contracted with Ernst & Young LLP (EY), an independent certified public accounting firm, to perform the Assessment. EY's services are advisory in nature. EY conducted the Assessment in accordance with standards of the American Institute of Certified Public Accountants. EY did not render an assurance report or opinion as a result of this Assessment, nor did EY's services constitute an audit, review, examination, forecast, projection or any other form of attestation as those terms are defined by AICPA.

Based on the information gathered during this Assessment, EY identified several risk categories that would generally be considered by organizations with a similarly-situated risk context. PBGC has the opportunity to further assess whether existing processes are commensurate with its new risk context.

EY is responsible for the attached report dated March 14, 2022. This report is intended solely for the information and use of the Inspector General, Management of PBGC, and Government Accountability Office and should not be used by anyone other than these specified parties.

We would like to take this opportunity to express our appreciation for the overall cooperation provided by PBGC during the performance of the Assessment.

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Memorandum

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14 March 2022

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American Rescue Plan Act of 2021
Special Financial Assistance Implementation Risk Universe Assessment for the Pension Benefit Guaranty Corporation

Background

On March 11, 2021, the American Rescue Plan Act of 2021 (ARP) was enacted to provide trillions of dollars in funding in an effort to speed up the United States' recovery from the economic and health effects of the COVID-19 pandemic. Funding was authorized to allow the Pension Benefit Guaranty Corporation (PBGC) to provide assistance to certain underfunded multiemployer plans (MEPs) through a Special Financial Assistance (SFA) program. The PBGC estimates that approximately $94 billion will be paid to over 200 plans that cover more than 3 million participants and beneficiaries[1]. ARP provides that qualifying MEPs are to receive lump sum payments meant to provide sufficient funding for benefit payments for a 30-year period. Based on publicly available information, some MEPs are expected to receive payments in excess of $1 billion, and one MEP is expected to receive a payment of approximately $40 billion[2].

Since its inception in 1974, the PBGC has provided protection for retirement benefits of millions of workers and retirees in participating single employer and multiemployer pension plans. The PBGC pays over $6 billion a year in benefit payments to retirees and beneficiaries in single-employer pension plans for which the plan sponsor was unable to continue making payments. More than 33 million workers are in plans that are insured by the PBGC.[3]

ARP directed the PBGC to develop detailed regulations, policies and corresponding procedures by July 2021 in order to allow qualifying MEPs to begin to apply for SFA funds. The PBGC published in the Federal Register the Interim Final Rule[4] ('the IFR') in July 2021. The IFR outlines the PBGC's interpretation of the ARP and provides instruction and guidance on the SFA application process, including the information that plan sponsors are required to submit.

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[1] https://www.pbgc.gov/arp-faqs
[2] https://crsreports.congress.gov/product/pdf/R/R46803
[3] https://www.pbgc.gov/sites/default/files/documents/pbgc-annual-report-2021.pdf
[4] www.federalregister.gov/documents/2021/07/12/2021-14696/special-financial-assistance-by-pbgc

ARP also directs the PBGC to review SFA applications and either approve or deny within 120 days of receipt. The IFR describes "priority groups" which stratify plans into categories with varying application eligibility dates based on the plan's size and funded status. The IFR also describes an emergency filing process to accept priority applications to the extent that a plan sponsor needs to apply for funds before it is otherwise eligible based on its priority category.

Applications are submitted through an on-line portal accessible through the PBGC's website[5]. The IFR directs PBGC to perform a high-level review of the estimated SFA amount contained in the application, as well as the underlying assumptions, for reasonableness. The IFR does not direct PBGC to perform any detailed calculations or use granular participant data to develop an independent estimate of an SFA amount to be paid. In the case of approval, the U. S. Department of Treasury provides funds to the PBGC who then distributes the payment to the plan sponsor. If the PBGC does not decide on an application within the 120-day timeframe, such application is deemed to have been automatically approved. The IFR does provide the PBGC with the option of closing its portal to new applications at the PBGC's discretion to manage application flow.

The IFR outlines expectations for plan sponsors to submit annual statements of compliance from the year SFA was received through 2051. The PBGC is also authorized to conduct periodic audits of a plan that has received SFA payments to review compliance with the terms of the IFR.

