IN THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 99-3775

HARRY BELLAS,

Appellee,

v.

CBS, INC.; WESTINGHOUSE PENSION PLAN,

Appellants.

Appeal from the Order of the United States District Court for
the Western District of Pennsylvania, entered on June 29, 1999, at
Civil Action No. 98-1455, granting Appellee's Motion for Partial Summary Judgment

BRIEF *AMICUS CURIAE* OF ASSOCIATION OF PRIVATE PENSION AND WELFARE PLANS IN SUPPORT OF APPELLANTS URGING REVERSAL

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1 and Third Circuit LAR 26.1, the Association of Private Pension and Welfare Plans ("APPWP") makes the following disclosure:

APPWP is a broad-based, non-profit trade association organized under IRC § 501(c)(6), which protects and fosters the growth of private, employer-sponsored, employee benefit plans in the United States. APPWP has no shareholders or parent corporations. Its members include many publicly owned corporations.

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INTEREST OF AMICUS CURIAE

The Association of Private Pension and Welfare Plans ("APPWP") is a broad-based, non-profit trade association founded in 1967 to protect and foster the growth of private, employer-sponsored, employee benefit plans in the United States. Its members include both small and large employer-sponsors of employee benefit plans, including many Fortune 500 companies. Its members also include numerous organizations that assist plan sponsors in providing benefits to employees, such as actuarial and consulting firms, insurers, banks, investment firms, and other professional organizations. Collectively, APPWP has more than 230 members who sponsor, or assist in the administration of, retirement and health plans covering more than 100 million Americans.

APPWP has a strong interest in this case for two reasons. First, the substantive question presented by this appeal is extremely important to the retirement plan community, as evidenced by this Court's decision to accept review by way of interlocutory appeal. Our economy is changing very rapidly, as certain industries are consolidating, others are being deregulated, and still others are being fundamentally changed by technological developments. In the context of such change and greatly increased global competition, companies must reevaluate every aspect of their business. Critical in this reevaluation process is a reexamination of employee compensation. Without competitive compensation packages, companies cannot compete for scarce employee talent. The question presented by this appeal is whether companies' efforts to update and rationalize their compensation systems will be hamstrung by an overly broad and unintended application of the anti-cutback rule. APPWP and its members believe that great harm would result from such an application.

Second, this case presents an exceptionally important question about process — namely, the reasonable reliance interests of plan sponsors. This Nation's pension laws are notoriously complex. Particular uncertainty surrounds the "anti-cutback rule" involved here, because the Treasury Department has not yet acted on Congress's instruction to issue regulations defining a "retirement-type subsidy." Under these circumstances, plan sponsors contemplating significant plan amendments necessarily must rely on the limited guidance that the Internal Revenue Service ("IRS") has provided. Exercising prudence, many sponsors take the prophylactic step that appellants took here — namely, seeking and obtaining from the IRS an advance "determination letter," which approved the plan amendment at issue after focusing specifically on the application of the anti-cutback rule.

Notwithstanding the IRS's prior approval, the district court has held — five years after the amendment was adopted — that appellants' action violated the law. If the considered judgment of the agency charged by Congress with interpreting this ERISA provision can be so lightly disregarded, plan sponsors could be subjected to massive financial liabilities, through no fault of their own. It is exceptionally important to the retirement plan community that courts accord proper deference to the considered judgments of the IRS upon which plan sponsors have reasonably relied. As a major association of organizations that sponsor and administer retirement plans, APPWP is well equipped to present the broad perspective of the employee benefits community on this crucial issue of reliance.

Appellants have consented to the filing of this brief, but appellee has declined consent. The brief is accordingly filed by leave of court pursuant to Federal Rule of Appellate Procedure 29(a).

ARGUMENT

I. THE ANTI-CUTBACK RULE DOES NOT APPLY TO THE BENEFIT AT ISSUE BECAUSE THAT BENEFIT IS NOT A "RETIREMENT-TYPE SUBSIDY"

The anti-cutback rule of ERISA § 204(g), as amended by the Retirement Equity Act of 1984, Pub. L. No. 98-397, § 301, 98 Stat. 1426 (1984) ("REA"), provides that a plan amendment may not eliminate or reduce a "retirement-type subsidy." The legislative history indicates that a shutdown benefit is not a retirement-type subsidy if it does not continue after normal retirement age. S. Rep. 575, 98th Cong., 2d Sess. 30 (1984), *reprinted in* 1984 U.S.C.C.A.N. 2547, 2576 ("Senate Report").[1] Because the actuarial subsidy provided by the Permanent Job Separation benefit (the "PJS benefit") under the Westinghouse Pension Plan (the "Westinghouse Plan") ends completely at normal retirement age, the PJS benefit is not a "retirement-type subsidy" within the meaning of ERISA § 204(g). It therefore is not subject to the anti-cutback rule. In ruling to the contrary, the district court misapplied the intent of Congress.

