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Treasury Issues Final and Proposed Regulations on Hybrid Plans

Treasury has issued final and proposed regulations on hybrid plans such as cash balance plans and pension equity plans (PEPs). The regulations interpret the changes to the cash-out and age discrimination rules made by the Pension Protection Act of 2006 (PPA).

The 2010 final regulations follow closely the regulations that Treasury proposed in 2007. The new 2010 proposed regulations follow closely Treasury's discussion in the preamble to the 2007 proposed regulations. The final regulations are generally effective for 2011 plan years; however, the market-rate-of-return rules of the final regulations generally are not effective until 2012 plan years. The 2012 effective date coordinates the final regulation's effective date for the market-rate-of-return rules with the effective date of the related provisions of the proposed regulations.

Background

The most common types of hybrid plans are cash balance plans and PEPs. Although in some aspects hybrid plans look like defined contribution plans, they are defined benefit pension plans and subject to the rules governing defined benefit plans, including how the plan determines the value of a lump sum payment and how the plan satisfies the rules against age discrimination.

Generally, in a cash balance plan, each participant has a hypothetical account balance. Each year, the plan credits the participant's hypothetical account with a principal credit, which is a percentage of the participant's compensation for that year. The plan also credits interest on the participant's hypothetical account balance at the plan's interest crediting rate for the year.

PEPs are structured differently than cash balance plans; however, the basic concept is similar. There are many variations of PEPs. Generally, each year the plan credits a participant with a specific amount of points usually based on the participant's age and service. At any point in time, the participant's benefit is stated in terms of a percentage of final average pay, with the percentage being the total number of points the participant has accumulated.

PPA made changes to the rules governing hybrid plans under the Internal Revenue Code (Code), Employee Retirement Income Security Act (ERISA), and the Age Discrimination in Employment Act (ADEA). Because of years of litigation on hybrid plan issues, and with many cases still pending in the courts, PPA applied the changes only going forward.

The regulations define a statutory hybrid plan as a plan with a statutory hybrid benefit formula. The regulations then divide that category into (a) plans with lump sum-based benefit formulas (generally the formulas under cash balance plans and PEPs) and (b) plans with formulas with an effect similar to lump sum-based benefit formulas (generally variable annuities). The final regulations exclude benefits attributable to after-tax employee contributions, rollover contributions, and similar arrangements from the definition of statutory hybrid benefit formula. Also excluded are variable annuity contracts with guaranteed interest rates of at least 5%. Treasury has asked for comments on whether a defined benefit plan that expresses a participant's accumulated benefit in the form of a current lump sum dollar amount but does not provide for interest credits should be treated as a statutory hybrid plan that is eligible for the special PPA rules.

For simplicity purposes, this For Your Information *will discuss the rules in terms of hypothetical account balances, which is the structure for cash balance plans. However, unless otherwise indicated, similar rules apply for the current value of the accumulated percentage of final average compensation, which is the structure for PEPs.*

> ***BUCK COMMENT.*** *The issuance of the 2010 final and proposed regulations finally allows employers to establish, convert to, and pay benefits from statutory hybrid plans with confidence as to the governing rules. However, the years of uncertainty, controversy, and lawsuits stopped the original momentum for employers switching to hybrid plans. It is still to be seen whether that momentum will be regained.*

Lump Sum Payments

In converting a benefit stated in the form of an annuity to a lump sum, a defined benefit plan must use interest and mortality assumptions that do not determine the lump sum as a value less than the value that would be calculated using the interest rate and mortality assumptions specified in Code Section 417(e). Depending on the provisions of a statutory hybrid plan, which is by definition a defined benefit plan, a participant's hypothetical account balance might be more or less than the amount determined using the 417(e) assumptions. Under pre-PPA law, if the hypothetical account balance exceeded the 417e-determined benefit, there was no problem with the plan paying the hypothetical account balance to the participant. However, if the 417(e) determined benefit exceeded the hypothetical account balance, participants argued – and courts generally agreed – that the plan would need to increase the payment to equal the amount determined using the 417(e) assumptions.

PPA eliminates the issue for statutory hybrid plans with lump sum-based benefit formulas by allowing such plans to pay a lump sum benefit equal to the hypothetical account balance regardless of the Section 417(e) calculation. However, a similar rule does not apply to statutory hybrid plans with formulas that have an effect similar to lump sum-based benefit formulas, such as plans with variable rate annuity formulas. Treasury has asked for comments on how Section 417(e) applies to such plans. The PPA rule applies to all distributions that the plan makes after PPA's enactment date of August 17, 2006.

