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MINIMUM REQUIRED AND MAXIMUM DEDUCTIBLE CONTRIBUTIONS

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- o IRC Section 404
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MR. DAVID P. KENDALL: I'm an ASA and an enrolled actuary with the Wyatt Company in the Milwaukee office. I've spent about the last 12 years working primarily in the defined benefit plan area. I'm going to present an outline of the current U.S. requirements for minimum and maximum funding as specified in Sections 412 and 404 of the IRS code. I'm going to pay particular emphasis to some of the changes that were required by recent legislation, particularly since the Omnibus Budget Reconciliation Act of 1987 (OBRA 87) and the Pension Protection Act.

Wayne Berney is going to discuss Canadian pension requirements. Wayne is with the Alexander Consulting Group in Edmonton, Alberta. Wayne is an FSA and a Fellow of the Canadian Institute of Actuaries (FCIA) with about 10 years of experience in the benefits field in Canada. Prior to his joining Alexander, Wayne was an education actuary for the Society and remains active in that area by serving on the Society's education and examination committee.

First, Chet Dash is going to present an overview of funding considerations in countries other than the U.S. and Canada. Chet is also an FSA and an EA, and he is with the Wyatt International Benefits Practice in Stamford, Connecticut. Chet has been involved in the international area for about five years now and has about 15 years of experience in the pension field.

MR. STANLEY A. DASH, JR.: Most of this session will cover the minimum required and maximum tax-deductible contributions in the U.S. and Canada, and Dave and Wayne will take care of that. As a basis of comparison, I will briefly outline the requirements of pension plans in a few other major countries. My comments will be limited to countries where funding is the norm and where, historically, large amounts of assets have been accumulated, as is the case in Canada and the U.S. Situations where it's usual to fund by means of insurance premiums, for example, in The Netherlands and

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some insured plans in Belgium, or where it's usual to establish book reserves, for example, France, Germany and Italy, and oftentimes the retirement allowance plan in Japan, will not be covered. Like I said, we're trying to do a comparison here with the funding requirements in the U.S. and Canada. Now, in each case the information presented has been supplied by a local actuary actually practicing within these countries. Most of my experience is in the expensing side with these countries, so I can't necessarily vouch for this information. If any of you out there have any further updates on some of this as we go through it, we'd appreciate your comments.

Table 1 shows the minimum and maximum funding requirements. In the case of Australia, to continue to receive all normal tax concessions, an actuarial valuation must be made at least once every three years. Company contributions are required in accordance with the actuary's recommendations. There are no government guidelines on minimum funding standards, and usually the actuaries follow the guidelines of the Institute of Actuaries in Australia. As far as the maximum is concerned, you'll see I left just that blank, and the reason for that was because the last piece of information I had stated that there was a current practice and then a proposed practice. The proposed practice was supposed to have gone into effect on July 1, 1990, but as late as yesterday I spoke to one of the Australian actuaries attending the conference who could not confirm that that proposed legislation had gone through. Apparently there's an enormous amount of bickering going back and forth on a number of issues in Australia, and this one may have been delayed.

In any event, as far as the maximums are concerned, the government set limits by an applied, not specified, formula. Basically, the formula is set up like a defined contribution formula where you use interest at 10%, salary scales at 8%, no decrements, and you have to use what is called the target benefit maximum. Even though the plan might call for a different projected benefit or level of benefits, you have to use government-set target benefits. Apparently they're setting some kind of limits on how much can be accumulated in the plan similar to what we do here in the States. The historical way of getting benefits in Australia is a lump sum. They're trying to encourage people to start receiving or accepting annuities. So, they set up these target maximums that encourage the selection of annuities. In doing this defined contribution approach, you have to use these government-mandated target benefits, and you come up with, effectively, on an individual basis, a contribution over the person's working lifetime.

In general, the maximum under the current legislation, you do the individually applied formulas on this defined contribution basis, 10% interest, 8% salary scale, no decrements, level contributions as a percentage of salary, target benefits specified by the government, differing depending on whether you're going to be taking a lump sum or an annuity or some combination of the two. That was the current legislation. The proposed was to raise the target benefits substantially so that you can have higher maximum tax-deductible contributions. They were also going to get rid of the interest and salary components. So, you just do a level percentage of pay based on these target benefits.

Next we'll move on to Brazil. Brazil's fairly simple. The minimum is normal cost plus payment to amortize the unfunded past service liability (PSL) over 20 years from the effective date of the plan, the maximum normal cost plus 100% of the unfunded past

TABLE 1

Minimum & Maximum Funding Requirements
in Other Major Countries

	Minimum	Maximum
Australia	In accordance with actuary's recommendations	
Brazil	Normal Cost + payment to amortize unfunded PSL over 20 years from effective date of plan.	Normal Cost + 100% of unfunded PSL. Any contribution in between max/min acceptable & deductible.
Belgium	If assets exceed liabilities on a minimum funding basis (7% interest, no salary, Belgium mortality), no contribution needed.	Maximum equal to contribution as determined under normal funding valuation.
Japan	TQPP: Normal Cost + interest on unfunded accrued liability. EPF: Normal Cost + (Current Payroll x Unfunded Accrued Liability at last valuation/Payroll at last valuation) x Present value factor for 20 years certain annuity.	TQPP: Normal Cost + either 20% of last unfunded accrued liability at last revaluation or 30% of unfunded accrued liability at end of last year-end. EPF: Normal Cost + (Current Payroll x Unfunded Accrued Liability at last valuation/Payroll at last valuation) x Present value factor for 7 years certain annuity.
Mexico	Minimum effectively zero.	Maximum is amount as determined by actuarial valuation.
South Africa	If in surplus on Fund Actuary's valuation basis (i.e., including COLI), no funding required.	No statutory maximum funding level. Employer cannot contribute more than 20% of total salaries to all approved funding arrangements.
Switzerland	If in surplus, minimum must: a. Be at least equal to employee contributions b. at least equal to the LPP/BVG amounts.	No maximum funding restriction within the bounds of reason.
U.K.	If in surplus, effectively no minimum contribution.	If assets exceed value of accrued liabilities by more than 5%, contributions are to be limited. Value of liabilities to be based on extremely conservative basis.

service liability. In the case of Brazil, there's no specific penalty for contributions below the minimum. Excess over the maximum is not tax deductible. You have to file with the controlling authorities, what they call the "Nota Technica," which contains the methods and assumptions that have to be approved by this controlling authority, and the maximum interest rate that can be used is 6% real. Brazil, as most of you probably are aware, has enormous inflationary problems. All actuaries down there use the real rates in doing their valuations, and the maximum you can use is 6%.

In the case of Belgium, now, once again, I referred to at the beginning that I would only be discussing the larger, noninsured plans, as opposed to the insured plans. Now, just to set the stage, though, in Belgium the insured plans use an agreed insurance tariff based on 4.75% interest, no allowance for salary increases, no decrements -- excuse me, they have the insured life mortality table, and the funding is usually on some sort of annual or single premium basis. In the case of noninsured plans, it's basically the same. The minimum funding basis is basically the same as the insured plans except you can use 7% interest. You can use other assumptions -- in the case of, for example, mortality and turnover and things like that -- or even higher interest rates, but you have to get authority approval. As far as the minimum is concerned, you need to be solvent throughout the entire period of the plan on this minimum funding basis. If you're solvent, you basically have freedom to fund -- to use any funding method assumption, set any kind of contribution rate that you wish, just as long as you satisfy this minimum solvency requirement. In that extent, if you're solvent, really the maximum is just equal to the contribution as determined under the normal funding valuation that the actuary will prepare.

