

that considerations of comity dictate that [it] defer to New Hampshire law on the matter of what person or persons should be deemed to speak for the state in [NRC] licensing proceedings.”²⁶ The Appeal Board went on to point out that since § 2.715(c) was issued in response to § 2741. of the AEA, which section had the stated purpose of furthering cooperation between the Commission and the states, “[i]t is reasonable to assume that the legislative contemplation was that the concerned state, and not this agency, would make the decision respecting who is to serve as its spokesman.”²⁷ Although the original version of § 2.715(c) was directed only to States, its reach was expanded in 1978 to political subdivisions of a State to “improve coordination with States, counties, and municipalities.”²⁸ The Appeal Board’s reasoning, with which the Commission agrees, also applies to local government bodies because restricting the representation choices of local government bodies does little to “improve coordination” with them.

This Appeal Board decision is especially persuasive because, under both current § 2.315(c) and the former § 2.715(c), interested government participants have rights similar in many important respects to the rights of those participating as parties. These rights include the opportunity to introduce evidence, interrogate witnesses, file proposed findings, and petition for review. Given this level of participation, it would seem that interested government participants are, in fact, “appearing” in NRC adjudications, which arguably puts decisions respecting their representation under the umbrella of § 2.314(b).²⁹ In any event, it would make little sense to impose representation choices on government bodies participating as parties that are different from the choices available to interested government participants.

In light of the above, the Commission sees no need to put conditions on the representation of a government body that neither State law nor the governing charter of the body see fit to impose. To do so could only serve to limit government participation and would be contrary to the interests of comity. So long as a person is duly authorized to represent the government body in question, in conformity with State law

and any applicable local government charter, that person, whether an attorney or not, may represent that government body in NRC proceedings.

Conclusion

Lincoln County petitioned for a rule amendment that would allow AULGs to participate in NRC proceedings through any duly-authorized representative, which could include a non-attorney consultant. As explained above, however, Lincoln County’s desired outcome is already provided for in the current regulations, making Lincoln County’s desired rulemaking unnecessary. For this reason, Lincoln County’s petition for rulemaking is denied.

Dated at Rockville, Maryland this 20th day of December 2007.

For the Nuclear Regulatory Commission.

Annette L. Vietti-Cook,

Secretary of the Commission.

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-104946-07]

RIN 1545-BG36

Hybrid Retirement Plans

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations providing guidance relating to sections 411(a)(13) and 411(b)(5) of the Internal Revenue Code (Code) concerning certain hybrid defined benefit plans. These regulations provide guidance on changes made by the Pension Protection Act of 2006. These regulations affect sponsors, administrators, participants, and beneficiaries of hybrid defined benefit plans.

DATES: Written or electronic comments and requests for a public hearing must be received by March 27, 2008.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-104946-07), Room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG-104946-07), Courier’s Desk, Internal Revenue Service, 1111 Constitution Avenue,

NW., Washington, DC, or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-104946-07).

FOR FURTHER INFORMATION CONTACT:

Concerning the regulations, Lauson C. Green or Linda S. F. Marshall at (202) 622-6090; concerning submissions of comments or to request a public hearing, Funmi Taylor at (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Income Tax Regulations (26 CFR part 1) under sections 411(a)(13) and 411(b)(5) of the Code. Generally, a defined benefit pension plan must satisfy the minimum vesting standards of section 411(a) and the accrual requirements of section 411(b) in order to be qualified under section 401(a) of the Code. Sections 411(a)(13) and 411(b)(5), which were added to the Code by section 701(b) of the Pension Protection Act of 2006, Public Law 109-280, 120 Stat. 780 (PPA ’06), modify the minimum vesting standards of section 411(a) and the accrual requirements of section 411(b).

Section 411(a)(13)(A) provides that an applicable defined benefit plan (which is defined in section 411(a)(13)(C)) is not treated as failing to meet either (i) The requirements of section 411(a)(2) (subject to a special vesting rule in section 411(a)(13)(B) with respect to benefits derived from employer contributions) or (ii) The requirements of section 411(c) or 417(e) with respect to contributions other than employee contributions, merely because the present value of the accrued benefit (or any portion thereof) of any participant is, under the terms of the plan, equal to the amount expressed as the balance in a hypothetical account or as an accumulated percentage of the participant’s final average compensation. Section 411(a)(13)(B) requires an applicable defined benefit plan to provide that an employee who has completed at least 3 years of service has a nonforfeitable right to 100 percent of the employee’s accrued benefit derived from employer contributions.

Under section 411(a)(13)(C)(i), a plan is an applicable defined benefit plan if the plan is a defined benefit plan under which the accrued benefit (or any portion thereof) of a participant is calculated as the balance of a hypothetical account maintained for the participant or as an accumulated percentage of the participant’s final average compensation. Under section

²⁶ *Id.* at 148.

²⁷ 25 NRC 144, 148-49.

²⁸ “Miscellaneous Amendments,” (43 FR 17798, 17798; Apr. 26, 1978).

²⁹ Section 2.314(b) governs who “may appear in an adjudication.”

411(a)(13)(C)(ii), the Secretary of the Treasury is to issue regulations which include in the definition of an applicable defined benefit plan any defined benefit plan (or portion of such a plan) which has an effect similar to a plan described in section 411(a)(13)(C)(i).

Section 411(b)(1)(H)(i) provides that a defined benefit plan fails to comply with section 411(b) if, under the plan, an employee's benefit accrual is ceased, or the employee's rate of benefit accrual is reduced, because of the attainment of any age. Section 411(b)(5), which was added to the Code by section 701(b)(1) of PPA '06, provides additional rules related to section 411(b)(1)(H)(i). Section 411(b)(5)(A) generally provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) if a participant's accrued benefit, as determined as of any date under the terms of the plan, would be equal to or greater than that of any similarly situated younger individual who is or could be a participant. Section 411(b)(5)(G) provides that, for purposes of section 411(b)(5), any reference to the accrued benefit of a participant shall be a reference to the participant's benefit accrued to date. For purposes of section 411(b)(5)(A), section 411(b)(5)(A)(iv) provides that the accrued benefit may, under the terms of the plan, be expressed as an annuity payable at normal retirement age, the balance of a hypothetical account, or the current value of the accumulated percentage of the employee's final average compensation.

Section 411(b)(5)(B) imposes several requirements on an applicable defined benefit plan as a condition of the plan satisfying section 411(b)(1)(H). Section 411(b)(5)(B)(i) provides that such a plan is treated as failing to meet the requirements of section 411(b)(1)(H) if the terms of the plan provide for an interest credit (or an equivalent amount) for any plan year at a rate that is greater than a market rate of return. Under section 411(b)(5)(B)(i)(I), a plan is not treated as having an above-market rate merely because the plan provides for a reasonable minimum guaranteed rate of return or for a rate of return that is equal to the greater of a fixed or variable rate of return. Section 411(b)(5)(B)(i)(II) provides that an interest credit (or an equivalent amount) of less than zero can in no event result in the hypothetical account balance or similar amount being less than the aggregate amount of contributions credited to the account. Section 411(b)(5)(B)(i)(III) specifies that the Secretary of the Treasury may provide by regulation for rules governing the calculation of a market

rate of return for purposes of section 411(b)(5)(B)(i)(I) and for permissible methods of crediting interest to the account (including fixed or variable interest rates) resulting in effective rates of return meeting the requirements of section 411(b)(5)(B)(i)(I).

Section 411(b)(5)(B)(ii), (iii), and (iv) contain minimum benefit rules that apply if, after June 29, 2005, an applicable plan amendment is adopted. Section 411(b)(5)(B)(v)(I) defines an applicable plan amendment as an amendment to a defined benefit plan which has the effect of converting the plan to an applicable defined benefit plan. Under section 411(b)(5)(B)(ii), if, after June 29, 2005, an applicable plan amendment is adopted, the plan is treated as failing to meet the requirements of section 411(b)(1)(H) unless the requirements of section 411(b)(5)(B)(iii) are met with respect to each individual who was a participant in the plan immediately before the adoption of the amendment. Section 411(b)(5)(B)(iii) specifies that, subject to section 411(b)(5)(B)(iv), the requirements of section 411(b)(5)(B)(iii) are met with respect to any participant if the accrued benefit of the participant under the terms of the plan as in effect after the amendment is not less than the sum of: (I) The participant's accrued benefit for years of service before the effective date of the amendment, determined under the terms of the plan as in effect before the amendment; plus (II) The participant's accrued benefit for years of service after the effective date of the amendment, determined under the terms of the plan as in effect after the amendment. Section 411(b)(5)(B)(iv) provides that, for purposes of section 411(b)(5)(B)(iii)(I), the plan must credit the participant's account or similar amount with the amount of any early retirement benefit or retirement-type subsidy for the plan year in which the participant retires if, as of such time, the participant has met the age, years of service, and other requirements under the plan for entitlement to such benefit or subsidy.

Section 411(b)(5)(B)(v) sets forth certain provisions related to an applicable plan amendment. Section 411(b)(5)(B)(v)(II) provides that if the benefits under two or more defined benefit plans of an employer are coordinated in such a manner as to have the effect of adoption of an applicable plan amendment, the plan sponsor is treated as having adopted an applicable plan amendment as of the date the coordination begins. Section 411(b)(5)(B)(v)(III) directs the Secretary of the Treasury to issue regulations to prevent the avoidance of the purposes of

section 411(b)(5)(B) through the use of two or more plan amendments rather than through a single plan amendment.

Section 411(b)(5)(B)(vi) provides a special rule for converting a variable interest crediting rate to a fixed rate for purposes of determining plan benefits in the case of a terminating applicable defined benefit plan.

Section 411(b)(5)(C) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) solely because the plan provides offsets against benefits under the plan to the extent the offsets are allowable in applying the requirements of section 401(a). Section 411(b)(5)(D) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides a disparity in contributions or benefits with respect to which the requirements of section 401(l) (relating to permitted disparity for Social Security benefits and related matters) are met.

Section 411(b)(5)(E) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides for indexing of accrued benefits under the plan. Under section 411(b)(5)(E)(iii), indexing means the periodic adjustment of the accrued benefit by means of the application of a recognized investment index or methodology. Section 411(b)(5)(E)(ii) requires that, except in the case of a variable annuity, the indexing not result in a smaller benefit than the accrued benefit determined without regard to the indexing.

Section 701(a) of PPA '06 added provisions to the Employee Retirement Income Security Act of 1974, Public Law 93-406 (88 Stat. 829) (ERISA), that are parallel to the above-described sections of the Code that were added by section 701(b) of PPA '06. The guidance provided in these proposed regulations with respect to the Code would also apply for purposes of the parallel amendments to ERISA made by section 701(a) of PPA '06.¹

Section 701(c) of PPA '06 added provisions to the Age Discrimination in Employment Act of 1967, Public Law 90-202 (81 Stat. 602) (ADEA), that are parallel to section 411(b)(5) of the Code. Executive Order 12067 requires all Federal departments and agencies to advise and offer to consult with the Equal Employment Opportunity Commission (EEOC) during the development of any proposed rules,

¹ Under section 101 of Reorganization Plan No. 4 of 1978 (43 FR 47713), the Secretary of the Treasury has interpretive jurisdiction over the subject matter addressed by these proposed regulations for purposes of ERISA, as well as the Code.

regulations, policies, procedures or orders concerning equal employment opportunity. The IRS and the Treasury Department have consulted with the EEOC prior to the issuance of these proposed regulations.

Section 701(d) of PPA '06 provides that nothing in the amendments made by section 701 should be construed to create an inference concerning the treatment of applicable defined benefit plans or conversions of plans into applicable defined benefit plans under section 411(b)(1)(H), or concerning the determination of whether an applicable defined benefit plan fails to meet the requirements of section 411(a)(2), 411(c), or 417(e) as in effect before such amendments solely because the present value of the accrued benefit (or any portion thereof) of any participant is, under the terms of the plan, equal to the amount expressed as the balance in a hypothetical account or as an accumulated percentage of the participant's final average compensation.

Section 701(e) of PPA '06 sets forth the effective date provisions with respect to amendments made by section 701 of PPA '06. Section 701(e)(1) specifies that the amendments made by section 701 generally apply to periods beginning on or after June 29, 2005. Thus, the age discrimination safe harbors under section 411(b)(5)(A) and section 411(b)(5)(E) are effective for periods beginning on or after June 29, 2005. Section 701(e)(2) provides that the special present value rules of section 411(a)(13)(A) are effective for distributions made after August 17, 2006.

Under section 701(e)(3) of PPA '06, in the case of a plan in existence on June 29, 2005, the 3-year vesting rule under section 411(a)(13)(B) and the market rate of return limitation under section 411(b)(5)(B)(i) are generally effective for years beginning after December 31, 2007. In the case of a plan not in existence on June 29, 2005, those sections are effective for periods beginning on or after June 29, 2005. Section 701(e)(4) of PPA '06 contains special effective date provisions for collectively bargained plans that modify these effective dates.

Under section 701(e)(5) of PPA '06, sections 411(b)(5)(B)(ii), (iii), and (iv) apply to a conversion amendment that is adopted after, and takes effect after, June 29, 2005.

Section 702 of PPA '06 provides for regulations to be prescribed by August 16, 2007, addressing the application of rules set forth in section 701 of PPA '06 where the conversion of a defined benefit pension plan into an applicable

defined benefit plan is made with respect to a group of employees who become employees by reason of a merger, acquisition, or similar transaction.

