Office of Inspector General
Pension Benefit Guaranty Corporation

July 11, 2016

RISK ADVISORY

To: Karen Morris
Acting Chief of Negotiations and Restructuring

From: Robert A. Westbrooks
Inspector General

Subject: Bundled Administrative Expenses in Financial Assistance Requests

This Risk Advisory is to report our observations related to management's acceptance of a bundled administrative expense agreement with a third-party administrator for a multiemployer (ME) plan receiving financial assistance from PBGC. The suggestions contained in this Risk Advisory do not constitute formal audit recommendations; therefore, no management response is required. If management does take action as a result of this Risk Advisory, we respectfully request a written summary of the action taken. Please be advised we will post this Risk Advisory on our public website in compliance with our responsibility under the Inspector General Act to keep the Board, Congress, and the public fully and currently informed about problems and deficiencies relating to the Corporation's programs and operations.

Summary

As you know, management is responsible for identifying internal and external risks that may prevent the Corporation from meeting its strategic goals and objectives, assessing risks to determine their potential impact, and applying the appropriate risk responses. One source of risk information is the OIG.

We have identified the following risk that warrants management's attention:

> *PBGC is paying a third-party administrator administrative expenses that may be in excess of expenses that are reasonable, necessary and adequately supported due to the acceptance of a bundled administrative expense agreement.*

To mitigate this risk, we suggest you review this agreement and any similar agreement with other third-party administrators to ensure PBGC only pays those administrative fees that are "reasonable, necessary and adequately supported."

Background

PBGC's ME pension insurance program protects about 10 million workers and retirees in about 1,400 pension plans. Collective bargaining agreements typically establish ME plans involving more than one unrelated employer, generally in one industry. Most employers and union trustees administer these plans jointly. Some may engage a third party to administer the plan, however, the trustees remain responsible for the plan. PBGC does not directly pay benefits to participants of failed or insolvent ME plans. Instead, under ERISA § 4261, the agency provides the insolvent ME plan "financial assistance in an amount sufficient to enable the plan to pay basic benefits under the plan." PBGC's financial assistance includes the amount of benefits owed, as well as an amount to cover administrative expenses to enable the plan to pay retirees and place new retirees into pay status.

The Multiemployer Program Division (MEPD), within the Office of Negotiations and Restructuring, is responsible for processing financial assistance requests. Once a plan files a Notice of Insolvency and a financial assistance request with PBGC, MEPD assigns the plan to a case auditor for processing. Upon receipt of requested documents and information, the MEPD auditor determines the appropriate amount of assistance the plan needs. Financial assistance consists of the amount of actual benefit payments and reasonable administrative expenses. MEPD procedures require field audits to ensure the initial financial assistance awarded goes to an insolvent plan and the plan is properly spending the proceeds of the PBBGC loan.

In FY 2015, PBGC paid $103 million in financial assistance loans to 57 ME plans (an increase from $89 million in financial assistance to 44 ME plans in FY 2013). In FY 2015, expenses for the ME program exceeded income for a net loss of $9.9 billion. This loss increased the deficit in the ME program to $52 billion – an all-time record high for the program. According to the latest PBGC projections report, it is more likely than not the program will run out of money by 2025. The ME program has been on the GAO's High-Risk List since 2009, and the fiscal sustainability of the program has been a long-standing concern of our office.

Risk

PBGC is paying a third-party administrator administrative expenses in excess of expenses that are reasonable, necessary and adequately supported due to the acceptance of a bundled administrative expense agreement.

ERISA § 404(a)(1) mandates that a "fiduciary shall discharge his duties with respect to the plan solely in the interest of the participants and beneficiaries and for the exclusive purpose of paying benefits and defraying reasonable expenses of administering the plan." ERISA § 408(c)(2) permits a fiduciary to receive "reasonable compensation for services rendered, or for the reimbursement of the expenses properly and actually incurred, in the performance of his duties with the plan [.]"

Our review focused on one plan wherein the plan administrator bundled expenses for administrative services rendered. In his 2012 Fiduciary and Administrative Services Agreement with the plan, the plan administrator states that he has filled the roles of Trustee, Plan Administrator, Plan Sponsor and Independent Fiduciary since 2000.

According to MEPD policy, administrative expenses incurred or charged to a plan should be "properly recorded, reasonable, and necessary" and such expenses be supported by adequate documentation. MEPD is to enforce this policy through field audits and financial assistance reviews designed to ensure plans meet the standards for financial assistance as provided by ERISA and PBGC regulations.[1] For this plan, MEPD reported in its 2007 field audit report that key documents to support plan expenses and cash on hand, such as bank statements and invoices, were missing. The field audit report further depicted the plan's records as "at best sketchy or not available."

In 2015, we found PBGC paid the plan administrator $264,000 ($22,000 per month) for administering benefits to approximately 2,500 participants. For these payments, PBGC allowed compensation to the plan administrator in the form of a fixed monthly fee for fiduciary and administrative services that were not reasonable or adequately supported. This occurred because the plan administrator bundled variable costs, such as billable staff wages and trustee fees, into his fixed monthly administrative fee. Since 2007, PBGC has paid the plan administrator's fee under this bundled fee arrangement. The plan administrator renegotiated his fixed fee once, in 2014, reducing it from $29,000 to $22,000 a month. After the reduction of the fee, PBGC continued to pay for bundled administrative services without requiring proper supporting evidence. MEPD's periodic reviews of the plan's administrative expenses did not go beyond the total monthly bundled amount to assess all costs incurred or charged, direct costs or otherwise.

