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# Congress of the United States

## U.S. House of Representatives

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September 26, 2007

The Honorable Henry M. Paulson, Jr.  
Secretary of the Department of the Treasury  
1500 Pennsylvania Avenue, N.W.  
Washington, D.C. 20220

Dear Mr. Secretary:

We are writing to seek your assistance regarding the Internal Revenue Service's application of the anti-backloading rules to hybrid pension plans. This issue impacts many of our constituents, including employers who offer these plans and the workers participating in them.

As you know, the Pension Protection Act of 2006 ("PPA"), signed into law on August 17, 2006, addressed the rules applicable to cash balance and other hybrid pension plans. Changes were enacted to provide legal certainty to sponsors of traditional defined benefit plans who may convert to hybrid pension plans, and to protect longer-service workers when a conversion occurs.

In one change from prior law, the PPA provides that on or after June 29, 2005, in any conversion from a traditional pension plan to a cash balance plan, a participant's accrued benefit after the plan amendment can be no less than the participant's accrued benefit prior to the conversion, plus the participant's accrued benefit under the cash balance or hybrid pension plan for years of service after the conversion. This requirement results in a conversion formula that can be represented as "A+B."

Prior to the enactment of the PPA, sponsors of converting plans adopted a range of transition benefits for workers. In many cases, the transition design adopted under the plan amendment offered participants a "greater of" benefit formula. Under this approach, benefits available under the traditional plan formula and under the cash balance plan formula are separately calculated to determine which formula provides the greatest benefit to the participant. The participant's accrued benefit after the conversion is equal to the benefit that is more generous. Such "greater of" transition benefits are more favorable for participants than the minimum "A+B" rule set forth in the PPA.

It has come to our attention that the IRS has adopted a position that could interpret the "greater of" benefit conversion feature to be in violation of the anti-backloading rules set forth in

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Section 411(b)(1)(B) of the Internal Revenue Code. The anti-backloading rules exist to ensure that worker benefits vest at least as quickly as required by the Employee Retirement Income Security Act of 1974 (ERISA). We do not believe this "greater of" transition benefit formula is a violation of the anti-backloading rules. Moreover, it is not our intent that the PPA's provisions relating to cash balance and hybrid plan conversions be applied to prohibit this plan benefit design which is clearly intended to benefit workers.

The IRS's position is drawn from an interpretation of Treasury regulation Section 1.411(b)-1(a) which provides:

"a defined benefit plan may provide that accrued benefits for participants are determined under more than one plan formula. In such a case, the accrued benefits under all such formulas must be aggregated in order to determine whether or not the accrued benefits under the plan for participants satisfy one of the alternative methods."

The agency is interpreting this guidance as requiring an aggregation of two benefit formulas that may be made available to participants in the context of "greater of" cash balance conversions. However, this interpretation is only one of several interpretations that could apply. One other reasonable interpretation would aggregate two benefit formulas in cases where one plan benefit formula applies to a participant for a period of time, and a second formula applies after the expiration of that period, but not where only one formula ultimately applies despite two preliminary calculations being made in determining the applicable formula. In the latter case, only the applicable benefit formula, standing alone, should be tested for compliance with the anti-backloading rules.


The use of a "greater of" formula in hybrid pension plan conversions that protects longer-service workers from a loss of future accruals should be encouraged, not penalized. Without action, plan sponsors that offered this transition benefit may face steep costs to avoid plan disqualification. Ironically, plan sponsors that did not provide this transition benefit face no sanctions. Moreover, without action, plan sponsors who may be considering a conversion to a hybrid plan may now have to provide less generous transition benefits upon conversion, or consider terminating their traditional defined benefit pension plan altogether.

We request that Treasury and the IRS reconsider the application of the anti-backloading rules to "greater of" transition benefits offered in the conversion of traditional defined benefit plans to hybrid pension plans. We further request that any reconsideration of this position be communicated to plan sponsors who are seeking determination letters for their converted hybrid pension plans. Additionally, we recommend that applicable Treasury regulations be amended to reflect this clarification in the normal course of the regulation process.

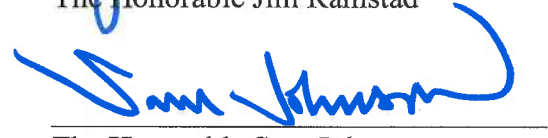
Thank you for your prompt attention and cooperation.