Proposed regulations (EE-184-86) under sections 411(b)(1)(H) and 411(b)(2) were published by the Treasury Department and the IRS in the **Federal Register** on April 11, 1988 (53 FR 11876), as part of a package of regulations that also included proposed regulations under sections 410(a), 411(a)(2), 411(a)(8), and 411(c) (relating to the maximum age for participation, vesting, normal retirement age, and actuarial adjustments after normal retirement age, respectively).²

Notice 96-8 (1996-1 CB 359), see § 601.601(d)(2)(ii)(b) of this chapter, described the application of sections 411 and 417(e) to a single sum distribution under a cash balance plan where interest credits under the plan are frontloaded (that is, where future interest credits to an employee's hypothetical account balance are not conditioned upon future service and thus accrue at the same time that the benefits attributable to a hypothetical allocation to the account accrue). Under the analysis set forth in Notice 96-8, in order to comply with sections 411(a) and 417(e) in calculating the amount of a single sum distribution under a cash balance plan, the balance of an employee's hypothetical account must be projected to normal retirement age and converted to an annuity under the terms of the plan, and then the employee must be paid at least the present value of the projected annuity, determined in accordance with section 417(e). Under that analysis, where a cash balance plan provides frontloaded interest credits using an interest rate that is higher than the section 417(e) applicable interest rate, payment of a single sum distribution equal to the current hypothetical account balance as a complete distribution of the employee's accrued benefit may result in a violation of section 417(e) or a

forfeiture in violation of section 411(a). In addition, Notice 96-8 proposed a safe harbor which provided that, if frontloaded interest credits are provided under a plan at a rate no greater than the sum of identified standard indices and associated margins, no violation of section 411(a) or 417(e) would result if the employee's entire accrued benefit is distributed in the form of a single sum distribution equal to the employee's hypothetical account balance, provided the plan uses appropriate annuity conversion factors. Since the issuance of Notice 96-8, four federal appellate courts have followed the analysis set out in the Notice: *Esden v. Bank of Boston*, 229 F.3d 154 (2d Cir. 2000), *cert. dismissed*, 531 U.S. 1061 (2001); *West v. AK Steel Corp. Ret. Accumulation Pension Plan*, 484 F.3d 395 (6th Cir. 2007), *reh'g and reh'g en banc denied*, No. 06-3442, 2007 U.S. App. LEXIS 20447 (6th Cir. Aug. 8, 2007); *Berger v. Xerox Corp. Ret. Income Guarantee Plan*, 338 F.3d 755 (7th Cir. 2003), *reh'g and reh'g en banc denied*, No. 02-3674, 2003 U.S. App. LEXIS 19374 (7th Cir. Sept. 15, 2003); *Lyons v. Georgia-Pacific Salaried Employees Ret. Plan*, 221 F.3d 1235 (11th Cir. 2000), *cert. denied*, 532 U.S. 967 (2001).

Notice 2007-6, 2007-3 IRB 272 (January 16, 2007), see § 601.601(d)(2)(ii)(b) of this chapter, provides transitional guidance with respect to certain requirements of sections 411(a)(13) and 411(b)(5) and section 701(b) of PPA '06. Notice 2007-6 includes certain special definitions, including: *accumulated benefit*, which is defined as a participant's benefit accrued to date under a plan; *lump sum-based plan*, which is defined as a defined benefit plan under the terms of which the accumulated benefit of a participant is expressed as the balance of a hypothetical account maintained for the participant or as the current value of the accumulated percentage of the participant's final average compensation; and *statutory hybrid plan*, which is a lump sum-based plan or a plan which has an effect similar to a lump sum-based plan. Notice 2007-6 provides guidance on a number of issues, including a rule under which a plan that provides for indexed benefits described in section 411(b)(5)(E) is a statutory hybrid plan (because it has an effect similar to a lump sum-based plan), unless the plan either solely provides for post-retirement adjustment of the amounts payable to a participant or is a variable annuity plan under which the assumed interest rate used to determine adjustments is at least 5 percent. The Notice provides a safe

² On December 11, 2002, the Treasury Department and the IRS issued proposed regulations regarding the age discrimination requirements of section 411(b)(1)(H) that specifically addressed cash balance plans as part of a package of regulations that also addressed section 401(a)(4) nondiscrimination cross-testing rules applicable to cash balance plans (67 FR 76123). The 2002 proposed regulations were intended to replace the 1988 proposed regulations. In Ann. 2003-22 (2003-1 CB 847), see § 601.601(d)(2)(ii)(b) of this chapter, the Treasury Department and the IRS announced the withdrawal of the 2002 proposed regulations under section 401(a)(4), and in Ann. 2004-57 (2004-2 CB 15), see § 601.601(d)(2)(ii)(b) of this chapter, the Treasury Department and the IRS announced the withdrawal of the 2002 proposed regulations relating to age discrimination.

harbor for applying the rules set forth in section 701 of PPA '06 where the conversion of a defined benefit pension plan into an applicable defined benefit plan is made with respect to a group of employees who become employees by reason of a merger, acquisition, or similar transaction. This transitional guidance, along with other guidance provided in Part III of Notice 2007-6, applies pending the issuance of further guidance and, thus, will cease to apply when these regulations are finalized and become effective.

Explanation of Provisions

Overview

In general, these proposed regulations would incorporate the transitional guidance provided under Notice 2007-6. However, the proposed regulations would utilize new terminology (such as statutory hybrid benefit formula and lump sum-based benefit formula) to take into account situations where plans provide more than one benefit formula. These proposed regulations would also provide additional guidance with respect to sections 411(a)(13) and 411(b)(5), taking into account comments received in response to Notice 2007-6.

Section 411(a)(13): Special Vesting Rules for Applicable Defined Benefit Plans and Applicable Definitions

The proposed regulations would reflect new section 411(a)(13)(A) by providing that an applicable defined benefit plan does not violate the requirements of section 411(a)(2), or the requirements of section 411(c) or 417(e), with respect to a participant's accrued benefit derived from employer contributions, merely because the plan determines the present value of benefits determined under a lump sum-based benefit formula as the amount of the hypothetical account maintained for the participant or as the current value of the accumulated percentage of the participant's final average compensation under that formula. However, section 411(a)(13) does not alter the definition of an accrued benefit under section 411(a)(7)(A) (which generally defines a participant's accrued benefit as the annual benefit commencing at normal retirement age), nor does it alter the definition of a normal retirement benefit under section 411(a)(9) (which generally defines a participant's normal retirement benefit as the benefit under the plan commencing at normal retirement age).

Section 411(b)(5)(G) provides that, for purposes of section 411(b)(5), any reference to the accrued benefit means the benefit accrued to date. The

proposed regulations refer to this as the accumulated benefit, which is distinct from the participant's accrued benefit under section 411(a)(7) (an annuity beginning at normal retirement age that is actuarially equivalent to the participant's accumulated benefit).

The regulations define a lump sum-based benefit formula as a benefit formula used to determine all or any part of a participant's accumulated benefit under which the benefit provided under the formula is expressed as the balance of a hypothetical account maintained for the participant or as the current value of the accumulated percentage of the participant's final average compensation. Under the proposed regulations, whether a benefit formula is a lump sum-based benefit formula would be determined based on how the accumulated benefit of a participant is expressed under the terms of the plan, and would not depend on whether the plan provides an optional form of benefit in the form of a single sum payment. Similarly, a formula would not fail to be a lump sum-based benefit formula merely because the plan's terms state that the accrued benefit is an annuity at normal retirement age that is actuarially equivalent to a hypothetical account balance. In addition, the regulations would provide that a participant is not treated as having a lump sum-based benefit formula merely because the participant is entitled to a benefit under a defined benefit plan that is not less than the benefit properly attributable to after-tax employee contributions.

Section 411(a)(13)(A) applies only with respect to a benefit provided under a lump sum-based benefit formula. Accordingly, if the present value rules of section 417(e) apply to a form of benefit under a plan and the plan provides benefits under a benefit formula that is not a lump sum-based benefit formula (including, for example, a plan that provides for indexing as described in section 411(b)(5)(E)), then the plan must set forth a methodology to determine the projected benefit under that formula at normal retirement age for purposes of applying the rules of section 417(e), as described in the "Analysis" section of Notice 96-8.

The proposed regulations use the term *statutory hybrid benefit formula* to describe the portion of a defined benefit plan that is an applicable defined benefit plan described in section 411(a)(13)(C)(i) or the portion of the plan that has a similar effect.

Specifically, the proposed regulations would define a statutory hybrid benefit formula as a benefit formula that is either a lump sum-based benefit formula

or a formula that has an effect similar to a lump sum-based benefit formula. For this purpose, under the proposed regulations, a benefit formula under a defined benefit plan has an effect similar to a lump sum-based benefit formula if the formula provides that a participant's accrued benefit payable at normal retirement age (or at benefit commencement, if later) is expressed as a benefit that includes periodic adjustments (including a formula that provides for indexed benefits described in section 411(b)(5)(E)) that are reasonably expected to result in a larger annual benefit at normal retirement age (or at commencement of benefits, if later) for the participant, when compared to a similarly situated, younger individual who is or could be a participant in the plan. Thus, a benefit formula under a plan has an effect similar to a lump sum-based benefit formula if the right to future adjustments accrues at the same time as the benefit that is subject to the adjustments.

The proposed regulations would set forth certain additional rules that are used in determining whether a benefit formula has an effect similar to a lump sum-based benefit formula. For example, the proposed regulations provide that a benefit formula that does not include periodic adjustments is treated as a formula with an effect similar to a lump sum-based benefit formula if the formula is otherwise described in the preceding paragraph and the adjustments are provided pursuant to a pattern of repeated plan amendments. See § 1.411(d)-4, A-1(c)(1). The proposed regulations would provide that, for purposes of determining whether a benefit formula has an effect similar to a lump sum-based benefit formula, indexing that applies to adjust benefits after the annuity starting date (for example, cost-of-living increases) is disregarded. In addition, the proposed regulations would provide that a benefit formula under a defined benefit plan that provides for a benefit properly attributable to after-tax employee contributions does not have an effect similar to a lump sum-based benefit formula. The proposed regulations would also provide that adjustments under a variable annuity do not have an effect similar to a lump sum-based benefit formula if the assumed interest rate used to determine the adjustments is at least 5 percent. Such an annuity does not have an effect similar to a lump sum-based benefit formula even if post-annuity starting date adjustments are

made using a specified assumed interest rate that is less than 5 percent.

Pursuant to new section 411(a)(13)(B), the proposed regulations would provide that, in the case of a participant whose accrued benefit (or any portion thereof) under a defined benefit plan is determined under a statutory hybrid benefit formula, the plan is not treated as meeting the requirements of section 411(a)(2) unless the plan provides that the participant has a nonforfeitable right to 100 percent of the participant's accrued benefit if the participant has 3 or more years of service. This requirement would apply on a participant-by-participant basis and would apply to the participant's entire benefit (not just the portion of the participant's benefit that is determined under a statutory hybrid benefit formula). Furthermore, if the participant is entitled to the greater of two benefits under a plan, one of which is a benefit calculated under a statutory hybrid benefit formula, the proposed regulations would provide that the 3-year vesting requirement applies to that participant even if the participant's benefit under the statutory hybrid benefit formula is ultimately smaller than under the other formula. The proposed regulations do not address how the 3-year vesting requirement applies in the case of floor-offset arrangements.³ See the discussion in this preamble under the heading "Comments and Requests for Public Hearing."

Section 411(b)(5): Safe Harbor for Age Discrimination, Conversion Protection, and Market Rate of Return Limitation

A. Safe Harbor for Age Discrimination

The proposed regulations under new section 411(b)(5)(A) would provide that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) with respect to certain benefit formulas if, as determined as of any date, a participant's accumulated benefit expressed under one of those formulas would not be less than any similarly situated, younger participant's accumulated benefit expressed under the same formula. A plan that does not satisfy this test is required to satisfy the general nondiscrimination test of section 411(b)(1)(H)(i).

Under the proposed regulations, the safe harbor standard for satisfying section 411(b)(5)(A) would be available only where a participant's accumulated benefit under the terms of the plan is expressed as an annuity payable at

normal retirement age (or current age, if later), the balance of a hypothetical account, or the current value of the accumulated percentage of the employee's final average compensation. For this purpose, if the accumulated benefit of a participant is expressed as an annuity payable at normal retirement age (or current age, if later) under the plan terms, then the comparison of benefits is made using such an annuity. If the accumulated benefit of a participant is expressed under the plan terms as the balance of a hypothetical account or the current value of an accumulated percentage of the participant's final average compensation, then the comparison of benefits is made using the balance of a hypothetical account or the current value of the accumulated percentage of the participant's final average compensation, respectively.

The proposed regulations would require a comparison of the accumulated benefit of each possible participant in the plan to the accumulated benefit of each other similarly situated, younger individual who is or could be a participant in the plan. For this purpose, the proposed regulations would provide that an individual is similarly situated to another individual if the individual is identical to that other individual in every respect that is relevant in determining a participant's benefit under the plan (including but not limited to period of service, compensation, position, date of hire, work history, and any other respect) except for age.⁴ In determining whether an individual is similarly situated to another individual, any characteristic that is relevant for determining benefits under the plan and that is based directly or indirectly on age is disregarded. For example, if a particular benefit formula applies to a participant on account of the participant's age, an individual to whom the benefit formula does not apply and who is identical to a participant in all respects other than age is similarly situated to the participant. By contrast, an individual is not similarly situated to a participant if a different benefit formula applies to the individual and the application of the different formula is based neither directly nor indirectly on age.

³ For example, if a plan provides for an election extended to all participants that affects a participant's accumulated benefit, then someone who makes such an election is similarly situated to a participant who makes such an election, and someone who does not make an election is similarly situated to a participant who does not make such an election.

The comparison of accumulated benefits is made without regard to any subsidized portion of any early retirement benefit that is included in a participant's accumulated benefit. For this purpose, the subsidized portion of an early retirement benefit is the retirement-type subsidy within the meaning of § 1.411(d)-3(g)(6) that is contingent on a participant's severance from employment and commencement of benefits before normal retirement age.

In addition, the comparison of accumulated benefits generally must be made using the same form of benefit. Thus, the safe harbor is not available for comparing the accumulated benefit of a participant expressed as an annuity at normal retirement age with the accumulated benefit of a similarly situated, younger participant expressed as a hypothetical account balance. Nevertheless, the proposed regulations would permit a plan that provides the sum of benefits that are expressed in two or more different forms of benefit to satisfy the safe harbor if the plan would separately satisfy the safe harbor for each separate form of benefit. Similarly, the proposed regulations would permit a plan that provides the greater of benefits that are expressed in two or more different forms of benefit to satisfy the safe harbor if the plan would separately satisfy the safe harbor for each separate form of benefit. For this purpose, a similarly situated, younger participant is treated as having an accumulated benefit of zero with respect to a benefit formula that does not apply to the participant. Thus, the safe harbor would be available if an older participant is entitled to benefits under more than one type of benefit formula, even if not all of those types of benefit formulas are available to every similarly situated participant who is younger.

The proposed regulations would reflect new section 411(b)(5)(C), which provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides offsets of benefits under the plan to the extent such offsets are allowable in applying the requirements under section 401 and the applicable requirements of the Employee Retirement Income Security Act of 1974, Public Law 93-406 (88 Stat. 829) (ERISA) and the Age Discrimination in Employment Act of 1967, Public Law 90-202 (81 Stat. 602) (ADEA). The proposed regulations incorporate the provisions of section 411(b)(5)(D) (relating to permitted disparity under section 401(l)) without providing additional guidance.

The proposed regulations would reflect new section 411(b)(5)(E), which

³ See Rev. Rul. 76-259 (1976-2 CB 111), see § 601.601(d)(2)(ii)(b) of this chapter, for certain standards applicable to floor-offset arrangements.

provides for the disregard of certain indexing of benefits for purposes of the age discrimination rules of section 411(b)(1)(H). The proposed regulations limit the disregard of indexing to formulas under defined benefit plans other than lump sum-based formulas. In addition, the proposed regulations limit the disregard of indexing to situations in which the extent of the indexing for a participant would not be less than the indexing applicable to a similarly situated, younger participant. Thus, the disregard of indexing is only available if the indexing is neither terminated nor reduced on account of the attainment of any age.

