October 12, 2001

William Sweetnam, Esq.
Benefits Tax Counsel
Office of the Benefits Tax Counsel
U.S. Department of the Treasury
Room 1000
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20020

Re: Proposed technical corrections to the pension provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001

Dear William:

Thank you for taking time to meet recently with representatives from the American Academy of Actuaries' Pension Committee. We are writing to follow up on our conversation regarding some areas that we believe should be addressed in an upcoming technical corrections bill.

- **Valuation timing**
  Although the Economic Growth and Tax Relief Reconciliation Act's (EGTRRA's) change in valuation timing rules may seem like a liberalization of current law, it contains a subtle change that adversely affects a number of employers. We are aware of many employers who collect pension census data prior to the end of the plan year so that they have time to develop FAS 87 figures for year-end disclosure in their corporate financial statements. Also, many plan sponsors with plan years that do not coincide with the calendar year prefer to collect census data on a calendar-year basis, utilizing W-2 databases.

  Rather than collecting census data a second time for pension funding, these companies project the census data to the valuation date using generally accepted actuarial methods. This should have only a negligible effect on the liabilities but saves a tremendous amount of time and energy in avoiding extra data collection.

  Also, the current EGTRRA rules do not seem to require reflection of significant changes in the plan's circumstances (other than significant demographic changes) if they qualify for the new timing rules. For example, if a well-funded, calendar-year plan is amended January 2, 2002, using the new EGTRRA rules could defer recognition of the amendment until the 2004 plan year – with additional cash contributions not required until September 15, 2005.

We propose an alternative to the EGTRRA rules:

- Allow the current rules for NRECA and other regulated utilities, which need to be able to budget costs in advance of setting their rates.
- For other plan sponsors:
  - Allow a valuation date up to twelve months prior to the beginning of the plan year for well-funded plans (as in EGTRRA) or up to three months prior to the beginning of the plan year for other plans. Asset values would be measured as of the valuation date.
  - Allow the collection of census data up to twelve months prior to the beginning of the plan year for all plans, with appropriate projection to the valuation date.

  - Require reflection of significant events (such as plan amendments) as outlined in the PBGC premium funding rules.

This would not only preserve the flexibility that employers currently enjoy relative to the collection of data, but would also result in more accurate, up-to-date valuations than the current EGTRRA rules for plans that experience significant events.

We also noted that there is an inconsistency in the funding requirements for flexibility in the timing of valuations – the Committee Report references thresholds of both 125% and 100%, whereas the actual EGTRRA language specifies a threshold of 125%. The Treasury Department may also want to look into whether the change was intended or whether a technical correction is required to conform the current threshold to Congressional intent.

- **Relief for plans that incorporate IRC section 415(b) by reference**
  Because the EGTRRA changes to IRC section 415(b) apply to limitation years <u>ending</u> in 2002, increases in the benefit limits apply immediately upon enactment to plans with non-calendar limitation years. As was recognized previously in Rev. Ruling 99-44, some employers (especially small employers) may prefer not to increase benefits in their qualified plans. We suggest that some relief be given for employers whose plans incorporate IRC section 415(b) by reference, and thus may experience immediate increases in their qualified plan benefits without the opportunity to choose whether or not to apply the new rules.

- **Catch-up contributions**
  Numerous issues arise under the current EGTRRA rules on catch-up contributions, mostly related to concerns about determining when an individual's contributions have exceeded other applicable limits, which is a requirement for determining when an individual can begin making catch-up contributions. This also affects testing under the average deferral percentage ("ADP") rules, and can result in "circular" testing – i.e., the testing would need to be completed to determine whether a particular highly-compensated employee had exceeded the contribution limits and therefore be eligible to make catch-up contributions, but this in turn would affect the results of the ADP testing.

  We suggest that the rules be changed to permit an employee who reaches age 50 by year-end to make catch-up contributions if he or she exceeded applicable contribution limits in the prior plan year. This avoids the above complications and is consistent with the look-back approach currently allowed for ADP testing.

- **References to OBRA '87 current liability**

  Several areas of the Code set thresholds based on OBRA'87 current liability funding ratios. Under EGTRRA the OBRA'87 full-funding limit will be phased out over the next few years, and actuaries will no longer need to measure OBRA'87 current liability on an ongoing basis – unless their clients need to determine whether their plans meet one of these thresholds.

  The RPA'94 current liability measurement is very similar to OBRA'87, but with more restrictions on assumed interest and mortality rates. Since it is required for ongoing calculations, it will be produced routinely as part of the annual plan actuarial valuations. We suggest that any references in the Code to the OBRA'87 current liability be changed to RPA'94 current liability. The financial effects of any such changes are negligible.

  These references are found in the following Code sections:

  — IRC section 412(c)(9)(B), added by EGTRRA, permitting additional flexibility in the timing of valuations for plans that are at least 125% funded based on OBRA'87 current liability, and

  — IRC section 420, permitting the transfer of pension assets to cover post-retirement medical costs in plans that are at least 125% funded based on OBRA'87 current liability.

We would be pleased to discuss these suggestions with you. Please feel free to call Bridget Flynn, Pension Policy Analyst at the Academy of Actuaries at (202) 785-7869 or flynn@actuary.org for further information.

Sincerely,

Donald J. Segal
Chair, Pension Committee

Carolyn E. Zimmerman
Vice Chair, Pension Commitee

The American Academy of Actuaries is the public policy organization for actuaries practicing in all specialties within the United States. A major purpose of the Academy is to act as the public information organization for the profession. The Academy is non-partisan and assists the public policy process through the presentation of clear and objective actuarial analysis. The Academy regularly prepares testimony for Congress, provides information to federal elected officials, comments on proposed federal regulations, and works closely with state officials on issues related to insurance. The Academy also develops and upholds actuarial standards of conduct, qualification and practice, and the Code of Professional Conduct for all actuaries practicing in the United States.