Sincerely,

  
The Honorable Jim McCrery  
Ranking Member

  
The Honorable Dave Camp

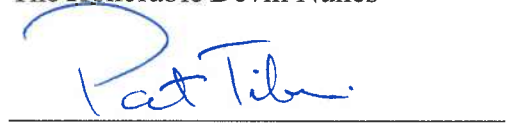
  
The Honorable Jim Ramstad

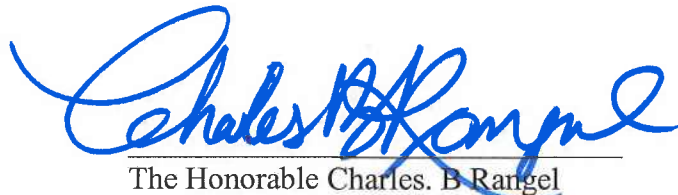
  
The Honorable Sam Johnson

  
The Honorable Phil English

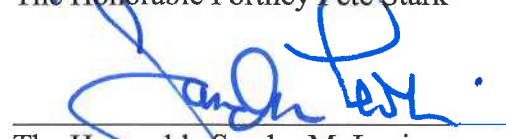
  
The Honorable Ron Lewis

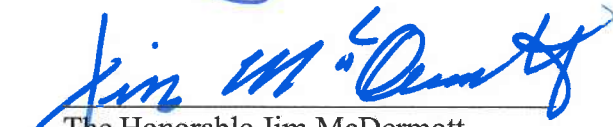
  
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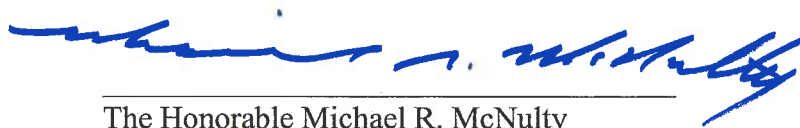
  
The Honorable Fortney Pete Stark


  
The Honorable Sander M. Levin

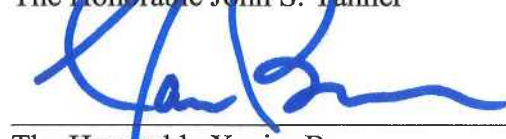
  
The Honorable Jim McDermott

  
The Honorable John Lewis

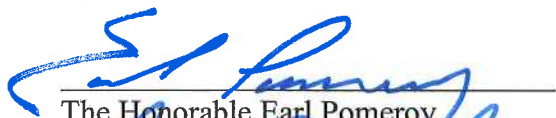
  
The Honorable Richard E. Neal

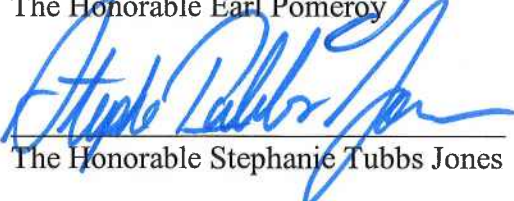
  
The Honorable Michael R. McNulty

  
The Honorable John S. Tanner

  
The Honorable Xavier Becerra

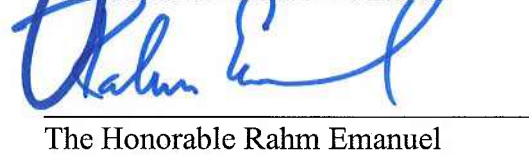
  
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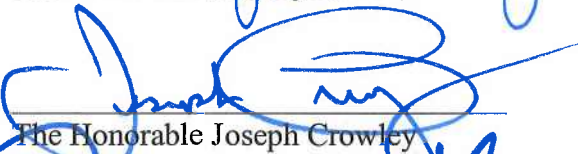
  
The Honorable Rahm Emanuel

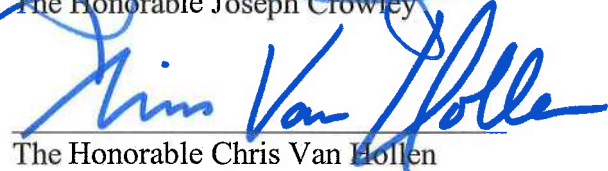
  
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