MEPD requires a plan to submit a written request each time it needs financial assistance. Aside from the request letter, MEPD is required to review other supporting documents, such as bank

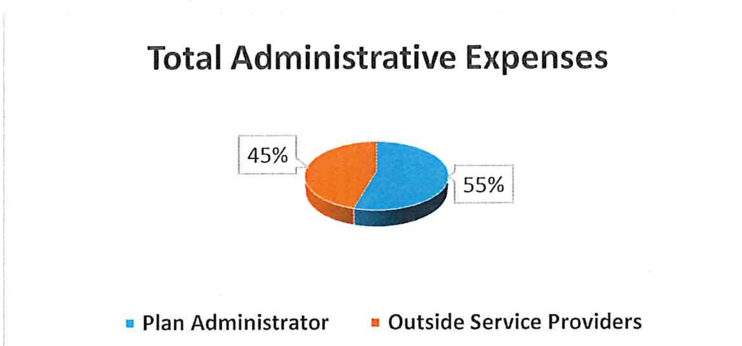
[1] MEPD Multiemployer Plan Procedures FY 2014, dated October 1, 2014, was the current criteria at the start of our review.

statements, invoices, cancelled checks and service agreements, as part of the financial package submission. The service agreement between the plan and the plan administrator in this case specified that compensation would cover his services and related bundled fiduciary, trust office, administrative, legal, and actuarial services. However, the documentation provided by the plan administrator to PBGC in support of the plan's financial assistance request only supported the plan administrator's flat fee, $29,000 or $22,000 – that is, there was no documentation of the expenses included within the flat fee. As recently as 2014, MEPD requested details for the bundled fee. In response, the plan administrator provided only an itemized list of services without listing the associated costs and MEPD did not request additional information.

The MEPD Program Manager advised the OIG that MEPD did not dispute the bundled administrative expenses, and that, generally, he would question only "high cost" plans. In terms of "high cost" plans, the Program Manager was referring to a comparison of this plan versus the average administrative expenses of the roughly 1,400 ME plans, whether insolvent or solvent. MEPD policy requires auditors to perform analytical reviews to identify possible misstatements and unreasonable, unnecessary and unsupported expenses incurred by the plan; it does not waive this requirement in the event the administrative expenses compare favorably to national averages.

According to information provided by the plan administrator and OIG analysis, the total administrative expenses received in 2015 ($264,000) can be divided into two categories: (1) payments to outside service providers and (2) payments to the plan administrator. Figure 1 below shows payments to outside service providers accounted for $120,100 (45 percent) of the administrative expenses, and payments to the plan administrator accounted for $143,900 (55 percent) of the administrative expenses.

Figure 1: Total Administrative Expenses Paid for Outside Service Providers Versus Plan Administrator, as of December 31, 2015.



The plan administrator provided service agreements for each professional services providers, and we conclude the payments to these providers were reasonable based on the terms of their agreements. In addition, the services provided (such as plan actuary service, benefits processing services and banking services) were necessary to the plan and adequately supported. For example, the plan administrator separately contracts with an individual to perform the duties of the benefits administrator. This benefits administrator averaged 30 hours per week, worked from their home, and received $54,000 a year. The benefits administrator's duties consisted of the day-to-day administration of the plan and managing a dedicated phone line for a 2,500-participant plan.

Regarding the payments to the plan administrator, we found that these payments were not reasonable or adequately supported. We discussed the invoices and payments with the plan administrator and he provided explanation and documentation. For 2015, the plan administrator did not provide a detailed allocation of expenses. For 2016, he projected $235,310 in plan expenses, of which $128,660 were payments to the plan administrator, estimated as follows:

- 15 average hours per month for the plan administrator for an annual payment of $89,460;
- 12 average hours per month for support staff within the plan administrator's office for an annual payment of $27,200; and
- $12,000 estimated annual allocable share of office rent, including share of common space.

The plan administrator estimated he averaged 15 hours per month and yet received a significantly higher salary than the benefits administrator, who is doing the substantive work from her home. In addition, while the benefits administrator explained her time billed to the plan, the plan administrator could only provide a rough estimate. Based on this misalignment of duties, we found the salaries of the plan administrator and support staff to be unreasonable and unnecessary in comparison to the salary and duties of the benefits administrator. We also note that salary amounts were unsupported estimates because no one in the plan administrator's office recorded hours worked in relation to the plan. Likewise, the plan administrator did not have an allocation method for determining overhead expenses such as rent and utility expenses.

We believe PBGC has paid administrative expenses that were not reasonable or adequately supported because their analytical reviews focused solely on the bundled amount, not the individual actual costs incurred by the plan. Moreover, in determining reasonableness of administrative expenses, the MEPD Program Manager relied upon a comparison of total administrative expenses with national averages, although there is no policy permitting this. The plan administrator was able to operate with little scrutiny by PBGC due to a bundled arrangement; thus, increasing the risk of improper payment of administrative expenses.

Suggestion

To reduce the risk of waste, fraud, and abuse, and to enhance program performance, we offer the following suggestion:

> The Chief of Negotiations and Restructuring should review this agreement and any similar agreements with third-party administrators who request financial assistance with bundled administrative expenses to ensure that PBGC pays only those administrative fees that are "reasonable, necessary and adequately supported."