Section 411(b)(5)(E) requires that the indexing methodology be a recognized methodology. The proposed regulations would treat only the following indexing methodologies as recognized for this purpose: indexing using an eligible cost-of-living index as described in § 1.401(a)(9)-6, A-14(b); indexing using the rate of return on the aggregate assets of the plan; and indexing using the rate of return on the annuity contract for the employee issued by an insurance company licensed under the laws of a State.

Under the proposed regulations, the section 411(b)(5)(E)(ii) protection against loss (“no-loss”) requirement for an indexed plan (which provides that the indexing not result in a smaller accrued benefit) would be implemented by applying the “preservation of capital” rule of section 411(b)(5)(b)(i)(II) to indexed plans. (The preservation of capital rule is discussed in this preamble paragraph heading “C. Market rate of return limitation.”) For this purpose, the exemption from the application of the no-loss rule for variable annuities would be limited to situations in which the variable annuity adjustment is based on the rate of return on the aggregate assets of the plan or the annuity contract. Thus, the exemption from the application of the no-loss rule would not apply if the variable annuity adjustment is based on the rate of return of a portion of the assets of the plan. In addition, this exemption would also apply for purposes of the preservation of capital requirement that applies to statutory hybrid plans.

B. Conversion Protection

The regulations would provide guidance on the new conversion protections under section 411(b)(5)(B)(ii), (iii), and (iv). Under the proposed regulations, a participant whose benefits are affected by a conversion amendment which occurred after June 29, 2005, must generally be provided with a benefit after the

conversion that is at least equal to the sum of the benefits accrued through the date of the conversion and benefits earned after the conversion, with no permitted interaction between these two portions. This would assure participants that there will be no “wear-away” as a result of a conversion, both with respect to the participant’s accrued benefits and any early retirement subsidy to which the participant is entitled based on the pre-conversion benefits.

The proposed regulations would provide an alternative mechanism under which the plan provides for the establishment of an opening hypothetical account balance as part of the conversion and keeps separate track of (1) The opening hypothetical account balance and interest credits attributable thereto, and (2) The post-conversion hypothetical contributions and interest credits attributable thereto. Under this alternative, the plan must provide that, when a participant commences benefits, the plan will determine whether the benefit attributable to the opening hypothetical account payable in the particular optional form of benefit selected is greater than or equal to the benefit accrued under the plan prior to the date of conversion and payable in the same generalized optional form of benefit (within the meaning of § 1.411(d)-3(g)(8)) at the same annuity starting date. For example, if a participant elects a straight life annuity payable at age 60, the plan must determine if the straight life annuity payable at age 60 that is attributable to the opening hypothetical account balance is greater than or equal to the straight life annuity payable at age 60 based on service prior to the conversion and determined under the terms of the pre-conversion plan. If the benefit attributable to the opening hypothetical account balance is greater, then the plan must provide that such benefit is paid in lieu of the pre-conversion benefit together with the benefit attributable to post-conversion contribution credits. If the benefit attributable to the opening hypothetical account balance is less, then the plan must provide that such benefit will be increased sufficiently to provide the pre-conversion benefit. In such a case, the participant must also be entitled to the benefit attributable to post-conversion contribution credits.

The proposed regulations would provide that, if an optional form of benefit is available on the annuity starting date with respect to the benefit attributable to the opening hypothetical account balance or opening accumulated percentage, but no optional form within the same generalized optional form of benefit was

available at that annuity starting date under the terms of a plan as in effect immediately prior to the effective date of the conversion amendment, then the comparison must still be made by assuming that the pre-conversion plan had such an optional form of benefit. For example, if the pre-conversion plan did not provide for a single sum distribution option, the alternative would require that any single sum distribution option that is attributable to the opening hypothetical account balance be greater than or equal to the present value of the pre-conversion benefit, where present value is determined in accordance with section 417(e).

The IRS and the Treasury Department are seeking comments on another alternative means of satisfying the conversion requirements that would involve establishing an opening hypothetical account balance, but in limited situations would not require the subsequent comparison. Any such alternative would be permitted only if it were designed to provide adequate protection to participants in plans that adopt conversion amendments. For example, such an alternative might be limited to situations in which the participant elects a single sum distribution, and where the pre-conversion plan either did not provide a single sum option or had a single sum option that was based on the benefit payable at normal retirement age (rather than the benefit payable at early retirement age). In those situations, the alternative might provide that the comparison is not necessary if (1) The opening hypothetical account balance is equal to the present value of the pre-conversion benefit determined in accordance with section 417(e), (2) The interest credits on the opening hypothetical account balance are reasonably expected to be no lower than the interest rate used to determine the opening hypothetical account balance, and (3) Either the plan provides a death benefit equal to the hypothetical account balance or no pre-retirement mortality decrement is applied in establishing the opening hypothetical account balance. Such an alternative could result in a single sum distribution attributable to the pre-conversion benefit that is lower, or higher, than the present value of the pre-conversion benefit, depending on whether the actual interest credits applicable to the opening hypothetical account balance during the interim are lower, or higher, than the interest rate used in determining the opening hypothetical account balance and whether the

applicable interest rate and applicable mortality table under section 417(e)(3) have changed in the interim.

The proposed regulations also would provide guidance on what constitutes a conversion amendment under section 411(b)(5)(B)(v). Under the proposed regulations, whether an amendment is a conversion amendment is determined on a participant-by-participant basis. The proposed regulations would provide that an amendment (or amendments) is a conversion amendment with respect to a participant if it meets two criteria: (1) The amendment reduces or eliminates the benefits that, but for the amendment, the participant would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula and under which the participant was accruing benefits prior to the amendment, and (2) After the effective date of the amendment, all or a portion of the participant's benefit accruals under the plan are determined under a statutory hybrid benefit formula.

The proposed regulations would provide that only amendments that reduce or eliminate accrued benefits described in section 411(a)(7), or retirement-type subsidies described in section 411(d)(6)(B)(i), that would otherwise accrue as a result of future service are treated as amendments that reduce or eliminate the participant's benefits that would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula. Under the proposed regulations, a plan is treated as having been amended for this purpose if, under the terms of the plan, a change in the conditions of a participant's employment results in a reduction or elimination of the benefits that the participant would have accrued in the future under a benefit formula that is not a statutory hybrid benefit formula (for example, a job transfer from an operating division covered by a non-statutory hybrid defined benefit plan to an operating division that is covered by a cash balance formula). However, in the absence of coordination between the formulas, the special requirements for conversion amendments typically will be satisfied automatically.

The proposed regulations would provide rules prohibiting the avoidance of the conversion protections through the use of multiple plans or multiple employers. Under the proposed regulations, an employer is treated as having adopted a conversion amendment if the employer adopts an amendment under which a participant's benefits under a plan that is not a

statutory hybrid plan are coordinated with a separate plan that is a statutory hybrid plan, such as through a reduction (offset) of the benefit under the plan that is not a statutory hybrid plan. In addition, if an employee's employer changes as a result of a merger, acquisition, or other transaction described in § 1.410(b)-2(f), then the two employers would be treated as a single employer for this purpose. Thus, for example, in an acquisition, if the buyer adopts an amendment to its statutory hybrid plan under which a participant's benefits under the seller's plan (that is not a statutory hybrid plan) are coordinated with benefits under the buyer's plan, such as through a reduction (offset) of the buyer's plan benefits, the seller and buyer would be treated as a single employer and as having adopted a conversion amendment. However, if there is no coordination between the plans, there is no conversion amendment.

The proposed regulations would provide that a conversion amendment also includes multiple amendments that result in a conversion amendment, even if the amendments would not be conversion amendments individually. Under the proposed regulations, if an amendment to provide a benefit under a statutory hybrid benefit formula is adopted within 3 years after adoption of an amendment to reduce non-statutory hybrid benefit formula benefits, then those amendments would be consolidated in determining whether a conversion amendment has been adopted. In the case of an amendment to provide a benefit under a statutory hybrid benefit formula that is adopted more than 3 years after adoption of an amendment to reduce non-statutory hybrid benefit formula benefits, there would be a presumption that the amendments are not consolidated unless the facts and circumstances indicate that adoption of an amendment to provide a statutory hybrid benefit formula was intended at the time of the reduction in the non-statutory hybrid benefit formula.

The proposed regulations would provide that the effective date of a conversion amendment is, with respect to a participant, the date as of which the reduction occurs of the benefits that the participant would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula. In accordance with section 411(d)(6), the proposed regulations would provide that the date of a reduction of those benefits cannot be earlier than the date of adoption of the conversion amendment.

C. Market Rate of Return Limitation

The proposed regulations would reflect the rule in section 411(b)(5)(B)(i)(I) under which a statutory hybrid plan is treated as failing to satisfy section 411(b)(1)(H) if it provides an interest crediting rate that is in excess of a market rate of return. The proposed regulations would define an interest crediting rate as the rate by which a participant's benefit is increased under the ongoing terms of a plan to the extent the amount of the increase is not conditioned on current service, regardless of how the amount of that increase is calculated. Thus, whether the amount is an interest credit for this purpose is determined without regard to whether the amount is calculated by reference to a rate of interest, a rate of return, an index, or otherwise.

The proposed regulations would require a plan to specify the timing for determining the plan's interest crediting rate that will apply for each plan year (or portion of a plan year) using one of two permitted methods—either pursuant to a daily interest crediting rate based on permissible interest crediting rates specified in the proposed regulations, or pursuant to a specified lookback month and stability period. For this purpose, the plan's lookback month and stability period must satisfy the rules for selecting the lookback month and stability period under § 1.417(e)-1(d)(4). However, the stability period and lookback month need not be the same as those used under the plan for purposes of section 417(e)(3).

In addition, the proposed regulations would require a plan to specify the periodic (at least annual) frequency at which interest credits are made under the plan. If, under a plan, interest is credited more frequently than annually (for example, monthly or quarterly), then the interest credit for that period must be a pro rata portion of the annual interest credit. Thus, for example, in the case of a plan the terms of which provide for interest to be credited at an interest crediting rate that would be permitted under the proposed regulations, if the plan provides for monthly interest credits and if the interest rate for a plan year has a value of 6 percent, then the accumulated benefits at the beginning of each month would be increased by 0.5 percent per month during the plan year. The proposed regulations would provide that interest credits are not treated as creating an effective rate of return in excess of a market rate of return merely because an otherwise permissible

interest crediting rate is compounded more frequently than annually.

The proposed regulations would provide that an interest crediting rate for a plan year is not in excess of a market rate of return if it is based on specified indices. As in Notice 2007-6, these include the safe harbor rates described in Notice 96-8, the interest rates on 30-Year Treasury securities, and the rate of interest on long-term investment grade corporate bonds (as described in section 412(b)(5)(B)(ii)(II) prior to amendment by PPA '06 for plan years beginning before January 1, 2008, and the third-segment bond rate used under section 430 for subsequent plan years). For this purpose, the third-segment bond rate is permitted to be determined with or without regard to the transition rules of section 430(h)(2)(G).

These rates would be required to change on at least an annual basis.⁵ These rates are market yields to maturity on outstanding bonds and do not reflect the change in the market value of an outstanding bond as a result of future changes in the interest rate environment or in a bond issuer's risk profile.⁶ As noted in the preceding paragraph, the proposed rules generally are similar to those described in Notice 2007-6 but do not provide guidance on a number of issues related to market rate of return. It is expected that these issues will be addressed in the first part of 2008.

The proposed regulations would reflect the preservation of capital rule in section 411(b)(5)(B)(i)(II) that requires a statutory hybrid plan to provide that interest credits will not result in a hypothetical account balance (or similar amount) being less than the aggregate amount of the hypothetical allocations. Under the proposed regulations, this requirement would be applied at the participant's annuity starting date. In addition, the proposed regulations would provide that the combination of this preservation of capital protection with a rate of return which otherwise satisfies the market rate of return limitation will not result in an effective interest crediting rate that is in excess of a market rate of return.

⁵ The requirement that an interest crediting rate change not less frequently than annually is intended to distinguish these rates from fixed rates, which are discussed later in this preamble. See also § 31.3121(v)(2)-1(d)(2)(i)(C)(2) of the Employment Tax Regulations, which permits a rate to be fixed for up to 5 years.

⁶ Because this interest rate does not reflect the change in the market value of an outstanding bond when an issuer becomes higher risk or the bond goes into default, the bonds have been limited to investment grade bonds in the top three quality levels where the risk of default is small.

While the second sentence of section 411(b)(5)(B)(i)(I) provides that a statutory hybrid plan is not treated as having an above-market rate merely because the plan provides for a reasonable minimum guaranteed rate of return or for a rate of return that is equal to the greater of a fixed or variable rate of return, these proposed regulations do not provide guidance for these alternatives. Moreover, the presence of a preservation of capital requirement indicates that Congress considered that a rate of return that could be negative in some years (such as a rate of return on an equity portfolio) could be permissible. However, as discussed in the following paragraphs, the Treasury Department and the IRS have concerns that the use of a minimum guaranteed rate of return or the use of the greater of a fixed and a variable rate could result in effective interest crediting rates that are above market rates of return and are soliciting comments on how to avoid that result.

Some commentators have suggested that it should be acceptable for a plan to adopt a fixed interest crediting rate that would apply without regard to changes in the interest rate environment. This is particularly important where the plan provides for hypothetical contributions that increase with age or service and the plan needs a minimum interest crediting rate in order to satisfy the accrual rules of section 411(b). While this issue is reserved under these proposed regulations, the approach suggested by commentators could be accomplished in two different ways. Under one possibility, the regulations might set forth a specific interest crediting rate (such as 4 percent or 5 percent) that a plan may be permitted to use. Under an alternative approach, the regulations might set forth a permitted methodology under which a plan would be permitted to establish a fixed interest crediting rate based on the then-applicable level of a permissible rate, such as the 3rd segment rate. For example, if the 3rd segment rate were 5.5 percent at the time the fixed rate is established under the plan, then under the alternative approach the plan might be permitted to fix the interest crediting rate at 5.5 percent. Comments are requested on these alternatives. In particular, comments are requested as to rules that the regulations could set forth that would avoid the potential for the fixed rate to be established at a time when interest rates are unusually high, such as occurred in the early 1980s.

With respect to the option for a plan to use an interest crediting rate that is the greater of a fixed or variable interest

rate, the Treasury Department and the IRS believe that the interaction between the two interest rates must be taken into account in determining whether the effective interest crediting rate under a plan which provides an interest crediting rate that is equal to the greater of a fixed or variable interest rate is above a market rate of return. Whether a statutory hybrid plan that is providing interest credits based on the greater of a fixed or variable interest rate effectively provides an interest crediting rate that exceeds a market rate of return depends on a number of factors, including how high the fixed interest rate is, how frequently the "greater of" determination is applied, and the volatility of the variable interest rate.