Moving on to Japan, now, TQPP stands for tax qualified pension plan, and in a tax-qualified pension plan, you must use an interest rate for valuation. It must be not less than 5%, but it's universal for most actuaries there to use 5.5%, and a standard set of assumptions and methods are normally used by the actuaries throughout Japan. On a minimum, of course, you've got normal cost and interest on the unfunded, accrued liability. On the maximum you've got normal cost plus either 20% of the last unfunded accrued liability at the last revaluation or 30% of the unfunded accrued liability at the end of the last plan year. The other major plan is what is known as an employee pension fund (EPF). Interest rate must be 5.5% there, and standard assumptions and methods are mandated. This is a little bit different from the TQPP because of who's responsible for the minimum in this respect. The Ministry of Health and Welfare apparently have control of the EPF, whereas the Ministry of Finance has complete control of the tax-qualified pension plan. The EPF, you can see, is normal cost plus a percentage that's basically the current payroll times the unfunded accrued liability at the last valuation over the payroll, at the last valuation, times the present value factor for a 20-year certain annuity, and the maximum, basically the same, except you use a seven-year certain annuity.

Moving on to Mexico, many plans in Mexico are book reserve, but there are some pension plans that are funded, and I'm concentrating on them. In the case of Mexico, the actuarial valuations determine the maximum -- they are used to determine the maximum deductible contribution, and, effectively, the contribution can be anywhere between zero and whatever the actuary comes up with in the valuation, and they're all tax

deductible. So, the minimum is zero. Maximum is the amount determined by the valuation. The actuarial assumptions are not regulated, but approval must be provided by the income tax authorities, and the income tax authorities will give approval if they judge them to be reasonable in the aggregate. Any of the common, accepted actuarial methods are acceptable. Mexican law does not enforce either a minimum or a maximum funding level. However, if the assets exceed the total present value of benefits, future contributions will not be tax deductible, even though the interest earnings on the funds apparently will remain tax deferred.

In the case of South Africa, an actuarial valuation must be done triannually and lodged with the Registrar of Pension Funds. There's no statutory valuation basis, but the actuary must be able to support that his assumptions are reasonable. The method is effectively equivalent to the projected benefit obligation (PBO) with salary scales. As far as I know, in South Africa, it's universal to use a cost-of-living increase for postretirement benefits, usually somewhere in the neighborhood of 7% or something like that. If the plan is sound financially, that is, if the assets divided by the PBO are greater than 100%, then no funding, effectively, is required, but if that ratio, assets divided by PBO, is less than 100%, the actuary must recommend a funding scheme to get to 100% within three years. The only exception to that is if the underfunding is due to changes in the fund benefits. You can use six years to make up for that underfunding. There's effectively no statutory maximum funding level except that the employer cannot contribute more than 20% of total salaries to all approved funding arrangements.

Now, in the case of Switzerland it's extremely complicated, mostly because of the absence of any clearly defined rules. The only general rule, and I'm putting that in parentheses, is the general tax principle that pension plans must be used to fund for pension plan benefits and are not to be used as devices to artificially reduce taxes, taxable income, either to the employer or the employees. There are unique things that can happen in Switzerland, and I'm just going to concentrate on what is known as the registered plans which provide what they call legal minimums. The term used there is LPP/BVG. I, personally, cannot pronounce what it stands for, so I won't even attempt it. Now, on these legal minimums there's something known as an Article 65 that stipulates that the plans must at all times meet their obligations on these legal minimums, but it's somewhat misleading because when they say that -- it's on a balance sheet basis, and, effectively, what they're really saying is that the present value of future benefits must equal the assets plus the present value of future contributions. In general, though, the actuaries like to ensure that the assets are sufficient to cover the legal minimum. There are some other requirements as far as minimums are concerned, and they're basically with respect to public relation requirements or plan requirements depending on what the plan will say, and, basically, it's normal for the employer to make a minimum contribution at least equal to what the employees are making, and, second, to also make a contribution at least equal to what is required to cover the legal minimum. As far as the maximums are concerned, there really are no maximum funding restrictions within the bounds of reason, and my contact in Switzerland has told me that he doesn't even know what those bounds are. He says as long as you're reasonable, apparently you will not be called on the carpet.

And, finally, the U.K. is one of the most interesting of all. Historically, the U.K. was never subject to any minimum funding requirement. The maximum was a broad requirement that annual contributions would not exceed twice the normal annual contributions under an established funding method. There have been quite a few changes over the past few years. Specifically, the Social Security Bill of 1990 was just passed on July 13, 1990, and in that respect you called that any deficit on a plan termination basis will become a debt to the sponsoring company. This impacts pension plans, especially final pay defined benefit plans, after what they call the appointed day. Now, the appointed day hasn't been determined yet. I understand it'll probably be some day set in either late 1991, maybe early 1992, but any pensions accruing after the appointed date must provide guarantee increases to pensions in payment in line with price inflation with a maximum of 5%. There was also a Finance Act of 1986 with effect from April 6, 1987. Let me step back for a minute. As far as the minimum is concerned, if it's in surplus, there's, effectively, no minimum contribution. If it's not in surplus, there is this debt to the corporation, and they'll just have to make up that contribution if there's a plan termination. Normally, most plans in the U.K. are very well-funded, extremely well-funded. If they were U.S. plans there'd be no contributions for a long time. As far as the maximum is concerned, the accrued liability is calculated using a 7% salary scale in the case of a final average pay plan, 8.5% interest, and an allowance for pension increases, either the guaranteed ones or discretionary ones. If the assets on that basis exceed the accrued liability by 5%, steps are required to eliminate the excess within a five-year period. If it's not eliminated within a five-year period, investment income on the excess assets over the 105% level will be subject to tax. And in this calculation they use a projected benefit obligation type method and what they call a discounted income approach for valuing the assets which is quite different from what we've seen here. It, effectively, has to do with a discounted value of the expected return on a theoretical asset distribution.

In general, those are the minimums and the maximums for some of the major countries. Like I said, we've skipped some like Germany, France, and Italy. Some of those plans in Italy, for example, are more in the lines of lump sum plans, termination pay plans, and retirement lump sum type situations. They're not really bona fide pension plans, so we haven't discussed them here. Now, as you can see from the chart, except for the U.K., the requirements in other countries are not really overly complicated like they are in Canada and the U.S. Historically, for many of the countries like the U.K., Belgium, and South Africa, there has been somewhat conservative funding. I do a lot of work with respect to FASB for these countries, and we always find, especially for those three countries, that they are tremendously overfunded. Part of that problem, of course, for FASB, you can't use a cost-of-living assumption in valuing for FASB if it's not either spelled out in your plan that this amount is provided or you can prove effectively that this has become such a habit of giving increases that you can say basically that it really is part of the plan.

Like I said, if anybody has any corrections to make to any of these comments, please, somewhere along the line, give me your comments so I can correct them. At this point I'm going to turn it over to Wayne, and he's going to talk about the Canadian requirements.

