



# NewsFlash<sup>SM</sup>

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## **CASH BALANCE DEVELOPMENTS**

Three noteworthy events in the controversy over cash balance plans occurred in the last week: A Federal District Court ruled that a cash balance plan was not age-discriminatory. The Treasury Department withdrew its 2002 proposed regulations on age discrimination rules for qualified plans, including cash balance plans. The House of Representatives Workforce Committee announced its intention to hold a hearing in July to examine cash balance plans.

### ***DISTRICT COURT DECISION – TOOTLE V. ARINC, INC.***

On June 10, a Federal District Court in Maryland said that the cash balance plan sponsored by ARINC, Inc. does not discriminate against employees because of their age. The Court agreed with an earlier district court decision (*Eaton v. Onan*) that ERISA's age discrimination provisions were enacted to protect employees after normal retirement age. The Court went on to say that, even if relevant ERISA provisions apply before normal retirement age, plaintiffs' suggested approach for testing for potential age discrimination – by examining the pattern of normal retirement annuities that accrue as an employee ages – would lead to illogical results. Instead, the court said that employers “should not be forced to calculate accrued benefits under a cash balance plan in terms of an age-65 annuity.”

The Court mentioned, but did not follow, the *Cooper v. IBM Corporation* case, in which a Federal District Court in Illinois reached the opposite conclusion. In *Cooper*, the court ruled that age discrimination arose because the same dollar of pay credit granted to two employees at different ages could purchase a larger annuity at normal retirement age of 65 for the younger employee (due to more years of interest credits). Although the *Cooper* Court acknowledged the sound economic argument that interest credits keep a pay credit from losing value as time passes, it concluded that ERISA required that the age-discrimination analysis be made on the basis of normal retirement annuity benefits, without adjustment for the time value of money. In contrast, the *Tootle* Court said that “The more sensible approach is to measure benefit accrual under cash balance plans by examining the rate at which amounts are allocated and the changes over time in an individual's account balance...”

The *Cooper* case is now in its remedies phase, and is almost certain to be appealed. Of the courts that have considered the issue, only the District Court in *Cooper* has ruled that a typical cash balance plan is age-discriminatory.

The *Tootle* decision is a favorable development for cash balance plan sponsors. However, the legal uncertainty on the age discrimination issue will persist until a clearer pattern of judicial decisions emerges or until Congress passes clarifying legislation.

## **TREASURY WITHDRAWS PROPOSED AGE DISCRIMINATION REGULATIONS**

On June 15, the Treasury Department announced the withdrawal of its 2002 proposed regulations covering age discrimination issues for tax-qualified plans. That guidance, if it had become final, would have been generally favorable to cash balance plans. This withdrawal is not surprising in light of a law passed in January, 2004 that required Treasury to propose legislation to provide transition relief for older and longer service participants affected by cash balance conversions and to clarify the legal status of cash balance plans.

In February, the Treasury proposed cash balance legislation. (See our News Flash dated February 4, 2004). That proposal clarifies that the typical cash balance design is not age-discriminatory. Treasury's withdrawal of the proposed regulations, therefore, should be viewed as a procedural matter rather than as a reversal of its position that the typical cash balance plan is not age-discriminatory. Although Congress has not yet taken up the Treasury proposal or any other cash balance related proposal, it appears poised to do so (as discussed below).

The Treasury also announced a continuation of the moratorium on issuing determination letters on cash balance conversions while cash balance issues are under consideration by Congress. Numerous determination letter requests have been held up at the IRS since September 15, 1999 when the moratorium went into effect. It seems likely that these letters will remain in limbo for quite a while longer.

## **CONGRESSIONAL HEARING ON CASH BALANCE ISSUES**

On June 15, a press release from the House Education & Workforce Committee, chaired by Rep. John Boehner, indicated that the Committee intends to hold a hearing in July as a first step toward drafting legislation. The Committee intends to "look for solutions to ensure cash balance pension plans remain a viable retirement security option for workers and employees." The press release referred to the Treasury decision to withdraw its proposed regulations on age discrimination and indicated that the Treasury action underscored "the need for Congress to carefully consider the issue in a thoughtful, deliberative manner." Chairman Boehner said "American workers deserve retirement security, and cash balance pension plans are an important tool in the defined benefit system for ensuring they have this security in a changing economy." Rep. Sam Johnson, chairman of the Employer-Employee Relations Subcommittee, said that "There are plenty of hybrid plans that currently need the certainty we will provide in our legislation."



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Acknowledgement by a key Congressional Committee of the need to clarify the legal environment for cash balance plans is an important development. While legislation this year seems unlikely, it is encouraging that a formal legislative process is about to begin.

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