



**THE NATIONAL COMMITTEE TO PRESERVE
SOCIAL SECURITY AND MEDICARE**



July 7, 2006

Dear Conferee:

It has come to our attention that you are in the final stages of reconciling the highly technical cash balance provisions of the pension reform bills. As you complete your work, we, the undersigned organizations collectively representing the interests of millions of employees and retirees, urge you to adopt the Senate bill's provisions on cash balance plans.

In exchange for legalizing these controversial plans, the Senate bill (Section 601 of S.1783) provides critical protections for older employees who otherwise suffer substantial losses when companies switch from traditional defined benefit plans to cash balance plans. In contrast, the House bill (Section 701 of HR 2830), rather than protecting older workers, would encourage new forms of age discrimination and could encourage companies to use a wider range of "offset" formulas. This could unfairly reduce the pensions of lower-wage and mobile employees, thus undercutting the beneficial features of cash balance plans for these employees. To make matters worse, the House bill amends rules that affect all defined benefit plans, not just cash balance plans, thus undermining the stability of existing law and opening up a Pandora's Box of potential problems.

Here are our specific concerns:

Unlike the Senate bill, the House bill provides no protections for older employees.

Thousands of older employees have found their promised pensions slashed – by as much as 50 percent – when their companies switched from secure traditional defined benefit plans to inferior cash balance formulas. These older employees – from such companies as AT&T, Duke Energy, Sempra, CIGNA, Bank of America and IBM – were told that, if they worked hard and remained loyal to their companies, they would be rewarded with generous pensions typically based on all their years of work and final earnings (often payable before age 65 in the form of special early retirement benefits). When companies switched to cash balance plans midstream, these older employees found their benefits cut dramatically and their dreams of a comfortable retirement shattered.

A recent Government Accountability Office study found that, without transition benefits, all older employees suffer significant losses in cash balance conversions. To mitigate these losses, the Senate bill provides minimal but critical bridge protections to ensure that the reasonable expectations of older employees are protected. The Senate bill protections are a carefully-constructed compromise, mirroring the practices of corporations that, in recent years, have provided modest bridge benefits to older employees in cash balance conversions. If such bridge protections are not included in the final bill, then Congress will be effectively lowering the bar. Companies that otherwise might do the “right thing” would be under pressure from their shareholders to provide only the minimum required by the law.

Providing such protections honors the reasonable expectations of loyal, hardworking employees who have spent their careers working in reliance on express pension promises made by their employers. Providing such protections is also consistent with the purpose of ERISA, a landmark law that made the security of pension promises a basic goal of federal policy. It should also be noted that providing such bridge benefits has a strong precedent: When Congress switched from the old Civil Service Retirement System to FERS, federal government employees were given a choice between the old and new plan.

The House bill would encourage practices that adversely impact older employees.

One of the most controversial practices in cash balance conversions is the practice of “wearaway,” which effectively allows companies to freeze the benefits of older, long-tenured employees when they are switched from a traditional defined benefit plan to a cash balance plan. This precludes them from earning additional benefits for many years while allowing younger, less tenured to earn new benefits. The result is that the employer has cut compensation for these older, longer-tenured workers while maintaining or even increasing compensation for younger workers with less tenure. While the Senate bill limits this inequitable practice with respect to future cash balance conversions, the House bill legalizes the worst forms of wearaway. In addition, through its offset provisions, the bill could invite new and even more egregious forms of wearaway.

The House bill, for instance, legalizes blatant age-discrimination: It allows companies to freeze the benefits that older workers have earned under the old plan, use the current value of those benefits as the starting account balance in the cash balance plan, and then prohibit these long-time employees from accumulating any new benefits until their cash balance accounts exceed the benefits they had earned for their time of service under the old, traditional plan. In extreme cases, older employees might earn no new benefits from the time of conversion until their retirement. The House bill also gives its blessing to company strategies that eliminate the value of early retirement benefits that employees have earned and relied on over their careers.

In contrast, the Senate bill prevents such manipulations by requiring that when companies convert to cash balance plans, all employees immediately start accumulating benefits under the new cash balance plans – they would not be stuck at the frozen value of their

old plan's benefits. In addition, the Senate bill provides for a critically important adjustment (sometimes called a "pop-up") in employees' account balances at retirement if they have satisfied their plans' criteria for earning subsidized retirement benefits.

The House bill's design language is so broad it could lead to a range of new abuses.

The House and Senate have taken decidedly different approaches to addressing the legal issues that underpin the cash balance plan controversy. The Senate bill develops a framework for age discrimination as it pertains to cash balance plans. The House bill, however, develops a new definition of age discrimination that extends far beyond cash balance plans to a wide range of other plans, including contributory and integrated defined benefit plans. While there have been years of debate about changing the accrual rules in cash balance plans, there has been no discussion about how a changed definition of benefit accrual would affect employees in other kinds of defined benefit plans. Yet the House bill does exactly that. This change could undermine other age discrimination protections and possibly undercut carefully-crafted nondiscrimination rules, resulting in unfair benefit reductions for older and lower-paid employees. It is inappropriate for Congress, without greater scrutiny, to change defined benefit accrual rules that have been in place for 30 years.

The House bill would sanction new forms of discrimination.

The House bill includes special exceptions to age discrimination for "transition" and "subsidized early retirement" benefits. These undefined terms are so vague that they could be construed to allow plans to put much larger amounts in the starting account balances of younger employees than those of older employees. Conceivably, a cash balance plan set up by a small employer could provide large so-called "transition" benefits for younger owners and younger favored employees while providing little or nothing for older, long-service rank-and-file employees – without being considered age discriminatory.

The House bill would adversely affect lower-income and shorter-service employees.

The House bill states that offsets of Social Security benefits from benefits earned under a cash balance plan, as well as offsets of pension, profit-sharing, 401(k) or other benefits earned under other plans provided by an employer, are not age discriminatory. Because most older employees will have earned greater Social Security and pension benefits than younger workers, allowing these benefits to be subtracted either from a starting account balance or from benefits earned under a cash balance plan would result in the older employees earning smaller cash balance benefits than younger employees and could further expand the wearaway period for older employees. Although Social Security integration and certain offset arrangements are currently legal, in a cash balance context they can be extremely age discriminatory, particularly to lower- and moderate-income, older employees. These practices are also inappropriate for a plan design that purports to be simple, fair and transparent.

Furthermore, the House bill permits employers to deny benefits to all employees who work fewer than five years. This would result in the forfeiture of benefits by most of the mobile employees that cash balance plans were supposedly designed to help. By contrast, the Senate bill would provide for vesting after three years.

We thank you for your consideration, and hope you will include the Senate cash balance provisions that are protective of employees and eliminate those House cash balance provisions that are overly-broad and could lead to new abuses. We thank you for your consideration on these issues.

Sincerely,

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cc: Conferees on S. 1783, H.R. 2830