

August 2012

New Law: Good News for Cash Balance and Defined Benefit Plans Accompanies Increases in PBGC Premiums

Legislation known as the 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 Cash Balance and defined benefit plans to use higher interest rate assumptions for certain funding calculations. This will decrease minimum required employer contributions and make it easier to meet funding requirements. MAP-21 also increases premiums for plans covered by the Pension Benefit Guaranty Corporation (PBGC).

Impact of Higher Interest Rates: Reduced Liabilities, Increased Funding Percentages

The use of these higher interest rates will reduce the measure of a plan's liabilities for some, but not all, calculations. It will **not affect the amount of benefits payable to any participant**, but it will reduce the liability amounts used to determine a plan's minimum required contribution and to determine whether or not certain benefit payment restrictions will apply. For example, if a plan's funding percentage is below 80%, it is generally not permitted to pay benefits in the form of a full (100%) lump sum, and all participants must be notified of the restriction. The higher interest rates allowed under MAP-21 will reduce plan liabilities and increase funding percentages, making benefit restrictions less likely.

Options for Plan Sponsors to Consider: New Rates May Offer an Advantage

The IRS released the new, MAP-21 interest rates on August 16, 2012. Since the new rates are effective as early as January 1, 2012 and we are well into the second half of the year, this raises some issues. Kravitz has already completed many actuarial valuations for 2012 using the old rates, and we have sent plan sponsors the signed actuarial certifications. We have also prepared benefit restriction notices based on liabilities determined using the old rates.

MAP-21 allows use of the old rates for 2012 provided the plan sponsor makes a written election to do so. For this reason, it may not be necessary to redo 2012 actuarial reports that have already been issued.

As long as there are no negative effects caused by the lower interest rates, there is likely no need to reissue these reports with revised certifications.

However, if the new, higher rates provide an advantage, it may be wise to revise the actuarial report. If the funding percentage is under 80% using the old rates, but over 80% using the new rates, a plan sponsor might want a revised actuarial report incorporating the new rates and thereby removing benefit restrictions.

Increased PBGC Premiums Beginning in 2013

PBGC premiums consist of two parts: a fixed premium and a variable premium. Both of these are increased under the new law, MAP-21.

The **fixed premium** prior to the new law was \$35 per participant. This will increase to \$42 in 2013 and to \$49 in 2014, with inflationary increases after 2014.

The **variable premium** is payable by plans with unfunded vested benefits. Prior to MAP-21, it was equal to 0.9% of a plan's unfunded vested liability. Beginning in 2014, this premium will increase to 1.3% and in 2015 to 1.8% of a plan's unfunded vested liability.

What Should Plan Sponsors Do Now?

Many Cash Balance and defined benefit plan sponsors will need to decide whether or not to use the higher interest rates for 2012, or to sign an election allowing the use of the old, lower interest rates. Kravitz will be contacting all affected plan sponsors to advise them of the pros and cons of this decision. Beginning in 2013, all Cash Balance and defined benefit plans will use the new, more favorable rates.

Please contact your Kravitz consultant if you have any questions in the meantime.

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