AMERICAN ACADEMY *of* ACTUARIES

May 2, 2012

Dear Conferees:

The American Academy of Actuaries[1] Pension Practice Council respectfully requests your consideration of the following comments regarding Sec. 40312, Pension Funding Stabilization of the MAP-21 Act (S.1813). The council acknowledges funding stabilization is a complex issue that must strike a balance among pension security, stability of contributions, and broader economic issues.

The Pension Protection Act of 2006 (PPA) established a funding target based on accrued benefits discounted at corporate bond interest rates. PPA permits averaging this rate to dampen the effect of volatility but limits the averaging to 24 months to assure that the resultant rate does not deviate significantly from current market rates. Proposed Sec. 40312 would add a corridor based on the 25-year average of corporate bond rates. Given the current low interest rate environment in which we now find ourselves relative to the last 25 years, the corridor would apply, increasing the current discount rate and lowering required contributions for 2012. When compared with current law, the proposed approach would be expected to have an effect for several subsequent years.

Under the Sec. 40312 approach, stabilizing contributions occurs by smoothing inputs (discount rates). This addresses an expressed concern about the current interest rate environment, that rates are too low. Although current rates are at historically low levels, they nevertheless reflect the current market. Liabilities determined using current rates (without the corridor) do approximate the amount necessary today to settle pension obligations or to structure a low-risk portfolio that funds the obligation, so they are meaningful in understanding a plan's funded status. Amounts determined using a 25-year average might be useful as an interim input to smooth current funding contributions. But these amounts are insufficient to settle obligations or fund obligations with a low risk portfolio and do not provide meaningful information about the current funded status of the plan.

To the extent the conference committee chooses to include in its conference agreement pension funding changes to create more stability in contributions, the Pension Practice Council believes this could be accomplished better by smoothing outputs (contribution requirements) rather than inputs (discount rates). Doing so would preserve the disclosures of current funded status and

[1] The American Academy of Actuaries is a 17,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

would provide a clear and transparent measurement of the contribution reductions, which could be uniform or scaled as Congress considers appropriate.

Stabilization of required contributions could be implemented by adopting a “stabilization collar” on the minimum funding requirement, changing the amortization period or method, or implementing similar measures. Benefit restrictions based on funded status could be addressed, if desired, by changing temporarily the 60 per cent and 80 per cent thresholds. Dealing with contributions and benefit restrictions directly preserves the meaningfulness of funded status levels, which are used for multiple purposes.

Notwithstanding the merits of smoothing outputs, if the smoothing of inputs is pursued, the council recommends maintaining disclosure of the funded status under the existing PPA assumptions. This will provide plan sponsors, plan participants and other interested parties with useful and relevant information.

The Pension Practice Council appreciates the opportunity to provide input on these important issues. We would be happy to discuss any of these items with you at your convenience. Please contact Jessica M. Thomas, the Academy’s senior pension policy analyst (202-785-7868, thomas@actuary.org) if you have any questions or would like to discuss these items further.

Sincerely,

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