Risk Context

"Playbook: Enterprise Risk Management for the U. S. Federal Government"[6] states "effective risk management needs to give full consideration to the context in which the organization functions and to the risk aspects of partner organizations. This broader risk context includes all factors that affect the ability of an agency to achieve its stated mission and program objectives, both internal and external." The SFA program has a different risk context from other programs administered by the PBGC due to the source of the funding, the size of the payments, the timing of responding to applications, and the intended time horizon of the payments.

Pre-ARP

The PBGC's Multiemployer Insurance Program (the Program) provides financial assistance to MEPs that would otherwise not be able to continue paying basic benefit payments. The program is funded by plan sponsor premiums and investment income. The Program does not have access to general taxpayer funds.

The PBGC provided $230 million in financial assistance to 109 MEPs in 2021 according to its FY 2021 Annual Report. The largest single payment made through this program since 2005 was $36.7 million according to data available on the PBGC's website[7]. Payments are made throughout the year, and applicants must reapply annually to the extent additional assistance is needed. The PBGC does not have a statutory deadline for responding to applications; instead, the PBGC may provide financial assistance at its discretion to financially troubled MEP to avoid hardship for plan participants as it is reviewing the application. The PBGC has authority to request additional information required to calculate or verify the amount of financial assistance necessary[8].

Post-ARP

[5] https://efilingportal.pbgc.gov/site/
[6] https://www.cfo.gov/wp-content/uploads/2016/07/FINAL-ERM-Playbook.pdf
[7] https://www.pbgc.gov/sites/default/files/fin-assistance-me.xlsx
[8] https://www.ecfr.gov/current/title-29/subtitle-B/chapter-XL/subchapter-J/part-4281/subpart-D/section-4281.47

For the first time in the PBGC's history, taxpayer dollars are being used to fund financial assistance under ARP. The first SFA payment in the amount of $112.6 million was paid in January 2022[9]. This single payment was the largest made in the PBGC's history. As noted earlier, future SFA payments are expected to have larger amounts, with several MEPs expected to receive payments in excess of $1 billion and one plan expected to receive up to $40 billion.

Whereas there is no statutory deadline for standard financial assistance applications, the PBGC must respond to SFA applications within 120 days. ARP does not require the PBGC to directly calculate SFA payments; as such, the PBGC reviews for reasonableness the assumptions and SFA amounts prepared by the actuaries engaged by the MEPs requesting SFA funds.

Whereas standard financial assistance is applied for on an annual basis, SFA applications are meant to cover thirty years of benefit payments. Approved applicants will receive lump sum payments in an amount intended to fund pension benefits through 2051. The Department of Labor is tasked with ensuring plans that receive SFA funds reinstate suspended benefits pursuant to ARP. Plan sponsors must submit annual statements of compliance to the PBGC through 2051.

Assessment Objective

The PBGC Office of Inspector General (OIG) is an independent entity within the PBGC. OIG provides independent oversight of PBGC to improve the agency's programs and operations and to prevent and detect fraud, waste, and abuse. OIG reports to the PBGC's Board of Directors and to the United States Congress. In light of different risk context noted above, OIG engaged Ernst & Young LLP (EY) to assist with its assessment of the risk universe associated with the implementation of a program such as the ARP SFA program.

EY Approach

Industry standards

We considered available guidelines and benchmarks that are relevant to the PBGC. Various resources exist to aid in the development of an enterprise risk management framework, most notably the U.S. Government Accountability Office's Standards for Internal Control in the Federal Government, widely known as the 'Green Book'. These standards contain a guide to constructing and organizing a risk management system for governmental entities. The Green Book was first published in 1999 and most recently revised in 2014 and remains one of the primary resources for risk management framework guidance for federal institutions.

Other industry standards for risk management (in addition to the Playbook and the Green Book) include the Committee of Sponsoring Organizations (COSO) Framework, International Organization for Standardization (ISO) 31000, and the Institute of Internal Auditors (IIA) Three Lines of Defense Model. The Three Lines of Defense model is an outline of an organizational structure for a functioning risk management system.

