PRS PENSION REVIEW SERVICES

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Funding Changes under the Pension Protection Act of 2006 and Final Regulations for Normal Retirement Age

Introduction

The 900 page plus Pension Protection Act of 2006 (PPA) made several changes to and in some parts completely revamped pension law. This report briefly summarizes some of the new funding requirements for defined benefit pension plans, and also discusses the recently released final regulations with respect to the definition of normal retirement age.

Defined Benefit Plan Funding Changes

Effective for plan years beginning on or after January 1, 2008, the minimum funding requirements for single-employer plans have been substantially revised. These changes modify the methods by which the calculations are made, including mandating the interest rates and mortality table assumptions that will have to be used. The interest rates will be based on the yield of corporate bonds over three different time periods (segment one is 5 years, segment two is 5 to 20 years and segment three is more than 20 years). The IRS has not yet issued the guidance needed with respect to determining the new minimum funding requirements.

For many defined benefit plans, the PPA also increased the maximum contribution that is tax deductible. Therefore, since contributions to the plan may be made in any amount between the minimum and the maximum, for many defined benefit pension plans, the plan sponsor will be comfortable with the new contribution range.

However, for other plan sponsors, the 2008 minimum required contribution may be higher than the 2007 minimum contribution was, and this contribution may exceed the amount that the Plan Sponsor would like to, or can afford to, pay. Because of the mandated actuarial assumptions, the actuary may no longer be able to vary each year’s contribution to meet the sponsors or accountant’s objectives for that year.

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Defined Benefit Plan Funding Changes continued

Therefore, we recommend that if you sponsor a defined benefit pension plan, in order to do proper financial planning for 2008, that you authorize PRS to project the 2008 contribution once the IRS issues the needed guidance. Determining a projected 2008 contribution in 2007 will provide the plan sponsor the opportunity to review the plan design and contribution range to see if these items continue to meet his or her objectives, and if needed, will provide the maximum flexibility to timely prepare participant notices and amend the Plan.

Final Regulations for Normal Retirement Age

Prior to the final regulations issued May 22, 2007, pension plans (both defined benefit and money purchase) generally could not pay benefits prior to a participant’s severance from employment. These new regulations provide that a pension plan is permitted to pay benefits upon an employee’s attainment of normal retirement age, even if the employee has continued employment.

In connection with permitting distributions to active participants after the attainment of normal retirement age, the regulations specify that the normal retirement age in the Plan cannot be earlier than age 62 (or the typical retirement age for the industry). If it is desired to have a normal retirement age less than 62, then there should be a good faith determination and justification of the typical retirement age for the industry, based on all relevant facts and circumstances.

What to do

For the reasons given in the funding changes section of the report, we recommend that if you sponsor a defined benefit pension plan, that you authorize PRS to prepare a projected 2008 contribution for the plan after the IRS issues the needed guidance. This is especially important if you may have trouble meeting what may be a higher minimum contribution requirement, or if your ability to make contributions varies from year to year.

For plans whose normal retirement age is less than age 62, unless a normal retirement age below age 62 can be justified, an amendment increasing the normal retirement age will need to be adopted by the due date of the Employer’s 2007 tax return (including extensions). PRS will prepare the needed amendment for those clients for whom we provide compliance services.

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