ASYMMETRICAL PENSION RISK AND OPTIONS FOR USING SURPLUS

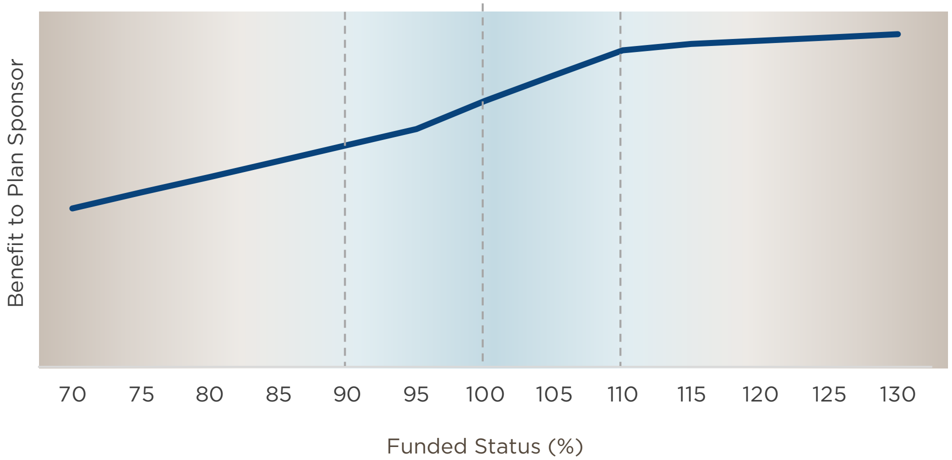
The recent market environment has propelled many defined benefit (DB) plans to an overfunded position. While shifting to a lower-risk asset allocation and maintaining a hedge ratio of close to 100% could reduce the risk of surplus volatility, how to use this surplus could be puzzling. A partial or full pension risk transfer (PRT) is one approach, but if the plan is terminating, any excess reversion to the sponsor would be subject to an excise tax of 20 to 50%.

ASYMMETRICAL PENSION RISKS

Past a certain point, surplus adds little benefit. But the associated risks are greater when funded status drops below 100%.

- Higher PBGC variable-rate premium
- Possibly higher contributions
- Negative valuation implications

- Increased safety net
- No variable-rate PBGC premium, but no savings in flat-rate premium without a PRT
- Hedge ratio possibly greater than 100%



Source: Capital Group

STRATEGIC OPTIONS FOR USING SURPLUS

ANYTIME BEFORE PLAN TERMINATION		ONLY AFTER PLAN TERMINATION
STRATEGIC TRANSACTIONS	OTHER POST-EMPLOYMENT BENEFITS (OPEBS)	QUALIFIED REPLACEMENT PLAN (QRP)
• A company may have two DB plans or acquire a company with an underfunded plan. • Two plans could be merged and the surplus used to improve an underfunded plan, or two trusts could be merged with no physical transfer of assets.	• The surplus could be used to fund OPEBs like retiree medical, life insurance, etc. • Transfer of funds to an OPEB plan requires a separate actuarial valuation of OPEB benefits.	• Surplus can be transferred to a QRP, such as a 401(k), 403(b), or DB plan from the same sponsor. • The sponsor could establish a new QRP.