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MAP-21 Brings Pension Funding Stabilization and Increased PBGC Premium Rates

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Authors: John D. Martini, Allison Warden Sizemore, Dennis R. Bonessa, Dodi Walker Gross, Russell J. Boehner

Legislation known as Moving Ahead for Progress in the 21st Century Act ("MAP-21") recently became law. This law contains long-awaited provisions that permit sponsors of single-employer defined benefit plans to use stabilized interest rate assumptions for certain funding calculations, thus decreasing required employer contributions and improving plan-funding attainment percentages for many plans over the next few years. MAP-21 also increases PBGC premiums effective in 2013, and expands availability of excess asset transfers.

Interest Rate Stabilization.

Because using a lower interest rate results in larger projected future plan liabilities, the recent historically low interest rates have led to increased minimum contributions and lower funding attainment percentages for most sponsors of defined benefit plans. MAP-21 changes certain interest rate assumptions by taking into account average interest rates over the most recent 25 years (a higher rate, on average), rather than rates drawn entirely from the currently lower short-term rates.

Previously, a plan sponsor could elect to calculate future pension obligations based on either the "yield curve" of corporate investment-grade bonds for the preceding month, or three "segment rates" that are drawn from the average yield curves over the most recent 24-month period. MAP-21 affects only the segment rate calculations. It has no effect on sponsors using the yield curve calculation, although such employers are permitted to switch to the segment rate.

After MAP-21, the segment rate must be within a specified range of the 25-year average segment rates. For plan years beginning in 2012, the floor is 90 percent and the cap is 110 percent. The floor is lowered and the cap is increased by 5 percent each plan year thereafter through 2016, such that by the 2016 plan year, the range is between 70 percent and 130 percent of the 25-year average rate. Applying the new segment rates will lessen required minimum contributions and increase funding level attainment percentages for many plan sponsors.

The revised segment rates will affect minimum required contributions and calculations for purposes of section 436 (funding level) benefit restrictions. They will not, however, change other plan calculations such as lump-sum cashouts, section 415 limits, deductible contribution limits, variable rate premiums, or PBGC reporting pursuant to section 4010 of ERISA. Plan sponsors may choose to use the stabilized rates beginning with plan years starting on or after January 1, 2012 or January 1, 2013, with some transition rules applying for 2012 adopters. Some sponsors that use the stabilized rates must provide an explanation of the change to participants in their Annual Funding Notice.

PBGC Premiums.

MAP-21 increased PBGC flat-rate premiums for single-employer plans from $35 per participant to $42 in 2013, and $49 in 2014, with inflationary adjustments thereafter. The flat rate premium for multiemployer plans increased from $9 per participant to $12 in 2013, with inflationary adjustments thereafter. The variable-rate premium for underfunded plans also increased from $9 per $1,000 of underfunding to at least $13 per $1,000 in 2014, and $18 per $1,000 in 2015. MAP-21 also established a cap on the variable rate premium of $400 per participant in 2013, adjusted for inflation thereafter.

Excess Asset Transfers.

Section 420 of the Code permits certain overfunded plans to use excess assets to fund retiree medical obligations. However, those provisions were set to expire in 2013. MAP-21 extends the availability of section 420 transfers through 2021, and adds the option of using excess assets to fund retiree group-term life insurance coverage.

Conclusion.

Pension funding stabilization is welcome news to most plan sponsors, but the increase in PBGC premiums is not. Although rate stabilization is positive for most, sponsors should carefully consider whether and when to implement the new rates. Please contact any of the authors listed if you have questions or would like further clarification on this topic.