MINIMUM REQUIRED AND MAXIMUM DEDUCTIBLE CONTRIBUTIONS

MR. WAYNE R. BERNEY: David called me up a couple months ago and asked me to provide you with an overview of minimum and maximum contribution requirements for pension plans in Canada, and as I was preparing for this it reminded me of the story of the accountant and the lawyer and the actuary who were all going for the same job within a company, and they all went through the interviews with flying colors. At the very end the CEO asked each of them the same question. He asked, "How much is two plus two?" The accountant said, after a moment's thought, "Well, the answer's four, but I'm not sure if it's a debit or a credit." The lawyer, after thinking about it for a little while, said, "The answer legally is four. No doubt about it." The actuary didn't have to think at all. He said, "What do you want it to be?" In a sense that's what the minimum and maximum requirements are for Canada. There is a considerable amount of actuarial control over what they are. We don't have detailed, prescribed methods and assumptions that have to be used, yet, and, as such, we think that's a fairly fortunate position to be in. As some of you may know, we do some things a little differently in Canada than here in the U.S., and pension regulation is no exception.

In order to get a feel for the situation, you have to understand the regulatory environment that exists in Canada. In the U.S. you have ERISA and the Internal Revenue Code to deal with. Well, that is certainly an awesome burden. You essentially deal only with the Internal Revenue Service, a branch of the federal government. In Canada the regulatory environment is different. Most pension plans fall under provincial jurisdiction, except for certain industries which are federally regulated and plans that have employers located in our two northern territories. The provinces are concerned with the solvency of these plans and members' rights under these plans. So, the provinces are concerned with the minimum contribution requirements. Pension legislation exists in all but one province, and that province has now put forth draft legislation which is expected to become law some time in the next five years, maybe. They do things quite a bit differently in British Columbia from the rest of the world.

Revenue Canada, our IRS, regulates pension plans from the perspective of taxation. Plans must be registered with both the province in which the employer has most of his employees and with Revenue Canada. You call pension plans qualified pension plans. We call them registered pension plans. Clearly, the province is concerned with minimum contributions, while Revenue Canada is concerned with maximum contributions. Because these are two, separate bodies, sometimes the minimum and the maximum conflict in not a very nice way.

Each province that has the law has essentially a similar law, although there are some nasty differences that make it awkward if you have members in more than one province, but they essentially require that the minimum contribution consists of what else but the normal cost of the plan for the current year, plus a series of amortization payments for various unfunded liabilities, experience deficiencies, etc. During the mid to late 1980s, the provinces all revised their legislation, so there are different amortization periods, in effect, for plans in different provinces depending on when the particular province put its legislation into force.

The plan's normal cost is determined by an actuary who must be a Fellow of the Canadian Institute of Actuaries. Provinces leave the choice of assumptions up to the

individual actuary. The Canadian Institute has formal standards of practice in this area that we call recommendations, and there's a whole bunch of other words after that, too. Nevertheless, there presently can be a wide range in acceptable assumptions and, hence, a wide range in the normal cost. While virtually any actuarial cost method is currently acceptable, most of the provinces ask for explanations of cost methods that are other than unit credit or projected unit credit. Essentially, anything that isn't unit credit or projected unit credit automatically goes to the actuarial departments of the various provincial regulators because apparently no one can understand anything other than unit credit or projected unit credit, other than the actuarial departments. Also, virtually all of the provinces that have legislation have their own set of acceptable ranges for economic assumptions and acceptable decrement tables. Anything not on a province's selected list or outside of their acceptable range will be questioned and must be justified. For example, most provinces will accept a valuation interest rate as high as 8% without question. However, if you wish to use 8.5% or 9 or anything higher, you will have to provide justification acceptable to the province, and if you do like we do and use streamed assumptions for interest rates starting at 10 or something and then grading down, you're pretty well questioned, at least the first time you present it to the province.

Now, the normal cost consists of employee contributions and employer contributions. I mention employee contributions because most pension plans in Canada require the employee to contribute. This is not all that bad because the employee gets to deduct his contributions from his tax return. Each province requires that the employee contributions be remitted by the employer monthly to the pension plan, whereas employer contributions are generally required to be remitted quarterly. An actuarial valuation of the plan, together with a cost certificate showing the normal cost of the plan, must be performed at least once every three years. If there is sufficient surplus, how ever you define it, employer contributions can be deemed to be made from that surplus. I think this is similar to how the funding standard account works, but I'll find out for sure later. However, the required employee contributions must be remitted monthly regardless of how much surplus is in the plan. The series of amortization payments must be made if the plan is not fully funded, at least with respect to accrued benefits. The payments can be broken down into three types. The first type represents any remaining special payments which were formerly in effect prior to all the new legislation coming into force in the mid to late 1980s, to retire an initial unfunded liability at plan inception or an experience deficiency as at various dates which correspond with the dates that the legislation came into effect. In my province, the legislation came into effect on January 1, 1987. I think in Ontario it's January 1, 1988, and in Quebec it's January 1, 1990, I believe, and it just varies all over the map, so you have to know where your plan is registered and what the particular requirements are. Under the previous legislation, initial unfunded liabilities could be amortized over a 15-year period. So, there could be five, 10, up to 14 more years of payments that need to be made for an initial unfunded liability, and the amortization rate is the valuation interest rate. Also, although it would be extremely rare, during the mid-1980s, experience deficiencies could have arisen, and they previously had to be amortized over a five-year period. So, there may be one or two or three years of amortization payments left for an old experience deficiency. And, again, the interest rate that is to be used is the valuation interest rate, and the amortization is with interest and principal.

The second type of amortization payment is any other unfunded liability determined on a going-concern basis such as could occur due to a plan improvement after the effective date of the new legislation or could occur due to poor experience of the plan. The going-concern basis is the actuary's valuation basis on the assumption that the plan is ongoing and continuing, which is the way all the valuations used to be done before we had the new legislation.

The third type of amortization payment is any payment required to amortize something called a solvency deficiency. In a sense this used to be called an experience deficiency, but the new legislation that's in effect generally requires that solvency valuations take place coincident with the going-concern valuations at least once every three years, and a solvency valuation is one in which the liabilities are valued as if the plan was terminated as of the valuation date. I think there are parallels with your current liability situation.

There are numerous special rules required to determine the value of assets and the value of the liabilities for solvency valuations. Solvency deficiencies, when they arise, must be amortized over a five-year period at the solvency valuation interest rate which could be different from the going-concern valuation interest rate. Generally, you might think that few plans would have solvency deficiencies, particularly if they were final average plans. So, when you do the valuation you don't have to project for final average salaries if the plan is about to terminate. However, there are special rules applying to plan termination in Canada. For example, accrued pensions become fully vested regardless of the vesting rules that are in effect. There are also special rules which come into effect on plan termination, at least in Ontario, which have the effect of giving members benefits as early as they would have had had the plan not terminated. This is particularly critical for plans that have enhanced early retirement benefits. Solvency deficiencies could arise if a plan has one or more of the following characteristics: if it had a large, unfunded actuarial liability on a going-concern basis, if it was a flat benefit plan with frequent negotiated improvements, if it was a career average plan that had periodic benefit updates, which I guess is the same thing, if it had rich, employer-provided early retirement provisions, or some plans that have been negotiated have generous benefits on plan termination or plan closure. Maximum contributions are determined by the Income Tax Act and regulations as recently amended by Bill C52 in June of this year and essentially are set as the normal cost plus any unfunded liabilities as certified to be required by an actuary who, again, must be a fellow of the Canadian Institute. Generally, if the valuation basis is acceptable to a province, it will be acceptable to Revenue Canada, but not always. They do have a few wrinkles with respect to the interrelationship of the economic assumptions. For example, the valuation interest rate must be at least 1% higher than the salary scale in final average plans. This is not in the regulations yet, but it was in the old information circulars that we had to follow.

