

AdvantEdge

A LEGISLATIVE & TECHNICAL UPDATE FOR OUR CLIENTS

President Bush Signs Worker, Retiree, and Employer Recovery Act of 2008

Provides Technical Corrections to Pension Protection Act; Funding Relief

On December 23, 2008, President Bush signed the Worker, Retiree, and Employer Recovery Act of 2008 (WRERA). WRERA provides funding relief for the defined benefit plans of many employers and protection against benefit restrictions. In addition, WRERA permits the waiver of the required minimum distributions for 2009 for defined contribution plans and IRAs. Finally, WRERA contains administrative corrections to the Pension Protection Act of 2006 (PPA).

This newsletter provides an overview of the main provisions of WRERA and their impact.

Benefit Accrual Restrictions

Under the PPA, if the ratio of the plan's assets to its liabilities falls below 60%, benefit accruals must become frozen. WRERA allows plans to substitute the prior year's funding ratio for the current year's ratio in determining whether the funding ratio is at least 60%. This means that a plan with a 2008 funding ratio of at least 60% will not face a mandatory accrual freeze in 2009, regardless of its 2009 funding ratio.

Restrictions Lifted on all Lump Sums Under \$5,000

Under PPA, plans with funding ratios below 60% may not pay plan benefits as a lump sum. Additionally, plans with funding ratios between 60% and 80% generally may pay only one-half of the benefit as a lump sum. WRERA excludes all lump sum payments under \$5,000 from the PPA restrictions.

Funding Requirements Reduced for Some Plans

In 2008, the PPA required plans with funding ratios under 92% to fund the entire shortfall amount (i.e., to 100%) over a 7-year period. For most defined benefit plans, WRERA reduces the shortfall amount that is required to be amortized over a 7-year period to the amount that is less than 92% (rather than 100%). For example, an eligible plan with a funding ratio of 90% in 2008 would have a shortfall charge based on a 7-year amortization of 2% (i.e., 92% - 90%) rather than the 10% (100% - 90%) required under the PPA. In 2009, "92%" becomes "94%", and in 2010 "96%". Plans considered eligible under this provision are those with less than 100 participants in 2007, and those plans with more than 100 participants in 2007 which did not have a deficit reduction contribution requirement in 2007.

Asset Smoothing

In determining the Actuarial Value of Assets, WRERA allows plans to use an asset smoothing method which is adjusted for expected earnings for the period. Previously, the PPA provided for an asset averaging method which did not include an earnings adjustment, which led to asset values which trailed market values, and resulted in the averaging method being widely ignored by plan sponsors.

Target Normal Cost

WRERA corrected a PPA oversight by requiring the Normal Cost of a plan to include expenses expected to be paid from plan assets for the plan year, and by excluding mandatory employee contributions for the plan year.

Minimum Required Distribution (for those over age 70 ½)

WRERA waives the required Minimum Required Distributions for 2009 from defined contribution plans and IRAs. Note that it does not impact Minimum Required Distributions from defined benefit plans.

Nonspouse Beneficiary Rollovers

WRERA clarifies that a plan is required to permit a nonspouse beneficiary of a deceased participant to roll over the death benefits.

Gap Period Income on Excess Deferrals

WRERA clarified that gap period income is not required on distributions of deferred amounts in excess of the Internal Revenue Code Section 402(g) limit.

WRERA Implications

With many plans expected to experience a decrease in their funding ratios from 2008 to 2009, the potential exists for sharply increased contribution levels and benefit restrictions for the 2009 plan year. WRERA softens the blow by (1) allowing plan sponsors to use the (higher) 2008 funding ratios for determining whether a benefit accrual freeze applies, and (2) by lowering the amortization contribution requirement for many plans. In addition, the use of asset smoothing techniques for single employer plans could result in lower 2009 contribution requirements than would be required in the absence of asset smoothing.

However, keep in mind that eventually your plan must “fund up”; whatever is not contributed near-term must be made up in contributions and/or investment return at a future date. While WRERA allows plan sponsors to fund at lower levels, plan sponsors should think carefully about their plan’s funding strategy, both short-term and long-term.

From a participant perspective, many retirees have lost a significant amount of their retirement assets in defined contribution and IRA plans. For various reasons many of these retirees may not want to withdraw money from these vehicles. WRERA recognizes this, and waives the mandatory distribution rules for 2009.

Pentegra’s Actuarial and Consulting groups will continue to keep you updated on the impact of this legislation on your plan. Feel free to contact Richard Rausser, Vice President, Consulting Services, at rrausser@pentegra.com, or call us at 800-872-3473.

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