As noted earlier, the proposed regulations would provide that including the preservation of capital rule does not cause the plan's effective interest crediting rate to be in excess of a market rate of return. This rule reflects the fact that the minimum rate under the preservation of capital rule is an interest rate of 0 percent which is applied on a one-time basis at the annuity starting date, and is premised on the expectation that the variable rate would rarely be negative for extended periods of time (so that the inclusion of the capital preservation rule should not significantly increase the effective rate of return under the plan). If the variable rate is the rate of interest on bonds that would be permitted under the proposed regulations, then that expectation is easily met.

By contrast, if the variable interest rate is the rate of return on an equity investment, the expectation that the capital preservation rule does not significantly increase the effective interest crediting rate is only applicable if the equity investment is a well-diversified portfolio. This is because a well-diversified portfolio should have sufficiently limited volatility so that the inclusion of the preservation of capital rule should not significantly increase the effective rate of return resulting from interest credits that are based on that portfolio. Accordingly, if the regulations were to permit the use of an interest crediting rate based on an asset portfolio as an interest credit, the regulations might limit the choice of portfolio to the actual plan assets (relying on the fiduciary rules to ensure that the portfolio is adequately diversified). Of course, any such regulations would only permit the use of an interest crediting rate based on an asset portfolio if the use of such a rate is prospective and is selected before the period during which the rate is determined.

Comments are requested on what other asset portfolios have sufficiently constrained volatility that they should be permitted to form the basis of a market rate of return for interest crediting under a statutory hybrid plan and whether it is appropriate to base an interest crediting rate on the value of an index. For example, are the assets under a regulated investment company (RIC) described in section 851 sufficiently diversified such that a statutory hybrid plan will not be treated as providing an effective interest crediting rate in excess of a market rate of return where it credits interest based on the rate of return on the RIC and also provides for the preservation of capital (as required for a statutory hybrid plan under section 411(b)(5)(B)(i)(II))? Similarly, if a statutory hybrid plan credits interest based on the rate of return on an equity index that is not a narrow-based equity index (as defined under section 3(a)(55) of the Securities Exchange Act of 1934) and which also provides for the preservation of capital, is the plan providing an interest crediting rate that is not in excess of a market rate of return?

If the determination of the greater of a fixed interest crediting rate and a variable interest crediting rate is made more frequently than required to comply with the capital preservation rule, the added frequency is more likely to result in an effective interest crediting rate that is in excess of a market rate of return. For example, if a statutory hybrid plan were to credit interest each day based on the greater of the actual rate of return on the plan assets for that day or 0 percent, the effective interest crediting rate would be far in excess of a market rate of return.

The Treasury Department and the IRS are considering providing that a plan will not have an effective interest crediting rate in excess of a market rate of return merely because it provides annual interest credits based on the greater of a reasonable fixed rate (such as 3 percent or 4 percent) and one of the rates of interest set forth in the proposed regulations. However, if a statutory hybrid plan were to provide interest credits based on the greater of a fixed rate (including a fixed rate of 0 percent) and the rate of return on plan assets or the value of an equity-based index, determined on an annual basis, then the effective interest crediting rate would typically be in excess of a market interest rate. Comments are requested on what types of reductions to the variable rate would be appropriate in order to ensure that the effective interest crediting rate under these situations does not exceed a market rate of return.

In addition, comments are requested on whether regulations should establish reductions in these situations where the determination of whether the fixed or variable interest crediting rate is greater is made more frequently than annually.

Pending issuance of guidance addressing this issue, plan sponsors should be cautious in adopting interest crediting rates other than those explicitly permitted in these proposed regulations. If such a rate were adopted, and it did not satisfy the requirement not to be in excess of a market rate of return under rules provided in future guidance, the rate would have to be reduced in order to satisfy the requirement.

The proposed regulations would provide that, to the extent that interest credits (or equivalent amounts) have accrued under the terms of a statutory hybrid plan, section 411(d)(6) is violated by a plan amendment that changes the interest crediting rate if the revised rate under any circumstances could result in a lower rate of return after the applicable amendment date of the plan amendment. An exception is provided that would permit certain changes in a plan's interest crediting rate without violating section 411(d)(6). Under this exception, the proposed regulations would permit an amendment to change the plan's interest crediting rate for future periods from the safe harbor market rates of interest (for example, rates based on eligible cost-of-living indices, or rates based on Treasury bonds with the margins specified in the proposed regulations) to the rate of interest on long-term investment grade corporate bonds. Such a change would not constitute a reduction in accrued benefits in violation of section 411(d)(6) because it is expected that the change would result in a reduction only in rare and unusual circumstances, and the change would be permitted only if the amendment is effective not less than 30 days after adoption and, on the effective date of the amendment, the new interest crediting rate is not less than the interest crediting rate that would have applied in the absence of the amendment. In addition, the IRS and the Treasury Department may provide additional guidance regarding changes to the ongoing interest crediting rate under a plan that would or would not constitute a reduction of accrued benefits in violation of section 411(d)(6).

Pension Equity Plans (PEPs)

These proposed regulations do not include any rules specifically relating to plans that are often referred to as pension equity plans, or PEPs (other

than defining a participant's accumulated benefit under a PEP as the accumulated percentage of final average compensation). Notice 2007-6 requested comments on the application of qualification requirements other than sections 411(b)(1)(H) and 417(e) to such plans, including the treatment of interest credited with respect to terminated vested participants. See § 601.601(d)(2)(ii)(b) of this chapter. The IRS and the Treasury Department have received a number of comments pursuant to this request. These comments indicate that, apart from determining the accumulated benefit as a percentage of final average compensation, this design often provides explicit or implicit interest credits by determining the normal retirement benefit to be: (1) The accumulated percentage of final average compensation divided by a deferred annuity factor (thus implicitly providing interest and mortality credits for deferred benefits); or (2) The lesser of (a) the current single sum benefit projected to normal retirement age and using an interest rate set forth in the plan or (b) the projected single sum benefit based on projected service to normal retirement age (taking into account the plan's formula for the accumulated percentage of final average compensation without salary increases), with the lesser of these two amounts converted to an annuity. The right to future interest credits under these designs is earned at the same time as the related percentage of final average compensation; however, the comments indicated that the interest typically commences only after active participation ceases.

The IRS and the Treasury Department will continue to evaluate comments received regarding PEPs and are focusing on the following questions in situations where the interest credit is credited only after active participation ceases:

- Are these designs properly treated as plans under which the accrued benefit is expressed "as an accumulated percentage of the participant's final average compensation" within the meaning of section 411(a)(13)(A)? After the date on which interest credits commence, should these designs be treated as plans under which the accrued benefit is expressed "as the balance of a hypothetical account" within the meaning of section 411(a)(13)(A)?

- Do any of the designs in (1) or (2) of the preceding paragraph provide for a lower rate of accrual for additional years of service (because no interest is credited if service is continued)? See

section 411(b)(1)(G). Alternatively, can this issue be avoided by treating the annual rate at which the normal retirement benefit accrues as declining with each additional year of service?

- How should the backloading rules of section 411(b)(1)(A)–(C) apply to these designs and do they raise issues on which comments were requested in Notice 2007–14 (2007–7 IRB 501)? See § 601.601(d)(2)(ii)(b) of this chapter.

Section 1107 of PPA '06 and Code Section 411(d)(6)

Under section 1107 of PPA '06, a plan sponsor is permitted to delay adopting a plan amendment pursuant to statutory provisions under PPA '06 (or pursuant to any regulation issued under PPA '06) until the last day of the first plan year beginning on or after January 1, 2009 (January 1, 2011 in the case of governmental plans). As described in Rev. Proc. 2007–44 (2007–28 IRB 54), this amendment deadline applies to both interim and discretionary amendments that are made pursuant to PPA '06 statutory provisions or any regulation issued under PPA '06. See § 601.601(d)(2)(ii)(b) of this chapter. If section 1107 of PPA '06 applies to an amendment of a plan, section 1107 provides that the plan does not fail to meet the requirements of section 411(d)(6) by reason of such amendment, except as provided by the Secretary of the Treasury.⁷

The IRS and the Treasury Department are considering whether relief from section 411(d)(6) should be provided for particular amendments that would be made pursuant to section 701 of PPA '06 or these proposed regulations. In the following provisions of this section of the preamble, the IRS and the Treasury Department have set forth a description of amendments that are and are not entitled to section 411(d)(6) relief. Comments are requested on whether section 411(d)(6) relief is or is not appropriate for any additional amendments related to section 701 of PPA '06 or these proposed regulations.

Until further guidance is provided by the IRS and the Treasury Department, section 411(d)(6) relief is not available

⁷ Except to the extent permitted under section 411(d)(6) and §§ 1.411(d)–3 and 1.411(d)–4, or under a statutory provision such as section 1107 of PPA '06, section 411(d)(6) prohibits a plan amendment that decreases a participant's accrued benefits or that has the effect of eliminating or reducing an early retirement benefit or retirement-type subsidy, or eliminating an optional form of benefit, with respect to benefits attributable to service before the amendment. However, an amendment that eliminates or decreases benefits that have not yet accrued does not violate section 411(d)(6), provided that the amendment is adopted and effective before the benefits accrue.

for the following amendments that are described in section 1107 of PPA '06:

- A conversion amendment where the effective date of the reduction in benefits that a participant, but for the amendment, would have accrued under a benefit formula that is not a statutory hybrid benefit formula is earlier than the date of adoption of the reduction amendment.

- An amendment that reduces a participant's hypothetical account balance or accumulated percentage of final average compensation below the amount on the date the amendment is adopted.

- An amendment to change the interest crediting rate from one of the rates specified in Notice 96–8 using a margin that is less than or equal to the maximum margin for that rate to the same or another rate specified in Notice 96–8 with an associated margin where the excess (if any) of the maximum margin under the second rate over the margin used for that second rate exceeds the excess (if any) of the maximum margin under the first rate over the margin used for that first rate.

Until further guidance is provided by the IRS and the Treasury Department, section 411(d)(6) is available for the following amendments that are described in section 1107 of PPA '06:

- As provided in Notice 2007–6, in the case of a plan that provides for a single sum distribution to a participant that exceeds the participant's hypothetical account balance or accumulated percentage of final average compensation, the plan may be amended to eliminate the excess for distributions made after August 17, 2006. See § 601.601(d)(2)(ii)(b) of this chapter.

- An amendment to change the interest crediting rate from one of the rates specified in Notice 96–8 using a margin that is less than or equal to the maximum margin for that rate to one of the other rates specified in Notice 96–8 with an associated margin where the excess (if any) of the maximum margin under the second rate over the margin used for that second rate does not exceed the excess (if any) of the maximum margin under the first rate over the margin used for that first rate.

These rules under section 1107 of PPA '06 will be reflected in future guidance on the market rate of return rules under section 411(b)(5)(B)(i). The IRS and the Treasury Department expect that section 411(d)(6) relief under section 1107 of PPA '06 will be available in the case of an amendment pursuant to that future guidance to change a plan's interest crediting rate (including credits on pre-August 18,

2006 accruals) from an interest rate that is above a market rate of return to an interest rate that constitutes a market rate of return, provided that any retroactive change in the crediting rate does not apply for periods before the date that section 411(b)(5)(B)(i) first applies to the plan. In addition, to the extent permitted under future guidance, the IRS and the Treasury Department expect that section 411(d)(6) relief under section 1107 of PPA '06 will be available in the case of an amendment to change the plan's interest crediting rate to a rate that is expected to be higher than the plan's current rate (such as an amendment to change to an equity-based rate of return).

Effective/Applicability Dates

Pursuant to section 701(e)(1) of PPA '06, the amendments made by section 701 of PPA '06 are generally effective for periods beginning on or after June 29, 2005. However, sections 701(e)(2) through 701(e)(5) of PPA '06 set forth a number of special effective/applicability date rules that are described earlier in the Background section of the preamble of these proposed regulations.

These proposed regulations reflect the statutory effective dates set forth in section 701(e) of PPA '06. Thus, the proposed regulations would reflect that section 411(a)(13)(A) applies to distributions made after August 17, 2006. In addition, the proposed regulations would reflect that, in the case of a plan that is in existence on June 29, 2005, section 411(a)(13)(B) applies to plan years beginning on or after January 1, 2008. At the date of issuance of these proposed regulations, bills have been introduced in the House of Representatives and the Senate which provide that (1) section 411(a)(13)(B) only applies to a participant who performs at least one hour of service on or after the effective date of section 411(a)(13)(B) with respect to the plan, and (2) in the case of a plan other than a plan described in section 701(e)(3) or 701(e)(4) of PPA '06, section 411(a)(13)(B) applies to years ending on or after June 29, 2005.⁸ Proposed § 1.411(a)(13)–1(e)(1)(iii)(A)(2) and § 1.411(a)(13)–1(e)(1)(iii)(B)(2) have been reserved in order to accommodate these changes.

These regulations are proposed to be effective for plan years beginning on or after January 1, 2009 (or, if later, the date that applies to certain collectively bargained plans pursuant to section 701(e)(4) of PPA '06). For periods after the statutory effective date and before

⁸ H.R. 3361 (Aug. 3, 2007) and S. 1974 (Aug. 2, 2007), at section 8(3)(B)(iv).

the regulatory effective date set forth in the preceding sentence, a plan must comply with sections 411(a)(13) and 411(b)(5). During these periods, a plan is permitted to rely on the provisions set forth in the proposed regulations for purposes of satisfying the requirements of sections 411(a)(13) and 411(b)(5).

These regulations should not be construed to create any inference concerning the applicable law prior to the effective dates of sections 411(a)(13) and 411(b)(5). See also section 701(d) of PPA '06.

Special Analyses

It has been determined that these proposed regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, these regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Requests for Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (one signed and eight (8) copies) or electronic comments that are submitted timely to the IRS.

The IRS and the Treasury Department specifically request comments on the clarity of the proposed regulations and how they may be made easier to understand.

In addition to the comments requested under the "Conversion protection" and "Market rate of return limitation" headings of this preamble (and in Part V of Notice 2007-6), comments are also requested on issues not addressed in these proposed regulations, including:

- The application of the 3-year vesting requirement in section 411(a)(13)(B) to a plan that is not a statutory hybrid plan when the plan is part of a floor-offset arrangement with a plan that includes a lump sum-based benefit formula.

- Whether guidance should be issued under section 411(b)(5) as to whether a characteristic is indirectly on account of age.

- Whether the age discrimination safe harbor in section 411(b)(5)(A) should be

available in the case of any plan that does not express a participant's accumulated benefit as either an annuity payable at normal retirement age (or current age, if later), the balance of a hypothetical account, or the current value of the accumulated percentage of a participant's final average compensation.

