

**National Retiree Legislative Network**  
**Washington D.C. Fly – IN Legislative Agenda Priorities**  
**September 15–17, 2009**

**PENSION BENEFIT GUARANTEE CORPORATION (PBGC) RULES REFORM**

**Loss of Pension Benefits Caused by Inequitable PBGC Rules**

The PBGC currently treats changes in the annual earnings limits, mandated by Congress, as modifications to the pension plans themselves, and has applied the lowest annual earnings limit during the five-year look-back period when calculating retiree benefits. These changes result from applying IRS code changes under sections 401(a) and 415(b).

By subjecting earnings limits to the five-year look-back reductions, the PBGC treats these limits as if they were contractual changes, resulting in the failure to pay retirees a large portion of the contractual pension benefits earned over their careers.

Current PBGC rules permit the disqualification of certain retiree vested pension benefits if granted within a five-year window prior to a pension plan termination. The result has been loss of retiree vested benefits that should be protected by the ERISA.

- The NRLN proposes that the **PBGC shall use the Defined Benefit Plan income and pension benefit limitations defined in IRS codes 401(a) and 415(b) in effect on the date of the plan termination** when calculating the pension benefits payable under Priority Category Three (PC3). These changes shall be retroactive and apply to all defined benefit plans terminated after Sept 11, 2001.
- The NRLN proposes that the PBGC rules be modified to require the **PBGC to use the retiree's age and length of service used to determine his / her benefit at retirement or termination whichever is higher** when calculating and determining the PBGC pension benefit.

**Need for Open and Full Disclosure of PBGC Rules to Plan Participants**

Current ERISA law does not require that the PBGC publish the rules by which they evaluate pension plans or determine PBGC benefits. Lack of disclosure denies critical information needed by plan participants to determine if they have been treated fairly and to exercise due process.

- The NRLN proposes that **PBGC rules** used to calculate or otherwise determine PBGC pension benefits, including those used to determine the termination values of plans **must be fully disclosed to plan participants upon request.**

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## PROTECTING RETIREE BENEFITS PENSION BENEFITS GUARANTY CORPORATION RULES REFORM

### EXECUTIVE SUMMARY

The PBGC currently treats changes in defined benefit pension plan annual earnings limits, mandated by Congress, as modifications to the pension plans themselves, and has applied the lowest annual earnings limit during a five-year lookback period when calculating retiree benefits. For example when the Delta Air Lines pilot defined benefit plan was terminated in 2006, the annual 401(a) earnings limit was \$220,000 but when calculating the pilots' protected benefits, the PBGC used the 2001 temporary earnings limit of \$170,000.

The punitive results of this lookback process have been **magnified** by the efforts of Congress to balance the federal budget by enacting the Omnibus Budget Reconciliation Act of 1993 which raised tax revenues by temporarily reducing corporate deductions used to fund qualified pension plans. In 1992, the maximum qualified pension earnings limit was \$235,840 but OBRA 93 **temporarily** reduced the limit to \$150,000 in 1993 with a phase-in process designed to eventually restore the limits. By using the OBRA 93 pension **earnings limits in effect five years prior** to a plan termination to determine a retiree's PC3 benefit, a priority category only paid out of available pension plan assets, the PBGC magnifies the impact of OBRA 93 on retirees and changes a **temporary limit** into a **permanent reduction** in retirement benefits.

Unfortunately, the impact of OBRA 93 on the retirement security of retirees goes even further than the draconian reductions applied by the PBGC in its calculation of PC3 protected benefits. Pensioners who had previously earned a relatively high wage, who retired during the period the earnings limits were temporarily rolled back, often had a significant portion of their retirement benefits fall into the non-qualified category as a result of the OBRA 93 funding reductions. These non-qualified benefits were usually eliminated in their entirety when the company underwriting the pension benefits went through a corporate restructuring during bankruptcy. This is another issue that was particularly troublesome for airline employees due to the devastating impact of the events of September 11th on that particular industry, an event that happened at the height of the OBRA reductions.