A. The Anti-Cutback Rule Does Not Apply To A Shutdown Benefit That Does Not Continue After Normal Retirement Age

When Congress amended ERISA § 204(g) in 1984, it directed the Treasury Department to promulgate regulations defining the term "retirement-type subsidy." S*ee* ERISA § 204(g)(2)(A); IRC § 411(d)(6)(B)(i); Senate Report at 30. To date, the Treasury Department has not satisfied this mandate. For this reason, employers and the courts have looked to the

[1] A contemporaneous press release from the Senate Finance Committee confirms that the reference in the Senate Report to "retirement age" is to "normal retirement age." *See* Addendum (1).

gloss on that term provided by the Senate Report. *See, e.g., Arndt v. Security Bank S.S.B. Employees' Pension Plan*, 182 F.3d 538, 542 (7th Cir. 1999); *Ashenbaugh v. Crucible Inc., 1975 Salaried Retirement Plan*, 854 F.2d 1516, 1527-28 (3d Cir. 1988), *cert. denied*, 490 U.S. 1105 (1989). The Senate Report states that "a subsidy that continues after retirement is generally to be considered a retirement-type subsidy" and that "a plant shutdown benefit (that does not continue after retirement age)" is not a "retirement-type subsidy." Senate Report at 30. The clear intent of Congress, therefore, was to apply the anti-cutback rule to a benefit subsidy, including a shutdown benefit, *only* if the subsidy continues after retirement age.

As this Court has explained, a "benefit subsidy" is "the excess of the value of a benefit over the actuarial equivalent of the normal retirement benefit." *See Ashenbaugh*, 854 F.2d at 1527-28; Senate Report at 28. Here, the "benefit subsidy" supplied by the PJS provision equals the economic value to the employee of receiving his or her normal retirement benefit immediately upon termination, without suffering the actuarial reduction that normally occurs when benefits commence prior to normal retirement age. This type of subsidy, which is comparatively common in retirement plans, is generally called an "actuarial subsidy." As demonstrated below, the actuarial subsidy under the PJS benefit terminates completely at normal retirement age.[2] Because the subsidy does not continue after normal retirement age, the PJS benefit is not subject to the anti-cutback rule. *See Ross v. Pension Plan for Hourly Employees of SKF Industries, Inc.*, 847 F.2d 329 (6th Cir. 1988).

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[2] As appellants explain (App. Br. at 31), the PJS benefit also includes a "social security supplement" within the meaning of IRC § 411(a)(9) which terminates completely at age 62. The Senate Report and Treasury Regulations confirm that a social security supplement is not subject to the anti-cutback rule. *See* Senate Report at 30; Treas. Reg. § 1.411(d)-4, Q/A-1(d).

B. The Actuarial Subsidy Under The PJS Benefit Does Not Continue After Normal Retirement Age

The actuarial subsidy incorporated in the PJS benefit does not continue beyond normal retirement age because 100% of that subsidy's economic value is consumed between the commencement of benefits upon early retirement and the employee's attainment of normal retirement age. Once the employee reaches normal retirement age, the monthly benefit payable under the PJS provision is the normal retirement benefit that any employee with a comparable length of service and similar compensation would have received under the Westinghouse Plan. In other words, the actuarial subsidy provides *a bridge* between involuntary termination and normal retirement age. The subsidy simply enables the employee to begin receiving benefits in an amount no less than what the employee would have received if he or she had deferred commencement of benefits until the age at which no actuarial reduction would have been applied.[3]

Pension benefits ordinarily are actuarially reduced when an employee elects to commence distributions prior to normal retirement age. The reduction is not a penalty; it simply adjusts the vested distributable amount to reflect that (1) an amount paid currently is worth more than the same amount paid later, (2) the periodic benefit is payable over a greater number of years, and (3) the risk that an employee will die before benefit payments commence

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[3] Subject to an exception for small benefits, employee consent generally is required for any distribution from a retirement plan prior to attainment of normal retirement age. *See* ERISA § 203(e)(1); IRC § 411(a)(11); Treas. Reg. § 1.411(a)-11(c)(4). Thus, an employee terminating at age 55 cannot begin receiving distributions until normal retirement age (typically, age 65), unless the employee makes an affirmative election to commence distributions.

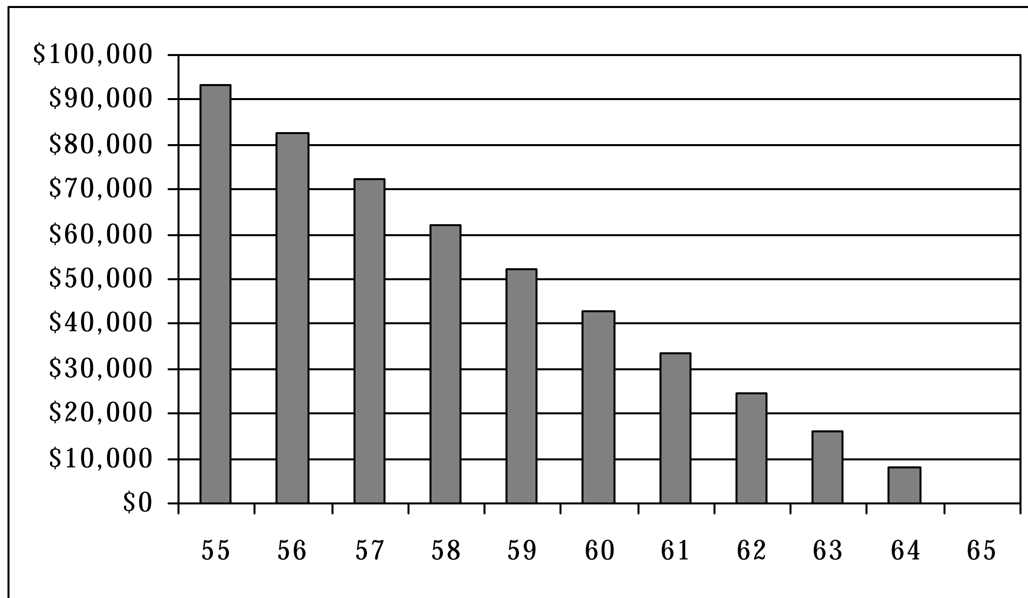
is reduced. The actuarial reduction is calculated by determining the benefit amount that would be payable at normal retirement age (on the basis of the participant's service and compensation to the date of early commencement), and by multiplying the benefit payable at normal retirement age by a discount factor. For useful discussions of the economics of actuarial subsidies, *see* D. McGill and D. Grubbs, Fundamentals of Private Pensions 131-35 (6th ed. 1989), *quoted in* J. Langbein & B. Wolk, Pension and Employee Benefit Law 378-80 (2d ed. 1995) (Addendum (2)), and Ethan Lipsig, Downsizing 257-58 (1996).