All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person who timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place of the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of these regulations are Lauson C. Green and Linda S. F. Marshall, Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and the Treasury Department participated in the development of these regulations.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding entries as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.411(a)(13)-1 also issued under 26 U.S.C. 411(a)(13). Section 1.411(b)(5)-1 also issued under 26 U.S.C. 411(b)(5). * * *

Par. 2. Section 1.411(a)(13)-1 is added to read as follows:

§ 1.411(a)(13)-1 Statutory hybrid plans.

(a) *In general.* This section sets forth certain rules that apply to statutory hybrid plans under section 411(a)(13). Paragraph (b) of this section describes special rules for certain statutory hybrid plans that determine benefits under a lump sum-based benefit formula. Paragraph (c) of this section describes the vesting requirement for statutory hybrid plans. Paragraphs (d) and (e) of this section contain definitions and effective/applicability dates, respectively.

(b) *Calculation of benefit by reference to hypothetical account balance or accumulated percentage.* Pursuant to section 411(a)(13)(A), a statutory hybrid

plan that determines any portion of a participant's benefits under a lump sum-based benefit formula is not treated as failing to meet the requirements of section 411(a)(2), or the requirements of section 411(c) or 417(e) with respect to the participant's accrued benefit derived from employer contributions, solely because, with respect to benefits determined under that formula, the present value of those benefits is, under the terms of the plan, equal to the balance of the hypothetical account maintained for the participant or to the current value of the accumulated percentage of the participant's final average compensation under that formula.

(c) *Three-year vesting requirement—*
(1) *In general.* Pursuant to section 411(a)(13)(B), if any portion of the participant's accrued benefit under a defined benefit plan is determined under a statutory hybrid benefit formula, the plan is not treated as meeting the requirements of section 411(a)(2) unless the plan provides that the participant has a nonforfeitable right to 100 percent of the participant's accrued benefit if the participant has 3 or more years of service. Thus, this 3-year vesting requirement applies with respect to the entire accrued benefit of a participant under a defined benefit plan even if only a portion of the participant's accrued benefit under the plan is determined under a statutory hybrid benefit formula. Similarly, if the participant's accrued benefit under a defined benefit plan is, under the plan's terms, the larger of two (or more) benefit amounts, where each amount is determined under a different benefit formula (including a benefit determined pursuant to an offset among formulas within the plan) and at least one of those formulas is a statutory hybrid benefit formula, the participant's entire accrued benefit under the defined benefit plan is subject to the 3-year vesting rule of section 411(a)(13)(B) and this paragraph (c). The rule described in the preceding sentence applies even if the larger benefit is ultimately the benefit determined under a formula that is not a statutory hybrid benefit formula.

(2) *Floor-offset arrangements involving a statutory hybrid plan.*
[Reserved]

(3) *Examples.* The provisions of this paragraph (c) are illustrated by the following examples:

Example 1. Employer M sponsors Plan X, pursuant to which each participant's accrued benefit is equal to the sum of the benefit provided under two benefit formulas. The first benefit formula is a statutory hybrid benefit formula, and the second formula is not. Because a portion of each participant's

accrued benefit provided under Plan X is determined under a statutory hybrid benefit formula, the 3-year vesting requirement described in paragraph (c)(1) of this section applies to each participant's entire accrued benefit provided under Plan X.

Example 2. The facts are the same as in *Example 1*, except that the benefit formulas described in *Example 1* only apply to participants for service performed in Division A of Employer M and a different benefit formula applies to participants for service performed in Division B of Employer M. Pursuant to the terms of Plan X, the accrued benefit of a participant attributable to service performed in Division B is equal to the benefit provided by a benefit formula that is not a statutory hybrid benefit formula. Therefore, the 3-year vesting requirement described in paragraph (c)(1) of this section does not apply to a participant with an accrued benefit under Plan X if the participant's benefit is solely attributable to service performed in Division B.

(d) *Definitions*—(1) *In general.* The definitions in this paragraph (d) apply for purposes of this section.

(2) *Lump sum-based benefit formula.* The term lump sum-based benefit formula means a lump sum-based benefit formula as defined in § 1.411(b)(5)–1(e)(3).

(3) *Statutory hybrid benefit formula*—(i) *In general.* A statutory hybrid benefit formula means a benefit formula that is either a lump sum-based benefit formula or a formula that is not a lump sum-based benefit formula but that has an effect similar to a lump sum-based benefit formula.

(ii) *Effect similar to a lump sum-based benefit formula.* Except as provided in paragraph (d)(3)(iii) of this section, a benefit formula under a defined benefit plan that is not a lump sum-based benefit formula has an effect similar to a lump sum-based benefit formula if the formula provides that a participant's accumulated benefit (within the meaning of § 1.411(b)(5)–1(e)(2)) payable at normal retirement age (or benefit commencement, if later) is expressed as a benefit that includes the right to periodic adjustments (including a formula that provides for indexed benefits under § 1.411(b)(5)–1(b)(2)) that are reasonably expected to result in a larger annual benefit at normal retirement age (or benefit commencement, if later) for the participant than for a similarly situated, younger individual (within the meaning of § 1.411(b)(5)–1(b)(5)) who is or could be a participant in the plan. A benefit formula that does not include periodic adjustments is treated as a formula with an effect similar to a lump sum-based benefit formula if the formula is otherwise described in the preceding sentence and the adjustments are provided pursuant to a pattern of

repeated plan amendments. See § 1.411(d)–4, A–1(c)(1).

(iii) *Exceptions*—(A) *Post-retirement benefit adjustments.* Post-annuity starting date adjustments of the amounts payable to a participant (such as cost-of-living increases) are disregarded in determining whether a benefit formula under a defined benefit plan has an effect similar to a lump sum-based benefit formula.

(B) *Certain variable annuity benefit formulas.* If the assumed interest rate used for purposes of the adjustment of amounts payable to a participant under a variable annuity benefit formula is at least 5 percent, then the adjustments under the variable annuity benefit formula are not treated as being reasonably expected to result in a larger annual benefit at normal retirement age (or benefit commencement, if later) for the participant than for a similarly situated, younger individual (within the meaning of § 1.411(b)(5)–1(b)(5)) who is or could be a participant in the plan, and thus such a variable annuity benefit formula does not have an effect similar to a lump sum-based benefit formula.

(C) *Contributory plans.* A benefit formula under a defined benefit plan that provides for a benefit equal to the benefit properly attributable to after-tax employee contributions does not have an effect similar to a lump sum-based benefit formula. See section 411(c)(2) for rules for determining benefits attributable to after-tax employee contributions.

(4) *Variable annuity benefit formula.* A variable annuity benefit formula means any benefit formula under a defined benefit plan which provides that the amount payable is periodically adjusted by reference to the difference between the rate of return of plan assets (or specified market indices) and a specified assumed interest rate.

(e) *Effective/applicability date*—(1) *Statutory effective/applicability date*—(i) *In general.* Except as provided in paragraphs (e)(1)(ii) and (e)(1)(iii) of this section, section 411(a)(13) applies for periods beginning on or after June 29, 2005.

(ii) *Calculation of benefits.* Section 411(a)(13)(A) applies to distributions made after August 17, 2006.

(iii) *Vesting*—(A) *Plans in existence on June 29, 2005*—(1) *General rule.* In the case of a plan that is in existence on June 29, 2005 (regardless of whether the plan is a statutory hybrid plan on that date), section 411(a)(13)(B) applies to plan years beginning on or after January 1, 2008.

(2) *Hour of service required.* [Reserved]

(3) *Exception for plan sponsor election.* See § 1.411(b)(5)–1(f)(1)(iii)(A)(2) for a special election for early application of section 411(a)(13)(B).

(B) *Plans not in existence on June 29, 2005*—(1) *In general.* In the case of a plan not in existence on June 29, 2005, section 411(a)(13)(B) applies for periods beginning on or after June 29, 2005.

(2) *Hour of service required.* [Reserved]

(C) *Collectively bargained plans.* Notwithstanding paragraphs (e)(1)(iii)(A) and (B) of this section, in the case of a collectively bargained plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified on or before August 17, 2006, the requirements of section 411(a)(13)(B) do not apply for plan years beginning before the earlier of—

(1) The later of—

(i) The date on which the last of those collective bargaining agreements terminates (determined without regard to any extension thereof on or after August 17, 2006), or

(ii) January 1, 2008; or

(2) January 1, 2010.

(D) *Treatment of plans with both collectively bargained and non-collectively bargained employees.* In the case of a plan where a collective bargaining agreement applies to some, but not all, of the plan participants, the plan is considered a collectively bargained plan for purposes of paragraph (e)(1)(iii)(C) of this section if at least 25 percent of the participants in the plan are members of collective bargaining units for which the benefit levels under the plan are specified under a collective bargaining agreement.

(2) *Effective/applicability date of regulations.* This section applies for plan years beginning on or after January 1, 2009 (or, if later, the date applicable under paragraph (e)(1)(iii)(C) of this section). For the periods after the statutory effective date set forth in paragraph (e)(1) of this section and before the regulatory effective date set forth in the preceding sentence, a plan must comply with section 411(a)(13). During these periods, a plan is permitted to rely on the provisions of this section for purposes of satisfying the requirements of section 411(a)(13).

Par. 3. Section 1.411(b)(5)–1 is added to read as follows:

§ 1.411(b)(5)–1 Reduction in rate of benefit accrual under a defined benefit plan.

(a) *In general.* This section sets forth certain rules related to reduction in the rate of benefit accrual under a defined

benefit plan. Paragraph (b) of this section describes certain plan design-based safe harbors (including statutory hybrid plans) that are deemed to satisfy the age discrimination rules under section 411(b)(1)(H). Paragraph (c) of this section describes rules relating to statutory hybrid plan conversion amendments. Paragraph (d) of this section describes rules restricting interest credits (or equivalent amounts) under a statutory hybrid plan to a market rate of return. Paragraphs (e) and (f) of this section contain definitions and effective/applicability dates, respectively.

(b) *Safe harbors for certain plan designs*—(1) *Accumulated benefit testing*—(i) *In general*. Pursuant to section 411(b)(5)(A), and subject to paragraph (b)(1)(ii) of this section, a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) if, as of any date, the accumulated benefit of a participant would not be less than the accumulated benefit of any similarly situated, younger participant. This test requires a comparison of the accumulated benefit of each individual who is or could be a participant in the plan with the accumulated benefit of each other similarly situated, younger individual who is or could be a participant in the plan. See paragraph (b)(5) of this section for rules regarding whether each younger individual who is or could be a participant is similarly situated to a participant. The comparison described in this paragraph (b)(1)(i) is based on—

(A) The annuity payable at normal retirement age (or current age, if later) if the accumulated benefit of the participant under the terms of the plan is expressed as an annuity payable at normal retirement age (or current age, if later);

(B) The balance of a hypothetical account if the accumulated benefit of the participant under the terms of the plan is expressed as a hypothetical account balance; or

(C) The current value of an accumulated percentage of the participant's final average compensation if the accumulated benefit of the participant under the terms of the plan is expressed as an accumulated percentage of final average compensation.

(ii) *Benefit formulas for comparison*—(A) *In general*. The safe harbor provided by section 411(b)(5)(A) and paragraph (b)(1)(i) of this section does not apply to a plan if the accumulated benefit of a participant under the plan is not described in paragraph (b)(1)(i)(A), (B), or (C) of this section. In addition, except as provided in paragraph (b)(1)(ii)(B) of

this section, that safe harbor also does not apply to a plan if the comparison required under paragraph (b)(1)(i) of this section involves comparing accumulated benefits that are described in different subparagraphs of paragraph (b)(1)(i) of this section. Thus, for example, if a plan provides an accumulated benefit that is expressed under the terms of the plan as an annuity payable at normal retirement age as described in paragraph (b)(1)(i)(A) of this section for participants who are age 55 or over, and the plan provides an accumulated benefit that is expressed as the balance of a hypothetical account as described in paragraph (b)(1)(i)(B) of this section for participants who are younger than age 55, the safe harbor described in section 411(b)(5)(A) and paragraph (b)(1)(i) of this section does not apply to the plan.

(B) *Greater-of and sum-of benefit formulas*. If a plan provides that a participant's accumulated benefit is equal to the sum of accumulated benefits that are described in different subparagraphs of paragraph (b)(1)(i) of this section, then the plan is deemed to satisfy paragraph (b)(1)(i) of this section if the plan satisfies the comparison described in paragraph (b)(1)(i) of this section separately for each of the different accumulated benefits. Similarly, if a plan provides that a participant's accumulated benefit is equal to the greater of accumulated benefits that are described in different subparagraphs of paragraph (b)(1)(i) of this section, then the plan is deemed to satisfy paragraph (b)(1)(i) of this section if the plan satisfies the comparison described in paragraph (b)(1)(i) of this section separately for each of the different accumulated benefits. For purposes of this paragraph (b)(1)(ii)(B), a similarly situated, younger participant is treated as having an accumulated benefit of zero under a benefit formula if the benefit formula does not apply to the participant.

(iii) *Disregard of certain subsidized benefits*. For purposes of paragraph (b)(1)(i) of this section, any subsidized portion of any early retirement benefit that is included in a participant's accumulated benefit is disregarded. For this purpose, the subsidized portion of an early retirement benefit is the retirement-type subsidy within the meaning of § 1.411(d)-3(g)(6) that is contingent on a participant's severance from employment and commencement of benefits before normal retirement age.

(2) *Indexed benefits*—(i) *In general*. Except as provided in paragraph (b)(2)(iv) of this section, pursuant to section 411(b)(5)(E) and this paragraph

(b)(2)(i), a defined benefit plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because a benefit formula under the plan (other than a lump sum-based benefit formula) provides for the periodic adjustment of accrued benefits under the plan, but only if the adjustment is by means of the application of a recognized investment index or methodology described in paragraph (b)(2)(ii) of this section and the plan satisfies paragraph (b)(2)(iii) of this section. A statutory hybrid plan that is not treated as failing to satisfy section 411(b)(1)(H) pursuant to the preceding sentence must nevertheless satisfy the qualification requirements otherwise applicable to statutory hybrid plans, including the requirements of § 1.411(a)(13)-1(c) (relating to minimum vesting standards), paragraph (c) of this section (relating to plan conversion amendments), and paragraph (d) of this section (relating to market rates of return).

(ii) *Recognized investment index or methodology*. An adjustment is made pursuant to a recognized investment index or methodology if it is made pursuant to—

(A) An eligible cost-of-living index as described in § 1.401(a)(9)-6, A-14(b);

(B) The rate of return on the aggregate assets of the plan; or

(C) The rate of return on the annuity contract for the employee issued by an insurance company licensed under the laws of a State.

