Client Alert

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The IRS does an "About-Face" on Restricting a Key Pension Plan De-Risking Strategy

If you are looking for options to lower your annual PBGC premiums and reduce overall pension liability (including plan termination liability), a retiree lump-sum window may again be a viable option. De-risking strategies are methods a company can implement to reduce its pension plan's administrative expenses, PBGC premiums and overall pension liability.

Prior to 2015 and the issuance of IRS Notice 2015-49, a common practice for pension plans to decrease their funding requirements, PBGC premiums and overall pension liability was to offer a "lump-sum window" to retirees who were already in pay status and receiving monthly payments from the plan. For some retirees (especially those with small monthly payments), it was a welcomed offer—they could elect to receive a lump-sum payment equal to the "present value" of their estimated future monthly payments and invest those amounts for future needs or use the lump-sum payment to cover much-needed expenses. For the company sponsoring the lump-sum window, it was an opportunity to decrease annual PBGC premiums (which are, in part, based on the number of participants) and lower the overall future pension liability (particularly upon plan termination, which can be a factor in a company's merger/acquisition favorability). For those retirees who elected the lump sum, it was a win-win for both the retiree and company.

But in 2015, the IRS issued Notice 2015-49 stating that this lump-sum window, if not offered in conjunction with a plan termination or other limited circumstances, could violate Code Section 401(a)(9), which deals primarily with minimum required distributions. It would seem odd that offering a lump sum would violate Code Section 401(a)(9), since those rules generally restrict a participant from postponing and not accelerating retirement benefits or receiving such small amounts of retirement benefits that the retirement benefits result in more estate planning and death benefits (and are not serving their purpose as retirement benefits). But, the regulations issued under Code Section 401(a)(9) also limit a pension plan from making changes to current monthly payments. It is based upon this limitation that the IRS issued Notice 2015-49 and essentially halted the practice of pension plans' seeking to offer lump-sum windows to retirees currently receiving benefits outside specific circumstances. But now the IRS has issued Notice 2019-18 (found here), overturning its prior guidance and allowing properly designed retiree lump-sum window programs to be used again going forward (outside of a plan termination).

If decreasing PBGC premiums and pension plan liability is your goal, consider the following options:

- Offer a limited 30- to 60-day window to current payees in your pension plan the opportunity to elect to receive a lump-sum payment. No further payments, statements or other disclosures to these participants would be necessary.
- If your company is paying high PBGC variable premiums, consider options for making additional payments to the plan to reduce these payments.
- Look to purchase an insurance annuity contract for certain groups of participants.
- Review distribution provisions in your plan to see if your plan contains limitations lump-sum distributions and whether these limitations may be increasing your annual PBGC premiums.
- Review administrative costs associated with terminated vested participants and consider options for decreasing such costs.

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The attorneys at Hunton Andrews Kurth LLP can assist you with considering and implementing these options as well as other compensation and benefits matters.

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