For example, a 55-year old employee who terminates employment with a vested monthly retirement benefit of $1,000 for life commencing at age 65 might be entitled to $400 per month for life commencing at age 55 after the actuarial reduction is made. A full actuarial subsidy, such as that provided under the PJS benefit, eliminates this actuarial reduction and so provides an employee with a level stream of benefits before and after normal retirement age, consisting of a monthly $1,000 subsidy until normal retirement age and the monthly $1,000 normal retirement benefit thereafter.

Because a full actuarial subsidy results in a level benefit stream regardless of the employee's age when benefits commence, it provides vastly different subsidy amounts to different employees, depending on their ages at the time of commencement. The actuarial subsidy is most valuable to the youngest employees who qualify for the subsidy, and it declines

steadily in value as an employee approaches normal retirement age.[4] For an employee attaining normal retirement age, the subsidy disappears entirely. This steady decline in subsidy is illustrated by the graph below:

Annual Present Value of Remaining Actuarial Subsidy[5]
with Benefit Commencement at Age 55 and Normal Retirement at Age 65



As this graph demonstrates, the economic value of the actuarial subsidy continues to decrease until normal retirement age – *at which point the subsidy disappears entirely*. Although the *benefit stream* continues after normal retirement age in the form of the normal retirement benefit, the *actuarial subsidy* is reduced to zero at that point. Because the subsidy does not

[4] This variation in subsidy value persists even among employees who receive otherwise equivalent monthly benefit payments. For example, an employee aged 55 who receives an immediate unreduced monthly benefit of $1,000 enjoys a much greater *subsidy* than an employee aged 60 who also receives an immediate unreduced monthly benefit of $1,000. The economic value of the subsidy is a function of age, not of the monthly benefit amount.

[5] The graph assumes a normal retirement benefit of $12,000 per year. Present value is determined assuming a 6% interest rate and applying the 1983 Group Annuity Mortality Table (50% Male, 50% Female). *See* Addendum (4) for supporting data.

continue after normal retirement age, it is not – in the language of the anti-cutback rule – a "retirement-type subsidy." *See* Senate Report at 30 ("A *subsidy* that continues after normal retirement age is generally to be considered a retirement-type subsidy.") (emphasis added).

Other forms of shutdown benefits do continue beyond normal retirement age and, thus, do constitute "retirement-type subsidies." For example, if a defined benefit plan provides a normal retirement benefit of 1% of pay multiplied by an employee's years of service, a shutdown benefit provided in the form of an increase in the normal retirement benefit multiplier – such as an increase from 1% to 1.5% of pay – has a clear effect beyond normal retirement age. Similarly, an imputed service credit by which an employee is deemed to have performed an additional number of years of service directly affects the benefit payable beyond normal retirement age. Plainly, these are the types of subsidies that Congress had in mind when it directed the Treasury Department to distinguish between subsidies that do, and subsidies that do not, continue beyond normal retirement age. The district court erred in concluding that the PJS benefit falls with the former class.

C. The Decision Of The District Court Elevates Form Over Substance

The district court disregarded the nature of the actuarial subsidy under the PJS benefit and focused instead on the semantics of the Westinghouse Plan. In rejecting appellants' argument that the subsidy does not continue beyond normal retirement age, the court relied on language in the Plan stating that "the amount calculated in accordance with [the PJS provision] shall be payable *for the lifetime of the Employee*." JA0075 (emphasis added). By focusing on the benefit *stream* rather than on the benefit *subsidy*, the district court misapprehended the clear intent of Congress.

Assume a 55-year-old employee who would be entitled to receive $1,000 per month for life at normal retirement age, but only $400 per month for life at age 55. Assume that this individual becomes entitled at age 55 to a full actuarial subsidy, *viz.*, the right to receive $1,000 per month beginning at age 55 instead of age 65. This individual enjoys a *benefit stream* of $1,000 per month that continues for life, but a *benefit subsidy* of $1,000 per month that continues only until normal retirement age.

In the district court's view, the PJS benefit is subject to the anti-cutback rule because it is phrased as an undifferentiated benefit stream of $1,000 per month for life. By contrast, the anti-cutback rule would not apply, on the district court's approach, if the Westinghouse Plan were phrased as an interim benefit of $1,000 per month until normal retirement age, followed by the normal retirement benefit of $1,000 per month for the rest of the employee's life. There is no substantive or economic difference between these two forms: each delivers a $1,000 monthly benefit *subsidy* that lasts only until normal retirement age. To construe the application of the anti-cutback rule as turning on the form of words used in the plan document is plainly contrary to the language of the statute and to congressional intent, which explicitly confines the rule's application to cutbacks reducing or eliminating a *subsidy* that continues after normal retirement age. ERISA § 204(g)(2)(A); IRC § 411(d)(6)(B)(i); Senate Report at 30.

