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Cash Balance Plans and Age Discrimination: The Statute Speaks and (Most) Courts Listen

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Critics of cash balance plans argue that these plans illegally discriminate on the basis of age as interpreted through the statute. In response, we make a purely statutory case in support of cash balance plans. We first show that critics have failed to overcome the decisive statutory obstacles they interpret from the statute. We then turn to the statutory arguments in favor of cash balance plans. We argue that the statute is better read as solely governing benefits earned after age 65. The legality of cash balance plans, however, does not depend on this reading. To illustrate, we assume that the statute also applies to pre-age-65 benefits. Under this assumption, we show that the statutory text compels the conclusion that the statute can be satisfied on the basis of the present value of the annuity benefit. When tested on a present value basis, cash balance plans satisfy the age discrimination rules.

The question of whether cash balance plans illegally discriminate on the basis of age has now been squarely addressed by four courts. *Engers v. AT&T Corp.,* No. 98-3660, letter op. (D. N.J. June 6, 2001); *Eaton v. Onan Corp.,* 117 F. Supp. 2d 812 (S.D. Ind. 2000); *Cooper v. IBM Personal Pension Plan,* 274 F. Supp. 2d 1010 (S.D. Ill.

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2003); *Tootle v. ARINC, Inc.,* 2004 U.S. Dist. LEXIS 10629 (D. Md. June 10, 2004). Of these, three have said cash balance plans do not discriminate on the basis of age (*Engers, Eaton,* and *Tootle*) and one has emphatically said cash balance plans do discriminate *(Cooper)*. The three courts deciding in favor of cash balance plans reached their conclusions after considering a variety of factors including the statute, legislative history, logic, economics, and public policy. By contrast, critics have argued that benefit accruals under cash balance plans are age discriminatory on the face of the statute. Given the clarity of the statute, they argue, further inquiry into other considerations is wrong.[1]

We find arguments for the legality of cash balance plans based on history, policy, and economics to be compelling. We do not, however, propose to rehearse these arguments. Rather, our limited purpose here is to summarize the purely statutory arguments for concluding that the cash balance critics are wrong and that benefit accruals under cash balance plans are not age discriminatory.

We first show that the premise of the critics' arguments—that age discrimination must be measured solely in terms of the accrued benefit expressed as the annuity beginning at age 65—must be wrong under the statute. We take pains with this section, because we believe that cash balance critics have not grappled with the statutory obstacles to this cornerstone of their own position.

If the statute does not measure age discrimination in terms of the annuity at age 65, what does it do? We show that the better reading is that the statute governs only benefit accruals earned after age 65 and thus does not affect cash balance plans.

While this reading is preferred, however, the legality of cash balance plans does not depend on it. To show this, we provisionally assume that the statute also governs benefit accruals earned before age 65. Under this assumption, we show that the statute decisively allows age discrimination to be measured in terms of the *present value* of the earliest available annuity under the plan. More precisely, we show that for age discrimination purposes, the statute decisively allows the benefit accrual to be measured as the present value of the annuity that would actually be paid under the plan if it commenced at the earliest time permitted under the terms of the plan. When measured on a present value basis, benefit accruals under a cash balance pension plan do not discriminate on the basis of age.

To reach our destination, we make a couple of long detours into legislative history, but the ultimate goal of our analysis is statutory. The legality of cash balance plans is not based on an illegitimate foray into extra-statutory considerations, as critics claim. Rather, it is compelled by the statutory text. Benefit accruals under a cash balance plan are not illegally age discriminatory, because the statute itself says they are not.