2010 Proposed Regulations. For a statutory hybrid plan with a lump sum-based benefit formula to be able to pay just the hypothetical account balance, the plan must satisfy certain other rules. These rules are set forth in the 2010 proposed regulations. First, the hypothetical account balance at normal retirement age must be at least actuarially equivalent, using reasonable actuarial assumptions, to the annuity that the participant would have received at normal retirement age. Second, in a plan that does not suspend benefits for a participant working after normal retirement age, the plan must provide for a high enough interest crediting rate after normal retirement age so that the rules on post normal retirement age accruals are satisfied by the combination of the interest crediting rate and the principal credit.

Third, the plan may reduce the hypothetical account balance for prior benefit payments, qualified domestic relations orders (QDROs), permissible forfeitures, or permitted amendments. The plan may also reduce the hypothetical account balance if the variable interest crediting rate is negative for a year. However, a plan may not reduce the current value of the accumulated percentage of final average pay (the PEP structure) by a negative interest rate. Fourth, where the plan benefit is defined as the greater of the benefit calculated under two formulas and only one of the formulas is eligible to be paid based on the hypothetical account balance, the plan must determine each of the benefit amounts separately using the appropriate rules for that formula. The participant receives the greater of the two amounts. Treasury has asked for further comment on this “greater of” approach.

The 2010 proposed regulations would allow a plan to determine optional forms of benefit payment, such as a five-year certain benefit, based on the hypothetical account balance (rather than based on the annuity at normal retirement age) as long as the plan made the determination using reasonable actuarial assumptions. The regulations apply a similar rule for conversions from one annuity form, such as a single life annuity, to another optional annuity form, such as a life annuity with a five-year period certain benefit, as long as the annuity starting date is not changed. These rules only address how the plan calculates the benefit. Nothing in the regulations eliminates the need to obtain spousal consent where otherwise required.

Vesting

Hybrid plans must provide that benefits attributable to employer contributions are 100% vested after three years of service. This rule applies on a participant-by-participant basis, but only to a participant who has an hour of service after the effective date of the PPA vesting provision, which generally is plan years beginning on or after January 1, 2008. Once a participant has an hour of service after the effective date, the three-year vesting rule applies to the participant’s entire benefit, including amounts accrued before the effective date.

The final regulations provide that if the plan determines one part of a participant’s benefit under a statutory hybrid benefit formula, the plan must apply three-year vesting to the entire benefit, even to the portion that is not based on the statutory hybrid benefit formula. Thus, three-year vesting applies to the participant’s entire benefit where a participant’s benefit is determined as the greater of, or the sum of, the benefit provided by a statutory hybrid formula and the benefit provided by another type of formula, and also where the participant’s benefit is determined as the excess of the benefit under one formula in the plan over the benefit under another formula in the plan, one of which is a statutory hybrid benefit formula. However, in the case of two separate plans, even if there is a floor-plan arrangement, three-year vesting only applies to the benefit in the plan that determines benefits under a statutory hybrid benefit formula.

Age Discrimination Safe Harbor

Most traditional defined benefit plans are able to satisfy the general age discrimination rules, which require that the plan not cease benefit accruals or reduce the rate of benefit accrual because of the attainment of any age. Statutory hybrid plans can continue to try to satisfy the general age discrimination rules; however, PPA offers an alternative safe harbor approach for satisfying the age discrimination rules.

The PPA safe harbor is based on the participant's accumulated benefit. This is the benefit that a participant has accumulated as of any date. The safe harbor applies only to a covered benefit formula, which is defined as a formula expressed in any of the following forms –

- As an annuity payable at normal retirement age (or current age, if later),
- As the balance of a hypothetical account, or
- As the current value of the accumulated percentage of final average compensation.

The safe harbor requires that no participant's accumulated benefit be less than the accumulated benefit of any similarly situated younger person who is or could be a participant. A participant is similarly situated to a younger person if everything is identical except for age. The plan must test the accumulated benefit of both individuals using the same benefit formula. In a situation where both individuals are under the same formula except that the older person also receives a benefit under a second formula that is not available to the younger person, the plan may treat the younger person as having no benefit under the extra formula. In testing a benefit that is based on the sum of two formulas, the greater of two formulas or a choice between two formulas, each formula must pass the rule separately.

