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Pension Funding Relief and PBGC Premium Increases Signed into Law

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The Moving Ahead for Progress in the 21st Century (MAP-21) Act was signed into law on Friday, July 06, 2012. This Act affects the interest rates used to calculate the Funding Target (Liability) for single-employer defined benefit (DB) plans subject to ERISA, and also raises Pension Benefit Guarantee Corporation (PBGC) premiums. In addition, MAP-21 requires additional disclosures for the annual funding notice and allows the transfer of assets from overfunded DB plans to fund group-term life insurance for retirees.

Funding Relief

The Pension Protection Act of 2006 (PPA) defines that ERISA funding liabilities are generally valued using three segment rates (plan sponsors may also use the "full-yield curve" option, more on that later). The three segment rates are based on a 24 month average of current market spot rates derived from a corporate bond yield curve. Over the past few years, as interest rates have declined, the segment rates have continued to decline as well. DB plan liabilities and interest rates have an inverse relationship, thus lower interest rates mean higher liabilities and ultimately higher pension contribution requirements for plan sponsors. MAP-21 provides funding relief by allowing higher interest rates to be used to value funding liabilities.

The MAP-21 Act is effective for plan years beginning in 2012, although plan sponsors can elect to not use the funding relief for 2012. The Act reduces the impact of short term changes to interest rates, by comparing the segment rates to a 25-year average of spot rates, and then applying a minimum/ maximum (shown below) to the 25-year average.

Year	Minimum/Maximum
2012	90%/110%
2013	85%/115%
2014	80%/120%
2015	75%/125%
After 2015	70%/130%

For example, suppose the first segment rate (used to value benefits payable in the first 5 years) is currently 2.0%. If the 25-year spot rate average in 2012 is 7.0%, the 2.0% would be compared to a floor of 6.3% (7.0% x 90%), and 6.3% would be used for the first segment rate. Alternatively, assuming the same example for 2016, the 2.0% would be compared to a minimum interest rate of 4.9% (7.0% x 70%), and 4.9% would be used for the first segment rate.

As a result, we estimate that funding liabilities for many DB plans will decrease by 10% - 20% for 2012 and future decreases will be phased out until 2015 and beyond.

For plan sponsors that have elected the full yield curve option under PPA to value pension liabilities, that election cannot be changed (prior to funding relief) without consent from the Secretary of the Treasury. MAP-21, however, allows plan sponsors a one-year window after the date of enactment to change to the segment rates (and apply funding relief) without consent.

Where Relief Does Not Apply

While the pension liability for ERISA funding purposes will decrease with the funding relief, the relief does not apply to all sections of the Internal Revenue Code (IRC). The following items below highlight areas where MAP-21 does not apply:

- Maximum deductible contributions under IRC Section 404
- Minimum lump sums under IRC section 417
- Excess assets under IRC section 420
- PBGC variable-rate premium liability calculations
- PBGC reportable events under ERISA 4010

PBGC Premium Increases

Currently, the PBGC flat-rate premium is $35 per participant (indexed for inflation). The PBGC variable rate premium is calculated as 0.9% of the unfunded vested benefits in a pension plan (not indexed for inflation). In 2012 for example, if the plan's assets are $50,000,000 and the vested liabilities are $56,000,000, the plan has $6,000,000 of unfunded vested benefits, and the variable rate premium for 2012 is $54,000, or 0.9% x $6,000,000.

MAP-21 increases the flat-rate premium per participant to $42 in 2013 and $49 in 2014 and beyond, with inflation indexing after 2014.

The variable rate premium percentage of unfunded benefits increases from 0.9% to 1.3% in 2014 and to 1.8% in 2015 and beyond, including inflation indexing after 2015. MAP-21 does limit the amount of the variable rate premium to $400 per participant (in the example above, if the plan has 100 participants, the $54,000 variable rate premium would be limited to $40,000, or 100 x $400).

Overall, most pension plans will see large increases to PBGC premiums after 2012, and underfunded pension plans will see much larger increases due to the changes to the variable rate premium laws.

Annual Funding Notice Disclosures

Generally, MAP-21 adds additional disclosures to the annual funding notice required of pension plans. The disclosures include statements describing that MAP-21 has modified interest rate methods used to value pension liabilities, and as a result that plan sponsors may contribute less to the pension plan. The Act also describes that the notice should include a table showing the pension liabilities and contribution requirements before and after the use of funding relief.

MAP-21 includes a statement that the Department of Labor will publish a revised model notice that includes the requirements of the new law.

Additional Information

We expect additional information to be released with further guidance on MAP-21. The actuaries at Atéssa Benefits, Inc. can help you determine how the new laws will affect your pension plan in the future. Please contact us at (858) 673-3690 for additional information.