(iii) *Similarly situated participant test*. A plan satisfies this paragraph (b)(2)(iii) if the aggregate periodic adjustments of each participant's accrued benefit under the plan (determined as a percentage of the unadjusted accrued benefit) would not be less than the aggregate periodic adjustments of any similarly situated younger participant. This test requires a comparison of the aggregate periodic adjustments of each individual who is or could be a participant in the plan for any specified period with the aggregate periodic adjustments of each other similarly situated, younger individual who is or could be a participant in the plan for the same period. See paragraph (b)(5) of this section for rules regarding whether each younger individual who is or could be a participant is similarly situated to a participant.

(iv) *Protection against loss*—(A) *In general*. Paragraph (b)(2)(i) of this section does not apply unless the plan satisfies section 411(b)(5)(E)(ii) and paragraph (d)(2)(ii) of this section (relating to preservation of capital).

(B) *Exception for variable annuity benefit formulas*. The requirement to

satisfy section 411(b)(5)(E)(ii) and paragraph (d)(2)(ii) of this section does not apply in the case of a benefit provided under a variable annuity benefit formula, but only if the adjustments under the variable annuity benefit formula are based on the rate of return on the aggregate assets of the plan or the rate of return on the annuity contract for the employee issued by an insurance company licensed under the laws of a State.

(3) *Certain offsets permitted.* A plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides offsets against benefits under the plan to the extent the offsets are allowable in applying the requirements of section 401(a) and the applicable requirements of the Employee Retirement Income Security Act of 1974, Public Law 93–406 (88 Stat. 829), and the Age Discrimination in Employment Act of 1967, Public Law 90–202 (81 Stat. 602).

(4) *Permitted disparities in plan contributions or benefits.* A plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides a disparity in contributions or benefits with respect to which the requirements of section 401(l) are met.

(5) *Definition of similarly situated.* For purposes of paragraphs (b)(1) and (b)(2) of this section, an individual is similarly situated to another individual if the individual is identical to that other individual in every respect that is relevant in determining a participant's benefit under the plan (including period of service, compensation, position, date of hire, work history, and any other respect) except for age. In determining whether an individual is similarly situated to another individual, any characteristic that is relevant for determining benefits under the plan and that is based directly or indirectly on age is disregarded. For example, if a particular benefit formula applies to a participant on account of the participant's age, an individual to whom the benefit formula does not apply and who is identical to the participant in all other respects is similarly situated to the participant. By contrast, an individual is not similarly situated to a participant if a different benefit formula applies to the individual and the application of the different formula is not based directly or indirectly on age.

(c) *Special rules for plan conversion amendments—*(1) *In general.* Pursuant to section 411(b)(5)(B)(ii), (iii), and (iv), if there is a conversion amendment within the meaning of paragraph (c)(4) of this section with respect to a defined benefit plan, then the plan is treated as

failing to meet the requirements of section 411(b)(1)(H) unless the plan, after the amendment, satisfies the requirements of paragraph (c)(2) of this section.

(2) *Separate calculation of post-conversion benefit—*(i) *In general.* A statutory hybrid plan satisfies the requirements of this paragraph (c)(2) if the plan provides that, in the case of an individual who was a participant in the plan immediately before the date of adoption of the conversion amendment, the participant's benefit at any subsequent annuity starting date is not less than the sum of:

(A) The participant's section 411(d)(6) protected benefit (as defined in § 1.411(d)–3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment; and

(B) The participant's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

(ii) *Rules of application.* For purposes of this paragraph (c)(2), except as provided in paragraph (c)(3) of this section, the benefits under paragraph (c)(2)(i)(A) and (B) of this section must each be determined in the same manner as if they were provided under separate plans that are independent of each other (for example, without any benefit offsets), and, except to the extent permitted under § 1.411(d)–3 or § 1.411(d)–4 (or other applicable law), each optional form of payment provided under the terms of the plan with respect to a participant's section 411(d)(6) protected benefit as in effect before the amendment must be available thereafter to the extent of the plan's benefits for service prior to the effective date of the amendment.

(3) *Establishment of opening hypothetical account balance—*(i) *In general.* Provided that the requirements of paragraph (c)(3)(ii) of this section are satisfied, a statutory hybrid plan under which an opening hypothetical account balance or opening accumulated percentage of the participant's final average compensation is established as of the effective date of the conversion amendment does not fail to satisfy the requirements of paragraph (c)(2) of this section merely because benefits attributable to that opening hypothetical account balance or opening accumulated percentage (that is, benefits that are not described in paragraph (c)(2)(i)(B) of this section) are

substituted for benefits described in paragraph (c)(2)(i)(A) of this section.

(ii) *Comparison of benefits—*(A) *Testing requirement.* For any optional form of benefit payable at an annuity starting date where there was an optional form of benefit within the same generalized optional form of benefits (within the meaning of § 1.411(d)–3(g)(8)) that would have been available to the participant at that annuity starting date under the terms of the plan as in effect immediately before the effective date of the conversion amendment, the requirements of this paragraph (c)(3)(ii) are satisfied only if the plan provides that the amount of the benefit under that optional form of benefit available to the participant under the lump sum-based formula that is attributable to the opening hypothetical account balance or opening accumulated percentage as described in paragraph (c)(3)(i) of this section, determined under the terms of the plan as of the annuity starting date (including actuarial conversion factors), is not less than the benefit under that optional form of benefit described in paragraph (c)(2)(i)(A) of this section. To satisfy this requirement, if the benefit under an optional form attributable to the opening hypothetical account balance or opening accumulated percentage is less than the benefit described in paragraph (c)(2)(i)(A) of this section, then the benefit attributable to the opening hypothetical account balance or opening accumulated percentage must be increased to the extent necessary to provide the minimum benefit described in this paragraph (c)(3)(ii)(A). Thus, if a plan is using the option under this paragraph (c)(3) to satisfy paragraph (c)(2) of this section with respect to a participant, the participant must receive a benefit equal to not less than the sum of:

(1) The greater of the benefit attributable to the opening hypothetical account balance as described in this paragraph (c)(3)(ii) and the benefit described in paragraph (c)(2)(i)(A) of this section, and

(2) The benefit described in paragraph (c)(2)(i)(B) of this section.

(B) *Special rule for post-conversion optional forms of benefit.* If an optional form of benefit is available on the annuity starting date with respect to the benefit attributable to the opening hypothetical account balance or opening accumulated percentage, but no optional form within the same generalized optional form of benefit (within the meaning of § 1.411(d)–3(g)(8)) was available at that annuity starting date under the terms of a plan as in effect immediately prior to the effective date of the conversion

amendment, then, for purposes of this paragraph (c)(3)(ii), the plan is treated as if such an optional form of benefit were available immediately prior to the effective date of the conversion amendment. In that event, paragraph (c)(3)(ii)(A) of this section must be applied by taking into account the optional form of benefit that is treated as if it were available on the annuity starting date under the terms of the plan as in effect immediately prior to the effective date of the conversion amendment. Thus, for example, if a single sum optional form of payment is not available under the plan terms applicable to the accrued benefit described in paragraph (c)(2)(i)(A) of this section, but a single sum form of payment is available with respect to the benefit attributable to the opening hypothetical account balance or opening accumulated percentage as of the annuity starting date, then, for purposes of paragraph (c)(3)(ii)(A) of this section, the plan is treated as if a single sum (to which section 417(e)(3) applies) were available under the terms of the plan as in effect immediately prior to the effective date of the conversion amendment.

(4) *Conversion amendment*—(i) *In general.* An amendment is a conversion amendment that is subject to the requirements of this paragraph (c) with respect to a participant if—

(A) The amendment reduces or eliminates the benefits that, but for the amendment, the participant would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula (and under which the participant was accruing benefits prior to the amendment); and

(B) After the effective date of the amendment, all or a portion of the participant's benefit accruals under the plan are determined under a statutory hybrid benefit formula.

(ii) *Rules of application*—(A) *In general.* Paragraphs (c)(4)(iii), (iv), and (v) of this section describe special rules that treat certain arrangements as conversion amendments. The rules described in those paragraphs apply both separately and in combination. Thus, for example, in an acquisition described in § 1.410(b)–2(f), if the buyer adopts an amendment under which a participant's benefits under the seller's plan that is not a statutory hybrid plan are coordinated with a separate plan of the buyer that is a statutory hybrid plan, such as through an offset of the participant's benefit under the buyer's plan by the participant's benefit under the seller's plan, the seller and buyer are treated as a single employer under

paragraph (c)(4)(iv) of this section and they are treated as having adopted a conversion amendment under paragraph (c)(4)(iii) of this section. However, pursuant to paragraph (c)(4)(iii) of this section, if there is no coordination between the two plans, there is no conversion amendment.

(B) *Covered amendments.* Only amendments that eliminate or reduce accrued benefits described in section 411(a)(7), or a retirement-type subsidy described in section 411(d)(6)(B)(i), that would otherwise accrue as a result of future service are treated as amendments described in paragraph (c)(4)(i)(A) of this section.

(C) *Operation of plan terms treated as covered amendment.* If, under the terms of a plan, a change in the conditions of a participant's employment results in a reduction of the participant's benefits that would have accrued in the future under a benefit formula that is not a statutory hybrid benefit formula, the plan is treated for purposes of this paragraph (c)(4) as if such plan terms constitute an amendment that reduces the participant's benefits that would have accrued after the effective date of the change under a benefit formula that is not a statutory hybrid benefit formula. Thus, for example, if a participant transfers from an operating division that is covered by a non-statutory hybrid benefit formula to an operating division that is covered by a statutory hybrid benefit formula, there has been a conversion amendment as of the date of the transfer.

(iii) *Multiple plans.* An employer is treated as having adopted a conversion amendment if the employer adopts an amendment under which a participant's benefits under a plan that is not a statutory hybrid plan are coordinated with a separate plan that is a statutory hybrid plan, such as through a reduction (offset) of the benefit under the plan that is not a statutory hybrid plan.

(iv) *Multiple employers.* If the employer of an employee changes as a result of a transaction described in § 1.410(b)–2(f), then the two employers are treated as a single employer for purposes of this paragraph (c)(4).

(v) *Multiple amendments*—(A) *In general*—(1) *General rule.* For purposes of this paragraph (c)(4), a conversion amendment includes multiple amendments that result in a conversion amendment even if the amendments are not conversion amendments individually. For example, an employer is treated as having adopted a conversion amendment if the employer first adopts an amendment described in paragraph (c)(4)(i)(A) of this section

and, at a later date, adopts an amendment that adds a benefit under a statutory hybrid benefit formula as described in paragraph (c)(4)(i)(B) of this section, if they are consolidated under paragraph (c)(4)(v)(A)(2) of this section.

(2) *Delay between plan amendments.* In the case of an amendment to provide a benefit under a statutory hybrid benefit formula that is adopted within three years after adoption of an amendment to reduce non-statutory hybrid benefit formula benefits, those amendments are consolidated in determining whether a conversion amendment has been adopted. Thus, the later adoption of the statutory hybrid benefit formula will cause the earlier amendment to be treated as a conversion amendment. In the case of an amendment to provide a benefit under a statutory hybrid benefit formula that is adopted more than three years after adoption of an amendment to reduce benefits under a non-statutory hybrid benefit formula, there is a presumption that the amendments are not consolidated unless the facts and circumstances indicate that adoption of the amendment to provide a benefit under a statutory hybrid benefit formula was intended at the time of reduction in the non-statutory hybrid benefit formula.

(B) *Multiple conversion amendments.* If an employer adopts multiple amendments reducing benefits described in paragraph (c)(4)(i)(A) of this section, each amendment is treated as a separate conversion amendment, provided that paragraph (c)(4)(i)(B) of this section is applicable at the time of the amendment (taking into account the rules of this paragraph (c)(4)).

(vi) *Effective date of a conversion amendment.* The effective date of a conversion amendment is, with respect to a participant, the date as of which the reduction of the participant's benefits described in paragraph (c)(4)(i)(A) of this section occurs. In accordance with section 411(d)(6), the date of a reduction of those benefits cannot be earlier than the date of adoption of the conversion amendment.

(5) *Examples.* The following examples illustrate the application of paragraph (c) of this section:

Example 1. (i) *Facts where plan does not establish opening hypothetical account balance for participants and participant elects life annuity at normal retirement age.* Employer N sponsors Plan E, a defined benefit plan that provides an accumulated benefit, payable as a straight life annuity commencing at age 65 (which is Plan E's normal retirement age), based on a percentage of highest average compensation

times the participant's years of service. Plan E permits any participant who has had a severance from employment to elect payment in the following optional forms of benefit (with spousal consent if applicable), with any payment not made in a straight life annuity converted to an equivalent form based on reasonable actuarial assumptions: a straight life annuity; and a 50 percent, 75 percent, or 100 percent joint and survivor annuity. The payment of benefits may commence at any time after attainment of age 55, with an actuarial reduction if the commencement is before normal retirement age. In addition, the plan offers a single sum payment after attainment of age 55 equal to the present value of the normal retirement benefit using the applicable interest rate and mortality table under section 417(e)(3) in effect under the terms of the plan on the annuity starting date.

(ii) *Facts relating to the conversion amendment.* On January 1, 2010, Plan E is amended to eliminate future accruals under the highest average compensation benefit formula and to base future benefit accruals on a hypothetical account balance. For service on or after January 1, 2010, each participant's hypothetical account balance is credited monthly with a pay credit equal to a specified percentage of the participant's compensation during the month and also with interest based on the third segment rate described in section 430(h)(2)(C)(iii). With respect to benefits under the hypothetical account balance attributable to service on and after January 1, 2010, a participant is permitted to elect (with spousal consent) payment in the same generalized optional forms of benefit (even though different actuarial factors apply) as under the terms of the plan in effect before January 1, 2010, and also as a single sum distribution. The plan provides for the benefits attributable to service before January 1, 2010, to be determined under the terms of the plan as in effect immediately before the effective date of the amendment, and the benefits attributable to service on and after January 1, 2010 to be determined separately, under the terms of the plan as in effect after the effective date of the amendment, with neither benefit offsetting the other in any manner. Thus, each participant's benefits are equal to the sum of the benefits attributable to service before January 1, 2010 (to be determined under the terms of the plan as in effect immediately before the effective date of the amendment), plus the benefits attributable to the participant's hypothetical account balance.

(iii) *Facts relating to an affected participant.* Participant A is age 62 on January 1, 2010 and, on December 31, 2009, A's benefit for years of service before January 1, 2010, payable as a straight life annuity commencing at A's normal retirement age (age 65) which is January 1, 2013, is \$1,000 per month. Participant A has a severance from employment on January 1, 2013, and, on January 1, 2013, the hypothetical account balance, with pay credits and interest from January 1, 2010, to January 1, 2013, has become \$11,000. Using the conversion factors under the plan as amended on January 1, 2013, that balance is equivalent to a straight life annuity of \$100 per month commencing

on January 1, 2013. This benefit is in addition to the benefit attributable to service before January 1, 2010. Participant A elects (with spousal consent) a straight life annuity of \$1,100 per month commencing January 1, 2013.