In addition, the plan may ignore any offsets permitted under the Code including Social Security disparity. The plan may also ignore the subsidized portion of an early retirement benefit. Finally, when testing a plan that provides periodic adjustments using an appropriate index, a plan need test only the aggregate adjustments made by the index if the plan applies three-year 100% vesting, satisfies the preservation-of-capital rule discussed below, and, in the case of a conversion amendment, follows the conversion rules also discussed below.

Conversions from Traditional Formulas to Hybrid Formulas

One of the most litigated hybrid plan issues has been whether a plan violates the age discrimination rules when a sponsor freezes the final average pay formula, converts to a hybrid formula for all years (past and future), and pays the participant the greater of the benefit under the frozen final average pay plan and the benefit under the hybrid formula. Because the final average pay formula benefit at the effective date of the conversion amendment is required to be protected from cutback, a participant will often earn no new benefits until the old benefit "wears away." Some employers avoid the wear-away problem by paying the sum of the benefit under the old frozen formula at conversion and the benefit under the new formula for future years. This A+B approach avoids the wear-away problem, and it is the method that PPA requires for all conversion amendments adopted and effective after June 29, 2005.

Conversion Amendment. Under the final regulations a conversion amendment does not have to be an actual amendment. If a job transfer results in a participant moving from having his or her benefits determined under a final average pay formula to having benefits determined under a statutory hybrid benefit formula, the transfer will be considered a conversion amendment with respect to that participant. Similarly, if because of a merger or acquisition, a participant that was covered by a final average pay benefit formula is now covered by a hybrid benefit formula, the merger or acquisition will be considered a conversion amendment if the participant's hybrid formula benefit is impacted by the participant's final-average-pay formula benefit.

A series of amendments within a three-year period that move a plan or individual from a traditional formula to a statutory hybrid benefit formula would be combined for purposes of determining whether there has been a conversion. If more than three years elapse between amendments, the presumption is that the amendments are not related. The final regulations define the effective date of the conversion amendment as the date the old final average pay formula stops.

> ***BUCK COMMENT.*** *If a sponsor allows the final average pay formula to continue for a period (such as five years) after the hybrid formula stars so that the participant receives the greater of the benefit under the formulas, the conversion amendment occurs when the final average pay formula stops, which is five years in this example.*

Final Regulation Opening Account Balance Approach. In addition to a pure A+B approach to avoiding age discrimination on conversion, the final regulations allow a plan to convert the frozen benefit (A) into an opening hypothetical account balance A_{ob} and treat A_{ob} + B as a single hypothetical account balance that is increased by same the interest crediting rate that applies to B. However, the sponsor must continue to maintain a record of the frozen benefit A. At the time a participant goes into pay status, the plan must test whether the benefit based on the opening balance A_{ob} is greater than the frozen benefit A using the applicable interest rate and mortality assumptions at the participant's annuity starting date. The plan must pay the greater of the two benefits in addition to B.

Proposed Regulation Opening Account Balance Approach. The 2010 proposed regulations offer a second "opening balance" approach that minimizes the need to do an annuity starting date comparison. However, this alternative is only available if all of the following conditions are satisfied –

- The participant elects a lump sum equal to the sum of the two parts of the hypothetical account balance (A_{ob} + B),
- The aggregate benefit (A_{ob} + B) is not less than the frozen benefit (A),
- The plan, prior to the conversion, did not include the value of any early retirement subsidies in the lump sum,
- The amount of the opening account balance (A_{ob}) was at least equal to what it would have been if it was determined using the 417(e) assumptions,

- In determining the opening account balance, the plan provides either a death benefit at least equal to the then-current value of the hypothetical account balance or does not apply a pre-retirement mortality decrement, and
- The interest crediting rate meets certain conditions such as being the third segment rate or similar rate.

For example, if a plan determines the opening balance using the 417(e) assumptions and the interest crediting rate were the third segment rate, the plan would satisfy this alternative method only if the third segment rate on the date of the conversion amendment is the highest segment rate. This option is not available for payments other than lump sums, nor is it available in PEPs. Treasury has asked for comments on whether this option should continue to be limited to lump sum payments and if the regulations were to expand the option to other payment forms, how Treasury could assure that the anti-cutback provisions were not violated.

> ***BUCK COMMENT.*** *Most participants are likely to take lump sum payments. Thus, even with its limited applicability, the alternative opening balance approach of the proposed regulations provides a somewhat simpler and more attractive option than the opening account balance approach in the final regulations.*

Market Rate of Return

A statutory hybrid plan must satisfy the market-rate-of-return rules. These rules require that a plan's interest crediting rate not exceed a market rate of return. Government plans have an exception from the market rate of return rules that permits them to use any interest crediting rate allowed by state or local law.