The final regulations, you'll not be surprised to hear, have not yet come out, but they have been promised for late October or early November of this year. We will see whether that happens. I'm pretty hopeful that it will.

You will note that the maximum contribution is any unfunded liability and not just the amortization payments. This provides a plan sponsor with considerable room to plan his tax-deductible contributions.

Revenue Canada imposes a number of restrictions on the benefits that can be provided under pension plans, and in this way they effectively limit the amount of the contributions that can go into defined benefit plans. Pension registration rules, as I said, have now been placed in the Income Tax Act and its regulations. Previously, I guess you could say they were written, but they were in the form of information circulars which were pretty general and seemed to change depending on which Revenue Canada person you talked to. The new rules will be part of the Income Tax Act and regulations and have essentially been set up to try to limit contributions to pension plans to a total of 18% of an individual's earnings up to specified dollar maximums. They specifically say that for money purchase arrangements. For 1991 the specified dollar maximum is $12,500, and that's scheduled to increase to $15,500 by 1994, and then be indexed according to average wages from then on. The government has equated defined benefit plans with defined contribution arrangements using a very actuarial factor of nine, that is, a dollar of pension entitlement is worth $9 of money purchase contributions regardless of how old you are.

This factor of nine has an obvious effect on the maximums. It's fairly convenient for employers, because they just have the one factor to worry about, but there are many more inconveniences in this whole process, including having to report the value of defined benefits plans on individual's T4s every year starting in February. The T4 is the same thing as your W-2. Now, Revenue Canada has restricted, a big but here, the ability of employers to contribute to pension plans if there is surplus. Previously, employers could contribute to pension plans regardless of how much surplus existed in the plan, but if the surplus exceeded two years' worth of employer normal cost, the employer could not deduct the contribution, but he could still contribute it. The changes to the Income Tax Act create the concept of permissible contributions or permissible employer contributions. Under the new rules, the employer will not be allowed to contribute to the plan if there is surplus greater than (1) 20% of the actuarial liability or (2) the greater of -- 10% of actuarial liabilities or two times the normal actuarial cost (Chart 1). This new rule takes effect in 1991, but it will be phased in so that only one-third of the existing surplus needs to be taken into account for calendar year 1991. Two-thirds of the surplus is taken into account for 1992, and then the rest of it in 1993, or, rather, 100% of it in 1993. If the plan is contributory, though, the employee required contributions must still go in the plan.

CHART 1

Maximum Contributions
If surplus greater than a) 20% of liabilities, or b) Greater of i) 10% of liabilities, or ii) 200% of normal cost Then employer cannot make contributions

Now, as part of the changes, Revenue Canada has introduced a new category of pension plans called designated pension plans. This category was introduced to go after executive pension plans which formerly fell under the old rules and provided considerable

room for employers to make large contributions for individuals, but Revenue Canada thought that was not the right thing to do anymore and is now trying to restrict the use of pension plans as tax shelters. Formerly, such individuals who are not also shareholders could receive substantial benefits. Shareholders could only have plans if they also provided a plan for all the other employees that was worth in total at least as much as their own plan. This tax deferral has now been restricted. Revenue Canada defines a designated pension plan as a plan which is primarily for the benefit of highly compensated employees or persons connected with the employer. Highly compensated employees are defined as employees who earn more than 2.5 times the Canada pension plan year's maximum pensionable earnings, which is about $70,000. So, this catches a lot of people. Persons connected with the employer are persons who have at least 10% of the shares of any class of shares of the employer or who are the spouse or child of such an individual. In a sense, Revenue Canada has now created a formalized, top-hat, pension plan. In some provinces, such plans may not be allowed because they can be completely selective in that only one individual needs to be in the plan so that an employer can set up such a plan for one individual, and the employer does not have to set up plans for anybody else. This obviously means that there are no discrimination rules to worry about. Instead, there are rules that restrict the benefits that can be provided under one of these plans which are generally such that a smaller benefit is provided, and smaller tax deferral is provided, than would be provided under a larger plan that included everybody else. The plan's maximum benefit is essentially a 2% defined benefit plan based on something called updated career average compensation. Updated career average compensation is the individual's compensation for the year increased with increases in the average wage in Canada from the year in which the compensation is earned to the year of retirement. So, for most people this is like a one-year final pay plan restricted to what average wages would go up. There are considerable restrictions on the ancillary benefits that can be put on these plans. The plan can be contributory or noncontributory, but for individuals who are not shareholders, there is an opportunity to include past service benefits. We believe that Revenue Canada may have opened a little Pandora's box here, and there may be considerable opportunity for a lot of these plans to go into force quite quickly, particularly with small employers.

At the present time, it looks as if there is greater tax deferral available under one of these plans than would be available under Revenue Canada's proposed new higher registered retirement savings plans limits which would then make these plans attractive for the mom-and-pop shop and the small employer, particularly because that small employer or shareholder doesn't have to provide a plan for the rest of his employees. Another advantage is that these plans, while subject to provincial legislation, make them creditor proof from personal and corporate creditors which doesn't happen with the other tax deferral arrangement, the registered retirement savings plan, unless the assets are part of an insurance company contract, and then they get protection under the insurance acts. And, finally, it's possible for the shareholder to set up his or her own plan and not worry about setting up a plan for anybody else. Now, that's what we think is going to happen. We haven't seen the regulation on this yet. We saw a draft regulation last December which would indicate that these are fairly attractive vehicles for tax deferral.

Basically, we think the next year or two is going to be quite interesting in Canada as these regulations and the new laws unfold, and we see how the provinces will react to it, but, as I said at the beginning, we still think we have a situation where the answer is what you want it to be, within extremely broad limits. I think David now will talk about the U.S. in some detail.

MR. KENDALL: I talked to one of our research actuaries recently. He told me his rule of thumb with the IRS is he puts a certain amount of credibility on any prediction of something that's going to come out within a month, but anything that is expected to take more than a month he basically has no hope for in the short term.

As far as the requirements in the U.S., I'm going to go rather quickly through some of what could be considered, perhaps, basic or ERISA type constraints and spend a little bit more time on some of the newer things that we're finding ourselves addressing with the Schedule Bs and things that we're doing now for our plans. I think at this point in the meeting, most of us are certainly getting the message that we need to be aware of what's going on with respect to some of these other countries in a number of areas, including the way that they're funding pension plans. I find it particularly interesting that Wayne pointed out that the provinces, at least, have indicated that they would perhaps question an interest rate assumption that was greater than 8%. In the U.S. the IRS has indicated, at least for small plans, that it may question interest rates less than 8%. So, it doesn't take an awful lot to see where the tendency is in terms of leading us towards a very narrow definition of what can actually be contributed to these plans. My basic philosophy with respect to these requirements is that they tend to work as sort of outside constraints. I, personally, still believe that we can do a pension valuation that's based on assumptions we believe are reasonable and come out with an answer, and then sort of as a last step we look to these minimum and maximum requirements to see exactly what we can and cannot do. Again, I'm going to go quickly through IRC Section 412 and IRC Section 404 and spend a little bit more time in particular on OBRA 87, which gave us the bulk of the changes with respect to these requirements.