BACKGROUND

A defined benefit pension plan violates ERISA Section 204(b)(1)(H) if under the plan "an employee's benefit accrual is ceased, or the rate of an employee's benefit accrual is reduced, because of the attainment of any age."[2] Substantially identical provisions appear in the Age Discrimination in Employment Act of 1967, as amended (ADEA), Section 4(i) and the Internal Revenue Code (IRC) Section 411(b)(1)(H).[3] Congress enacted the provisions as part of the Omnibus Reconciliation Act of 1986 (OBRA) and intended that they be interpreted in a consistent manner.[4] OBRA also included similar rules for defined contribution plans, requiring that the "rate at which amounts are allocated to an employee's account" may not be reduced because of the employee's age.[5]

Cash balance plans are defined benefit plans. Unlike the benefit in a traditional defined benefit plan, however, the cash balance benefit is not expressed as a monthly annuity commencing at age 65. Rather, the benefit formula mimics a defined contribution plan. Each participant has a benefit expressed as an account balance. At specified periods, a participant's account under the plan is credited with "pay credits" equal to a stated percentage of compensation, and with "interest credits" earned on the account balance at a stated rate. A typical cash balance plan, for example, might award pay credits equal to 4 percent of compensation and "interest credits" equal to the interest rate specified under IRC Section 417(e).

A participant's rights under an ERISA defined benefit pension plan are generally measured in terms of his or her "accrued benefit." ERISA Section 3(23)(A) defines the accrued benefit in a defined benefit plan as the "accrued benefit determined under the plan" and, with exceptions we will visit later, the accrued benefit is "expressed in the form of an annual benefit commencing at normal retirement age." Many commentaries shorthand "normal retirement age" as age 65, and the "annual benefit commencing at normal retirement age" as the "age-65 annuity." We also assume these positions.[6]

When pay credits to the account balance are measured as additions to the age-65 annuity, an issue arises. Consider two employees, ages 35 and 55, each granted a pay credit of $100 to his or her cash balance account. Measured as an addition to the age-65 annuity, the identical $100 pay credit yields an annual payment of roughly $43 for the younger employee but only $16 for the older one.[7] Why? Because to reach its projected age-65 value, the pay credit has a longer time to grow at the plan's stated interest rate for the younger employee than for the older one. For the older employee, the result is a smaller projected age-65 account balance, and thus a smaller age-65 annuity, than for the younger one. Thus, when the "accrued benefit" is expressed as the age-65 annuity, the identical pay credit yields a smaller addition to the accrued benefit for the 55-year-old than for the 35-year-old.

This math has led critics of cash balance plans to conclude that the rate of benefit accrual in such plans is illegally age discriminatory under ERISA Section 204(b)(1)(H). The critics' reasonings were adopted by the Federal District Court, Southern District of Illinois, in *Cooper,* 274 F. Supp. 2d 1010 (S.D. Ill. 2003). The *Cooper* court reasoned that the "rate of benefit accrual" under ERISA Section 204(b)(1)(H) means rate of growth in the "accrued benefit," which the court read to mean the age-65 annuity. Because identical pay credits would yield a smaller addition to the age-65 annuity for an older employee than a younger one, the court held that the "rate of benefit accrual" in the IBM cash balance plan was reduced "because of age" in violation of ERISA Section 204(b)(1)(H).[8]

Three courts have reached the opposite conclusion and decided that benefit accruals under cash balance plans are not age discriminatory. All three reached their conclusion in part or in whole by deciding that ERISA Section 204(b)(1)(H) applies only to benefit accruals earned after age 65.[9]

Two of the courts issued an alternative holding as well. Even provisionally assuming that the rule applied to benefit accruals earned before age 65, they disagreed with the reasoning adopted by the *Cooper* court and held that the "rate of benefit accrual" does not have to be measured as additions to the age-65 annuity. Rather, the rule may be measured in terms of the defined contribution-type benefit as expressed in the plan. That is, by "the change in the employee's cash balance account from one year to the next."[10] When measured as additions to the account balance, cash balance accruals are identical for any two employees of equal pay without regard to age and do not violate ERISA Section 204(b)(1)(H).