> ***BUCK COMMENT.*** *The final regulations treat the market-rate-of-return requirement as a qualification requirement for statutory hybrid plans. Thus, interest crediting rates must satisfy the requirement even if the sponsor has frozen principal credits.*

A plan determines the interest crediting rate for a period by looking at the increase or decrease in the participant's accumulated benefit over the specified period. The interest crediting rate is the plan's effective rate of return determined by dividing the sum of interest credits for a period by the participant's accumulated benefit at the beginning of the period. The plan ignores increases or decreases conditioned on current service or imputed service. The plan also ignores any increase in the accumulated benefit resulting from an amendment adjusting the interest crediting rate unless there is a pattern of repeated amendments.

The final regulations require that the plan specify how it will determine the interest crediting rate and specify the time when interest will be credited. Plans must credit interest at least annually. Crediting must occur as of the last day of the relevant period. The interest crediting rate must not exceed a market rate of return, so the annual rate must be decreased pro rata if the period is less than 12 months. An interest rate will not violate this pro-rata rule because of compounding. Plans that want to use daily crediting may determine the maximum daily market rate of return by dividing the annual interest crediting rate by 360. The 2010 proposed regulations provide that a plan does not need to provide for interest credits on amounts distributed during the interest crediting period.

Permissible Interest Crediting Rates. The final regulations provide that an interest crediting rate will not be treated as exceeding the market-rate-of-return if the crediting rate is always no greater than the rate on long-term investment grade corporate bonds. For plan years beginning on or after January 1, 2008, the rate on long-term investment grade corporate bonds is the third segment rate of the yield curve. Under PPA, there are different yield curves for making funding calculations and for determining the value of lump sums. The final regulations allow the plan to use either method. For years where transition rules apply to the funding or the lump sum third segment rate calculation, the plan may make the determination with or without the transition rules.

The final regulations also allow the plan to use a rate no greater than the interest rate on 30-year Treasury securities, the interest rate on shorter-term Treasuries with the associated margins that were proposed safe harbor rates under earlier IRS guidance (Notice 96-8), the first or second segment rate of the yield curve (with the same flexibility as applies to the third segment rate) and certain cost of living indices.

> ***BUCK COMMENT.*** *The description in the final regulations of the rates allowed by Notice 96-8 is somewhat different than the description in Notice 96-8 itself. However, Treasury has said that there was no intent to make a substantive change.*

Generally, the final regulations require a plan to determine the interest crediting rate for each period as the effective interest rate that applies over that period. However, for plans that use the third segment rate or any of the rates discussed in the preceding paragraph, the plan may determine the interest crediting rate using stability and lookback periods. The plan's stability and lookback periods for this purpose must follow the same rules as apply for setting the stability and lookback periods for minimum lump sum payment calculations under Code Section 417(e) but the periods chosen can differ from those the plan uses for the lump sum calculation.

The final regulations also allow an indexed plan to satisfy the market-rate-of-return requirement by using the actual rate of return on plan assets as long as the plan's assets are diversified in a way that will satisfy ERISA. In addition a plan can use the rate on a plan annuity contract subject to satisfying a specific anti-abuse rule. The 2010 proposed regulations expand the definition of market rate of return to allow all types of hybrid plans (not just indexed plans) to use the actual-return-on-plan-assets rule. In addition, the 2010 proposed regulations add the rate of return on a regulated investment company (RIC) as a return that satisfies the market-rate-of-return requirement if the return is not expected to be more volatile than the return would be based on the broad U.S. equities market or similar broad international equities markets. The rates discussed in this paragraph may not be based on lookback and stability periods.

> ***BUCK COMMENT.*** *The market rates of return specified in the final and proposed regulations are the only permissible market rates of return; they are not simply safe harbors. Plans may use other interest crediting rates only if the rate will always be less than one of the listed rates.*

Fixed and Blended Rates. PPA left to regulations the issue of when fixed interest rates and combinations of fixed and variable interest rates exceed a market rate of interest. The 2010 proposed regulations provide that the following rates do not exceed a market rate of return –

- Fixed rate of 5%.

- Fixed rate of 4% as an annual floor on a variable bond rate.
- Fixed rate of 3% as a cumulative floor on an equity or variable bond index.

The 2010 proposed regulations also provide that an annual floor is not permitted in combination with an equity index.

