AMERICAN ACADEMY of ACTUARIES

Minimum Required Distributions for Retirement Plans

A Public Statement by the Pension Practice Council
of the
American Academy of Actuaries

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Thank you for the opportunity to testify today on the recently issued regulations regarding minimum required distributions. The American Academy of Actuaries is a non-partisan public policy organization that represents actuaries nationwide. It is our goal to provide clear, objective actuarial analysis in the pursuit of sound public policy. Today, as a member of the Academy's Public Plans Task Force, which is charged with monitoring issues concerning public employee retirement systems, I am here to address concerns that the task force has with temporary regulation 1.401(a)(9)-6T related to the treatment of cost of living adjustments as well as optional forms of benefits.

As provided, the regulations appear to require that a plan's annual cost of living adjustment (or COLA) be no greater than the increase in the consumer price index (CPI). This requirement would affect many public employee retirement systems that allow for other forms of COLAs, especially those that would allow for adjustments that could, in any given year, be greater than the CPI. For example, many state systems, such as California, Florida, and Illinois, provide for a fixed percentage increase while states like Wisconsin provide a COLA based on a plan's investment performance. Police and Fire public employee retirement systems in Colorado have a COLA that provides increases based on the increases in the wages of active workers. These are examples of states with non-CPI based COLAs, however, some states like New York, actually have a CPI-based COLAs, yet they still provide a minimum floor percentage that would be applicable in the event that the CPI is too low. As you can see, any of these alternatives could potentially exceed the CPI in a given year.

It is also important to note that, as a part of the benefit structure, these types of COLAs may be protected under state law against diminishment. As a contractual agreement, both accrued and future pension benefits are protected. Should these regulations be made permanent, public retirement systems would be unable to conform to both state and federal statutes. As such, the task force recommends that the regulations be modified to allow for non-CPI based COLAs.

In addition to the requirements placed on cost of living adjustments, we are also concerned with the new restrictions placed on the joint and survivor form of benefit for non-spouse beneficiaries in which the beneficiary is more than 10 years younger than the participant. A benefit of this type actually has great value in instances when, for example, a retiring participant is attempting to provide future income for a disabled child. Generally, public sector employees are not high net-worth individuals and would not opt for a reduction in benefits unless they have legitimate beneficiary protection concerns like that of a disabled child.

As you are aware, IRS Revenue Ruling 72-241 already requires 50 percent of the present value of the benefit be distributed over the participant's expected lifetime, which makes the necessity of these new restrictions unclear. Based on this ruling any benefit option that would violate the 50 percent rule would simply not be allowed, and with average retirement ages in the 50s for many public retirement system employees, this particular joint and survivor benefit option could be provided without violating revenue ruling 72-241. The task force, therefore, requests that this restriction be removed.

Similarly, as outlined in this regulation, the prohibition of a lump sum benefit option payable upon the death of a member in retirement is unnecessary. Typically, this type of benefit is chosen by a participant in order to pay for burial expenses or in lieu of an annuity for a beneficiary. With appropriate limits to the lump-sum amounts, this benefit could also be provided without violating the 50 percent rule provided in revenue ruling 72-241 but with reductions that are no greater than the reductions for acceptable forms of benefit, such as period certain and joint and survivor benefits. As with the previously discussed joint and survivor benefit option, the task force recommends that this restriction be removed.

Our understanding is that the goal of these regulations is to minimize a retiree's ability to defer receipt of benefits and thereby defer payment of taxes. However, this temporary regulation limits the options for defined benefit pension plan payouts. And, as stated earlier, revenue ruling 72-241 already exists to provide limits for the payouts of specific benefit options.

In conclusion, the Public Plans Task Force respectfully requests that this section of the regulation be modified to allow for different forms of COLA benefits, and we recommend that the restrictions on optional forms of benefits be removed. Any of these requirements could be interpreted as violations of state constitutional protections and subsequently result in an indefensible situation for state systems as they would be unable to conform to both federal and state statutes. Furthermore, given the typically low pay status and early average retirement age of participants in public systems, the restrictions are simply not needed.

Thank you for your time and consideration of this matter. If you have any questions, at this time, I will be happy to respond.