

109th Congress: 2005-2006

Pension Plan Funding and PBGC Solvency Problems

July 2005

Bush Administration Plan

Strengthening Funding for Single Employer Pension Plans

Feb 2005

To protect workers and retirees receiving PBGC guaranteed benefits, to improve the financial status of the PBGC and to encourage the continued participation in the nation's voluntary private pension system by healthy plans, the Administration recommends:

- reforming the funding rules for private defined benefit plans to ensure that employers fully fund their retirement promises,
- adjusting the premiums that plan sponsors pay to the Pension benefit Guaranty Corporation (PBGC) to better reflect plan risk; and
- improving the disclosure of information about defined benefit pension plans to workers, investors and regulators to ensure greater transparency and accountability.

Strengthen Minimum Funding Rules – Base funding rules on meaningful and accurate asset and liability measures. Require plans to make-up funding short-falls in a reasonable period of time. Allow employers to make additional tax-deductible contributions when their plans are fully funded. Restrict the ability of financially strapped companies to promise more new benefits than they can afford to deliver.

Reform the Pension Insurance Premium Structure – Increase the current per participant flat rate premium (FRP) paid by all plans from \$19 to \$30. Impose risk-based premiums on under-funded plans pegged to the gap between each plan's funded status and its obligations under the Administration's *interest rate reform proposal*. Allow the PBGC to periodically adjust the risk-based premium so that premium revenue will cover expected losses and improve the agency's financial condition.

Improve Information Disclosure Requirements – Provide more accurate and timely information about plan solvency and funding trends. Publicize currently confidential information about under-funded plans.

Note - Until recently, defined benefit plan funding requirements have been determined using an interest rate based on the interest rate on 30Year Treasury securities. Beginning in 2008, the Administration has proposed that current liabilities be determined using a blended corporate bond rate - a series of rates drawn from a yield curve of high quality zero-coupon bonds of varying maturities selected to match the amounts and timing of payments that plans must make to settle their obligations to plan participants.

Representative John Boehner (R-OH-08)

The Pension Protection Act of 2005 (HR 2830)

June 2005

Purposes – To amend the Employee Retirement Income Security Act (ERISA) and the Internal Revenue Code (IRC) to strengthen funding standards for single-employer and multi-employer (collectively-bargained) defined benefit plans.

Plan Funding Requirements – Single employer plans will have to make sufficient contributions to meet a 100% full-funding standard, based on a modified yield curve interest rate and smoothing rules. Under-funded plans will have seven years to make up funding short-falls. Accelerated contributions will be required if a plan's funded status falls below 60%. The allowable tax-deductible contribution limit will be increased from 125% to 150% of current liabilities.

The bill also includes extensive multi-employer plan funding reforms.

PBGC Premiums - Flat rate premiums will be increased from \$19 to \$30 per participant and be phased in, beginning in 2008, on a schedule based on each plan's funded status.. Variable rate premiums (to be re-named "risk-based premiums) will also be increased by indexing them to the rate of growth of average wages. The new risk-based premium will be imposed on all under-funded plans, irrespective of their status in prior years.

Disclosure Requirements – The bill requires additional disclosures about each plan's funding status in annual reports to plan participants and beneficiaries, including notice of bankruptcy filings. Currently confidential information about plans that are under-funded by \$50 million or more will have to be released to participants as well as the PBGC.

Investment Advice – Allows plan sponsors and fiduciaries, other than fiduciary advisors, to provide investment advice to plan participants.

Cash Balance and Other Hybrid Plans – Provisions describing how cash balance and other hybrid plans that have characteristics of defined benefit and defined contribution plans should be tested to ensure that they are not age discriminatory are included in the Pension Preservation and Portability Act (HR 2831) and may be added to HR 2830 or to another pension reform proposal at a later date.

House Action

HR 2830 Introduced – June 9, 2005

Referred to the Education & Workforce and the Ways & Means Committees

Ordered reported by the Education & Workforce Committee – June 30 (27-0)

Senators Chuck Grassley (R-IA) and Max Baucus (D-MT)

National Employee Savings and Trust Equity Guarantee (NESTEG) Act (S 219)

January 2005

Purposes – To amend the Employee Retirement Income Security Act (ERISA) and the Internal Revenue Code (IRC) to protect the retirement security of American Workers by strengthening defined benefit plan funding rules; increasing PBGC premiums; ensuring that pension assets are appropriately diversified and by providing workers with access to more adequate information about their plans.

Plan Funding Rules – Single employer plans will have to make sufficient contributions to meet a 100% full-funding standard, based on an interest rate derived from a high quality corporate bond fund yield curve, and have 7 years to amortize minimum required funding contributions..

The deficit reduction contribution requirement currently imposed on under-funded plans will be eliminated. Single employer plans maintained by commercial airline companies will be allowed to amortize minimum required funding contributions over 14 years

PBGC Premium Rates – Increases flat rate premiums paid to PBGC from \$19 to \$30 per participant for all plans. The \$9 per \$1,000 of under-funding variable rate premium is not changed, but the under-funding amount calculation methodology is changed to comply with the new plan funding rules.

Establishes a new \$5 per participant flat-rate premium for new plans with 100 or fewer employees for the first five years of the new plans existence

Plan Information Disclosure and Benefit Statement Requirements – Expands disclosures about plan funding status that sponsors must include in actuarial reports to the PBGC and in summary annual reports to participants and beneficiaries.

Imposes new disclosures for *transaction suspension periods* when investment rights are suspended or reduced and a stipulation that plan managers will be held financially liable for losses incurred during black-out periods if they fail to make required disclosures.

Investment Advice and Education Provisions – Employers and plan fiduciaries will not be held liable under ERISA *fiduciary rules* with respect to investment advice offered by qualified investment advisors. [Does not provide relief from ERISA and IRC *prohibited transaction rules*]

Employers will also be permitted to offer employees a choice between cash compensation and “qualified retirement planning services” provided by “eligible investment advisors” on a pre-tax basis (capped at \$1,000 per participant per year)

Cash Balance and Other Hybrid Plans – Addresses issues relating to 1) the treatment of cash balance and other hybrid plans under age discrimination rules, 2) “whipsaw” problems and 3) requirements for cash balance plan conversions.

Defines (for the first time) a cash balance plan. Directs Treasury to define other hybrids.

Diversification Rules – Imposes new diversification requirements on defined contribution plans holding publicly traded employer securities. Employee elective deferrals can be diversified at any time. Employer non-elective contributions will be diversifiable after an employee completes 3 years of service.

Defined Contribution Plan Vesting and Portability Rules – All employer contributions (not just employer matching contributions) to all defined contribution plans must vest under either a three-year cliff or a six-year graded vesting schedule.

Permits distributions from qualified plans, tax-deferred annuities and governmental 457 plans to be transferred (rolled-over) directly into Roth IRAs, subject to current law Roth IRA conversion rules. Any pre-tax contributions will be immediately subject to tax.

Direct rollovers to and from Simple IRAs and other eligible plans (401(k), 403(b) and Section 457 plans) will also be permitted.

Spousal Protections – Adds a new “qualified optional survivor annuity” that will provide a more generous survivor annuity than the current joint and survivor option.

Senate Action

S 219 Introduced – Jan 31, 2005
Referred to the Senate Committee on Finance

Ordered reported – July 26, 2005

Q:cpc/2005legis/DBPlan.Proposals