Treasury has asked for comments on whether a different approach on fixed and combined rates is appropriate and, if so, how does Treasury assure that the rate is not considerably above a market rate or return or above a market rate of return for a long period of time. Treasury has also asked for comments on whether plans should be able to offer participants a menu of hypothetical investments, and, if so, how Treasury should deal with switches between investments, the elimination of an investment option, the switch to or from an option with a cumulative limit, and switches to the special termination rates.

> ***BUCK COMMENT.*** *What fixed rates and floor rates are considered not to exceed the market rate of return has been controversial. Based on what Treasury has said and done in the 2007 proposed regulations, the 2010 final regulations, and the 2010 proposed regulations, Treasury is unlikely to significantly change its view of the limits of a market rate of return in future regulations. However, since most of the market-rate-of-return regulatory provisions are not effective until 2012 plan years, a plan sponsor with a rate that would not satisfy the regulations still can argue that its rate satisfies the statutory requirement. Plans with rates that do not satisfy the statutory definition are already in violation and will most likely need to use the IRS's EPCRS program to correct.*
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> *Some plans may currently be using a fixed rate that is higher than would be permitted under the 2010 proposed regulations in order to satisfy the accrual rules. These plans will have to redesign their benefit formulas significantly to avoid a conflict between the accrual rules and the market rate of return rules. While there is a delayed effective date until the 2012 plan year for most of the market-rate-of-return regulatory rules, sponsors whose plans need major redesign should start the analysis now.*

Preservation-of-Capital Rule. In addition to satisfying the market-rate-of-return rules, a plan must satisfy a preservation-of-capital rule. The final regulations require that a participant's benefit under the statutory hybrid benefit formula not be less than the sum of all the principal payments credited by the plan for the participant including those credited before the effective date of PPA. The rule is equivalent to a cumulative floor of 0% on the interest crediting rate.

The final regulations provide that combining this preservation-of-capital floor with a rate of return that otherwise is a market rate of return will not result in an effective interest crediting rate that exceeds the market rate of return. The final regulations make clear that the preservation-of-capital rule needs to be satisfied only on a participant's annuity starting date (taking into account prior distributions). At interim times, the hypothetical account balance can fall below the preservation level.

Plan Termination. PPA has special rules that address what happens when a plan terminates. If that plan has a variable interest crediting rates or uses a variable interest rate for annuity conversion, the plan must include a provision that provides that the rate will be adjusted at plan termination to a fixed rate equal to the average rate over the five-year period ending on plan termination. The proposed regulations address how years, partial years, weighting, and the arithmetic average are determined. The proposed regulations also provide a special averaging rule when a plan's interest crediting rate is an equity index or a rate that exceeds a market rate of return. In those cases, the average of the rate for the third segment of the yield curve for the last month prior to the start of each of the five interest crediting periods before plan termination is substituted for the equity rate or non-market rate that would otherwise apply.

Accrual Rule (Backloading)

The 2010 proposed regulations include a special rule with respect to statutory hybrid plans that use a variable interest crediting rate when conducting the 133-1/3% backloading accrual test. Under the 133-1/3% rule, variable factors are treated as remaining constant for the following year for testing purposes. This creates a problem with a variable interest crediting rate that can be negative. To address the issue, the proposed regulations would allow the plan to treat any negative value as zero for the following year. Treasury has asked for comments on how to deal with a variable interest crediting rate that could be negative in the context of the fractional accrual rule for participants whose benefit formula cannot satisfy the 133-1/3% rule.

> ***BUCK COMMENT.*** *If a plan that provides higher principal credits for participants with longer service has a fixed interest crediting rate that is greater than the permitted market rate of return and the plan needs that high fixed rate to satisfy the 133-1/3% rule, sponsors will need to redesign the plan's principal credits so that the plan does not need a fixed rate above the market rate of return.*

Protected Benefit

Right to Future Interest Credits. The final regulations treat the right to future interest credits with respect to the existing hypothetical account balance, even if the participant separates from service, as a protected benefit under the anti-cutback rules of Code Section 411(d)(6). Therefore, any change in the interest crediting rate must satisfy the anti-cutback rules when an amendment to the rate could result in interest credits that are smaller as of any date than the interest credits that would have been provided without the amendment.

The final regulations provide that there is no violation merely because the plan switches from one of the Notice 96-8 rates (or from the first or second segment rate) to the long-term investment grade corporate bond rate (the third segment rate) if the change only applies to future credits, the amendment is not effective for 30 days, and on the effective date of the amendment, the new rate is not lower than the old rate. The proposed regulations expand this relief to include a change from a 5% fixed rate to the third segment rate.

