NRLN
NATIONAL RETIREE
LEGISLATIVE NETWORK

Pension Asset Protection (PAP)

Limiting the Use of Pension Assets for Severance Will Strengthen Defined Benefit Retirement Security

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Talking Points:

The use of pension assets to pay for lump sum severance payments during a corporate restructuring is a “back door reversion” that circumvents the Congressional policy against reverting pension assets to pay corporate operating expense. Severance, layoff or other lump sum benefit increases to terminating individuals should be paid out of the company’s operating expenses, not from the pension trust, unless the pension plan has a substantial surplus.

Congress should require that any ad hoc plan amendment that gives a subset of participants a benefit increase payable in the form of a lump sum must be immediately funded *if* the plan’s adjusted target funding level is (a) less than 120% or (b) would be less than 120% after taking into account the cost of the amendment.

Although ERISA explicitly prohibits the use of qualified pension assets for “layoff benefits,” companies can amend a plan at any time not only to offer older workers enhanced early retirement benefits (by awarding extra years of service credit), but even to offer lump sum severance payouts equal to a year’s salary or more as part of a corporate restructuring.

The 2006 Pension Protection Act limited this practice somewhat by requiring plan sponsors to pre-fund a plan amendment that increases benefit liabilities to the extent the plan’s funding level would fall below 80%. However, as the 2008 stock market meltdown demonstrated, a plan that is 80% funded during a bull market could end up below 60% funded in a bear market – and in default with the Pension Benefit Guaranty Corporation (PBGC) if the plan sponsor declares bankruptcy.

The most effective way for Congress to protect retirees and other plan participants is simply to **amend Internal Revenue Code section 436(c) [and ERISA Section 206(g)] to require that any ad hoc plan amendment that gives a subset of terminating participants a benefit increase payable in the form of a lump sum must be immediately funded *if* the plan’s adjusted target funding level is (a) less than 120%, or (b) would be less than 120% after taking into account the cost of the amendment.**

In addition, plan sponsors should be given more flexibility concerning the use of surplus assets (e.g., assets greater than 120% of vested obligations). The NRLN recommends that **Congress amend ERISA to permit the reversion of any surplus assets above 120% funding for any purpose that solely benefits plan participants (including early-out payments and funding health and welfare benefits), or for reversion to the company for any purpose if 50% of the reversion amount is distributed as a one-time benefit enhancement to all vested plan participants on a *pro rata* basis** (e.g., a 2% monthly benefit increase).

For a copy of an NRLN whitepaper on this subject, contact Alyson Parker at 813-545-6792 or executivedirector@nrln.org