



Funding Relief for Single-Employer Defined Benefit Plans

This update will discuss the key components in a long-awaited pension relief/technical corrections bill, which President Bush is expected to sign within the next several days. Outlined below are only those provisions of the bill that will provide relief to Defined Benefit (“DB”) plans.

Background

The ongoing economic crisis has raised the specter of a number of DB plan sponsors facing the daunting choice of failing to meet funding obligations under the Pension Protection Act of 2006 (“PPA”), or ceasing future benefit accrual, or terminating the plan if possible. In some extreme cases, the plan sponsor can meet funding requirements only at the risk to the company’s financial survival or to jobs of some of its employees. This goes directly against the intent of PPA, which has the purpose of strengthening the funding of these plans and protecting the benefit security of plan participants.

Some Relief

On December 11, 2008, Congress passed the Worker, Retiree, and Employer Recovery Act (“WRER”) which helps alleviate the problem and also gives guidance in the form of technical corrections to PPA. Although many of the recommendations made by the American Benefits Council and other pension practitioners are not included in this bill, it certainly is helpful and a much needed step in the right direction. We are hopeful that further relief will be provided in legislation passed during 2009.

Key Provisions of WRER Affecting Single-Employer DB Plans

Relief under WRER comes in several forms: eased funding requirements, less stringent benefit accrual restrictions and removal of the prohibition from paying certain lump sums.

Eased Funding Requirements

- Under PPA, a shortfall base must be established and amortized over seven years if assets are less than a transition percentage multiplied by a funding target liability. For eligible plans (those with no deficit reduction contribution requirement in 2007), the transition percentage is 92% in 2008, 94% in 2009 and 96% in 2010. If assets fall short of target, the shortfall base would be set up for the full difference to 100% of the liability. Under WRER, the shortfall base must close the gap only to the transition percentage times the liability. This can reduce the required contribution significantly for many plans.
- Under PPA, if a shortfall base is established in any year, future transition percentages are 100%. WRER removes this requirement for eligible plans, allowing the transition percentages to remain as they are, regardless of whether a previous shortfall base had been established.
- PPA allows “averaging” of adjusted market values of assets, based on a period of up to 24 months preceding the first day of the plan year. Past market values in the averaging period are adjusted upward for subsequent contributions and downward for subsequent disbursements. WRER allows past market values in the averaging period to also be adjusted upward by expected investment return with a maximum on the assumed rate, resulting in a larger asset value. However, because the averaged asset value is limited under PPA to 110% of the current market value, this liberalization will have no immediate effect for many plans. The pre-WRER averaged asset value is often already in excess of 110%. Hopefully, 2009 legislation will remove the 110% ceiling or increase it to the pre-PPA limit of 120%.

Benefit Accrual Restrictions and Prohibition from Paying Small Lump Sums

- Under PPA, benefit accruals must cease if the ratio of plan assets (with adjustments) to funding target liability falls below 60%. This ratio is called the Adjusted Funding Target Attainment Percentage (“AFTAP”). For plan years beginning on any date between October 1, 2008 and September 30, 2009, WRER allows the AFTAP for benefit accrual restriction determination to be the higher of this year’s or last year’s ratio. For example, suppose for a calendar plan year the January 1, 2009 AFTAP is 58% and on January 1, 2008 it was 61%. Under PPA, benefit accrual would have to immediately cease. Under WRER, benefit accrual would continue, since the larger of the two ratios does not fall below 60%.
- PPA restricts lump sum payments to essentially 50% if the AFTAP falls below 80%, and prohibits lump sum payments if the AFTAP falls below 60%. WRER lifts the lump sum prohibition for distributions of \$5,000 or under, regardless of the magnitude of the AFTAP.

[Summary](#)

There are still many questions that need to be resolved and additional opportunities for pension legislative relief. Most of these changes are effective retrospectively to the plan year commencing during 2008. As we learn more, we will pass the information on to you in future client updates.