2010 Proposed Regulations. If an amendment changes the plan's interest crediting rate for future periods from an interest crediting rate (old rate) that is not in excess of the market rate of return to a different interest crediting rate (new rate) that is also not in excess of the market rate of return, the plan must provide that a participant's benefit will not be less than it would have been if the old rate had continued with respect to the existing account balance at the time of the amendment. The 2010 proposed regulations provide that merely creating such a floor rate would not make the plan's rates greater than permitted under the market-rate-of-return restriction.

The 2010 proposed regulations also provide that a rate will not be considered in violation of the market rate of return merely because the plan provides that the participant's benefit at each annuity starting date after the participant's normal retirement age is equal to the greater of the benefit determined using a rate that satisfies the market-rate-of-return requirements and a benefit that satisfies the accrual rules for post normal retirement age accruals.

Treasury has said that it expects to grant further relief from Section 411(d)(6) for market-rate-of-return as long as the sponsor adopts the amendments before the final regulations on market rate of return apply to the plan. However, the relief will be limited to amendments that changes the interest crediting rate no more than is necessary to satisfy the market-rate-of-return requirement. IRS had previously required the amendments to be made before the end of the 2010 plan year. Treasury has asked for comments on whether plans should be allowed to switch to any maximum rate or only to a rate of the same type (e.g., only from a high fixed rate of return to 5%). Treasury has also asked for comments on how to deal with situations where a RIC or a variable index ceases to exist.

> ***BUCK COMMENT.*** *This relief would not allow any reduction beyond the minimum necessary to satisfy the market-rate-of-return rules. Thus, plans could not switch among permissible rates without following the rule discussed above requiring at least 30 days advance notice, applicability only to future credits, and the new rate not being lower than the old rate on the effective date. A plan also may not adopt a Notice 96-8 rate that has a margin without using the maximum permissible margin.*

Effective/Applicability Dates

The final regulations are generally effective for plan years beginning on or after January 1, 2011. However, the market-rate-of-return provisions of the final regulations are not effective until plan years beginning on or after January 1, 2012, the same time the proposed regulations are effective.

> ***BUCK COMMENT.*** *It is quite possible that the promulgation of final regulations on the 2010 proposals will slip because of the large number of regulatory projects on which Treasury is working. If that is the case, the January 1, 2012 effective date will be deferred. The 2012 effective date for most of the market-rate-of-return provisions allows a plan with an interest crediting rate that does not currently satisfy the final regulation to argue that the rate satisfies the statutory definition and thus delay making changes in the market rates of return. If the interest crediting rate does not satisfy the statutory definition, then the plan has been in violation of the requirement since PPA's effective date and the sponsor will have to look to IRS's EPCRS program.*

The statutory PPA changes generally apply prior to the final regulations' 2011 effective date and the proposed regulations' tentative 2012 effective date. For plan years before the final regulations are effective, Treasury allows plans to comply with PPA by relying on Notice 2007-6, the 2007 proposed regulations, the 2010 final regulations, and the 2010 proposed regulations. This reliance rule also applies for 2011 and later years with respect to the matters not addressed by the 2010 final regulations.

Several special effective date rules apply –

- A benefit formula is not treated as having an effect similar to a lump sum-based benefit formula in the case of any participant who does not have an hour of service after the regulatory effective date.
- In the case of a conversion amendment that has an effective date on or after the statutory effective date, the conversion protection requirements of the regulations, to the extent they go further than the statute, apply only to a participant who has an hour of service on or after the regulatory effective date. However, once the conversion protection is triggered for a participant, the protection requirements apply to the participant's entire benefit going back to the effective date of the conversion amendment.
- A plan that has some participants who receive benefits pursuant to a collectively bargained formula and some who do not is treated as a collectively bargained plan for purposes of the PPA delayed effective date if either 25% of the total participants receive benefits based on a collective bargaining agreement or 50% of active participants do so.

Conclusion

PPA made major changes to the rules governing hybrid plans but left a lot of issues for Treasury to resolve by regulation. The final regulations address some of the simpler issues, while the 2010 proposed regulations address many of the more difficult issues. Treasury is still is trying to determine the most workable approach on some of the remaining issues without violating the market-rate-of-return requirement. However, enough issues have been resolved to allow sponsors to make decisions on plan design.

Buck's consultants are ready to assist you with hybrid plan design or redesign, and answer any questions you might have.

This FYI is intended to provide general information. It does not offer legal advice or purport to treat all the issues surrounding any one topic.