WHAT THE STATUTE SAYS

The *Cooper* decision on the one hand and the *Eaton, Engers,* and *Onan* decisions on the other define the boundaries of the debate over whether cash balance plans are inherently age discriminatory. If the "rate of benefit accrual" must be measured for all participants as additions to the age-65 annuity, then ERISA Section 204(b)(1)(H) may indeed raise problems for most cash balance plans.[11] If the rule, however, applies only to benefit accruals earned after age 65 or if the rule may be measured in terms of pay credits added to the account balance, then benefit accruals under cash balance plans are not inherently age discriminatory.

"Rate of Benefit Accrual" Cannot Mean the Age-65 Annuity

A look at the statute shows that, on the basis of statutory construction alone, the cash balance critics are wrong, and "rate of benefit accrual"

cannot mean rate of growth in the "accrued benefit" measured as the age-65 annuity. This conclusion has been reached before by ourselves and others and in our opinion has not been refuted.[12] We summarize the main arguments against critics' interpretation of the meaning of "rate of benefit accrual," and, for each, we summarize the critics' responses and their failure, in our opinion, to overcome the statutory obstacles to their own position.

When Congress Limits Accrued Benefits, It Says So

First, the critics' interpretations of the meaning of "rate of benefit accrual" ignore standard principles of statutory construction. Where Congress intends to regulate the "accrued benefit" expressed as the age-65 annuity, it says so expressly. For example, the anti-backloading rule of ERISA Section 204(b)(1)(B) (which governs the yearly rate at which workers can earn additions to the accrued benefit measured as the age-65 annuity) is stated in terms of the rate at which a participant "accrues the retirement benefits *payable at normal retirement age*." ERISA Section 204(b)(1)(G) provides that the participant's "accrued benefit" may not decrease with increasing age or service. Congress did not use the same language in limiting the "rate of benefit accrual" under ERISA Section 204(b)(1)(H)—an omission which shows it intended no limitation of the age-65 accrued benefit.[13] In short, when Congress means to legislate regarding accrued benefits, it says so, and in ERISA Section 204(b)(1)(H), it does not say so.

Cash balance critics have not addressed this first obstacle to their position. The argument was brushed off by the *Cooper* court as semantic quibbling. Acknowledging the difference between "accrued benefit" and "benefit accrual," the court reasoned that the "syntax differs ever so slightly" in order to "comport with the requirements of good English usage." The court concluded, however, that "the concept is exactly the same."[14] The court's unanalyzed assertion ignores longstanding principles of ERISA statutory construction, where courts have held small differences in statutory language in this complex statute to denote large differences of meaning.[15]

Statutory Contradiction with ERISA Section 204(c)(2)(B)

Second, the critics' interpretations lead to irreconcilable statutory contradictions, a point first made by Shea, Francese, and Newman in their 2000 *Virginia Tax Review* article.[16] Some defined benefit plans are "contributory"; that is, they are funded in part by mandatory employee contributions. Under ERISA Sections 204(c)(2)(B) and (C), the age-65 accrued benefit derived from an employee's contributions equals the sum of those contributions plus interest credited at a statutory rate to age 65. Thus, the age-65 accrued benefit in a contributory defined benefit plan is computed precisely like

the one in a cash balance plan—on the basis of an account balance equal to contributions stated as a percentage of pay plus interest earnings projected to age 65. Because the age-65 accrued benefit in a contributory plan is governed by the same math that governs the accrued benefit in a cash balance plan, benefit accruals that are identical when measured as an employee's contributions to his or her account balance are smaller for an older employee than for a younger one when measured as additions to the age-65 accrued benefit. Under the critics' interpretations of ERISA Section 204(b)(1)(H), benefit accruals under contributory defined benefit plans are illegally age discriminatory. To believe this reading, one must believe that Congress in one section of ERISA outlawed the computation of the accrued benefit in plans that was created under another section. This argument to our minds is dispositive, and has not been refuted by cash balance critics.