We find from Wayne's discussion quite a number of similarities, I think, on the Canadian side. We have a minimum requirement which in general is the normal cost plus an amortization payment (Chart 2). We have a funding standard account credit balance that we can offset. We adjust for interest. And then we have some additional considerations. The periods that we use to amortize are set in the code, for the most part, and you're familiar with them. Some of them were changed under OBRA 87, in particular, the requirement for the amortization of experience gains and losses and changes in assumptions. There are also quite a few changes with respect to the availability and counting for waivers of funding deficiencies (Table 2).

CHART 2

Minimum Funding Contribution =
Normal Cost + Minimum Amortization Payment - Funding Standard Account Credit Balance + Interest

TABLE 2
Minimum Amortization Periods

Base	Number of Years
Initial Unfunded Liability	30
Plan Amendments	30
Experience Gains and Losses	5
Change in Actuarial Assumptions	10
Waived Funding Deficiency	5
Switchback from Alternative Minimum Funding Standard	5

Some of the other considerations that we have to look at when we're trying to figure out exactly what that minimum requirement is is the full funding limitation. We'll get into a little bit of the mechanics of that when we talk about the OBRA 87 changes, but generally the idea is that the minimum requirement shouldn't be a number that's bigger than what would fund the accrued liability under the plan as of the end of the year. As I mentioned, there are waivers that are available for plans for employers that are experiencing financial difficulty, and we'll get into some of the requirements of those as well. Those were, as I said, changed substantially by OBRA. There's an availability of extension of amortization periods under certain circumstances. Another new wrinkle that OBRA brought us is a deficit reduction contribution for plans that are underfunded with respect to the current liability which we'll define a little bit later. And contributions are now required to be made on a quarterly basis which is obviously another attempt to get the dollars in a little bit quicker on underfunded plans.

On the maximum side, we also have sort of a general model equal to a normal cost plus an amortization payment, plus interest (Chart 3).

CHART 3

Maximum Deductible Contribution =
Normal Cost + Maximum Amortization Payment + Interest

The amortization period here is generally 10 years for all bases. There are a couple of different ways that we can account for that. We can either maintain bases and write them down each year based on the actual payment to the unfunded or we can use a fresh start approach, and, given the actual unfunded each year, amortize that over a 10-year period. The additional considerations on the maximum side are similar to those on the minimum side. We're still limited by full funding. We can't pay in more than the accrued liabilities. The full funding limitation is a little bit different on the maximum side than it is on the minimum side, particularly with respect to the assets that we use to determine the amount of fundedness. We also have a new availability for plans with more than 100 employees, that they may contribute as much as the unfunded current liability. We've always had the availability of being able to deduct an amount at least equal to the minimum that's required in a given year. We do need to be careful if the

tax year and plan year do not overlap, that we account for the maximum requirement on a consistent basis. We have a couple of different options on how we do that. We have excise taxes now that we need to be considerate of. In the past you may have had clients who were nontaxpaying entities that didn't care all that much about nondeductible contributions, but they certainly care about additional taxes or penalties that they may have to pay to the IRS if they contribute too much.

We have already mentioned some of the things that OBRA brought us. Current liability is a new animal that we have to determine each year and that may, depending on the circumstances of the plan, impact either the minimum or the maximum contribution that we're going to make. The full funding limitation, as I said, has been changed or decreased. There were also the changes to the waiver, the availability of the waivers, the new deficit reduction contribution, and the quarterly requirements. There were some other changes, too, which indirectly affected the amount that you'd be able to or be required to contribute to a plan, things such as a change in the asset valuation methods that are required, some of the restrictions on reversions, additional requirements for plan terminations and other secondary considerations as far as funding.

Basically, current liability that we look at each year is similar to the present value of accrued benefits, not vested benefits. It's described as all liabilities to the beneficiaries and the participants under the plan. It's determined on a plan termination basis. There's another item that is new called an unpredictable contingent event benefit and a liability for those types of benefits. In general, what we're looking at are plant shutdown type benefits or special benefits that are triggered by something other than reaching a certain age or a certain amount of service or are based on death or disability. For calculating current liability, the original OBRA required or allowed you to disregard certain preparticipation service for participants with less than five years of participation. Rules on that have been changed somewhat, which I will discuss later. One of the last items that relates to the current liability that OBRA came out with was a discussion of assumptions and, in particular, interest rates. The new requirement on assumptions found at the bottom of Schedule B is that the assumptions are either individually reasonable or produce the same contribution as assumptions that in the aggregate are reasonable. There's certainly been some discussion as to, "What does that mean? Are you supposed to do two valuations? If you've been using implicit assumptions, can you still do so? What's required in terms of proving that you're going to come up with the same result?" My belief is that you still can use implicit assumptions, but you have to be careful. There are a couple of instances where we may not have been always as considerate as we should have been as to what the impact on certain things that we do are. We may have said that as long as we have a certain amount of spread between the interest rate and the salary scale, that's going to produce reasonable results, which certainly is true with respect to projected benefits, given that the salary scales are going to apply. When we're doing things like determining current liability, which is a value of accrued benefits, depending on the method that you're using to determine those benefits for a salary-related plan and given that you're using the salary scale backwards in some cases to determine the benefit amount, you may get the opposite result of what you're looking for. In addition, under some of the TRA 86 requirements we now have a salary cap. So, for some higher-paid individuals who may be accounting for a great deal of the

liability, a salary increase may not have any impact at all. So, again, I think we just need to be careful.

