August 2014

PENSION ANALYST

Important information—Legislation

Prudential
Bring Your Challenges

Highway and Transportation Funding Act of 2014 extends MAP-21 interest rates

Who's affected

These developments affect sponsors of most qualified single-employer and multiple employer defined benefit plans. They do not affect multiemployer plans, governmental plans or church plans that do not elect to be covered by ERISA ("non-electing church plans").

Background and summary

On August 8, 2014, President Obama signed into law the "Highway and Transportation Funding Act of 2014 (HTFA)." Although the new law primarily provides funding for highway and transportation expenditures through May 2015, it also includes a provision for pension funding relief.

On July 6, 2012, President Obama signed into law "The Moving Ahead for Progress in the 21st Century Act (MAP-21)", which provided welcome funding relief for plan sponsors to use higher rates when calculating plan liabilities. The use of higher interest rates allows plan sponsors to contribute less money to the plan to satisfy funding obligations.

HTFA extends the pension funding relief provided by MAP-21 through 2017. This is good news for plan sponsors since the continued use of higher interest rates will decrease funding liabilities and reduce required minimum contributions.

In addition, HTFA:

- Requires additional information in the annual funding notice; and
- Includes a provision regarding prohibited payments during a period in which a plan sponsor is in bankruptcy.

However, HTFA does not affect the Pension Benefit Guaranty Corporation (PBGC) flat rate premium or the variable rate premium percentage. It also does not affect the interest rate used to determine the liability for the variable rate premium.

Action and next steps

The provisions of this new law impact plan funding and administration. Plan sponsors should carefully read the information contained in this *Pension Analyst* and should discuss the law's impact on their plans with their enrolled actuary.

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RSMH080

Pension funding provisions

Defined benefit pension plans are subject to minimum funding rules that require plan sponsors to make annual contributions to fund plan benefits. The Pension Protection Act of 2006 (PPA) made extensive changes to the minimum funding requirements for both single-employer and multiple employer defined benefit plans. PPA specifies the interest rates used in determining the present value of a plan's normal cost and funding target. Present value is determined using three interest rates (segment rates), each of which applies to benefit payments expected to be paid during a certain period.

MAP-21 revised the rules for determining segment rates by adjusting a segment rate if it is outside a specified range of the average of the segment rates for the preceding 25-year period. If a segment rate for the applicable month is less than the applicable percentage, the segment rate is adjusted upward to match that percentage. If a segment rate is more than the maximum percentage, the segment rate is adjusted downward. MAP-21 defined the average segment rate as the average of the segment rates determined under the PPA rules for the 25-year period ending September 30 of the calendar year preceding the calendar year in which the plan year begins.

HTFA revises the MAP-21 applicable minimum and maximum percentages for the 2013-2017 plan years for determining when a segment rate is adjusted upward or downward. Because of the narrow corridors between the minimum and maximum percentages, plan sponsors can continue to reduce their minimum required contributions for these plan years.

Beginning with the 2018 plan year, the corridors between the minimum and maximum percentages begin to widen. The specified percentage depends on the calendar year in which the plan year begins as indicated below:

Calendar year	Applicable minimum percentage	Applicable maximum percentage
2012-2017	90	110
2018	85	115
2019	80	120
2020	75	125
After 2020	70	130

This provision is generally effective retroactively for plan years beginning after December 31, 2012. However, for the 2013 plan year only, plan sponsors can elect to apply these changes for all purposes or apply them for benefit restriction purposes only. This election will not violate the anti-cutback rules.

However, the revised interest rates do not apply for purposes of:

- Lump sum payments;
- Limits on deductible contributions;
- PBGC variable rate premiums; and
- The funding target attainment percentage for financial reporting to the PBGC for certain underfunded plans (ERISA Section 4010 reporting).

Prohibited payments in bankruptcy

Under PPA, a plan cannot make a prohibited payment for participants with annuity starting dates occurring when the:

- Plan has an adjusted funding target attainment percentage (AFTAP) of less than 60%; or
- Employer is in bankruptcy and the plan's AFTAP is less than 100%.

A "prohibited payment" is any:

- Payment exceeding the monthly amount payable under a single life annuity (plus any social security supplements) to a participant or beneficiary whose annuity starting date occurs during a period when the benefit restriction is in effect;

- Payment for the purchase of deferred annuities from an insurer to pay benefits; and
- Other payment specified by the IRS.

The most common prohibited payment is a lump sum payment.

HTFA requires that for determining whether plans can issue prohibited payments if the employer is in bankruptcy, the revised segment rates cannot be used in calculating whether the AFTAP is less than 100%. This provision applies to plan years beginning after December 31, 2014. In the case of a plan maintained pursuant to one or more collective bargaining agreements, the provision applies to plan years beginning after December 31, 2015.

Plan sponsors must amend their plans as of the last day of the first plan year beginning on or after January 1, 2016, but must operationally comply with this requirement as of the effective date.

Annual funding notices

Effective for plan years beginning on or after January 1, 2008, PPA requires plan administrators to provide an annual funding notice, disclosing the plan's funding target liability and the value of plan assets. Plan administrators must provide the annual funding notice to:

- Plan participants;
- Plan beneficiaries;
- Alternate payees under Qualified Domestic Relations Orders (QDROs);
- Labor organizations representing participants and beneficiaries (e.g., unions); and
- The Pension Benefit Guaranty Corporation (PBGC).

In 2009, the Department of Labor (DOL) published Field Assistance Bulletin 2009-01, which provided guidance regarding the new annual funding notice requirements, including a model notice.

MAP-21 required plan administrators to disclose additional information on the annual funding notice regarding the MAP-21 segment rates and the effect of these rates on the plan's funding. The DOL issued Field Assistance Bulletin 2013-01, which addressed the disclosure requirements mandated by MAP-21.

HTFA amends the annual funding notice requirements by:

- Requiring that the annual funding notice include references to HTFA interest rates, in addition to MAP-21 rates; and
- Revising the period that plan administrators must disclose this additional information on the annual funding notices beginning after December 31, 2011 and before January 1, 2020 (extended from January 1, 2015).

Next steps

Plan sponsors should read the guidance discussed in this newsletter. They will need to decide whether to apply HTFA interest rates retroactively for the 2013 plan year and consider the impact of HTFA on their plan's funding policy.

If you have questions about the new funding provisions, you should contact your plan's enrolled actuary. Prudential Retirement's enrolled actuaries are well prepared to respond to your questions regarding the effect of the new law on your plan and develop solutions to comply with the new law's requirements.

Prudential Retirement will continue to monitor and keep you informed as additional guidance is published that clarifies the provisions of HTFA.

Pension Analyst by Prudential Retirement
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