The argument has been made by some cash balance critics that the definition of the accrued benefit for a contributory defined benefit plan under ERISA Section 204(c)(2)(B) is only an *allocation* rule, not a definition of the "accrued benefit." That is, in the typical contributory defined benefit plan, the total accrued benefit is determined by a formula expressed in terms of the annuity commencing at age 65—for example, as an age-65 annuity equal to $10 for each month of service. Since the total accrued benefit is described by a formula, according to the critics' arguments, it follows that ERISA Section 204(c)(2)(B) merely acts to allocate the part of the total accrued benefit that is attributable to employee contributions and the part that is attributable to employer contributions. Such allocation is necessary because ERISA requires that the portion of the accrued benefit attributable to employee contributions must be immediately vested, while the portion attributable to employer contributions may vest according to the more stretched-out schedules allowed for employer contributions generally.[17]

We respond, however, that the critics' arguments are not supported by the statute. In many cases, ERISA Section 204(c)(2)(B) does not merely allocate pieces of the accrued benefit; rather it describes the entirety of the accrued benefit. This could happen, for example, for a young, short-service participant in a contributory defined benefit plan with a large required employee contribution. In early years of service, the age-65 annuity based on his or her contributions will be *greater* than the age-65 annuity described under the formula ($10 per month of service, or whatever). The employee is always entitled to the greater of the two amounts; so during these early years, the benefit attributable to employee contribution is the entirety of this participant's accrued benefit, until the formula benefit catches up. Before the catch-up point, the employee's accrued benefit is the age-65 annuity based on his or her contributions to the account balance plus

interest credited to age 65 at the statutory rate. Because of the same math that applies to cash balance plans, this accrued benefit—compelled by statute—is made illegal by the critics' readings of ERISA Section 204(b)(1)(H). This statutory contradiction shows that the critics' readings cannot be correct.

Carve-Out for Benefit Subsidies Rendered Meaningless

Third, the critics' interpretations make a portion of the statute meaningless. ERISA Section 204(b)(1)(H)(v) states that subsidized early retirement benefits may be "disregarded" in determining compliance with the age discrimination rules. The need for an express carve-out for early retirement subsidies shows that the statutory term "rate of benefit accrual" must include the early retirement subsidy. (The value of the early retirement subsidy shrinks as the participant approaches age 65, when it goes to zero. Thus, an exception is needed so that the subsidy, which steadily shrinks in value with age, is not age-discriminatory.) The term "accrued benefit," however, does not include the early retirement subsidy.[18] This is because, by statute, the accrued benefit paid before age 65 is the reduced amount which is the actuarial equivalent of the accrued benefit payable at age 65.[19] The early retirement subsidy is any excess over this reduced amount. By definition, the subsidy cannot be part of the accrued benefit. If "rate of benefit accrual" means rate of growth in the age-65 accrued benefit, as critics contend, the express carve-out under ERISA Section 204(b)(1)(H) for early retirement subsidies is rendered meaningless and redundant—a result which shows their interpretation cannot be right.

The critics' attempts to rebut this point is, in our opinion, unsuccessful. It has been pointed out by cash balance critics that at the time of OBRA's enactment, the question whether the early retirement subsidy was part of the "accrued benefit" was a matter of debate in case law; thus the carve-out had to be pinned down by statute.

We would respectfully disagree. There was no such debate. The debate—to the extent one existed—pertained solely to whether the early retirement subsidy was an accrued benefit for the sole purpose of the anti-cutback rule of ERISA Section 204(g). Only one court held in the affirmative.[20] The *Amato* court expressly confined its holding to ERISA Section 204(g) and reached its conclusion on the basis of IRS regulations that the court conceded were applicable solely to the anti-cutback rule of the section, and not necessarily consistent with the regulation's definition of "accrued benefit" for other purposes.[21]

Moreover, *Amato* applied only to benefits before 1984. In 1984, Congress settled the "accrued benefit" definition for ERISA Section 204(g), and they settled it in a way showing decisively that the definition did *not* include early retirement subsidies.[22] By 1986, there was no need for Congress to believe it needed to revisit the definition of