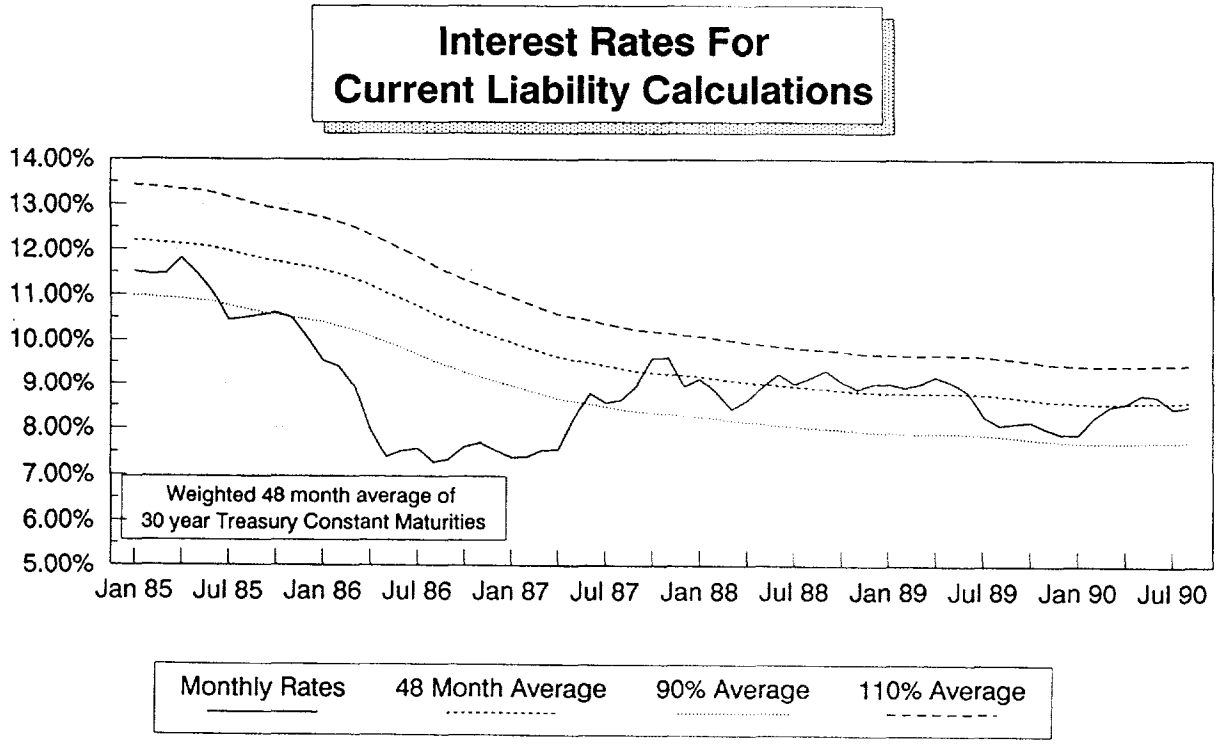
There are requirements for the interest rates to be used in calculating the current liability. It's kind of interesting when you read it. It says that generally you use the same rate as what you're using for valuation. However, you have these additional constraints. Basically, the range that we're given is a 10% corridor around a weighted 48-month average of 30-year Treasury Notes. One thing that we did when that came out was sort of go back and look at what would have happened in the past had we used those rates, had this requirement been around historically, and we found that certainly back when interest rates were extremely volatile, and we could well be substantially outside of that range for a given period, that we could have certainly come up with results that we would not have been happy with. We see that the trend, at least in the last couple of years, has been that, although there's still some volatility, it's been a little bit less, so things seem to be evening out a little bit, and we may feel a little bit more comfortable within that range (Chart 4).

Full funding limitation has been changed (Chart 5). As I said, there's been a new clause added on. We now have the lesser of 150% of current liability or the accrued liability, including the normal cost over the lesser of the fair market value of assets or the actuarial value of assets. For minimum funding purposes, the assets are required to be adjusted for the credit balance, if any. Although this is the way the statute reads, we were given some guidance from the IRS on the 150% of current liability requirement as to how to bring that forward to the end of the year. We were basically told that we need to separately project current liability to the end of the year, including any expected benefit payments, using the current liability interest rate, and if we were using a different interest rate for our funding valuation, that we should use that interest rate to project assets forward. So, the end-of-the-year requirement may be different than the beginning of the year requirement plus a given interest rate.

What happens when we hit the full funding limitation? When we hit the old full funding limitation then, as we're used to doing, we get to wipe out amortization bases. We consider the plan funded, but we don't get to do that if we only hit the new requirement. Instead, we must account for what we would now call a missed contribution and, in effect, amortize that over a period of 10 years. If we do hit the full funding limit on the old basis, we determine whether we get to take a full funding credit. We look at the minimum funding requirement, which is basically the amount that would be required to avoid a deficiency without taking into account the credit balance or any contributions that may have already been made for the plan year, and to the extent that the minimum funding requirement is in excess of the full funding limitation, then we get to take the full funding credit.

I just want to briefly explain about how we apply this on the Schedule B. It gets a little bit tricky when we have these overfunded plans as to how we account for these amortizations and what we do with the balance equation. We like to be able to show that our unfunded amount is equal to our remaining outstanding bases less the credit balance. Typical example, and this is with respect to the ERISA type calculation of the full funding limitation. We're assuming that the 150% of the current liability is in excess of

CHART 4


Interest Rates For
Current Liability Calculations
14.00%
13.00%
12.00%
11.00%
10.00%
9.00%
8.00%
7.00%
6.00%
5.00%
Weighted 48 month average of
30 year Treasury Constant Maturities
Jan 85
Jul 85
Jan 86
Jul 86
Jan 87
Jul 87
Jan 88
Jul 88
Jan 89
Jul 89
Jan 90
Jul 90
Monthly Rates
48 Month Average
90% Average
110% Average

Full Funding Limitation

Lesser of:

(1) 150% of Current Liability, or

(2) Accrued Liability (Including Normal Cost)

Minus

Lesser of:

(1) Fair Market Value of Assets, or

(2) Actuarial Value of Assets

the accrued liability plus the normal cost. We have a plan, and we're using an 8% interest rate, and the accrued liability and the normal cost add up to $190,000, and there are $195,000 in assets (Table 3).

TABLE 3

Example 1	
Assumed Interest Rate	8.00%
Accrued Liability	170,000
Normal Cost	20,000
Actuarial Value of Assets	195,000
FSA Credit Balance	15,000
Minimum Amortization	5,000
Full Funding Limit	10,800
Full Funding Credit	16,200

For maximum funding purposes, the plan is over-funded, and the most you can contribute on the maximum side is zero. However, if you were required to contribute more on the minimum side, you could. So, we need to go through and figure out if we are required to put anything in on the minimum side. We look at the minimum funding requirement, which is the normal cost plus the amortization payment brought to the end of the year, in this case that's $25,000 plus interest, $27,000. The full funding limitation, as we've said, we are adjusting those assets. We're subtracting out the funding standard account credit balance. That brings us down to $180,000 on the assets versus the $190,000 of liability and normal cost. So, we've got a $10,000 limitation. As of the end of the year that's $10,800. The difference between the $27,000 requirement and the $10,800 limit gives you the credit of $16,200. When we go to update our Schedule B, then we plug in that $16,200 credit, and the net effect is that when we get to the bottom we brought forward our prior year's credit balance with interest. Again, that's what we do for the funding standard account. When we take the next step and say what is the minimum requirement, we look at the normal cost plus the amortization payment, but then we get to reduce it by the funding standard account credit balance. So, the minimum payment, again, assuming that we've made that minimum payment some time on or after the end of the year, is what's going to bring forward the credit balance with interest.

On the other hand, if we have a similar situation with the same total amount of accrued liability and normal cost, same assets and same credit balance, but the minimum funding requirement is less because our remaining amortization bases are less, then we have the same full funding limitation, the $10,800, but in this case the minimum funding requirement is the $5,000 plus $2,000, $7,000 at the beginning of the year or $7,560 is the end of the year which is less than the full funding limit. So, we don't get to take a full funding credit (Table 4). On the maximum side we are limited to zero and on the minimum side we're also now limited to zero because the $15,000 credit balance is larger than the $7,000 requirement. However, we've not taken a full funding credit. So, we do not, in this instance, wipe out the bases as we did in the previous example. In other words, when we go to do the next year's valuation, we maintain those same bases.

