Pension Section News

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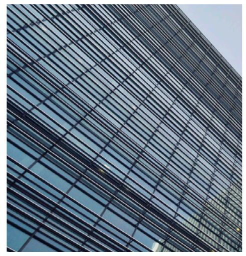
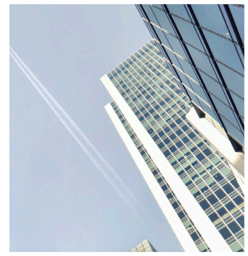
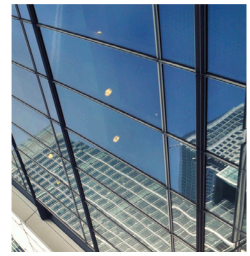
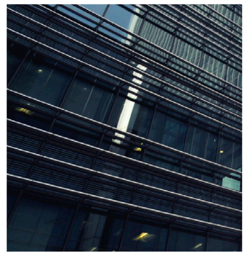

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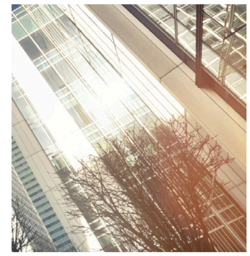

SEARCHING FOR REVENUE IN A VERY WRONG PLACE

By Mitchell I. Serota

Mike is a freshman at University of Illinois, majoring in actuarial science. He lives off I-294 and school is easily accessible from I-57. Looking at a map of northern Illinois, one can observe I-294 clearly intersecting I-57, but there are no ramps to connect the two. To get to school, Mike either has to backtrack on I-80 or exit the highway system for a two-mile stretch through a questionable neighborhood. By the time Mike is a senior, he will be able to glide from I-294 to I-57 via brand new ramps. He has MAP-21 to thank for his good fortune. Moving Ahead for Progress in the 21st Century, the official title of the law, was enacted July 6, 2012. Fundamentally, it is a highway and infrastructure improvement act, which brought relief to areas in desperate need of rehabilitation, most notably Appalachia.

Buried in the act's provisions was relief for defined benefit plan sponsors who were experiencing cash flow problems and could not afford to pay the minimum required contribution for 2012. Offsetting that relief was a quantum jump in PBGC premiums and variable rate premium rates. Why were all these provisions mixed together? Because any legislation enacted by Congress has to be "revenue neutral." That is, if Congress is going to spend additional money, there has to be a source of revenue to pay for the spending. For better or for worse, the Republicans have convinced the Democrats that no bill without revenue neutrality can ever be passed by Congress.

In MAP-21, the appropriation for highway improvements is $80 billion. Without these funds, the Highway Trust Fund would have been depleted. Transit systems are allocated $20 billion. Add other infrastructure needs, Federal Lands Transportation Projects, disadvantaged business enterprises, hazardous waste, etc. and the total

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outlays for MAP-21 amounted to $118 billion. Some revenue to pay for these improvements is referenced in Title II of the Act, "Pension Funding Stabilization." Buried in legislation otherwise devoted to transportation, the Act amended the Internal Revenue Code to stabilize segment rates. There was some logic, Congress-style, to link the two.

The intent to provide defined benefit plan funding relief is specifically stated in the conference report: "The plan sponsor may contribute less money to the plan when interest rates are at historical lows." By contributing less money, corporations deduct less on their corporate income tax, which, as a result, increases revenue to the federal government. But upon reflection, the corporate plan sponsors that are taking most advantage of this relief to reduce their contributions are the ones facing cash flow problems. Might this group be paying little or no corporate income tax anyway, because they are operating in or close to a deficit? Moreover, the SOA has clearly demonstrated that the afforded relief in the first few years will be totally dissipated and reversed by 2017, meaning that minimum required contributions will increase and corporate income tax receipts will decline commensurately.[1]

Immediately following the provisions for relief to plan sponsors was the hike in PBGC premiums. The PBGC charge per person jumps from $30 in 2012 to $49 in 2014. The charge would increase with inflation thereafter. The variable premium rate of $9 per $1000 of Unfunded Vested Liability increases to $19 in 2015. But there is a leveraging effect to also consider. By reducing the minimum required contribution in the first five years, the act provides incentive for pension plans to become more unfunded by the amount of that reduction, relative to where they would have been without the act. Between these two provisions, revenue for this program from defined benefit plans has been estimated at $18 billion.[2]

MANY POLICYMAKERS AND OTHERS HAVE FORGOTTEN TO TAKE A MACROECONOMIC VIEW. BUDGET SCORING USING "TAX EXPENDITURES" HAS CHANGED THE WAY CONGRESS THINKS ABOUT EMPLOYEE BENEFITS AND FINANCIAL SECURITY.