(iv) *Conclusion.* Participant A's benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section because Participant A's benefit is not less than the sum of Participant A's section 411(d)(6) protected benefit (as defined in § 1.411(d)-3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment, and Participant A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 2. (i) Facts involving plan's establishment of opening hypothetical account balance and payment of pre-conversion accumulated benefit in life annuity at normal retirement age. The facts in this *Example 2* are the same as the facts under paragraph (i) of *Example 1*.

(ii) *Facts relating to the conversion amendment.* On January 1, 2010, Plan E is amended to eliminate future accruals under the highest average compensation benefit formula and to base future benefit accruals on a hypothetical account balance. An opening hypothetical account balance is established for each participant, and, under the plan's terms, that balance is equal to the present value of the participant's accumulated benefit on December 31, 2009 (payable as a straight life annuity at normal retirement age or immediately, if later), using the applicable interest rate and applicable mortality table under section 417(e)(3) on January 1, 2010. Under Plan E, the account based on this opening hypothetical account balance is maintained as a separate account from the account for accruals on or after January 1, 2010. The hypothetical account balance maintained for each participant for accruals on or after January 1, 2010, is credited monthly with a pay credit equal to a specified percentage of the participant's compensation during the month. A participant's hypothetical account balance (including both of the separate accounts) is credited monthly with interest based on the third segment rate described in section 430(h)(2)(C)(iii).

(iii) *Facts relating to optional forms of benefit.* Following severance from employment and attainment of age 55, a participant is permitted to elect (with spousal consent) payment in the same generalized optional forms of benefit as under the plan in effect prior to January 1, 2010, with the amount payable calculated based on the hypothetical account balance on the annuity starting date and the applicable interest rate and applicable mortality table on the annuity starting date. The single sum distribution is equal to the hypothetical account balance.

(iv) *Facts relating to conversion protection.* The plan provides that, as of a participant's annuity starting date, the plan will determine whether the benefit attributable to the

opening hypothetical account payable in the particular optional form of benefit selected is greater than or equal to the benefit accrued under the plan through the date of conversion and payable in the same generalized optional form of benefit with the same annuity starting date. If the benefit attributable to the opening hypothetical account balance is greater, the plan provides that such benefit is paid in lieu of the pre-conversion benefit, together with the benefit attributable to post-conversion contribution credits. If the benefit attributable to the opening hypothetical account balance is less, the plan provides that such benefit is increased sufficiently to provide the pre-conversion benefit, together with the benefit attributable to post-conversion contribution credits.

(v) *Facts relating to an affected participant.* On January 1, 2010, the opening hypothetical account balance established for Participant A is \$80,000, which is the present value of Participant A's straight life annuity of \$1,000 per month commencing at January 1, 2013, using the applicable interest rate and applicable mortality table under section 417(e)(3) in effect on January 1, 2010. On January 1, 2010, the applicable interest rate for Participant A is equivalent to a level rate of 5.5 percent. Thereafter, Participant's A's hypothetical account balance for subsequent accruals is credited monthly with a pay credit equal to a specified percentage of the participant's compensation during the month. In addition, Participant A's hypothetical account balance (including both of the separate accounts) is credited monthly with interest based on the third segment rate described in section 430(h)(2)(C)(iii).

(vi) *Facts relating to calculation of the participant's benefit.* Participant A has a severance from employment on January 1, 2013 at age 65, and elects (with spousal consent) a straight life annuity commencing January 1, 2013. On January 1, 2013, the opening hypothetical account balance, with interest credits from January 1, 2010, to January 1, 2013, has become \$95,000, which, using the conversion factors under the plan on January 1, 2013, is equivalent to a straight life annuity of \$1,005 per month commencing on January 1, 2013 (which is greater than the \$1,000 a month payable at age 65 under the terms of the plan in effect before January 1, 2010). This benefit is in addition to the benefit determined using the hypothetical account balance for service after January 1, 2010.

(vii) *Conclusion.* The benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant A because A's benefit is not less than the sum of (A) the greater of Participant A's benefits attributable to the opening hypothetical account balance and A's section 411(d)(6) protected benefit (as defined in § 1.411(d)-3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment, and (B) Participant A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 3. (i) Facts involving a subsequent decrease in interest rates. The facts are the same as in *Example 2*, except that, because of a decrease in bond rates after January 1, 2010, and before January 1, 2013, the rate of interest credited in that period averages less than 5.5 percent, and, on January 1, 2013, the effective applicable interest rate under section 417(e)(3) under the plan's terms is 4.7 percent. As a result, Participant A's opening hypothetical account balance plus attributable interest credits has increased to only \$87,000 on January 1, 2013, and, using the conversion factors under the plan on January 1, 2013, is equivalent to a straight life annuity commencing on January 1, 2013, of \$775 per month. Under the terms of Plan E, the benefit attributable to A's opening account balance is increased so that A's straight life annuity commencing on January 1, 2013, is \$1,000 per month. This benefit is in addition to the benefit attributable to the hypothetical account balance for service after January 1, 2010.

(ii) *Conclusion.* The benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant A because A's benefit is not less than the sum of (A) the greater of A's benefits attributable to the opening hypothetical account balance and A's section 411(d)(6) protected benefit (as defined in § 1.411(d)-3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment, and (B) A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 4. (i) Facts involving payment of a subsidized early retirement benefit. The facts are the same as in *Example 2*, except that under the terms of Plan E on December 31, 2009, a participant who retires before age 65 and after age 55 with 30 years of service has only a 3 percent per year actuarial reduction. Participant A has a severance from employment on January 1, 2011, when A is age 63 and has 30 years of service. On January 1, 2011, A's opening hypothetical account balance, with interest from January 1, 2010, to January 1, 2011, has become \$86,000, which, using the conversion factors under the plan (as amended) on January 1, 2011, is equivalent to a straight life annuity commencing on January 1, 2011, of \$850 per month.

(ii) *Facts relating to calculation of the participant's benefit.* Under the terms of Plan E on December 31, 2009, Participant A is entitled to a straight life annuity commencing on January 1, 2011, equal to at least \$940 per month (\$1,000 reduced by 3 percent for each of the 2 years that A's benefits commence before normal retirement age). Under the terms of Plan E, the benefit attributable to A's opening account balance is increased so that A is entitled to a straight life annuity of \$940 per month commencing on January 1, 2013. This benefit is in addition to the benefit determined using the hypothetical account balance for service after January 1, 2010.

(iii) *Conclusion.* The benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this

section with respect to Participant A because A's benefit is not less than the sum of (A) the greater of Participant A's benefits attributable to the opening hypothetical account balance (increased by attributable interest credits) and A's section 411(d)(6) protected benefit (as defined in § 1.411(d)-3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment, and (B) Participant A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 5. (i) Facts involving addition of a single sum payment option. The facts are the same as in *Example 2*, except that, before January 1, 2010, Plan E did not offer payment in a single sum distribution for amounts in excess of \$5,000. Plan E, as amended on January 1, 2010, offers payment in any of the available annuity distribution forms commencing at any time following severance from employment as were provided under Plan E before January 1, 2010. In addition, Plan E, as amended on January 1, 2010, offers payment in the form of a single sum attributable to service before January 1, 2010, which is the greater of the opening hypothetical account balance (increased by attributable interest credits) or a single sum distribution of the straight life annuity payable at age 65 using the same actuarial factors as are used for mandatory cashouts for amounts equal to \$5,000 or less under the terms of the plan on December 31, 2009. Participant B is age 40 on January 1, 2010, and B's opening hypothetical account balance (increased by attributable interest credits) is \$33,000 (which is the present value, using the conversion factors under the plan (as amended) on January 1, 2010, of Participant B's straight life annuity of \$1,000 per month commencing at January 1, 2035, which is when B will be age 65). Participant B has a severance from employment on January 1, 2013, and elects (with spousal consent) an immediate single sum distribution. Participant B's opening hypothetical account balance (increased by attributable interest) on January 1, 2013, is \$45,000. The present value, on January 1, 2013, of Participant B's benefit of \$1,000 per month, commencing immediately using the actuarial factors for mandatory cashouts under the terms of the plan on December 31, 2009, would result in a single sum payment of \$44,750. Participant B is paid a single sum distribution equal to the sum of \$45,000 plus an amount equal to B's January 1, 2013, hypothetical account balance for benefit accruals for service after January 1, 2010.

(ii) *Conclusion.* Because, under Plan E, Participant B is entitled to the sum of (A) the greater of the \$45,000 opening hypothetical account balance (increased by attributable interest credits) and \$44,750 (present value of the benefit with respect to service prior to January 1, 2010, using the actuarial factors for mandatory cashout distributions under the terms of the plan on December 31, 2009), plus (B) An amount equal to B's hypothetical account balance for benefit accruals for

service after January 1, 2010, the benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant B. If Participant B's hypothetical account balance under Plan E was instead less than \$44,750 on January 1, 2013, Participant B would be entitled to a single sum payment equal to the sum of \$44,750 and an amount equal to B's hypothetical account balance for benefit accruals for service after January 1, 2010.

Example 6. (i) Facts involving addition of new annuity optional form of benefit. The facts are the same as in *Example 2*, except that, after December 31, 2009, and before January 1, 2013, Plan E is amended to offer payment in a 5-, 10-, or 15-year term certain and life annuity, using the same actuarial assumptions that apply for other optional forms of distribution. When Participant A has a severance from employment on January 1, 2013, A elects (with spousal consent) a 5-year term certain and life annuity commencing immediately equal to \$935 per month. Application of the same actuarial assumptions to Participant A's benefit of \$1,000 per month (under Plan E as in effect on December 31, 2009), commencing immediately on January 1, 2013, would result in a 5-year term certain and life annuity commencing immediately equal to \$955 per month. Under the terms of Plan E, the benefit attributable to A's opening account balance is increased so that, using the conversion factors under the plan (as amended) on January 1, 2013, A's opening hypothetical account balance (increased by attributable interest credits) produces a 5-year term certain and life annuity commencing immediately equal to \$955 per month commencing on January 1, 2013. This benefit is in addition to the benefit determined using the January 1, 2013, hypothetical account balance for service after January 1, 2010.

(ii) *Conclusion.* This benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant A.

Example 7. (i) Facts involving addition of distribution option before age 55. The facts are the same as in *Example 5*, except that Participant B (age 43) elects (with spousal consent) a straight life annuity. Under Plan E, the straight life annuity attributable to Participant B's opening hypothetical account balance at age 43 is \$221 per month. Application of the same actuarial assumptions to Participant B's benefit of \$1,000 per month (under Plan E as in effect on December 31, 2009), commencing immediately on January 1, 2013, would result in a straight life annuity at age 43 equal to \$219 per month.

(ii) *Conclusion.* Because, under its terms, Plan E provides that Participant B is entitled to an amount not less than the present value (using the same actuarial assumptions as apply on January 1, 2013, in converting the \$45,000 hypothetical account balance attributable to the opening hypothetical account balance to the \$221 straight life annuity) of Participant B's straight life annuity of \$1,000 per month commencing at January 1, 2035, and the \$221 straight life annuity is in addition to the benefit accruals for service after January 1, 2010, payment of

the \$221 monthly annuity would satisfy the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant B.

(d) *Market rate of return*—(1) *In general*—(i) *Basic test*. Subject to paragraph (d)(3) of this section, a statutory hybrid plan satisfies the requirements of section 411(b)(1)(H) and this paragraph (d) only if, for any plan year, the interest crediting rate under the terms of the plan is no greater than a market rate of return.

(ii) *Definition of interest crediting rate and interest credit*. For purposes of this paragraph (d), a plan's interest crediting rate means the rate by which a participant's benefit is increased under the ongoing terms of the plan to the extent the amount of the increase is not conditioned on current service, regardless of how the amount of that increase is calculated. The amount of such an increase is an interest credit. Thus, whether the amount is an interest credit for this purpose is determined without regard to whether the amount is calculated by reference to a rate of interest, a rate of return, an index, or otherwise.

(iii) *Single rates*. Except as is otherwise provided in this paragraph (d)(1), an interest crediting rate is not in excess of a market rate of return only if the plan provides an interest credit for the year at a rate that is equal to one of the following rates that is specified in the terms of the plan:

(A) The interest rate on long-term investment grade corporate bonds (as described in paragraph (d)(4) of this section);

(B) An interest rate that is deemed to be not in excess of a market rate of return under paragraph (d)(5) of this section; or

(C) An interest rate that is described in paragraph (d)(6) of this section.

(iv) *Timing rules*—(A) *In general*. A plan must specify the timing for determining the plan's interest crediting rate that will apply for each plan year (or portion of a plan year) using either of the methods described in paragraph (d)(1)(iv)(B) of this section and must specify the frequency of interest crediting under the plan pursuant to paragraph (d)(1)(iv)(C) of this section.

(B) *Methods to determine interest crediting rate*. A plan is permitted to provide daily interest credits using a daily interest crediting rate based on the permitted rates specified in paragraph (d)(1)(iii) of this section. Alternatively, a plan is permitted to provide an interest credit for a stability period that is based on the interest crediting rate for a specified lookback month with respect to that stability period. The stability period and lookback month must satisfy

the rules for selecting the stability period and lookback month under § 1.417(e)–1(d)(4). (However, the interest rates can be any of the rates in paragraph (d)(1)(iii) of this section and the stability period and lookback month need not be the same as those used under the plan for purposes of section 417(e)(3).)

(C) *Frequency of interest crediting*. Interest credits under a plan must be made on an annual or more frequent periodic basis. If a plan provides for the crediting of interest more frequently than annually (for example, monthly or quarterly), then the interest credit for that period must be a pro rata portion of the annual interest credit. Thus, for example, if a plan's terms provide for interest to be credited monthly and for the interest crediting rate to be equal to the interest rate on long-term investment grade corporate bonds (as described in paragraph (d)(4) of this section), and that interest rate for a plan year is 6 percent, the accumulated benefits at the beginning of each month would be increased by 0.5 percent per month during the plan year. Interest credits under the terms of a plan are not treated as creating an effective rate of return that is in excess of a market rate of return merely because an otherwise permissible interest crediting rate is compounded more frequently than annually.

(v) *Lesser rates*. An interest crediting rate is not in excess of a market rate of return if the plan provides an interest crediting rate that, under all circumstances, is always less than one of the rates described in paragraph (d)(1)(iii) of this section.

