



AMERICAN BENEFITS
COUNCIL

STATEMENT OF

MICHAEL L. HADLEY

ON BEHALF OF THE

AMERICAN BENEFITS COUNCIL

BEFORE THE

**DEPARTMENT OF TREASURY AND
INTERNAL REVENUE SERVICE**

**HEARING ON PROPOSED REGULATIONS
RELATING TO MODIFICATIONS
TO MINIMUM PRESENT VALUE REQUIREMENTS
FOR PARTIAL ANNUITY DISTRIBUTION OPTIONS
UNDER DEFINED BENEFIT PLANS**

JUNE 1, 2012

Good morning,

My name is Mike Hadley and I am a partner in the law firm of Davis & Harman. I am testifying today on behalf of the American Benefits Council. The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Thank you for holding this hearing today.

The issue we are here to discuss today is something the Council raised with the agencies in an October 2010 joint comment letter with the National Coordinating Committee for Multiemployer Plans. It's a critical issue for many plans and we look forward to continuing to work with Treasury and the Service to provide an effective solution to this issue. In addition, I want to reiterate the Council's support for the range of projects that you, and your colleagues at the Department of Labor, are working on to help Americans manage their assets in retirement.

This project provides a much needed clarification of the treatment of benefits paid partially as an annuity and partially in another form. We believe that plan participants can be well served by having the opportunity to elect to receive a portion of their retirement benefits in an annuity form, so that they can protect themselves against longevity risks while having access to liquidity during retirement years. As folks here have said repeatedly, we want to get participants past the "all or nothing" approach.

While the Council supports this clarification to the section 417(e) regulations, we disagree with the position taken in the preamble in the notice of proposed rulemaking regarding the interpretation of the current state of the law. In the preamble, Treasury

and the Service say that, under current law, when one portion of a retirement benefit distribution subject to the section 417(e) factors is a “decreasing” benefit, both portions of the distribution are subject to the minimum present value requirements of section 417(e)(3). The Council believes that the current regulation does not clearly require that, and can be reasonably interpreted to reach the opposite result. Due to this uncertainty, the Council believes that the clarification of the rules, as provided by the proposed regulations, should apply prospectively, and that Treasury and the Service should clearly state that no inference should be drawn regarding the law prior to the effective date of the final regulation.

Generally speaking, lump sums and certain other distributions paid from defined benefit pension plans must be no less than the amount calculated using the interest and mortality assumptions provided under section 417(e). The regulations apply the 417(e) valuation requirement to all payment forms that are not explicitly exempted. As I alluded to earlier, one exemption relates to nondecreasing annuities. The crux of this interpretive issue is whether the exemption applies to the annuity portion of a split-distribution option.

Let’s look at the exact words in the regulation, which says that the 417(e) present value requirement “does not apply to an amount of a distribution paid in the form of an annual benefit that does not decrease during the life of the participant.” If the requirement applies to the whole benefit if any portion of the benefit decreases, then saying it does not apply to “an amount” of a distribution is unnecessary. Rather, the

regulation would have just said 417(e) does not apply to “a distribution” or to “an optional form” that does not decrease during the life of the participant.

This seems like a natural reading of the regulation and, in fact, the Council understands that some plans have received favorable determination letters from the Service, even though the plan language follows this reading of the 417(e) regulation and uses those factors only for the lump sum portion.

The Council recognizes that reasonable minds might differ on the meaning of the regulation, which is exactly why we support a clarification. We also think that an approach that says no inference should be drawn as to the law in effect before this regulation is finalized is the best resolution.

Our comment letter also makes a few technical comments to ensure that the regulation works as intended, in particular that the “three bucket” approach in the regulation does not result in a plan design being inadvertently excluded from the relief because the design does not fit into one of the three kinds of bifurcated benefits. Three quick examples. First, we point out in our letter that the first category of bifurcated benefits – separately determined benefits with separate elections – could be read to imply that the plan must allow the participant to “mix and match” all of the benefit forms, which we think is not appropriate for a number of reasons. Second, since we filed our letter, a Council member pointed out to us that it would be helpful to clarify that this first category of bifurcated benefits is available for plans that provide for separate elections for a legacy benefit and for the remainder of the total benefit minus that legacy benefit—often described as a B and A-B benefit – as long as those separate

portions are calculated without regard to the optional form chosen. Third and finally, we are unsure as to why the third category of bifurcated accrued benefit applies only to a plan that allows single sums, as it would seem to be appropriate to apply it to other decreasing forms, like installments, that are the equivalent of the accrued benefit payable at normal retirement age and not available with respect to the entire accrued benefit.

In conclusion, we appreciate the efforts by Treasury and the IRS to develop a proposal to clarify the treatment of optional forms of benefits paid in the form of a partial annuity under the section 417(e) regulations. We agree that retirement plan participants will be better served by having this option going forward. In order to effectively implement the regulations, we request that the proposed regulations, when finalized, apply prospectively only and without any inference to current law.

We thank you again for the opportunity to testify today, and we're happy to take your questions.