But this MAP-21 story is so 2012. Last year, under the guise of a "Bipartisan Budget Act of 2013," Congress went back to the same till for revenue. The rate of $19 per $1000 of underfunding is now set to increase to $29 in 2016, from $9 in 2013. And the fixed rate of $49 per participant jumps to $64 per participant in 2016. The increase in revenue is estimated at $7.9 billion over 10 years.[3]

As a profession, we have been here before. Recall the Retirement Protection Act of 1994, which was part of The General Agreement on Tariffs and Trade (GATT) enabling legislation. (Back then, Congress was mixing pensions with tariffs and trade.) As stated in 1995 in *The National Law Journal*, "The purpose of the act's pension reforms is to help the government raise some of the money lost due to lower tariffs under GATT. Whether revenues increase will depend on how well the government anticipated taxpayer response to the changes. The reforms impose increased plan funding and management costs on employers and their success will depend on the ability of employers to bear the added burden. Enough plans could be terminated that government revenues would decrease rather than increase."[4]

The warning in 1994 was as clear as it was prescient. There was little to no outcry, because there was at least some cover of protecting retirement plan sponsors. MAP-21 also provided relief which was desperately needed at the time. But the bipartisan budget gratuitously enacted punitive measures against defined benefit plans. Plans will be forced to pay 2.9 percent of their underfunding using *PBGC* segment rates of course, not the *IRS* segment rates which afforded the relief. Overfunded plans, presumably with much less risk, are not granted any reduction in premium.

As applied to defined benefit plans, this whole procedure of "revenue neutrality" is a farce. Rather than acknowledge that the Highway Trust Fund is an investment in the future which needs periodic replenishment, Congress plays ridiculous games to make it appear that there is actually money to pay for it by taxing defined benefit plan sponsors.

Even now, Congress is invoking the same contorted logic as GATT, MAP-21 and the BBA to increase revenue at the expense of retirement plans. To pay for an unemployment benefit extension, Senate Bill1845 proposes giving defined benefit plans additional funding relief with PBGC premium increases. Simultaneously, the latest budget proposal seeks to limit the amount that a defined contribution account can grow over the course of one's working lifetime. That provision would raise $28 billion to fund the President's infrastructure and job-training package.

As before, the projected revenue increases are mythical. In theory, at least, they remain bipartisan. "There isn't really much of a partisan difference in the types of gimmicks each side prefers, though Republicans tend to prefer those that produce revenues on paper without actually increasing taxes and Democrats prefer those that appear to reduce spending without actually cutting spending."[5]

Michael's mother is sincerely pleased that the highways are getting fixed to alleviate his travel to school and back. But she also knows that the burden for these improvements is being carried on the back of the ever weakening defined benefit pension system. Her advice to Congress is the same as her outcry to Michael and his brothers during their interminable horse play: "CUT IT OUT!" ■

ENDNOTES

1. http://www.soa.org/research/research-projects/pension/proposed-pension-funding.aspx
2. http://www.transportationissuesdaily.com/cheat-sheet-for-map21-new-federal-transportation-bill/
3. http://www.cbo.gov/sites/default/files/cbofiles/attachments/hr4348conference.pdf
4. http://www.readabstracts.com/Law/US-pension-law-reform-under-GATT-Retirement-Protection-Act-trims-benefits-in-Congressional-effort-to.html#ixzz2uOxUeMs8
5. http://www.rollcall.com/news/for_budgeting_tough_accounting_for_gimmicks-230991-1.html?pg=2