

Analysis of future effects of Pension Protection Act

The AMO Pension Plan and the AMO 401(k) Plan continue to review the requirements for implementing changes required under the Pension Protection Act (PPA), while the Internal Revenue Service (IRS) continues to issue guidance and some temporary relief. Below is a discussion of some of the changes, and the interim relief provided by the IRS.

DISTRIBUTION CHANGES

Many of the PPA changes are beneficial. Non-spouse beneficiaries will now be able to rollover distributions into an IRA money purchase benefit and 401(k) account. Participants and other beneficiaries will be able to rollover distributions into a Roth IRA. Participants in the 401(k) Plan will be able to take hardship distributions for medical, tuition, and other permitted expenses of their designated beneficiary, even if that beneficiary is not their dependent spouse or child. And in light of certain PPA changes, the Trustees have decided to amend the Pension Plan to provide a 100 percent joint and survivor annuity and 100 percent pre-retirement survivor annuity for all married participants.

NORMAL RETIREMENT AGE

The PPA also amends the Internal Revenue Code to specifically allow for payment of pension benefits upon attainment of age 62 even if the participant does not retire. While this is a positive change for many whose plans do not currently allow for in-service distributions, it may not be a positive one for our Plan. The reason for this is that the implementing regulations provide that the normal retirement age under a plan must not be earlier than the earliest age that is reasonably representative of the typical retirement age for the particular industry. A normal retirement age of 62 or above is deemed to be reasonable; a good faith determination by Plan Trustees that a normal retirement age between 55 and 62 is reasonable will be given deference; but a normal retirement age below age 55 is presumed to be earlier than the earliest age that is reasonably representative absent approval by the IRS. Since a participant in the AMO Pension Plan could retire prior to age 55, and could receive an in-service lump sum distribution prior to age 55, it will be necessary to either limit in-service distributions to participants who are at least age 55, or seek an IRS determination that the current retirement age under the Plan is reasonably representative of the typical retirement age for the maritime industry. The consensus of the Trustees is that "if a valid position can be stated, the Trustees will seek an IRS determination that our current retirement age (age + years of service equals 75) is reasonably representative of the typical retirement age for the maritime industry." If the IRS agrees with the Plan's position, the In Service Lump Sum distribution will continue to be available when a participant's age plus their years of service equal 75. If the IRS does not agree, the Plan will be forced to limit In Service Lump Sum distributions to participants who are at least age 55 or older.

Delayed Effective Date: Fortunately, we have some time to make this determination. The change made by the PPA in the definition of normal retirement age is not effective

for the AMO Pension Plan until the plan year beginning October 1, 2010. The IRS has issued various guidance that gives the Trustees at least until that time to amend the Plan or make a good faith determination that no amendment is required. If no amendment is made and the IRS ultimately determines that the Plan's definition is not reasonably representative, an amendment increasing the retirement age will need to be made, but any change will not be effective prior to October 1, 2010, and possibly later.

LUMP SUM BENEFIT

The other PPA change of critical concern to participants is the change in the assumptions to be utilized in calculating lump sum benefits. The AMO Pension Plan has allowed for lump sum payments since 1988. Since that time, there have been numerous changes in the laws governing lump sum payments. Initially, Plans had a great deal of flexibility in setting and changing the factors used to calculate lump sum amounts. (The lump sum is determined by converting a life annuity to a single payment, taking into account the expected future investment return on the money and the participant's life expectancy). Later, the IRS restricted the ability of Plans to change the lump sum factors, and eventually Congress legislated specific factors to be used. The Pension Plan was required to adopt the statutory lump sum factors, and has consistently done so, although the latest factors have resulted in the Plan paying higher lump sum amounts than was originally contemplated.

Congress recognized that the use of the statutory 30-year Treasury Rate was resulting in inflated lump sum amounts, and a corresponding drain on plan assets, and tried to address this problem in the PPA by modifying the applicable interest rate and mortality table. Since the effect of the interest rate change will generally be a reduction in lump sum payments, Congress provided for implementation of the change over a five-year period. The new basis will reduce the inflation of the lump sum amounts produced by the current methodology and subsequently reduce the drain on plan assets. As participants accrue additional credit and the Plan is sufficiently funded to move forward the wage freeze, which benefits all participants, the impact will be less.

While there has been discussion over the need to use the new PPA factors, the AMO Pension Plan has consistently utilized the legislatively mandated factors, and to do otherwise would result in the Plan subsidizing the lump sum benefit. In addition, there are a number of other, interrelated regulatory requirements that need to be considered. For example, the law requires that the joint and survivor benefit be the most valuable benefit under the Plan. If assumptions other than those required under the PPA were used, the Plan would be required to perform multiple calculations to ensure that the joint and survivor benefit continues to be the most valuable and could potentially be required to increase the amount of that benefit, further impacting the funded status of the Plan, and its ability to offer lump sum payments. This is one of the reasons the Plan has consistently utilized the statutory factors. A current estimate of cost to subsidize the lump sum is in excess of \$30 million dollars. The actuary estimates that the subsidy would be significantly higher because the Plan will be required to increase the joint and survivor benefit. The increase in cost to utilize the mortality table required by law will be

approximately \$12 million dollars.

Relief until October 2010: Once again the AMO Pension Plan has caught a bit of a break. Because the Plan has an October 1 thru September 30 plan year, implementation of the change in lump sum factors does not begin until October 1, 2008, and the change will not be fully effective until the plan year beginning October 1, 2012. Moreover, the IRS has now announced interim relief that will allow the Trustees to amend the Plan to provide that until October 1, 2010, lump sum benefits will be calculated at the more favorable of the amount calculated using the pre-PPA applicable interest rate and mortality factors, or the amount calculated using the post-PPA applicable interest rate and mortality table. Under the IRS ruling, the Plan will not fail to satisfy the most valuable benefit requirement discussed above during this interim period, but the special treatment will not apply after September 30, 2010. This means that our Plan will be required to utilize 60 percent of the new factors and 40 percent of the 30-year Treasury Rate as of October 1, 2010. As of October 1, 2011, the Plan will be required to utilize 80 percent of the new factors and by October 1, 2012, 100 percent of the new factors.

The Pension Plan will continue to track developments as the various changes under the PPA become effective, and will keep participants advised of any changes.