

June 13, 2007

The Honorable Max Baucus
Chairman, Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Charles Grassley
Ranking Member, Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510

Re: Urgent Request to Correct IRS Interpretation Penalizing Pension Plans for Pro-Participant “Greater Of” Design

Dear Chairman Baucus and Ranking Member Grassley:

The undersigned organizations, representing employers of all sizes that provide retirement plan benefits to employees as well as the service providers that help administer these benefit plans, write with great concern to urge swift action to correct an Internal Revenue Service interpretive position that will harm employees and unfairly penalize employers.

As you are aware, many employers have in recent decades converted their defined benefit plans from traditional final average pay plans to cash balance and pension equity plans. Hybrid plans provide portable, transparent benefits while maintaining the employer financial commitment inherent in defined benefit plans. To ensure that older and longer-service workers were treated fairly in such conversions, employers adopted a range of transition benefits. One of the most favorable of all such transition approaches for employees -- one that was praised repeatedly by Members of Congress during the cash balance deliberations of recent years -- is known as “greater of.” Under this transition method, benefits are calculated under both the traditional and hybrid formulas and employees are given the greater benefit. The IRS is now saying -- in the context of the recently opened determination letter process for hybrid pension plans -- that the “greater of” transition approach violates the rules designed to prevent backloading of pension accruals because the increase in benefits is too large when one formula outstrips the other.

While the hybrid context is where this issue has first arisen, we are learning more each day about the range of defined benefit plan designs that are jeopardized by the IRS interpretation. For example, under the interpretation a backloading violation would frequently result when defined benefit plans offer minimum guaranteed benefits, which are often found in multi-employer union plans, because the employee is entitled to the greater of the plan’s regular accruals or the guaranteed minimum benefit. Likewise, backloading violations could occur as a result of acquisitions, when employers often provide employees with the greater of the benefits under the prior employer’s defined benefit plan formula or its own formula.

We feel strongly that the IRS’s formalistic interpretation does not make sense, is not required by the statute and will do significant harm to defined benefit plan participants and sponsors. As their name suggests, the backloading rules were designed to prevent undue accrual of benefits in an employee’s later years of service as a way around the vesting rules. Providing the “greater of” two benefit formulas does not backload benefits in any such way and indeed often involves some frontloading of benefits, a pro-employee accrual pattern that was blessed

in the conference report of ERISA itself. Moreover, each of the formulas involved in a “greater of” design satisfies the backloading rules and employees ultimately receive benefits under only one formula.

If the current IRS position is left to stand, employers will not adopt the pro-employee “greater of” approach and future employees will be left with less generous benefits when pension formulas are changed. If the position is left to stand, employers that have already adopted these most employee-friendly of transition techniques and benefit designs will be stunned to learn that they may have to pay potentially millions of dollars to avoid plan disqualification and cure this backloading “problem.”

This unfair, counterproductive and unnecessary interpretation simply cannot be left in place. A pension system that penalizes employers for adopting the most employee-friendly designs possible is one in which no rational businessperson will choose to remain. And it goes without saying that the last thing defined benefit plan sponsors need is another significant deterrent to continuing to offer these valuable plans to their employees.

Both of you have dedicated yourselves to encouraging a vibrant employer-sponsored benefits system in which defined benefit plans are a viable option and to fostering generous benefits for the nation’s workers. As a result, we know you will share our extreme distress and frustration with the current IRS position. We urge you to contact Treasury Secretary Paulson and Acting IRS Commissioner Brown immediately to urge that the IRS abandon this interpretation of the backloading rules. If a change in course by the regulators is not possible, we urge you to move legislation through Congress as expeditiously as you can to correct this interpretation and prevent the many harms that will otherwise result. We stand ready to do whatever we can to assist you in achieving this objective.

Thank you for your prompt consideration of this pressing and critically important issue.

Sincerely,

American Benefits Council
American Council of Life Insurers
American Society of Pension Professionals & Actuaries
Business Roundtable
Coalition to Preserve the Defined Benefit System
Committee on Investment of Employee Benefit Assets
ERISA Industry Committee
Financial Executives International’s Committee on Benefits Finance
HR Policy Association
National Association of Manufacturers
National Coordinating Committee for Multiemployer Plans
Society for Human Resource Management
U.S. Chamber of Commerce

cc: Members of the Senate Finance Committee