TABLE 4

Example 2	
Assumed Interest Rate	8.00%
Accrued Liability	185,000
Normal Cost	5,000
Actuarial Value of Assets	195,000
FSA Credit Balance	15,000
Minimum Amortization	2,000
Full Funding Limit	10,800
Full Funding Credit	0

What you run across sometimes, and overfunded plans are ones where not only is the minimum funding requirement less than the full funding limitation, but the minimum funding requirement may be negative for a year, you're in basically the same situation (Tables 5 and 6). You're obviously limited on the maximum and minimum side to zero, and the question is just, "What do you do to the Schedule B?"

TABLE 5

Example 3	
Assumed Interest Rate	8.00%
Accrued Liability	185,000
Normal Cost	5,000
Actuarial Value of Assets	195,000
FSA Credit Balance	15,000
Minimum Amortization	(7,000)
Full Funding Limit	10,800
Full Funding Credit	0

TABLE 6

Example 4	
Assumed Interest Rate	8.00%
Accrued Liability	185,000
Normal Cost	5,000
Actuarial Value of Assets	195,000
FSA Credit Balance	15,000
Minimum Amortization	(7,000)
Full Funding Limit	10,800
Full Funding Credit	(2,160)

If you look at the wording on how to determine the credit, it's the excess of the minimum funding requirement over the full funding limit which would lead you to say that it would be zero. The problem that you have with that is that the result of this entry in the Schedule B is that you're going to increase the credit balance when you get to the end of the year by that amount of negative requirement. I'm not sure if that's appropriate or

not. One idea or suggestion is to come up with a negative full funding credit whose net result again is to bring you to the point where you've got your beginning of your credit balance only increased for interest and not increased due to the negative minimum funding requirement. As I said before, we found on overfunded plans where we try to maintain the balance equation, we've wiped out bases in the past and the outstanding amount is zero. We've got an unfunded amount equal to some large negative number. We've got a credit -- we may have a credit balance in there which may be smaller than the amount of overfundedness. So, in order to get the balance equation to work, the IRS has suggested that we would, in effect, set up a gain equal to the difference between the unfunded and the negative credit balance. Once we've done that, if we've set up that gain, then it seems that we should amortize it. So, we wind up sometimes with these large negative credits to the funding standard account, and it's not clear whether those should be used to increase the credit balance.

MR. ROBERT ALAN KLEIN: In a situation like this, you could have a situation where your minimum amortization caused you to have this negative -- on a short-term basis -- difference in the amortizations, actually carrying forward or enlarging your credit balance in a temporary situation, such as having experience gains that are being amortized over five years and having other pieces that are being amortized over 15 or 30 years. When your credit balance increases by that, it is just a temporary phenomenon.

MR. KENDALL: I think that makes sense when you actually have sort of real actuarial gains and losses that you're amortizing, but if what you've done is what I've just described to you, set up an example, a typical one together. Let's say you've got a large, well-overfunded plan with a relatively small credit balance. You've got this big number now that the IRS is saying, "Well, maybe you should call it a gain so that everything balances out," and you're going to set up a five-year amortization of that number which kind of wipes out the credit balance. It seems to me what you're doing is artificially inflating the credit balance, and I'm not sure that's required. I'm not suggesting that this is necessarily the correct answer. Depending on what you think should be done to maintain the credit balance, I'm saying that perhaps that's an option.

Regarding some of the changes with respect to waivers, OBRA has reduced the number allowable within a 15-year period from five to three. That doesn't apply to multi-employer plans. There's a requirement for the interest rate to be used, to be the larger of the funding interest rate or 150% of the federal mid-term rate.

There's a requirement for single employer plans now that the financial hardship driving the request must be proved to be temporary. The timing for the request has also been speeded up a little bit. Under the old rules, you had until the end of the following plan year to request a waiver. Now you must request it within 2.5 months after the end of the plan year for which it's being requested. There was a transition rule in the first year that it came out, in 1988. There's also the notice requirement for waivers. Basically, all participants, beneficiaries, alternate payees under the Qualified Domestic Relation Order (QDRO), and unions representing employees have to be notified, and, in addition, the notice must also disclose the funding percentage or the current liability funded percentage.

The next thing we want to go through here is the calculation of this deficit reduction contribution (Chart 6). The deficit reduction contribution is defined as the first two of those items, an unfunded old liability amount, and now plus an unfunded new liability amount. It gets reduced by certain amortization charges or credits. Basically, those would be for things other than gains and losses, the original unfunded liability amounts and plan changes and those types of things. We also may have an amount to fund for these unpredictable contingent events. If your plan provides for those type of benefits, there's a limitation on that overall number; the deficit reduction contribution is adjusted by the amortization charges and including the unpredictable contingent event amount cannot be greater than the unfunded current liability. For small plans there are special rules. If there are less than 100 participants, then there is no requirement for this additional contribution and it grades in if there are between 100 and 150 participants. The unfunded old liability amount is basically an 18-year amortization of the unfunded current liability that existed as of the first plan year for which this became applicable. In the case of a plan that was in existence prior to 1988 we would have determined -- say it's -- or a calendar year plan, we would have determined the unfunded current liability as of January 1, 1988, and the first payment on that would be due at the beginning of 1989. There's also, in addition to what originally appeared to be a portion of the unfunded old liability amount and has now been clarified to be a separate, additional piece for collectively bargained plans, there may be some liability with respect to benefit increases that had already been negotiated but had not been in effect yet.

CHART 6

Deficit Reduction Contribution =
Unfunded Old Liability Amount
+ Unfunded New Liability Amount
- Certain Amortization Amount
+ Unpredictable Contingent Event Amount
Special Rules for Small Plans

The unfunded new liability amount, then, after we determine what the unfunded new liability is, we apply a certain percentage to that, and we come up with that amount. If we go through an illustration here (Table 7), you'll notice that I've got an 8% current liability rate as of January 1, 1988. That's actually outside the bounds of what was allowable at that point, so you could ignore that or change it. Again, for this calendar year plan we would have gone through as of January 1, 1988 to determine what the total amount of current liability is. We would have taken the assets which we have adjusted by subtracting off the credit balance for purposes of determining what the deficit reduction contribution is, determine the unfunded current liability, I guess, as of the prior plan year. Whether you call it old or new doesn't seem to make all that much difference, and that's as far as you go. There's no payment due in the first year.

We then go to the next year, and we sort of start over again. We determine at that point, based on the current situation in the plan, current assumptions, what current liability is as of that date.

TABLE 7

412(l) Additional Contribution	January 1, 1988	January 1, 1989
Current Liability Rate	8.00%	8.00%
No. of Participants	196	204
Total Current Liability	156,647	250,688
Adjusted Assets	94,505	152,677
Funded CI Percent	60.33%	60.90%
Unfunded CI	62,142	98,011
Old	0	67,113
UCEB	0	0
New	62,142	30,898
Appl. Percentage		23.52%
Amount - New		7,269
Amount - Old		6,631
Def. Red. Contribution		13,899
Net Amortization Adjustment		5,711
UCE Amount		0
Additional Funding Charge		8,188
Lesser of AFC or UF CL		8,188
Interest Adjustment		655
Additional Charge (EOY)		8,843

To separate it out into old, new, and unpredictable, we first have to determine what the remaining balance is in the old current liability pot. There's some confusion, I guess, here as to what would be considered the remaining amount. Basically, the statute says that you're amortizing this. You determine it as of January 1, 1988. You amortize it with your first payment beginning January 1, 1989. Does that mean that you bring it up with interest to January 1, 1989 or is it just the $62,142 as of January 1, 1989, payable in 18 level installments of interest and principal? I'm not sure. I normally take this approach. There are other practitioners that just determine it as of January 1, 1988, just carry the number forward without any adjustment for interest, and determine it that way. In this instance we don't have any unpredictable contingent events. We determine that the plan doesn't appear to allow for any. And then the balance of the unfunded current liability over the old amount is the new amount.

