Katten
Katten Muchin Rosenman LLP
CORPORATE & FINANCIAL
WEEKLY DIGEST

Corporate & Financial Weekly Digest

Posted at 12:32 PM on July 23, 2010 by [Daniel B. Lange]

Congress Provides Pension Funding Relief

Co-authored by [Michael Durnwald]

On June 25, President Obama signed legislation that provides short-term funding relief to sponsors of underfunded defined benefit pension plans. The new law, known as the Preservations of Access to Care for Medicare Beneficiaries and Pension Relief Act of 2010 (the Relief Act), permits temporary modification of existing pension funding rules by allowing plan sponsors of single-employer plans to elect one of two methods for delaying payments to pension plans. By delaying those payments, sponsors should have more cash available in the short term to help fund ongoing operations—a result which is likely to be seen as a benefit to many plan sponsors given recent economic turmoil. However, because the delay methods do not decrease the net amount that must eventually be contributed to a pension plan, use of the Relief Act provisions will likely result in contributions for later years being larger than they otherwise would have been. Sponsors should keep in mind the probable effect of increased contributions in later years when deciding how to satisfy their plan funding obligations.

Under current pension funding rules, which were enacted in 2006 and apply to most single-employer plans, a pension plan's funding shortfall for any year is required to be amortized and paid into the plan over a seven year period. The Relief Act's methods for delaying payments allow a plan sponsor to choose either to (a) make "interest only" payments (using the plan's effective interest rate) for two years, and then amortize the shortfall for the following seven years, or (b) amortize the shortfall over 15 years. Plan sponsors are also free to use existing funding rules and not take advantage of the assistance provided under the Relief Act. To chose one of the methods under the Relief Act, sponsors must follow rules which are expected to be released by the IRS, and must also notify the Pension Benefit Guaranty Corporation (PBGC) and plan participants pursuant to rules to be released by the PBGC. If either of the Relief Act's methods is selected, in order to help ensure that sponsors do not misuse the increased short-term cash flow created by a reduction in the current pension funding obligation, certain make-up contributions may be required if a sponsor pays annual compensation to any employee in excess of $1 million (including by way of contributing assets to a rabbi trust), or pays an extraordinary dividend.

For more information, the Relief Act can be found [here].

Katten Muchin Rosenman LLP
Charlotte Chicago Irving London Los Angeles New York Washington, DC