EY assessment process

We began our assessment by gaining an understanding of the SFA program, considering the full program timeframe and impacted stakeholders. To accomplish this, we reviewed the IFR and held preliminary conversations with personnel in

[9] https://www.pbgc.gov/news/press/releases/pr22-01

departments that were indicated by the PBGC. Next, we identified risk categories that would generally be considered by organizations with similarly situated risk context to that described above. We then held follow-up meetings with the identified personnel to confirm applicability of the key risk categories to the SFA program. We compared our observations to expectations based on industry standards as described above and suggested areas for further consideration.

Key observations

Relevant inherent risk categories

Based on the information gathered during the assessment process, we established the following risk categories that would generally be considered by organizations with a similarly situated risk context to that described above.

Governance, risk management and oversight risks: The Green Book outlines that "management should identify, analyze, and respond to significant changes that could impact the internal control system". The introduction of a new program that operates under a new risk context, as described above, constitutes a significant change. A comparable organization in a similar situation would ensure that existing controls are functioning properly, residual risk is considered, and respond to the change with a commensurate level of risk preparedness.

Actuarial, data, and information risks: A program making one-time payments that are meant to last for thirty years has inherent risks related to the underlying census data and the actuarial assumptions used in the calculation. If the organization making the payment does not directly calculate the amount it presents additional third-party risks. The Green Book outlines that management should ensure internal and external data is "reasonably free from error and bias…", which would apply to the SFA program outlined above.

Application and assessment risks: An application process for large financial assistance payments with a statutory deadline to respond presents a number of considerations for the organization. Examples include effective management of the application process, consistent decision making, and the effectiveness of application guidance and written procedures. A standard risk assessment would consider new risks introduced by the application timing and assess whether actions are needed to manage these risks.

Operational risks: Organizations should consider the impact that the introduction of a new program will have on existing operations. Examples include consideration for internal resource sufficiency and collateral risks and internal control effectiveness. Leading organizations consider whether controls in place are commensurate to a new risk context and monitor the effectiveness of said controls.

Reporting, disclosure, and communication risks: An entity subject to reporting requirements and auditing of such reporting would consider its level of preparedness to undertake the necessary reporting steps. The level of transparency would affect the importance of accurate, consistent, and timely reporting and communication to stakeholders. Similarly positioned entities would ensure that all documents that are publicly published are clear and supported with appropriate correspondence.

Plan sponsor and Trustee compliance, oversight, and longevity risks: A program with a thirty-year time horizon introduces risks related to the oversight of the funds and ensuring they are being used as required by law. The Green Book outlines management's key compliance objectives and oversight responsibilities. Leading organizations would consider whether current controls and processes are sufficient in achieving these objectives given the new risk context.

PBGC response to ARP

We understand that the PBGC has performed the following actions in the last ten months in response to ARP. The effectiveness of these actions was outside the scope of this assessment.

- Drafted the IFR to establish the application process; requested and obtained feedback from the public
- Updated the PBGC website to include resources and guidance related to ARP
- Held two public webinars to cover a wide range of SFA topics, including the application process
- Hired additional staffing for the SFA program
- Implemented interdepartmental processes, procedures, and controls
- Initiated the development of audit procedures

Conclusion and Considerations

PBGC published the Rule less than 4 months after ARP was enacted, which has allowed the PBGC to begin receiving and processing applications in 2021. Additional processes and procedures were implemented to allow the PBGC to approve initial SFA applications, and even disburse the funds to one applicant as of the date of this Report, 10 months after ARP was enacted. Changes were needed to internal processes and staffing, which required the coordination of multiple PBGC departments.

Now that initial steps have been taken to implement the SFA program, the PBGC has the opportunity to further assess whether existing processes are commensurate with its new risk context. Similarly situated organizations would consider existing risks relevant to the program, the likelihood and impact of those risks when considering mitigation strategies.

In particular, similarly situated organizations often will consider the following when implementing a program such as the SFA program.

