ASPPA
WORKING FOR AMERICA'S RETIREMENT

4245 North Fairfax Drive, Suite 750
Arlington, VA 22203
P 703.516.9300 F 703.516.9308
www.asppa.org

Outline of Issues for the Public Hearing on Proposed Regulations Relating to Hybrid Retirement Plans under §411(a)(13) and §411(b)(5)

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Department of Treasury
Internal Revenue Service
26 CFR Part 1
[REG-104946-07]

Issues to be discussed:

I. Conversions (four minutes)

A. Remove the participant-by-participant determination of conversion date. The statute prohibits wear-away of benefits accrued before the effective date of an "applicable plan amendment". The proposed regulations determine the effective date on a participant-by-participant basis – not with respect to when the amended terms of the plan apply, but when any transition relief provided by the amendment, usually in the form of a "greater of" benefit, no longer applies.

ASPPA recommends the final regulations remove the "participant-by-participant" determination of conversion date. The proposed regulations go beyond the intent of the statute, and the likely impact is to discourage the provision of "greater of" benefits in future conversions.

B. Provide a clear definition of what is meant as a "pre-June 29, 2005" amendment. PPA, and the Proposed Regulations, provide that a conversion amendment is covered under the new rules only if the amendment is both adopted and effective after June 29, 2005. A common sense interpretation of an adoption date would lead one to assume only a plan amendment adopted by the board (or other responsible party) after June 29, 2005, could trigger the new conversion requirements. However, that isn't clear under the proposed regulations. For example, the proposed regulations state that an amendment has occurred if a participant transfers from a division with a non-hybrid formula to a division with a hybrid formula. A plausible interpretation is that the adoption and effective

dates of this deemed amendment would be the date of transfer, but this is not clearly stated.

ASPPA recommends that final regulations provide a more explicit and robust definition of a "pre-June 29, 2005 amendment" along with illustrative examples.

C. Establishment of opening account balances. The Proposed Regulations contemplate alternate means of satisfying the "A+B" conversion requirements involving establishing an opening account balance, without requiring subsequent comparison to the pre-conversion plan benefit. Comments in the preamble would limit the circumstances to an arrangement where there was no early retirement subsidy, interest credits were expected to be no lower than the rates used to establish the opening balance, and there is no discount for death or 100% of the balance is to be paid on death.

ASPPA recommends that final regulations adopt the proposed exception outlined in the preamble, but without restricting applicability to participants that elect lump sum payment. Final regulations should make it clear that, if the opening balance is determined using 417(e) segment rates, and the interest crediting rate is the third segment rate (or the largest of the three segment rates), the interest credits would meet the requirements.

II. General Interest Crediting Issues (two minutes)

A. Transition relief for a change from any interest crediting rate in Notice 96-8 to any other PPA permissible rate. The Preamble to the Proposed Regulations states that until further guidance is provided, an amendment to change the interest crediting rate from one of the rates in Notice 96-8 to another will be afforded IRC §411(d)(6) relief only if the difference between the maximum permissible margin and the actual margin for the new rate does not exceed the same differential as the old rate. The Preamble goes on to say IRS anticipates IRC §411(d)(6) relief will be available when a plan is amended to change a plan's interest crediting rate from an above market rate of return to a market rate of return, provided the change is not applicable to periods before the time IRC §411(b)(5)(b)(i) first applies to the plan.

ASPPA recommends that any transition relief available in the final regulations for changing the interest crediting rate from an above-market rate to a market rate of return also be available for changing the interest crediting rate from one of the rates in Notice 96-8 to any other permissible rate.

B. Any of the three segment rates, or the greatest of the three rates, should be a safe harbor rate. The Proposed Regulations provide that the third segment rate is a safe harbor rate. Most commonly, the first and second segment rates will be less than the third segment, and so will not be in excess of a market rate of return. However, occasionally the third segment rate will not be the highest rate, and a plan that uses an interest crediting rate of the first or second segments may exceed a safe harbor rate.

ASPPA recommends any of the segment rates, or the highest of the three rates, be deemed safe harbor rates. This would avoid the flurry of concern that will otherwise arise when the third segment rate is not the highest rate. The safe harbor should explicitly be available to 417(e) as well as 430(h) segment rates.

III. Market Rate of Return (one minute)

A. A reasonable fixed rate minimum should be available without adjustment. The preamble states that the Service is considering permitting the greater of a reasonable fixed rate and one of the safe harbor rates without adjustment, but is contemplating requiring an adjustment where the variable rate is equity-based.

ASPPA recommends the final regulations permit an interest crediting rate equal to the greater of 4% or a safe harbor (non-equity) rate without further adjustment. ASPPA also recommends the Service consider permitting a cumulative floor of a reasonable (such as 4%) fixed rate of return with no adjustment to any otherwise permitted market rate of return.

IV. Miscellaneous (two minutes)

A. Determining the amount of annuity payments. There are multiple compliance issues that require determination of the annuity payable at retirement, including application of the 133 1/3 percent rule, 401(a)(4) testing and disclosure in the relative value regulations, among others. Guidance should be provided on how to make this determination when the interest crediting rate is a variable rate.

ASPPA recommends that final regulations provide guidance on determining the amount of an annuity payable at retirement age, and the methodology for determining "greater of" benefits, when the interest crediting rate is a variable rate.

B. Participant elections regarding the interest crediting rate. Some plans allow the participant to elect which investment index will apply to his or her hypothetical account. The regulations should comment on when this is permissible, and any rules that would apply when the election is changed.

ASPPA recommends final regulations clarify how and when a participant may be permitted to make an election with regard to the interest crediting rate.

C. Access to the volume submitter program. Volume submitter documents make the establishment of retirement plans more economical and efficient for plan sponsors, practitioners and the Service.

ASPPA recommends hybrid retirement plans become eligible for the Volume Submitter program when regulations on Hybrid Retirement Plans are finalized.

V. General Comments (one minute)

It is important that guidance be comprehensive enough to enable compliance. There always will be gray areas, but there are also issues that the IRS and Treasury see as black and white, some practitioners see as white and black, and explicit answers are at best found in a gray book – not formal guidance. To the extent additional, clear guidance could be provided, we can all minimize surprises. Employers and their advisors can avoid being surprised that a design they thought was appropriate is flawed, and now they need to provide additional benefits. Practitioners that thought a design was flawed who find it is not can begin offering it. Everybody wins.