It was precisely this same wooden reading of plan language that led the Fifth Circuit to err in *Harms v. Cavenham Forest Industries, Inc.*, 984 F.2d 686, 691-92 (5th Cir.), *cert. denied*, 510 U.S. 944 (1993). *Cf. Wallace v. Cavenham Forest Industries, Inc.*, 707 F. Supp. 455, 459-50 (D. Or. 1989) (interpreting same plan). In *Harms*, the court failed to analyze the economic value of the actuarial subsidy provided under a shutdown benefit; it simply concluded that the benefit, because payable in a life annuity, must be a retirement-type subsidy. Compounding its failure to

carry out the congressionally-ordained inquiry into whether the *subsidy* continues after normal retirement age, the *Harms* court neglected to consider the important pronouncement by the IRS in General Counsel Memorandum 39869 (Oct. 2, 1991), which, as demonstrated below, is the key administrative interpretation of the anti-cutback rule for shutdown benefits.[6]

Conversely, the district court failed to give proper weight to the Sixth Circuit's opinion in *Ross v. Pension Plan for Hourly Employees of SKF Industries, Inc.*, 847 F.2d 329 (6th Cir. 1988), which held that an actuarial subsidy incorporated in a shutdown benefit is not a retirement-type subsidy. The appellee in *Ross* specifically framed this issue for decision by the court:

> The plant shutdown benefit is the benefit that is payable solely because of the shutdown. This consists of the benefits payable before normal retirement age, since a person entitled to shutdown benefits would in any event have been entitled to the amounts payable after normal retirement age (that part of the benefits is equal to the normal retirement benefits). Since the plant shutdown benefit does not continue after normal retirement age, under the Senate Report, it is not a retirement-type subsidy.

See Addendum (3), Appellee's Brief at 23. The *Ross* court implicitly recognized that the key inquiry is whether the subsidy – not the stream of benefit payments – continues after normal retirement age. Although the Sixth Circuit's analysis was somewhat terse, the court clearly held that an actuarial subsidy under a shutdown benefit – almost identical to the PJS benefit at issue here – was not subject to the anti-cutback rule of ERISA § 204(g).

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6 In an opinion that was later withdrawn, the Ninth Circuit also erroneously analyzed a shutdown benefit in terms of whether the benefit itself was payable after retirement age, not whether the subsidy continued after retirement age. *See Richardson v. Pension Plan of Bethlehem Steel Corp.*, 67 F.3d 1462, 1467-1469 (9th Cir. 1995), *withdrawn and reh'g granted*, 112 F.3d 982 (9th Cir. 1997). As a withdrawn opinion, *Richardson* has no precedential value. *See, e.g.*, *United States v. Manges*, 110 F.3d 1162, 1173 (5th Cir. 1997), *cert. denied*, 118 S. Ct. 1675 (1998).

Finally, the decision of this Court in *Ashenbaugh*, 854 F.2d at 1527-28, is not to the contrary. There, this Court held certain employees not to be entitled to a plan benefit because they had not performed the 30 years of service required for that benefit. Although the dispute in *Ashenbaugh* pre-dated the REA amendments to the anti-cutback rule, this Court considered the REA amendments and assumed that the benefit at issue, which included an actuarial subsidy but which was not a shutdown benefit, would be a "retirement-type subsidy" under ERISA § 204(g) and IRC § 411(d)(6). *Ashenbaugh*, 854 F.2d at 1528. However, the *Ashenbaugh* case did not require the Court to consider the REA legislative history clarifying that a "retirement-type subsidy" requires a *subsidy* (as opposed to a benefit stream) that continues beyond normal retirement age. Nor did this Court inquire whether the actuarial subsidy in fact continued after normal retirement age.[7] In any event, the Court's observation was *dictum*. [8]

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[7] Similar considerations apply to the position stated by the IRS in Revenue Ruling 85-6, 1985-1 C.B. 133. Additionally, in *Dade v. North American Philips Corp.*, 68 F.3d 1558, 1562 n.1 (3d Cir. 1995), this Court recharacterized the *dictum* as stating that the *Ashenbaugh* benefits were "early retirement subsidies" – rather than "retirement-type subsidies."

[8] The anti-cutback rule also protects an "accrued benefit," an "optional form of benefit" and an "early retirement benefit." *See* ERISA § 204(g). The PJS benefit falls into none of these categories. *Ross*, 847 F.2d at 333 (actuarial subsidy under plant shutdown benefit not an accrued benefit, an optional form of benefit, or an early retirement benefit). An accrued benefit is "an annual benefit commencing at normal retirement age," *see* Treas. Reg. § 1.411(a)-7(a)(1)(i), but the PJS benefit both begins and ends before normal retirement age (and does not even accrue until an employee is involuntarily terminated). The PJS benefit is not an optional form of benefit because it does not offer a different form or option (such as a lump-sum payment) for the distribution of plan benefits. *See* Treas. Reg. § 1.401(a)(4)-4(d); Treas. Reg. § 1.411(d)-4, Q/A-1(b)(1). Finally, the PJS benefit is not an early retirement benefit because it is conditioned on a contingency – generally, an involuntary termination – other than simply the employee's age, service, and compensation. *See Roper v. Pullman*, 859 F.2d 1472, 1474 (11th Cir. 1988). *Compare* Treas. Reg. § 1.401-1(b)(1)(i). The district court found no need to reach this third question.

