Strategies to Reduce PBGC Premiums

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The PBGC, or the Pension Benefit Guaranty Corporation, is a U.S. government agency responsible for protecting the retirement incomes of private sector employees with defined benefit plans.[1] One can think of the PBGC as an insurance company for pension plans. To help achieve its mission, the PBGC collects annual premiums from pension Plan Sponsors of single employer and multiemployer plans. This article addresses the premiums for single employer plans.

Each plan's annual premium is comprised of two parts: the per participant rate, better known as the Flat Rate Premium, as well as the Variable Rate Premium which is based on each individual plans' unfunded vested benefit. The Flat Rate Premium is set at $101 per participant for plan year 2024. Over the past ten years this has doubled from $49 per participant in 2014. The Variable Rate Premium for plan year 2024 is set at $52 per $1,000 (or 5.2%) of unfunded vested benefit up to a cap of $686 per participant. This has also seen large increases over the past ten years, ballooning from $14 per $1,000 (1.4%) of unfunded benefit with a cap of $412 per participant in 2014.[2]

Unlike required minimum contributions, PBGC premiums do not help improve the plan's funded position but instead are comparable to tax on the plan. So, the question many Plan Sponsors are asking (or should be asking) is "can anything be done to reduce these premiums?" Fortunately, for many Plan Sponsors, the answer is 'yes'!

Premium Reduction Opportunities

Let's review a few of those considerations. First, reducing the number of participants in the plan will reduce the flat rate premium as well as the variable premium if the plan is above the variable premium cap, all else equal. Strategies to reduce the number of participants include instituting or increasing the lump sum force out limit up to $7,000, thanks to the SECURE Act 2.0.[3] However, this may not yield significant savings. Alternatively, Plan Sponsors could also consider offering a one-time lump sum

[1] https://www.pbgc.gov/about/who-we-are
[2] https://www.pbgc.gov/prac/prem/premium-rates
[3] https://www.bloomberglaw.com/external/document/XDO6N2SC000000/retirement-benefits-professional-perspective-secure-2-0-provisio

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window to participants who are no longer active, and/or transferring the future payments to participants currently receiving a benefit to an annuity provider to reduce headcount.

A quick and relatively straightforward strategy is to pay the required quarterly contribution early. For instance, for calendar year plans, consider paying the October 15 required employer contribution by September 15 (i.e., the plan's Form 5500 regular due date). By moving up this payment by one month, the PBGC will consider these assets in their calculations of the plan's funded position. For plans below the per participant cap, this will likely reduce the variable premium due. For calendar plans, this could equate to a return of 5.2% on the amount contributed just one month sooner.[2]

Other strategies are more complex but can generate potential savings. These include changing the method by which the discount rate is selected for calculating the PBGC variable premium (Standard vs Alternative methods). Historically, most Plan Sponsors have utilized the Alternative method, which allows for the use of 24-month average discount rates within a corridor around 25-year average interest rates. Up until recently these rates had been higher than the rates used under the Standard method (interest rates averaged over the one-month period prior to the valuation date). However, with the current elevated level of interest rates, the two rates have now converged, and switching to the Standard method may lead to lower liability valuations and therefore lower PBGC variable rate premiums.

When making potential changes sponsors should keep in mind that changing the election from either the Standard or Alternative Method locks in that method for the next five years. However, sponsors that made a change within the past five years also have the option of changing to the "Full Yield Curve" method for funding calculations, which will then be used for calculating PBGC variable premiums. Similar to the Standard method, the Full Yield Curve election uses the yield curve as of the valuation date to value the plans liabilities. This change, however, is permanent and should be evaluated carefully.[4]

Paying PBGC premiums can be financially painful, create frustration and even lead to a sense of helplessness for Plan Sponsors; however, there are strategies that can help manage and control costs going forward. Working in collaboration with the plan's actuary can lead to better outcomes for the plan and its participants. Please reach out to your consultant for more information and how Fiducient Advisors can help.

Please visit fiducientadvisors.com for more information about our defined benefit practice as well as information on our firm and the markets.

[2]https://www.pbgc.gov/prac/prem/premium-rates
[4] https://www.milliman.com/en/insight/should-you-switch-standard-method-2023-pbgc-premiums)

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About the Author

Matt services institutional clients by providing counsel and guidance on portfolio design, asset allocation, manager selection, investment policy statements and performance monitoring. Matt also serves on the firm's Defined Benefit Business Council. He joined Fiduciary Investment Advisors, LLC in 2014, which combined with Fiducient Advisors in 2020. He received a BA from Assumption College and enjoys playing hockey and golf in his free time.

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