(vi) *Greater-of rates*. If a statutory hybrid plan provides for an interest credit that is equal to the interest credits determined under the greater of 2 or more different interest crediting rates, the effective interest crediting rate is not in excess of a market rate of return only if each of the different rates satisfies the requirements of paragraph (d)(1)(ii) of this section and the additional requirements of paragraph (d)(7) of this section are satisfied.

(2) *Preservation of capital requirement*—(i) *In general*. A statutory hybrid plan is treated as failing to meet the requirements of section 411(b)(1)(H) if the requirements of paragraph (d)(2)(ii) of this section are not satisfied.

(ii) *Preservation of capital defined*—(A) *In general*. The requirements of this paragraph (d)(2)(ii) are satisfied if the plan provides that, as of the participant's annuity starting date, the participant's benefit under the plan is no less than the benefit determined as of that date based on the sum of the

hypothetical contributions credited under the plan (or the accumulated percentage of the participant's final average compensation, or the participant's accrued benefits determined without regard to any indexing under section 411(b)(5)(E), as applicable).

(B) *Hypothetical contributions defined*. For purposes of this paragraph (d)(2)(ii), a hypothetical contribution is any amount credited under a statutory hybrid plan other than an interest credit (as defined in paragraph (d)(1)(ii) of this section). Thus, if an opening hypothetical account balance or opening accumulated percentage of the participant's final average compensation is established pursuant to paragraph (c)(3) of this section, that opening hypothetical account balance or opening accumulated percentage as of the date established is treated as a hypothetical contribution and, thus, is taken into account for purposes of the preservation of capital requirement of this paragraph (d)(2)(ii).

(3) *Plan termination*—(i) *In general*. Except as provided in paragraph (d)(3)(ii) of this section, a statutory hybrid plan is treated as meeting the requirements of paragraph (d)(1) of this section only if the terms of the plan provide that, upon termination of the plan, a participant's benefit as of the termination is determined using the interest rate and mortality table otherwise applicable for determining that benefit under the plan (without regard to termination of the plan).

(ii) *Variable interest rates*. A statutory hybrid plan is treated as meeting the requirements of paragraph (d)(1) of this section only if the terms of the plan provide that, upon termination of the plan, any interest rate used to determine a participant's benefits under the plan (including any interest crediting rate and any interest rate used to determine annuity benefits) that is a variable rate is determined as the average of the rates of interest used under the plan for that purpose during the 5-year period ending on the termination date.

(4) *Long-term investment grade corporate bonds*. For purposes of this paragraph (d), the rate of interest on long-term investment grade corporate bonds means the third segment rate described in section 430(h)(2)(C)(iii) (determined with or without regard to the transition rules of section 430(h)(2)(G)), provided that such rate floats on a periodic basis not less frequently than annually. However, for plan years beginning prior to January 1, 2008, the rate of interest on long-term investment grade corporate bonds means the rate described in section

412(b)(5)(B)(ii)(II) prior to amendment by the Pension Protection Act of 2006, Public Law 109-280 (120 Stat. 780) (PPA '06).

(5) *Safe harbor rates of interest—(i) Rates based on Treasury bonds with margins.* An interest crediting rate is deemed to be not in excess of a market rate of return if the rate is adjusted at least annually and is equal to the sum of any of the following rates of interest for Treasury bonds and the associated margin for that interest rate:

Treasury bond interest rates	Associated margin
The discount rate on 3-month Treasury Bills.	175 basis points.
The discount rate on 12-month or shorter Treasury Bills.	150 basis points.
The yield on 1-year Treasury Constant Maturities.	100 basis points.
The yield on 3-year or shorter Treasury bonds.	50 basis points.
The yield on 7-year or shorter Treasury bonds.	25 basis points.
The yield on 30-year or shorter Treasury bonds.	0 basis points.

(ii) *Eligible cost-of-living indices.* An interest crediting rate is deemed to be not in excess of a market rate of return if the rate is adjusted no less frequently than annually and is equal to the rate of increase with respect to an eligible cost-of-living index described in § 1.401(a)(9)-6, A-14(b), except that for purposes of this paragraph (d)(5)(ii), the eligible cost-of-living index described in § 1.401(a)(9)-6, A-14(b)(2), is increased by 300 basis points.

(iii) *Additional safe harbors.* The Commissioner may, in guidance of general applicability, specify additional interest crediting rates that are deemed to be not in excess of a market rate of return. See § 601.601(d)(2)(ii)(b) of this chapter.

(6) *Other interest rates—(i) Reasonable minimum guaranteed rate of return.* [Reserved]

(ii) *Equity-based rates.* [Reserved]

(7) *Combinations of rates of return—*

(i) *In general.* If a plan provides an interest crediting rate that is equal to the interest credits determined under the greater of 2 or more different interest crediting rates where each of the different rates satisfies the requirements of paragraph (d)(1)(iii) of this section, then the interest credits provided by the plan satisfy this paragraph (d)(7) only if one or more of the different interest crediting rates under the plan are adjusted as provided in paragraphs (d)(7)(iii) or (d)(7)(iv) of this section in order to provide that the effective interest crediting rate resulting from the

use of the greater of 2 or more rates does not exceed a market rate of return. This paragraph (d)(7) provides the exclusive rules that may be used for this purpose and, therefore, a plan does not satisfy the requirements of this paragraph (d) if the plan provides for interest credits determined using the greater of 2 or more interest crediting rates and that combination of interest crediting rates is not specifically permitted by this paragraph (d)(7).

(ii) *Coordination with preservation of capital rule.* No adjustment under this paragraph (d)(7) is required merely because the plan satisfies the requirements of paragraph (d)(2) of this section.

(iii) *Combination of fixed and variable interest rates.* [Reserved]

(iv) *Other combinations.* [Reserved]

(8) *Section 411(d)(6)—(i) General rule.* Except as provided in this paragraph (d)(8), to the extent that benefits have accrued under the terms of a statutory hybrid plan that entitle the participant to future interest credits, an amendment to the plan to change the interest crediting rate for such interest credits violates section 411(d)(6) if the revised rate under any circumstances could result in a lower interest crediting rate as of any date after the applicable amendment date of the amendment (within the meaning of § 1.411(d)-3(g)(4)) changing the interest crediting rate. For additional rules, see § 1.411(d)-3(a)(1).

(ii) *Adoption of long-term investment grade corporate bond rate or safe harbor rate.* An amendment to a statutory hybrid plan to change the interest crediting rate for future periods from an interest crediting rate described in paragraph (d)(5) of this section to the interest crediting rate described in paragraph (d)(4) of this section does not constitute a decrease of an accrued benefit and, therefore, does not violate section 411(d)(6). However, an amendment described in this paragraph (d)(8)(ii) cannot be effective less than 30 days after adoption and, on the effective date of the amendment, the new interest crediting rate cannot be less than the interest crediting rate that would have applied in the absence of the amendment.

(iii) *Other changes not treated as prohibited reduction of accrued benefit.* [Reserved].

(e) *Definitions—(1) In general.* The definitions in this paragraph (e) apply for purposes of this section.

(2) *Accumulated benefit.* A participant's accumulated benefit at any date means the participant's benefit, as expressed under the terms of the plan, accrued to that date. For this purpose,

the accumulated benefit of a participant may be expressed under the terms of the plan as either the balance of a hypothetical account or the current value of an accumulated percentage of the participant's final average compensation, even if the plan defines the participant's accrued benefit as an annuity beginning at normal retirement age that is actuarially equivalent to that balance or value.

(3) *Lump sum-based benefit formula—(i) In general.* A lump sum-based benefit formula means a benefit formula used to determine all or any part of a participant's accumulated benefit under a defined benefit plan under which the benefit provided under the formula is expressed as the balance of a hypothetical account maintained for the participant or as the current value of the accumulated percentage of the participant's final average compensation. Whether a benefit formula is a lump sum-based benefit formula is determined based on how the accumulated benefit of a participant is expressed under the terms of the plan, and does not depend on whether the plan provides an optional form of benefit in the form of a single sum payment.

(ii) *Exception for contributory plans.* A participant is not treated as having a lump sum-based benefit formula merely because the participant is entitled to a benefit under a defined benefit plan that is equal to the greater of the otherwise applicable benefit formula and the benefit properly attributable to after-tax employee contributions.

(4) *Statutory hybrid benefit formula.* A statutory hybrid benefit formula means a statutory hybrid benefit formula as defined in § 1.411(a)(13)-1(d)(3).

(5) *Statutory hybrid plan.* A statutory hybrid plan means a defined benefit plan that contains a statutory hybrid benefit formula.

(6) *Variable annuity benefit formula.* A variable annuity benefit formula means a variable annuity benefit formula as defined in § 1.411(a)(13)-1(d)(4).

(f) *Effective/applicability date—(1) Statutory effective/applicability dates—(i) In general.* Except as provided in paragraph (f)(1)(iii) of this section, section 411(b)(5) applies for periods beginning on or after June 29, 2005.

(ii) *Conversion amendments.* The requirements of section 411(b)(5)(B)(ii), (iii), and (iv) apply to a conversion amendment (as defined in paragraph (c)(4) of this section) that is adopted after, and takes effect after, June 29, 2005.

(iii) *Market rate of return*—(A) *Plans in existence on June 29, 2005*—(1) *In general.* In the case of a plan that is in existence on June 29, 2005 (regardless of whether the plan is a statutory hybrid plan on that date), section 411(b)(5)(B)(i) only applies to plan years beginning on or after January 1, 2008.

(2) *Exception for plan sponsor election.* Notwithstanding paragraph (f)(1)(iii)(A)(1) of this section, a plan sponsor of a plan that is in existence on June 29, 2005 (regardless of whether the plan is a statutory hybrid plan on that date) may elect to have the requirements of section 411(a)(13)(B) and section 411(b)(5)(B)(i) apply for any period after June 29, 2005, and before the first plan year beginning after December 31, 2007. In accordance with section 1107 of the PPA '06, an employer is permitted to adopt an amendment to make this election as late as the last day of the first plan year that begins on or after January 1, 2009 (January 1, 2011, in the case of a governmental plan as defined in section 414(d)) if the plan operates in accordance with the election.

(B) *Plans not in existence on June 29, 2005.* In the case of a plan not in existence on June 29, 2005, section 411(b)(5)(B)(i) applies to the plan on and after the later of June 29, 2005, and the date the plan becomes a statutory hybrid plan.

(2) *Effective/applicability date of regulations.* This section applies for plan years beginning on or after January 1, 2009 (or, if later, the date applicable under paragraph (f)(3) of this section). For the periods after the statutory effective date set forth in paragraph (f)(1) or (f)(3) of this section and before the regulatory effective date set forth in the preceding sentence, a plan must comply with section 411(b)(5). During these periods, a plan is permitted to rely on the provisions of this section for purposes of satisfying the requirements of section 411(b)(5).

(3) *Collectively bargained plans*—(i) *In general.* Notwithstanding paragraph (f)(1)(iii) of this section, in the case of a collectively bargained plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified on or before August 17, 2006, the requirements of section 411(b)(5)(B)(i) do not apply to plan years beginning before the earlier of—

(A) The later of—

(1) The date on which the last of those collective bargaining agreements terminates (determined without regard to any extension thereof on or after August 17, 2006), or

(2) January 1, 2008; or

(B) January 1, 2010.

(ii) *Treatment of plans with both collectively bargained and non-collectively bargained employees.* In the case of a plan where a collective bargaining agreement applies to some, but not all, of the plan participants, the plan is considered a collectively bargained plan for purposes of paragraph (f)(3)(i) of this section if at least 25 percent of the participants in the plan are members of collective bargaining units for which the benefit levels under the plan are specified under the collective bargaining agreement.

Linda E. Stiff,

Deputy Commissioner for Services and Enforcement.

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DEPARTMENT OF AGRICULTURE

Forest Service

36 CFR Part 294

Public Meeting to Receive Comments on the Proposed Rule for the Management of Roadless Areas in the State of Idaho

AGENCY: Forest Service, USDA.

ACTION: Notice of meeting.

SUMMARY: There will be a public meeting in Washington, DC to discuss the proposed rule for the management of roadless areas on National Forest System lands in the State of Idaho.

DATES: The meeting will be held January 14, 2008, from 5 p.m. to 10 p.m.

ADDRESSES: The meeting will be held at the United States Department of Agriculture, South Building, Jefferson Auditorium, 1400 Independence Avenue, SW., Washington, DC. Comments on the proposed rule may be sent via e-mail to IDcomments@fsroadless.org. Comments also may be submitted via the world wide web/Internet at <http://www.regulations.gov>. Written comments concerning this notice should be addressed to Roadless Area Conservation-Idaho, P.O. Box 162909, Sacramento, CA 95816-2909, or via facsimile to 916-456-6724. All comments, including names and addresses, when provided, are placed in the record and are available for public inspection and copying. The public may inspect comments received at <http://roadless.fs.fed.us>.

FOR FURTHER INFORMATION CONTACT: Brad Gilbert, Idaho Roadless Rule Team Leader, at (208) 765-7438.

Individuals using telecommunication devices for the deaf (TDD) may call the Federal Information Relay Service (FIRS) at 1-800-877-8339 between 8 a.m. and 8 p.m. Eastern Standard Time, Monday through Friday.

SUPPLEMENTARY INFORMATION: Attendees wishing to comment orally will be allotted three minutes to speak on a first come, first served basis. Meeting attendees will need to pass through USDA security in order to enter the building. To ensure arriving to the meeting on time, attendees are encouraged to arrive at the USDA South Building before 5 p.m. You will need photo identification to enter the building.

Attendees are encouraged to provide their names to security prior to the meeting in order to gain quicker access to the building. Attendees can submit their names to a comment line by calling 202-205-1776. In the message you should identify yourself as wanting to attend the public meeting on the Idaho rule, and then both say and spell your name. Names should be submitted by close of business on January 10, 2008. Any bags that attendees bring will have to go through screening; you are therefore encouraged not to bring bags in order to speed up the screening process.

A copy of the proposed rule, draft environmental impact statement (DEIS), the DEIS summary, dates for public meetings in Idaho, and other information related to this rulemaking will be available at the national roadless Web site <http://www.roadless.fs.fed.us> as well as by calling Brad Gilbert, Idaho Roadless Rule Team Leader, at (208) 765-7438. Reviewers may request printed copies or compact disks of the DEIS and the summary by writing to the Rocky Mountain Research Station, Publication and Distribution, 240 West Prospect Road, Fort Collins, CO 80526-2098. Fax orders will be accepted at 970-498-1122. Order by e-mail from rschneider@fs.fed.us. When ordering, requesters must specify if they wish to receive the summary or full set of documents and if the material should be provided in print or on disk.

Dated: December 20, 2007.

Anne J. Zimmerman,

Acting Associate Deputy Chief, NFS.

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