II. EVEN IF THE PJS BENEFIT IS A RETIREMENT-TYPE SUBSIDY, THE ANTI-CUTBACK RULE DID NOT APPLY TO THAT BENEFIT PRIOR TO APPELLEE'S INVOLUNTARY TERMINATION

Even if this Court were to determine that the PJS benefit is a "retirement-type subsidy" within the meaning of ERISA § 204(g), the 1994 amendment to the Westinghouse Plan did not violate the anti-cutback rule for a second and independent reason. Under a longstanding IRS interpretation, the anti-cutback rule does not apply to a shutdown benefit prior to the occurrence of the contingent event on which the shutdown benefit is based – in this case, appellee's involuntary termination. Because the Westinghouse Plan was amended years before appellee was terminated, the amendment did not violate the anti-cutback rule.

A. The IRS Has Stated Clearly That The Anti-Cutback Rule Does Not Apply To A Shutdown Benefit Prior To The Occurrence Of A Plant Shutdown

In General Counsel Memorandum 39869 (Oct. 2, 1991) ("GCM 39869"), the IRS specifically considered the applicability of the anti-cutback rule under IRC § 411(d)(6) (the tax code companion provision to ERISA § 204(g)) in the case of a shutdown benefit that is a "retirement-type subsidy" within the meaning of the anti-cutback rule.[9] The IRS determined unequivocally that "[s]hutdown benefits that are retirement-type benefits * * * become an accrued benefit and therefore protected under [IRC §] 411(d)(6) upon the occurrence of the event that triggers the right to the benefits (*i.e.*, the contingent event)." As the IRS explained, this conclusion harmonizes with, and is strongly supported by, the funding rules under IRC § 412 and

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[9] Under section 101(a) of Reorganization Plan No. 4 of 1978, 44 Fed. Reg. 1065 (Jan. 3, 1979), the IRS has sole administrative authority to interpret the anti-cutback rule of ERISA § 204(g) and IRC § 411(d)(6).

ERISA § 302(d) for "unpredictable contingent event benefits."[10] Under this approach, it is the plan terms that determine when the relevant contingent event occurs:

> For example, a plan may provide that shutdown benefits will be offered to all affected participants "upon the resolution by the board of directors to close a facility." In this case, the resolution of the board is the event that triggers the shutdown benefit. Other plans provide that benefits will be offered to all terminated participants "upon notice to plan participants of a plant shutdown." Still other plans provide that the "actual termination of operations at a particular facility" is the triggering event. *The plan's description of a specific event is also the triggering event for determining when the shutdown benefit becomes a section 411(d)(6) protected benefit*.

GCM 39869 (emphasis added).

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[10] Under ERISA and the Internal Revenue Code, an unpredictable contingent event benefit may not be taken into account in determining a plan's current funding liability "until the event on which the benefit is contingent occurs." ERISA § 302(d)(7)(B); IRC § 412(l)(7)(B). The legislative history to the Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203, § 9303, 101 Stat. 1330, which added these provisions, makes clear that they are intended to address "benefits that depend on contingencies that, like facility shutdowns or reductions or contractions in workforce, are not reliably or reasonably predictable." H.R. Conf. Rep. 495, 100th Cong., 1st Sess. 855 (1987), *reprinted in* 1987 U.S.C.C.A.N. 2313, 1601. As appellants brief aptly demonstrates (at 25-28), it is essential that accrual and funding of plant shutdown benefits be symmetrical.

The position of the IRS could not be clearer. A shutdown benefit does not become a "retirement-type subsidy" subject to the anti-cutback rule until the relevant contingency occurs. In this case, the contingent event was appellee's involuntary termination. Prior to that time, the PJS benefit was not covered by the anti-cutback rule. Because the amendment modifying the PJS benefit was adopted years before appellee's involuntary termination, that amendment did not violate the anti-cutback rule. Indeed, the IRS so determined with respect to appellee and all similarly situated employees under the Plan when it granted CBS a determination letter in 1994 that focused specifically on this modification of the PJS benefit. *See* JA0265.

B. General Counsel Memorandum 39869 Is A Correct Interpretation Of The Anti-Cutback Rule

The district court refused to follow the IRS' interpretation of the anti-cutback rule because it believed there was no support, either in the text or the legislative history of ERISA § 204(g), for a distinction between "contingent" and "non-contingent" retirement-type subsidies. The district court's analysis of this point was superficial. Examination of the Senate Report confirms that Congress did intend to make a distinction between "contingent" and "non-contingent" benefits and that Congress intended to apply the anti-cutback rule to contingent benefits only after occurrence of the contingency that creates a right to the benefit.

The distinction between contingent and non-contingent benefits appears clearly in the Senate Report's description of ancillary benefits that are not subject to the anti-cutback rule. When it first enacted ERISA in 1974, Congress preserved the longstanding differential between retirement benefits and ancillary benefits, concluding that "[t]o require the vesting of * * * ancillary benefits would seriously complicate the administration and increase the cost of plans whose primary function is to provide retirement income." H.R. Rep. 807, 93rd Cong., 2d Sess. 60 (1974), *reprinted in* 1974 U.S.C.C.A.N. 4670, 4726. The Senate Report confirms that

Congress did not intend to upset this distinction when amending ERISA § 204(g) in 1984. Rather, the Senate Report specifically states that enumerated ancillary benefits – including a qualified disability benefit, a medical benefit, a social security supplement, a death benefit (including life insurance), and a plant shutdown benefit that does not continue after normal retirement age – are not subject to ERISA § 204(g) at all. *See* Senate Report at 30.

