Comments on Benefit Determinations for Cash Balance and Hybrid Plans at Plan Termination

March 7, 2001

Office of the General Counsel
Pension Benefit Guaranty Corporation
Suite 340
1200 K. Street, N.W.
Washington, D.C. 20005-4026

Re: Comments on Benefit Determinations for Cash Balance and Hybrid Plans at Plan Termination

Dear General Counsel:

ASPPA is a national organization of over 4,000 members who provide actuarial, consulting, administrative, legal and other professional services for about one-third of the qualified retirement plans in the United States, the majority of which are maintained by small businesses. ASPPA's mission is to educate pension actuaries, consultants, administrators and other benefits professionals and to preserve and enhance the private retirement system as part of the development of a cohesive and coherent national retirement income policy. Its large and broad based membership gives it unusual insight into current practical problems with ERISA and qualified retirement plans, with a particular focus on the issues faced by smaller employers.

The PBGC has requested that ASPPA comment on how to make benefit determinations for cash balance and hybrid plans at plan termination.

The PBGC has been analyzing the termination (and anticipated termination) of underfunded cash balance plans. As part of the termination process, it is necessary to estimate the present value of benefit liabilities. This calculation does not just affect the money that a sponsor owes the PBGC. It can also affect what the plan participants receive under ERISA 4044.

In a cash balance plan, the actual value of the applicable index (*e.g.*, 30-year Treasury rates) determines the accrued annuity benefit payable at normal retirement age from the current cash balance. The specific calculation, which is the problem, is the very determination of the accrued benefit which is payable as a qualified joint and survivor life annuity. Ongoing plans do not have a problem as it is simple to determine the actual index at the point in time that a benefit is paid. However, a terminating plan can only estimate the accrued annuity benefit since the actual value of the index at normal retirement age can only be estimated. When a plan does not have language in the document adequate to describe the procedure after plan termination, the burden falls on the Plan Administrator or, in the case of a distress termination, the PBGC to calculate the accrued annuity benefit.

One might think that since the PBGC only has to pay deminimus lump sums (under $5,000) under a distress termination, that the problem is minimal. That is not so. There is a problem with how the PBGC regulations say to pay deminimus lump sums. First, apply the variable rate index to get a benefit at NRA; then use PBGC lump sum assumptions to get the prevent value. If the value is less than $5,000, then the PBGC can pay a lump sum; if not, then PBGC can't. Importantly, this value will be different than the cash balance account balance. A change in the regulations would be needed to get a different result.

The determination of the estimated index in the calculation of the accrued annuity benefit can also have a large effect on benefit liabilities, on the allocation of assets at plan termination, and finally on what amounts participants are allocated under ERISA 4044. Furthermore, without any certainty as to the index, it is impossible to give participants a firm idea of their accrued annuity benefit until actual retirement.

ASPPA suggests that one way to manage the problem is to have the IRS require adequate Plan language to spell out what happens to a variable index on plan termination or, perhaps, to indicate that 411(d)(6) protection does not apply to changes in the determination of the rate future interest credits, so long as the new rate is not less than the old rate as of the date of the change (both the effective date and the adoption date). An incentive for the first approach would be for the IRS to give plans with such language a swifter determination letter process at plan

termination.

Without adequate language in the Plan document, the PBGC must still act in its best judgment in order to fulfill its responsibilities under ERISA and to each Plan and Plan participant. While it can be argued that the PBGC must be allowed, under the law, to have adequate discretion to make a reasonable judgment on the issues without being subject to undue review, many of the same issues can also be faced by a plan sponsor when a plan satisfies the criteria for a standard plan termination. In such cases, the Plan Administrator must be able to precisely determine each participant's accrued benefit so as to be able to inform the participants and, of course, to pay benefits. In these circumstances, the decision of the administrator may be questioned. Thus it would be most helpful to the formation of cash balance plans (and defined benefit plans in general) to be able to address these issues with some certainty.

In order to assist the PBGC and Plan Administrators, it would be helpful for the IRS and Treasury to provide adequate latitude to allow terminating plans to deal effectively with the issues of 411(d)(6) protection, definitely determinable benefits, and back-loading concerns.

Considering that cash balance plans which allow Participants to elect which index to use for their cash balance account are being anticipated, some method of dealing with the issues under "simpler" cash balance plans must be found.

These comments are filed on behalf of ASPPA by Kurt Piper, Chair of the PBGC subcommittee, Brian Graff, Executive Director, R. Bradford Huss and Bruce Ashton as Co-chairs of ASPPA's Government Affairs Committee, and Teresa Lensander, Chair of the Administrative Relations Committee.

Sincerely,

Kurt Piper, MSPA,
PBGC Subcommittee

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