**This table illustrates the impact of the OBRA 93 reductions to the qualified pension limits:**

(Data between years 1992 and 1998 is omitted, but is consistent with other data)

Year	2006	2005	2004	2003	2002	2001	2000	1999	1991
Original 401(a)17 limits	325,000	315,000	305,000	300,000	295,000	285,000	275,000	270,000	222,220
OBRA 93 reduced limits	220,000	210,000	205,000	200,000	200,000	170,000	170,000	160,000	N/A

The PBGC, under category PC-3, bases its pension obligation to a retiree on the terms of the plan 3 years prior to termination. It also uses the income and age of the retiree at that same 3-years-prior point as the basis for calculating the individual's PC-3 pension benefit. The purpose is to prevent unscrupulous companies from inflating pension obligations in anticipation of a plan termination. However, specifically anticipated changes in the IRS code that are contractually acknowledged prior to the 3-year lookback period, are NOT equivalent to changes in the retirement plan itself, nor can they possibly be viewed as being implemented in anticipation of plan termination.

### EFFECT OF REMOVING IRS 401A & 415B LIMITS FROM PBGC PENSION CALCULATIONS

The following table summarizes the retirement calculations for 3 different retirees:

(Over)

1. Retired at age 60 with 25 years of service August 31, 2005 with a Final Average Earnings (FAE) of \$250,000.
2. Retired at age 55 with 25 years of service August 31, 2005 with an FAE of \$250,000.
3. Retired at age 55 with 25 year of service August 31, 2003 with an FAE of \$250,000.

All variations in the retirees' qualified annuities are due to one or more of the PBGC lookbacks on IRS limitations, age, and length of service. Percentages represent the portion of the retiree's pre PBGC Qualified annuity that is or would be paid under the given limitations.

Individual pensions Example #	2006 Qualified annuity Pre PBGC penalty	PBGC Qualified Annuity / % of 2006 Annuity	Remove IRS 401a 5 year lookback	Remove IRS 401a (5 yr.) & 415b (3 yr.) lookback	Use retiree's actual age at retirement in PBGC calculations	Also Use retiree's actual length of service
1 – Retired 8/31/2005 At age 60	\$51,000	\$ 13,210 / 26%	\$33,965 / 67%	\$33,965 / 67%	\$40,920 / 80%	\$51,000 / 100%
2 – Retired 8/31/2005 At age 55	\$37,843	\$ 7,568 / 20%	\$14,425 / 38%	\$24,349 / 64%	\$34,782 / 92%	\$37.843 / 100%
3 – Retired 8/31/2003 At age 55	\$37,843	\$22,950 / 60%	\$31,867 / 84%	\$37,843 / 100%	\$37,843 / 100%	\$37,843 / 100%

In addition to a clarification of the PBGC's lookback authority in determining pension benefits to be paid out of a terminated plan's remaining assets, there needs to be more transparency regarding the factors the PBGC uses to determine a pension plan's funding status under the distress termination guidelines.

Another area that currently lacks full disclosure is the percentage of a terminated pension plan that the PBGC returns to the plan beneficiaries as opposed to the portion of the plan's assets that the PBGC keeps for its own operations. The NRLN believes that beneficiaries of terminated pension plans should receive 100% of the remaining plan assets. The PBGC's operating expenses and pension guarantees for other terminated plans should be covered by employer premiums, not by taking earned benefits away from retirees.

Incorporating IRS code changes under sections 401(a) and 415(b) in Defined Benefit Plans is an integral part of collectively bargained contracts in accordance with the provisions of OBRA 93. By subjecting the earnings limits, reduced temporarily by Congress in 1993, to the five-year lookback reductions by the PBGC treats these limits as if they were contractual changes, resulting in the failure to pay retirees a large portion of the contractual qualified pension benefits earned over their careers. To clarify what we believe to be existing Congressional intent to protect retiree benefits, we propose that the following legislation be enacted:

**The Pension Benefit Guarantee Corporation shall use the Defined Benefit Plan income and pension benefit limitations defined in IRS codes 401(a) and 415(b) in effect on the date of the plan termination when calculating the pension benefits payable under Priority Category Three (PC3). In addition the greater of the retiree's age and length of service used to calculate the pension at the time of retirement, or the retiree's age and length of service at plan termination, will be used when calculating benefits protected under Priority Category PC3. Regardless of these provisions, the PC-3 benefit shall not exceed the qualified benefit to which the plan participant was entitled on the day before the plan was terminated. These changes shall be retroactive and apply to all defined benefit plans terminated after Sept. 11, 2001.**

**In addition, the PBGC rules used to determine the termination values and funding levels of pension plans and all other PBGC rules and guidelines should be fully disclosed to recipients (or designated representatives) of covered pension plans. These provisions should be made part of the Pension Protection Act (PPA) of 2006.**