Risk culture and risk governance maturity

As noted earlier, the Green Book recommends that organizations take steps to assess whether their risk governance is commensurate to its risk context. This may include assigning an empowered risk professional that either reports to PBGC Board or a similar governance forum, or the Executive Director with regular reports directly to the Board; confirming that their Board or other designees are sufficiently aware of new risk contexts; and assessing existing controls to confirm they are commensurate with new risk context. Assessing adequacy of controls requires organizations to assign clear risk tolerances that align with the organization's objective, to then understand whether any persisting risk that may occur after a mitigation is in place is acceptable.

Third party and time horizon risks

Decision making that takes place in a short time frame but has long-term implications creates unique challenges, particularly when there is reliance on a third party for information to inform that decision making process. In cases where an entity relies on others to perform functions such as payment processing and compliance enforcement, the entity would be subject to external risk in relation to these third parties as well. Similarly situated organizations would consider the risks from this combination of factors to ensure that those risks have been fully assessed and also mitigated to the extent possible.

Stewardship role of funds

The introduction of a program that makes a one-time payment to cover a thirty-year period when multiple parties are involved with carrying out processes within the program, such as the case with SFA, may raise questions as to the party responsible for ongoing oversight of payments who would aid in the ongoing management of the program and management of reputational risk. Though risks related to such a program may not solely be within control of the payment executor, and may even require policy changes to address in some cases, one of the first steps in addressing these risks would be to identify a risk universe to aid in classification of ownership of individual risks.

Disclaimer

The Office of Inspector General (“OIG”) engaged Ernst & Young LLC (“EY”) to assist with its risk assessment of the PBGC’s implementation of the provisions under ARP.

The nature and scope of EY’s services were determined by the OIG and are reflected in the statement of work provided by OIG in August 2021. EY’s procedures were limited to those requested by OIG. This report is intended solely for the information and use of the Inspector General and Management of PBGC and is not intended to be and should not be used by anyone other than these specified parties. Other persons who read this Report do so at their own risk and are not entitled to rely on it for any purpose. EY does not assume any duty, obligation or responsibility whatsoever to any other parties that may obtain access to the Report.

EY’s services were advisory in nature. While EY’s work in connection with this Report was performed under the standards of the American Institute of Certified Public Accountants (the “AICPA”), EY did not render an assurance report or opinion under the Agreements, nor did EY’s services constitute an audit, review, examination, forecast, projection or any other form of attestation as those terms are defined by the AICPA. None of the services EY provided constituted legal opinions or advice. This Report is not being issued in connection with any issuance of debt or other financing transaction.

PBGC has the knowledge, experience and ability to form its own conclusions. Any assumptions, forecasts or projections contained in this Report are solely those of PBGC or are based on publicly available information.

In assisting in the preparation of this Report, EY relied on information provided by the PBGC or available from public sources. EY has not conducted an independent assessment or verification of the completeness, accuracy or validity of the information obtained. Consequently, EY provides no assurance of any kind with respect to, or on, the information relied upon.

PBGC
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Office of the Director

March 16, 2022

MEMORANDUM

To: Nicholas J. Novak
Inspector General

From: Gordon Hartogensis Gordon Hartogensis Digitally signed by Gordon Hartogensis Date: 2022.03.16 17:50:48 -04'00'
Director

Subject: Management Response to the American Rescue Plan Act of 2021 Special Financial Assistance Implementation Risk Universe Assessment for the Pension Benefit Guaranty Corporation Report

Thank you for the opportunity to comment on the Ernst & Young (EY) report on American Rescue Plan Act of 2021 Special Financial Assistance Implementation Risk Universe Assessment for the Pension Benefit Guaranty Corporation (PBGC). PBGC met with representatives from EY and the Office of Inspector General (OIG) on March 14, 2022, to review the observations and analysis in the report. The dialogue was both informative and insightful.

We appreciate the work that EY and OIG have done in reviewing the risk environment of the American Rescue Plan Act of 2021 Special Financial Assistance Program. PBGC management is reviewing the observations in the report and will keep the OIG informed as we continue to implement, manage, and strengthen the risk governance and stewardship of the American Rescue Plan Act of 2021 Special Financial Assistance Program.

Please contact Frank Pace should you have any questions.

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