The reason for this is plain. The anti-cutback rule is intended to protect the expectations of employees that retirement benefits and retirement-type subsidies promised to them will not be reduced or eliminated before the employees have satisfied the requisite age and service conditions. Retirement benefits generally commence at normal retirement age, are paid over a period of years (usually for life), and are measured by factors such as years of service and compensation. *See* Treas. Reg. § 1.401-1(b)(1)(i). Retirement benefits also accrue on a ratable basis over a participant's employment. *See* IRC § 411(b) and ERISA § 204(b) ("anti-backloading" rules). Thus, employee expectations with respect to normal retirement benefits are firm and predictable, and an employee's entitlement to those benefits is not triggered by events beyond his or her control. Congress amended ERISA § 204(g) in order to protect these legitimate expectations by ensuring that employees will always be able to "grow into" the promised non-contingent benefits. *See* Senate Report at 28.

By contrast, ancillary or contingent benefits – such as qualified disability benefits, medical benefits, and death benefits – serve as insurance against catastrophic events. These benefits do not accrue over time, but only upon the occurrence of events that employees cannot predict and do not desire. Thus, where benefits are conditioned on a contingency beyond the control of the employee, expectations prior to the contingency are purely speculative. Congress specifically did not want to extend anti-cutback protection to such benefits conditioned on events

beyond an employee's control – at least not until the events had come to pass. Shutdown benefits – benefits that "become available to plan participants upon the occurrence of a specific event described in the plan that causes the participant's employment to terminate as a result of a change in the organization or operation of the employer" (GCM 39869) – fall within this class of contingent benefits. Thus, even where offered as retirement-type subsidies, shutdown benefits remain speculative and contingent benefits until the "plant shutdown" as defined by the plan occurs.

In GCM 39869, the IRS correctly discerned Congress' intent not to apply the anti-cutback rule to contingent benefits prior to the occurrence of the contingency and ruled that a shutdown benefit that continues past normal retirement age becomes an accrued benefit only upon the occurrence of the stated contingent event. In so ruling, the IRS faithfully implemented Congress' intent that protection from reduction or elimination depends on whether an employee has a legitimate expectation of receiving a benefit once he or she has satisfied the age and service conditions for such benefit. The IRS was right to reach the conclusion that it did in GCM 39869, and the district court was wrong to disregard the IRS' well reasoned analysis.

III. APPLYING THE ANTI-CUTBACK RULE TO SHUTDOWN BENEFITS PRIOR TO A PLANT SHUTDOWN WOULD SERIOUSLY DISRUPT SETTLED PRACTICES AND WOULD HAVE VERY ADVERSE CONSEQUENCES FOR RETIREMENT PLANS, EMPLOYERS, AND EMPLOYEES

In structuring retirement plans, employers have long relied on the stated position of the IRS that the anti-cutback rule of IRC § 411(d)(6) and ERISA § 204(g) never applies to a shutdown benefit prior to the occurrence of the contingent triggering event – namely, the plant shutdown. This considered view of the IRS has encouraged the widespread employer practice of offering shutdown benefits in many different forms, perhaps most commonly in the actuarial-subsidy form at issue in this case. The IRS has reaffirmed its interpretation of the anti-cutback

rule, having repeatedly approved retirement plan documents and amendments (like the 1994 amendment to the Westinghouse Plan) that follow the Service's position as to the proper application of IRC § 411(d)(6) and ERISA § 204(g). To apply the anti-cutback rule here, in defiance of the IRS' long-standing position, would seriously and unfairly disrupt many retirement plan provisions drafted in reliance on the IRS' view of the law. Besides frustrating employers' legitimate reliance interests, such an outcome would expose many employers and employees to significant adverse tax consequences, and it would ultimately discourage employers from offering shutdown benefits.

A. Shutdown Benefits Are A Common And Important Feature Of Retirement Plans

Providing shutdown benefits under a tax-qualified retirement plan is a common employment practice. *See* GCM 39869 ("Many pension plans provide for shutdown benefits to participants.") These benefits exemplify one of the strengths of the defined benefit plan: the employer's flexibility to adjust the level of an employee's plan benefits to respond to changing economic and business conditions. Offering a shutdown benefit enables the employer to provide an immediate, targeted, and determinate enhancement of an employee's plan benefits upon the occurrence of a contingency that otherwise would have no effect on those benefits. *See* GCM 39869 ("Shutdown benefits are event-based benefits that become available to individuals upon the occurrence of an event that causes an individual's employment to change.").

Additional flexibility is afforded by the fact that numerous options exist for delivering a shutdown benefit to employees. *See* Ethan Lipsig, Downsizing 101-104 (1996) (discussing various incentive mechanisms under retirement plans). Very commonly, a shutdown benefit is provided in a form similar to the actuarial subsidy in the Westinghouse Plan: an amount equal to the unreduced normal retirement benefit is made immediately available to an employee who has

not yet reached normal retirement age, but who has satisfied stated age and service conditions. Other means of delivering a shutdown benefit include an enhancement to the age or service component of the plan benefit formula (*e.g.*, deeming each employee to be five years older or to have performed an additional ten years of service); providing an additional benefit option (*e.g.*, offering a lump-sum distribution option not otherwise available); or simply increasing the amount of the normal retirement benefit for an employee affected by the plant shutdown. As the IRS has stated, "[t]he characteristics of shutdown benefits may vary depending upon the purpose the employer hopes to achieve by providing the benefit." GCM 39869. This considerable flexibility in defining the terms of the shutdown benefit contributes greatly to its prevalence and importance as a vehicle for employee compensation. In extending the anti-cutback rule even to shutdown benefits that do not continue past the normal retirement age, and even prior to occurrence of the contingent event, the district court's decision substantially reduces employers' flexibility to offer shutdown benefits subject to adjustment in light of changing economic conditions.

