



GATT COULD REDUCE YOUR PENSION PAYOUT

Your future retirement benefits could soon be reduced—if they haven't been already—by GATT.

You may vaguely remember those initials. They stand for the General Agreement on Trade and Tariffs, a world-trade agreement among nations. When the U.S. Congress passed enactment legislation back in late 1994 for its participation in GATT, it tucked in a little-noticed provision called The Retirement Protection Act. The impact of that act is coming due for retirees at the turn of the millennium. If you belong to a company defined benefit pension plan, the act, among other things, could affect your decision whether to retire early or to take an annuity or a lump sum payout at retirement.

Here's how. People who belong to a pension plan most commonly choose to annuitize their payout. The GATT legislation does not affect annuity payouts. It only affects the second major payout option, the lump sum.

Not all pension plans offer a lump sum option, but many do. Some require a lump sum payout if a participant is owed only a small amount when leaving employment. A lump sum represents the "present value" of your annuity payments—that is, the size of the lump sum is based on what the lump sum needs to earn at a certain interest rate, so that the total of the lump sum and the interest earned equals what the retiree would have received in expected total annuity payments. (This assumes, by the way, that you invest the lump sum, not spend it.) Thus, the size of the lump sum depends not only on your age, life expectancy, number of years you worked with the company, salary, and so on, but on what interest rate the plan assumes.

This is where GATT figures in. Generally, pension plans have used interest rates set monthly by the federal Pension Benefit Guaranty Corporation. But under GATT, plans can start using the interest rates set by 30-year Treasury bonds to calculate the lump sum. Interest rates for Treasury bonds typically have been *higher* than the PBGC rates—roughly 1.75 percent higher annually the last few years. A higher interest rate assumption translates into a smaller lump sum payout because the payout is expected to earn more over the subsequent years.

These smaller lump-sum payouts are slightly offset by GATT legislation requiring employers to use a longer standardized mortality table. The longer the employee's life expectancy, the more money the employer must put into the plan.

The precise impact of this change on individual plan participants will vary depending on the interest-rate assumption of the plan and on the worker's age, years of service and other factors. But here are some examples, based on one plan, of just how much a future retiree might lose. A 60-year-old who would receive a lump sum payout of \$84,900 under recent PBGC interest rates would receive a lump sum of only \$74,500 under a GATT rate that is 1.75 percent higher. That's a payout loss of 12 percent. A 30-year old who might receive a lump sum of \$5,300 under PBGC rates would get only \$2,600 under GATT rates—a 51 percent loss!

Pension plans have until the year 2000 to amend their plans according to the new GATT rules. They can use the Treasury bond rates or lower rates (which means a larger lump sum payout for the retiree). Many plans have already adopted the Treasury bond rates because they mean smaller payouts. Other plans haven't decided yet what rates they will adopt, but they may provide only short notice to employees once they do decide.

Employees may have to make some tough decisions. First, if you are thinking of retiring soon, and you learn that the plan intends to adopt the Treasury bond rates, an early retirement under the old PBGC rates may be a better choice than waiting. If retirement is a ways off, or your plan has already adopted the GATT rates, you may need to decide whether it is more beneficial to take an annuity option than a lump sum. Your Certified Financial Planner professional can help you run the numbers to decide which option is best for you.

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