

Author: Mark L. Lofgren

If you have questions, please contact your regular Groom attorney or any of the attorneys listed below:

Kendall W. Daines
kdaines@groom.com
(202) 861-5406

Elizabeth T. Dold
edold@groom.com
(202) 861-5406

David N. Levine
dlevine@groom.com
(202) 861-5436

Mark L. Lofgren
mlofgren@groom.com
(202) 861-6614

Louis T. Mazawey
lmazawey@groom.com
(202) 861-6608

David W. Powell
dpowell@groom.com
(202) 861-6600

Jeff Witt
jwitt@groom.com
(202) 861-6651

Cash Balance Plans – IRS Further Delays Reasonable Interest Rate Rules and Provides Guidance for Plans with Rates Affected by Map-21

We understand that the IRS and Treasury continue to work on developing final regulations to implement the market rate of return limitations that apply to interest credits made to cash balance accounts. This has proved to be a particularly difficult area for the government to address and one that has received significant comments from cash balance plan sponsors and practitioners. As a result, we still do not have final rules in this area, despite the publication of proposed regulations (and partial final regulations) back in 2010. However, the IRS recently provided an update on the ultimate timing of the final market rate regulations and on how the "MAP-21" (the Moving Ahead for Progress in the 21st Century Act) pension funding relief rules may impact interest credits under some cash balance plans.

In Notice 2012-61, which addresses a number of issues related to pension funding stabilization rules enacted in MAP-21, the IRS has provided the following important guidance regarding cash balance plans:

- Final cash balance "market rate" regulations not effective prior to 1/1/14. The Notice indicates that the regulations governing the market rate of return limits that apply to cash balance plan interest credits will not become effective earlier than plan years that begin on or after January 1, 2014. This is welcome news since another year is nearing an end without final regulations in this area. If final regulations are issued later this fall (there is some chance of this, though we are not holding our breath), plan sponsors will not be forced to comply with the rules until after the 2013 plan year.
- Possible impact of MAP-21 changes for cash balance plans that use the segment rates to determine interest credits. As permitted under existing IRS guidance, some cash balance plans use one of the segment rates under Code section 430(h)(2)(C) to determine the interest credits to be added to participants' cash balance accounts under the plan. The Notice addresses how the smoothing of these rates for plan funding purposes may impact the interest credits to be made to cash balance accounts in these plans.
 - MAP-21 smoothing impact is permissible (for now), but not required. If a cash balance plan defines its interest crediting rate with reference to one of the segment rates, the plan administrator can reasonably interpret plan terms to either apply or not apply the MAP-21 smoothing to the specified segment rate in determining interest credits. Further, if such a plan is amended to specify which approach is being taken and the amendment is adopted by the deadline set by the IRS to meet the final cash balance market rate of return requirements (which will not be prior to 1/1/14), the amendment will not be considered an impermissible cut-back of benefits under Code section 411(d)(6) and will not trigger an advance participant

notice under ERISA section 204(h) (this is the notice generally required when an amendment results in the significant reduction in future benefit accruals).

- Application of MAP-21 smoothing. If a plan is interpreted to apply the MAP-21 smoothing to determine interest credits, the plan must apply the new rate to determine interest credits beginning either (1) the first day of the first plan year for which the MAP-21 rates apply for funding purposes, or (2) the first day of the plan year beginning in 2012. Once a plan has been interpreted to use the smoothing in determining interest credits, the plan cannot be changed to stop using the smoothing for this purpose without triggering the 411(d)(6) anti-cutback protections (unless future guidance provides otherwise).
- MAP-21 smoothing may not meet final market rate rules. The Notice cautions that it is not a foregone conclusion that the MAP-21 adjusted segment rates will be approved as within the market rate limitations. If the final market rate regulations do not permit a cash balance plan to use the MAP-21 segment rates for interest crediting, then any plan using such rates must change to a permissible rate in accordance with applicable transition rules that will be set out by the IRS. Given this caution about whether the MAP-21 adjusted rates will be permissible in the long run, plan sponsors that currently use a segment rate for interest credits will want to carefully consider the potential implications of moving to the MAP-21 modifications for this purpose prior to the issuance of final IRS guidance on the market rate rules.

In our experience, it is unusual for the IRS to indicate that the plan administrator is permitted to make this sort of plan interpretation without a corresponding plan amendment. In any event, plan sponsors in this position will want to carefully consider with their counsel the pros and cons of both approaches.

This publication is provided for educational and informational purposes only and does not contain legal advice. The information should in no way be taken as an indication of future legal results. Accordingly, you should not act on any information provided without consulting legal counsel. To comply with U.S. Treasury Regulations, we also inform you that, unless expressly stated otherwise, any tax advice contained in this communication is not intended to be used and cannot be used by any taxpayer to avoid penalties under the Internal Revenue Code, and such advice cannot be quoted or referenced to promote or market to another party any transaction or matter addressed in this communication.