B. Employers Have Relied On The Long-Standing Position Of The IRS That The Anti-Cutback Rule Never Applies To Shutdown Benefits Until A Plant Shutdown Occurs

The utility and desirability of providing shutdown benefits in retirement plans has made it particularly important for employers to know whether and when the anti-cutback rule applies to these benefits. Congress did not expressly answer this question when it enacted REA in 1984; instead, it directed the Treasury Department to issue regulations on the subject. But the Treasury Department's regulations under IRC § 411(d)(6) do not address this point, and no other federal agency has jurisdiction to interpret either IRC § 411(d)(6) or ERISA § 204(g). As a result, the position that the IRS announced eight years ago in GCM 39869 has become exceptionally

influential and important. Employers desiring to provide shutdown benefits in their retirement plans have had no choice but to rely on this well-established IRS position in determining the application of the anti-cutback rule to shutdown benefits.[11]

The statutory text of the anti-cutback rule does not expressly address shutdown benefits. Instead, ERISA § 204(g) provides generally that the "accrued benefit" of a plan participant may not be decreased by an amendment to the plan, and that a plan amendment having the effect of eliminating or reducing a "retirement-type subsidy (as defined in regulations)" for a benefit attributable to service before the amendment is treated as reducing an accrued benefit. The statute thus leaves entirely open the question whether – and under what circumstances – a shutdown benefit embodies a "retirement-type subsidy." The statute simply states that "regulations" will define this crucial term.

The legislative history is not much more expansive. The Senate Report reiterates that Treasury Regulations shall define the term "retirement-type subsidy," expressing its intent that a "subsidy that continues after retirement is generally to be considered a retirement-type subsidy." Senate Report at 30. Conversely, the Report indicates that certain benefits – including "a plant shutdown benefit (that does not continue after retirement age)" – should not be considered a retirement-type subsidy. *Ibid*. Beyond this directive to the Treasury Department and this statement of legislative intent, Congress was silent as to how the anti-cutback rule applies to shutdown benefits.

The Treasury Regulations issued in 1988 under IRC § 411(d)(6) do not fulfill the Congressional mandate to construe the term "retirement-type subsidy" and they do not address

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[11] Appellants have ably demonstrated that GCM 39869 is entitled to judicial deference as an administrative interpretation of the anti-cutback rule, and that point will not be re-argued here.

the application of the anti-cutback rule to plant shutdown benefits. *See* Treas. Reg. § 1.411(d)-4.[12] Although the Department of Labor has jurisdiction over certain aspects of ERISA, it has no power to fill this gap, because it is without jurisdiction to issue regulations interpreting ERISA § 204(g). In this respect, IRC § 411(d)(6) and ERISA § 204(g) explicitly confine the grant of regulatory authority to the Secretary of the Treasury. Moreover, Section 101(a) of Reorganization Plan No. 4 of 1978 abolished the authority of the Secretary of Labor to issue "regulations, rulings, opinions, variances, and waivers" under various ERISA provisions (including § 204(g)) and transferred that authority exclusively to the Secretary of the Treasury. 44 Fed. Reg. 1065 (Jan. 3, 1979).

Thus, the IRS issued GCM 39869 against a background of almost complete legislative and regulatory silence on the application of the anti-cutback rule to shutdown benefits. GCM 39869 is the sole pronouncement on this subject from the sole agency with authority to make any pronouncement at all. For this reason, employers have had little choice but to attach great significance to the position set forth in the IRS memorandum. Indeed, the IRS recognized the importance of the guidance it was providing by stating that GCM 39869 would discuss shutdown benefits generally rather than specific instances of shutdown benefits provided under particular plans.[13] And, unlike the terse statement of intent found in the Senate Report, the position set out

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[12] The preamble to the final regulations specifically acknowledges this point. It states: "With one exception [not relevant in this case], the regulations do not provide specific guidance with respect to the benefits described in section 411(d)(6)(A), early retirement benefits, or retirement-type subsidies. *Thus, for example, the regulations do not address the extent to which a plant closing or shutdown benefit under a plan constitutes an early retirement benefit or a retirement-type subsidy*." 53 Fed. Reg. 26050, 26051 (July 11, 1988) (emphasis added).

[13] GCM 39869 begins by stating: "Although your request resulted from technical advice requests regarding shutdown benefits provided by two employers, you have indicated that our response should address whether qualified pension plans may generally provide for shutdown benefits and, if so, whether shutdown benefits are protected benefits under section 411(d)(6)."

in GCM 39869 concerning shutdown benefits is comprehensive and clear: the anti-cutback rule does not apply at all to a shutdown benefit that is an ancillary benefit, and the rule applies to a shutdown benefit that continues past the normal retirement age only when the relevant contingency – the plant shutdown – takes place. Employers have understandably

relied on this clear statement of the law in designing, drafting, and amending their retirement plans.[14]

The IRS has reinforced its legal interpretation of the anti-cutback rule by granting administrative approval – embodied in "determination letters" – to plans and plan amendments that follow the position set forth in GCM 39869. This is not, in other words, a legal issue that the IRS has overlooked in the eight years since the memorandum was issued. Quite the contrary: in continually reaffirming its position, the IRS has invited the reliance of employers on this point.

