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PENSION ANALYST

Important information—Legislation

New law impacts single-employer defined benefit plans

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"). A separate publication discusses the changes affecting multiemployer defined benefit plans.

Background and summary

On July 6, 2012, President Obama signed into law the "Moving Ahead for Progress in the 21st Century Act (MAP-21)." Although the new law primarily provides highway funding and student loan relief, it also contains several provisions that impact defined benefit plans.

The new law provides welcome funding relief for plan sponsors whose plan assets have declined due to the downturn in the economy and low interest rates that have increased plan funding obligations. For example, it provides pension interest rate stabilization, which allows plan sponsors to use higher interest rates when calculating plan liabilities. The use of higher interest rates allows plan sponsors to contribute less money to the plan to satisfy their plan funding obligations.

In addition, MAP-21:

- Increases flat-rate premiums paid to the Pension Benefit Guaranty Corporation (PBGC);
- Increases the PBGC variable rate premium;
- Makes several changes to PBGC governance; and
- Extends the provision allowing transfers of excess assets to retiree health accounts through December 31, 2021.

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 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 to be used in determining the present value of a plan's normal cost and funding target. Present value is now determined using three interest rates (segment rates), each of which applies to benefit payments expected to be paid during a certain period.

New interest rates

MAP-21 revises the rules for determining the 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 minimum 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. This provision will improve a plan's funded status and reduce minimum required contributions for the next few years.

The new law defines the average segment rate as the average of the segment rates determined under the current law for the 25-year period ending September 30 of the calendar year preceding the calendar year in which the plan year begins.

The applicable minimum and maximum percentages depend on the calendar year in which the plan year begins as indicated below:

Calendar year	Applicable minimum percentage	Applicable maximum percentage
2012	90	110
2013	85	115
2014	80	120
2015	75	125
2016 or later	70	130

This provision is generally effective for plan years beginning after December 31, 2011. However, for the 2012 plan year only, plan sponsors can elect to not apply the changes for all purposes or to not apply them for benefit restriction purposes only.

If an employer has elected, as of July 6, 2012, to elect to use a monthly yield curve in determining contributions, rather than segment rates, the employer may revoke the election (and use segment rates) without IRS approval. The revocation:

- Must be made at any time before July 6, 2013; and
- Will be effective for the first plan year to which the amendments made by the provision apply and all later years.

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

- Lump sum payments;
- Limits on deductible contributions;
- PBGC variable rate premiums; and
- Financial reporting to the PBGC for certain underfunded plans (ERISA Section 4010 reporting).

Impact on annual funding notice

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 funded current liability and the value of plan assets. 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. 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).

MAP-21 requires plan administrators to disclose additional information on the annual funding notice for plan years beginning after December 31, 2011, and before January 1, 2015, if the plan:

- Had 50 or more participants on any day during the preceding plan year;
- Has a funding target that is less than 95% of the funding target determined using rates prior to MAP-21; and
- Has a funding shortfall greater than $500,000, determined using the rates prior to MAP-21.

In this situation, the following additional information must be provided on the annual funding notice:

- A statement that MAP-21 modified the method for determining the interest rates used to determine the actuarial value of benefits earned under the plan, providing for a 25-year average of interest rates to be taken into account in addition to a 2-year average;
- A statement that, as a result of MAP-21, the plan sponsor may contribute less money to the plan when interest rates are at historical lows; and
- A table showing, for the applicable plan year and each of the preceding two plan years, the plan's funding target attainment percentage, funding shortfall and the employer's minimum required contribution, each determined both using rates under MAP-21 and rates prior to MAP-21.

For plan years beginning before January 1, 2012, the plan's funding target attainment percentage, funding shortfall, and the employer's minimum required contribution are determined using rates before the new law.

MAP also requires the DOL to update the model funding notice to include the additional information required by the new law. The model notice must include the additional information in a prominent manner, for example, on a separate first page, before the remainder of the notice.

PBGC provisions

Flat-rate premium increases

Sponsors of qualified defined benefit plans that are subject to the ERISA plan termination insurance rules must file and pay annual plan termination insurance premiums to the PBGC.

For single-employer and multiple employer plans, a flat-rate premium is due for each individual who is a participant in the plan during the applicable plan year. The participant count must be taken as of the "premium snapshot date," which is generally the last day of the plan year preceding the premium payment year. Currently, the PBGC flat-rate premium for each individual is $35 per participant.

MAP-21 provides for the following flat-rate premium increases:

- $42 for plan years beginning in 2013; and
- $49 for plan years beginning in 2014.

Adjustments for inflation will be made in future years.

Variable rate premium increases

Single-employer and multiple employer plans must also pay a PBGC variable rate premium (VRP) if they are underfunded. Under PPA, the variable rate premium limit for employers with plans that cover fewer than 25 lives is no more than $5. MAP-21 did not revise this provision. For all other plans, the VRP is $9 for each $1,000 of unfunded vested benefits.

MAP-21 increases the current $9 variable rate premium as follows:

- $13 per $1,000 of unfunded liability in 2014; and
- $18 per $1,000 in 2015.

In future years, the amount will be adjusted for inflation. However, the amount of variable rate premium is capped at $400 per participant starting in 2013. This figure will also be adjusted for inflation after 2013.

The new law also requires the PBGC to establish a new Participant and Plan Sponsor Advocate position. This individual will act as a liaison between the PBGC and participants in terminated pension plans and will assist plan sponsors in resolving disputes.

Transfer of excess assets

Current law permits a plan with assets exceeding 125% of the plan's current liability (or funding target) to transfer retiree medical costs to a health account under the plan. This provision was scheduled to expire after December 31, 2013. However, MAP-21 extends through December 31, 2021, the ability of plan sponsors to transfer excess assets to a retiree health account.

In addition, the new law extends through December 31, 2021, the ability to transfer assets to fund the purchase of retiree group-term life insurance in accordance with the following rules:

- The assets transferred for the purchase of group-term life insurance must be held in a separate account within the plan, which is separate from both retiree medical account assets and basic defined benefit plan assets; and
- The group-term life insurance purchased with transferred assets cannot exceed $50,000; and
- The accounts must comply with various limits on frequency of transfers. These limits are applied separately to the retiree medical account and the retiree group-term life account.

Next steps

Plans sponsors should read the guidance discussed in this newsletter. If you have questions about the new provisions regarding funding requirements or PBGC premiums, you should contact your plan's enrolled actuary. Prudential Retirement's enrolled actuaries are well prepared to respond to your inquiries 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 made available that clarifies the provisions of MAP-21.

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Editor: Mitzi Romano (860) 534-2768