So, for 1989, then, we determine what the pieces of the contribution are. We apply a formula to figure out what the payment towards the new piece is. Basically, we look at the funded percentage which determines for us what the applicable amount is. The applicable amount, then, is basically 30% less a .25% for the differences between the funded percentage and 60%. We determine the applicable percentage. We apply that to the amount of new current liability, and we come up with the payment towards the new amount. The old amount again is the amortization. Whether we brought it forward

with interest or whether we didn't bring it forward with interest, we're going to have a little bit of a difference in what the number is there, and the total of those two is the deficit reduction contribution. We then go back and look at what we've got as far as amortization payments for items other than gains or losses. We've had some clarification as to what you do if you've combined bases in the past. The original law seemed to say you couldn't do anything. You didn't have the availability of making the adjustment, and the new regulations seem to say that you can go back. If you have sufficient information to split that out, you can do so. So, we reduce it by that amortization adjustment, and then if we do have an unpredictable contingent event amount, we add that in as well, and that's the additional funding charge. As I said, that additional funding charge is limited to the amount of unfunded current liability, and then we further have an interest adjustment to the end of the year on the basis of the current liability interest rate. Again, if you have a different rate for your funding valuation, you don't just determine the beginning of the year minimum and bring the whole thing to the end of the year. With the funding valuation rate this is supposed to have interest at the current liability rate. Kind of an interesting question here is then -- sort of in general, "How do you maintain the base on the old unfunded current liability amount?" Do you write it down by the actual payments? Do you continue to increase for interest? Do you just figure out at one time what that 18-year amortization is and continue to use that each year? It's not clear. Let's say in a year or two on down the road there is no unfunded current liability. So, there's no payment in that year. I think you have a couple of different options. In the following year you can either consider that to be wiped out. I don't think that that's clearly stated any place you can do that. You can, as I said, just go back to that same dollar figure that you had originally determined, add that in, or perhaps you could -- say that you want to maintain the 18 years, and it's going to be on the basis of some actual base that you've maintained which has not been decreased because you didn't make a payment last year. I'm not sure.

And then one of the last things on OBRA is the quarterly requirement (Chart 7). Those payments are required to be made 15 days following the end of each quarter. We have, again, an applicable percentage that we need to calculate. We applied an applicable percentage to a required annual payment, and we determine what that amount is. The applicable percentage is graded in over the transition period. It was 6.25% in 1989, and it'll be 25% in 1992. The required payment is the lesser of 90% of the current minimum or 100% of the prior year minimum. In determining what those minimum amounts are, we need to adjust for the credit balance and any contributions that were included in the credit balance that were not made, but basically what we do is determine the minimum without regard to the credit balance each year to figure out what that minimum amount is, then we apply the percentage, and then we can reduce the requirement by the amount of the credit balance but only to the extent that contributions that were used in determining that credit balance have actually been made. In other words, if you had put in a contribution that was due and accrued as of the end of the year for the prior plan year, if it hadn't actually gotten in as of the point that the quarterly contribution was required, you can't account for it.

There are penalties for the failure to make the required contributions. Basically, you have a new charge to the funding standard account that you didn't have before; there is an additional interest charge.

PANEL DISCUSSION

CHART 7

Quarterly Contribution Requirement

Payable April 15, July 15, October 15, January 15 for Calendar Plan Year
Applicable Percentage of Required Annual Payment
Applicable Percentages Grades from 6.25% in 1989 to 25% in 1992
Required Annual Payment = Lesser of:
(1) 90% of Current Minimum Requirement, or
(2) 100% of Amount Required for Prior Year
Adjust for Credit Balance, Accrued Contributions

There is availability of a lien if the deficit is very large. The most notable one is the requirement of a notice to all affected parties. If the contributions are not made, the OBRA 89 has added onto that a penalty of up to $100 per day per participant if those notices aren't sent out. And then the excise tax on the minimum has been increased as well from 5-10%.

Just quickly, a couple of the things that came out of the Technical Corrections Act of 1988. There was some clarification in a couple of different areas, how the $200,000 compensation limit was to be included basically under the -- it appears not only in the sort of benefit section of the code but also in the maximum deductible code that you can't use compensation in excess of the $200,000, and it was clarified that you are not to account for future cost-of-living increases on the maximum side. It was clarified -- the wording was not all that clear under OBRA. There was some wording in there about aggregating plans to determine -- and it was clarified that that was only to determine if you had the 100 employees or not for purposes of perhaps reducing the deficit reduction contribution. It was also clarified that if you had defined benefit, defined contribution plans, then the availability of an overall limit equal to the required minimum contributions -- was meant to be -- include the new requirement that you can contribute up to the unfunded current liability as well. And then it was clarified under what circumstances you were supposed to reduce assets for the credit balance and what circumstances you weren't. Basically, for minimum funding requirements you're supposed to, and for other purposes you're not.

I think I've already mentioned some of the things that came out of OBRA 89: $100 per day per participant penalty (Chart 8). It was clarified as to what the transition rule is supposed to be when we switch from 15-year to five-year gains and losses. Basically, you now have a lot of flexibility as to whether you want to use it over five years or 15 years or going from 15 to four years or whichever way you want to do it. There was some additional clarification on the treatment of contributions made after the end of the year as to how the 8.5 months are now part of the statute, as opposed to the other regulations. I think the other ones we've already talked about. We also have the new requirement for annual valuations.

That summarizes what we have.

MINIMUM REQUIRED AND MAXIMUM DEDUCTIBLE CONTRIBUTIONS

CHART 8

OBRA 89 -- Revenue Reconciliation Act

$100/Day/Participant Penalty
Amortization of Gains/Losses Recognized January 1, 1988
Contributions Made After Plan Year End
Penalty for Overstatement of Liability
When to Reduce Assets by Credit Balance
Annual Valuation Requirement

MR. JAN R. HARRINGTON: I have a question for Wayne. If you have to make quarterly contributions, how quick can you get your valuation out so you know what they have to be, and if you've already put in too much on an estimate, can you recharacterize employer contributions as employee contributions for sort of later in the year?

MR. BERNEY: It's generally not a problem to -- in making the contributions. The new rules about permissible contributions go into effect in 1991. So, we don't really know. Before, it was not a problem because the money could stay in the plan and didn't have to be withdrawn. There are no excise taxes or anything like that. There don't appear to be -- I'm not sure if there are anything like excise taxes, but the -- it's a provincial requirement for the quarterly contributions, not a federal one. It's going to be difficult to tell, to really determine whether that's going to be a problem. Most of the plans are pretty well funded by U.S. standards. So, I think that employers will go slow at first.