The case at hand well illustrates the measure and reasonableness of employers' reliance on the IRS. Here, CBS sought and received a favorable IRS determination letter that the 1994 amendment to the Westinghouse Plan modifying the PJS benefit would not adversely affect the Plan's tax-qualified status. CBS specifically highlighted the anti-cutback issue in its application to the IRS seeking a determination letter. *See* JA0233 n.1. Subsequently, the IRS specifically discussed with CBS' counsel the status of the plan amendment under the anti-cutback rule. *See* JA0250, JA0258. After specific consideration of the anti-cutback issue, the IRS issued a favorable determination letter. *See* JA0265. Under these circumstances, CBS – like many other similarly-situated employers – had every reason to believe that its amendment fully complied with the anti-cutback rule.

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[14] Under the IRS interpretation, a shutdown benefit that is a retirement-type subsidy becomes protected by the anti-cutback rule when an employee is involuntarily terminated, and a shutdown benefit that is not a retirement-type subsidy never becomes protected by the anti-cutback rule. In practice, this is usually a distinction without a difference. Few if any employers would seriously consider eliminating shutdown benefits for an employee *after* the employee had been involuntarily terminated. Thus, many employers have relied on GCM 39869 for the rule that a shutdown benefit is never subject to the anti-cutback rule until the involuntary termination

C. Applying The Anti-Cutback Rule To Shutdown Benefits Prior To The Benefit-Triggering Event Would Have Very Adverse Consequences For Retirement Plans, Employers, And Employees

Application of the anti-cutback rule to shutdown benefits before occurrence of the contingency triggering payment of such benefits would seriously disrupt the settled employment practices that have developed in reliance on the IRS position stated in GCM 39869. Shutdown benefits that have been written into plans on the expectation that they could be modified or removed prior to an actual plant shutdown would by law become permanent features of those plans. That result could create significant funding difficulties for plans, perhaps pushing some into under-funded status as shutdowns occur. Moreover, because the substantive rules under IRC § 412(l) and ERISA § 302(d) significantly limit the pre-funding of shutdown benefits, the additional funding demands that would be placed on plans by the unexpected application of the anti-cutback rule could not be mitigated effectively by prospective measures. Indeed, the increased funding demands placed on employers by the inability to modify or remove shutdown benefits could be particularly difficult to meet for plant shutdowns that occur in times of business or general economic distress, possibly compromising the plan's ability to satisfy the genuine *retirement* benefits promised under the plan.

Additionally, application of the anti-cutback rule to shutdown benefits prior to the occurrence of the triggering contingency would expose many plans to the threat of immediate disqualification for federal income tax purposes because adoption of an amendment that violates IRC § 411(d)(6) causes a plan to be disqualified. *See* IRC §§ 411(d)(6) & 401(a)(7).[15]

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takes place, without having to determine *a priori* whether a particular shutdown benefit is or is not a retirement-type subsidy.

[15] Disqualification would be a risk only where plan sponsors (unlike appellants here) did not secure an advance determination letter from the IRS approving the amendment. Plans are not

Disqualification has enormously adverse tax consequences. When a plan is disqualified, employees must include currently in gross income part or all of their interests in the plan, or the contributions made to the plan on their behalf. For its part, the employer loses some or all of its deductions for contributions to the plan, and the trust that holds the assets of the plan becomes subject to federal income tax. IRC §§ 402(b), 404(a)(5) & 501(a). Those adverse tax consequences would apply notwithstanding the employer's reasonable reliance on the IRS' well-known position, set out in GCM 39869, that a shutdown benefit never becomes subject to the anti-cutback rule prior to the occurrence of a plant shutdown.

Besides the adverse consequences for plans that already have shutdown benefits (or that have been amended to modify or eliminate shutdown benefits), the district court's decision – unless reversed – will strongly discourage employers from adding future shutdown benefits. Thus, the district court's interpretation of the anti-cutback rule would likely result in fewer employees receiving those benefits after experiencing involuntary terminations.

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required to seek such a letter, and presumably many plan sponsors did not do so, relying on GCM 39869.

CONCLUSION

The district court's partial summary judgment order should be reversed.

Respectfully submitted,

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November 22, 1999

CERTIFICATE OF BAR MEMBERSHIP

Pursuant to Third Circuit LAR 46.1, I certify that I am a member of the bar of this Court.

____

Trevor W. Swett III*

* Counsel of Record

Dated: November 22, 1999

CERTIFICATE OF WORD COUNT

Pursuant to Federal Rule of Appellate Procedure 32(a)(7)(c), I certify that the word-processing system used to write this brief displays a word count of 6,980 words.

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Dated: November 22, 1999

ADDENDA

1. Senate Finance Committee Press Release issued approximately July 31, 1984

2. Dan M. McGill and Donald S. Grubbs, Jr. Fundamentals of Private Pensions 131-35 (6th ed. 1989)

3. Excerpt from Brief of Appellee, *Ross v. Pension Plan for Hourly Employees of SKF Industries, Inc.*, 847 F.2d 329 (6th Cir. 1988)

4. Supporting data for chart showing value of actuarial subsidy

CERTIFICATE OF FILING AND SERVICE

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