MAP 21: President Obama Signs Transportation Bill with Pension Funding Provisions

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The House and Senate approved the conference report to the Surface Transportation Extension Bill of 2012 (H.R. 4348) (later renamed as the Moving Ahead for Progress in the 21st Century Act (MAP-21), P.L. 112-141), a highway reauthorization and student loan bill that contains provisions to stabilize pension interest rates and raise PBGC premiums. The bill would also extend the ability of employers to transfer excess pension assets to fund retiree health benefits and expand the provision to allow transfers for retiree life insurance. The President signed the legislation on July 6, 2012. Some of the provisions affecting pension plans are summarized below.

Interest Rate Stabilization

For pension funding purposes, plan liabilities are calculated by discounting projected future payments to a present value by using legally required interest rates based on corporate bonds. The interest rates and related liability have an inverse relationship, meaning, the lower the rate, the greater the liability. Under the bill, pension plan liabilities would continue to be determined based on corporate bond segment rates, which, in turn, are based on average interest rates over the preceding two years. However, beginning in 2012 for purposes of the minimum funding rules, any segment rate must be within ten percent (increasing to 30% in 2016 and thereafter) of the average of such segment rates for the 25-year period preceding the current year. This provision would stabilize the fluctuation of interest rates from year to year. Certain plans will need to disclose the effect of the stabilized interest rates to participants on their Annual Funding Notice. This applies to plans with 50 or more participants, a funding shortfall of $500,000 or more (based on rates without stabilization), and stabilized Funding Target less than 95% of the Funding Target without stabilization.

The impact of this law is just starting to show the effect on a company's pension plan funding requirements. For example, AK Steel Holding Corp. reduced its 2013 required pension contribution by $100 million by opting to use the higher interest rate and, as a result, announced it would reduce its expected $300 million pension plan contribution to $200 million.

PBGC Premium Increases

Currently, employers that sponsor defined benefit plans are required to pay a fixed-rate premium to the Pension Benefit Guaranty Corporation (PBGC) equal to $35 per participant per year (indexed for inflation) and a variable rate premium equal to $9 per $1,000 in underfunding (no maximum limit). Multiemployer plans must pay premiums equal to $9 per participant, indexed for inflation.

The bill would (1) adjust the variable premium for inflation beginning in 2013; (2) set a maximum variable premium of $400 beginning in 2013; (3) increase the variable premium by $4 in 2014 and by an additional $5 in 2015; (4) Increase the fixed rate premium by $6 in 2013 and by an additional $7 in 2014; and (5) increase multiemployer premiums by $2 beginning in 2013.

The legislation also includes a number of provisions designed to improve the governance of the PBGC.

Retiree Group Term Life Transfers

The new legislation also adds a provision allowing for the transfer (from overfunded DB plans) of assets to fund retiree group-term life insurance, on a basis similar to the current rules for transfers to fund retiree health benefits. Under current law, a transfer is permitted only if, after the transfer, the pension fund still has assets equal to more than 120% of the liabilities of the fund. The pension fund is protected by the funding level requirement (which also narrows the number of companies that can use the provision).