Current contributions made in excess of the minimum required amount can be added to a “Prefunding Balance”. The Prefunding Balance is adjusted for earnings each year, using the actual earnings rate on plan assets for the year.

Following are some of the rules surrounding Prefunding Balances. For simplicity, the due dates shown below are for a calendar year plan. In addition, we have not attempted to describe the requirements that allow a sponsor to apply Prefunding Balances to quarterly installments and have excluded specific discussion for pre-PPA carryover balance accounting.

- In order for a plan sponsor to add to a Prefunding Balance as of January 1, the sponsor must provide a written election to the plan’s actuary no later than September 15 of that year. The election must include the specific dollar amount to be added to the Prefunding Balance. If the actuary has not yet calculated the interest discounting on your contributions for the prior plan year, you will not know the exact amount available. We frequently receive information on deposit dates and amounts too late to do this calculation in time to be of use.

- In order for a plan sponsor to use a Prefunding Balance toward minimum funding requirements for the current plan year, the Funded Ratio Percentage in the prior plan year must be at least 80% and the sponsor must provide a written election to the plan’s actuary no later than September 15 of the following year, including the specific amount to be applied. As noted above, if we have not calculated the interest discounting on contributions already deposited, you will not know the exact amount required.

- Certain measurements and disclosures use the ratio of the value of the plan’s assets reduced by any Prefunding Balances to the value of the plan liabilities. Because Prefunding Balances reduce these ratios, a sponsor may decide to voluntarily waive all or a portion of the balances. The affected ratios may be disclosed to plan participants, and may determine whether quarterly installments are required. In order for a plan sponsor to waive a Balance as of January 1, the sponsor must provide a written election to the plan’s actuary no later than December 31 of that year. The election must include the specific dollar amount to be waived.

- In certain circumstances, the law requires that a portion of any Prefunding Balance be waived, if that waiver will prevent funding-based benefit restrictions from going into effect. (Because Prefunding Balances reduce the assets used in the funding ratio, waiving a balance will increase the funded ratio.) Also, if the plan’s funded ratio is less than 80% in a given year, the sponsor is not permitted to apply any portion of a Prefunding Balance to the next year’s funding requirements. Even if you elect to maintain Prefunding Balances, you may not be able to keep them or use them when you want to.

Note that most elections are irrevocable once made.

The implications of waiving a Prefunding Balance will vary depending on the circumstances of the plan. For example, the minimum funding requirement (before application of any Prefunding Balance) will be reduced by roughly 15% to 20% of the amount of the Prefunding Balance waived. If the Prefunding Balance cannot be applied to minimum funding because the prior year funding ratio was less than 80%, then waiving is the only way to reduce the current year’s minimum required contribution.

If you would like further clarification, or want to discuss the effects of waiving any Prefunding Balances you may currently have, please contact your IAI consultant.