"accrued benefit" for any purpose. Had the definition of "accrued benefit" applied outside the anti-cutback rule of ERISA Section 204(g), which it did not, then the *Amato* definition would have made early retirement subsidies illegal under ERISA Section 204(b)(1)(G), providing that a participant's "accrued benefit" may not be reduced "on account of any increase in his age or service." The value of an early retirement subsidy is by definition reduced with each increase in the participant's age before age 65. If the subsidy was part of the accrued benefit, it would be illegal under ERISA Section 204(b)(1)(G). Congress could not have thought there was any doubt that "accrued benefit" included the early retirement subsidy or Congress would have had to amend ERISA Section 204(b)(1)(G) when it enacted ERISA Section 204(b)(1)(H) and its carve-out for early retirement subsidies.

The bottom line is that outside of the anti-cutback rule, where the debate was exclusively confined, the "accrued benefit" never even arguably included the early retirement subsidy. The statute does not state that the accrued benefit did include the early retirement subsidy—neither the IRS nor the courts ever said it did, and Congress never thought it did. The only way to explain the carve-out for early retirement subsidies in ERISA Section 204(b)(1)(H) is to conclude that the "rate of benefit accrual" in that section does not mean the rate of growth in the age-65 accrued benefit.

Inconsistent with Actuarial Increases in the Post-Age-65 Accrued Benefit

Fourth, the critics' interpretations make the statute's treatment of post-age-65 benefit accruals self-contradictory. This point has been made as an argument from legislative history.[23] We think the argument also follows from the statute.

The basic problem is this. Generally, ERISA Section 3(23)(A) expresses the "accrued benefit" under a defined benefit plan as the annuity beginning at age 65. When payment of the accrued benefit first begins after age 65, ERISA Section 204(c)(3) states that the accrued benefit must be the "actuarial equivalent" of the age-65 annuity. This means that when payment of the benefit first begins after age 65, the amount of each annual payment must be adjusted upward, so that larger annual payments compensate the participant for the shorter expected time he or she will receive them before death. For example, because of this actuarial adjustment, the same "accrued benefit" measured as a $10 annual payment beginning at age 65 might be a $12 annual payment if its beginning is delayed until age 66, a $14 annual payment if delayed until 67, and so forth.[24]

If "rate of benefit accrual" meant the earned annual increment to the age 65 "accrued benefit," we would expect that each new accrual first earned for service after age 65 would be similarly adjusted upward.

For example, consider a plan in which participants earn an annuity beginning at age 65 equal to $10 per year of service. If "rate of benefit accrual" means the earned annual increment to the "accrued benefit," then the additional benefits earned by a participant who continues to work after age 65 should be actuarially adjusted upward to, for example, $12 at age 66, $14 at age 66, and so forth. If the plan continues to provide benefit accruals of only $10 per year of service after age 65, then this participant's annual benefit accruals—while equal when measured as the immediate annuity—decrease in value when measured as increments to the age-65 annuity. It is, however, precisely this latter pattern—that is, flat benefit accruals or equal immediate annuities—that is blessed by legislative history and Treasury guidance. In their 2000 *Virginia Tax Review* article, Shea, Francese, and Newman point out that the OBRA Conference Committee report describes precisely such a plan—where benefit accruals continue after age 65 in flat increments of $10 per year—as an example of compliance with ERISA Section 204(b)(1)(H). The *Eaton* court found this example from legislative history decisive in holding that "rate of benefit accrual" could not mean rate of increase in the age-65 accrued benefit.[25] Similarly, Treasury guidance governing ERISA Section 204(b)(1)(H) expressly blesses examples in which each benefit accrual first earned after age 65 is not actuarially adjusted upwards to equal the same accrual at age 65. Rather, each benefit accrual earned after age 65 is the unadjusted amount under the plan's pre-age-65 benefit accrual formula—proof that the Treasury does not read the "benefit accrual" under ERISA Section 204(b)(1)(H) to mean earned increments to the age-65 "accrued benefit."[26]

The statute shows that legislative history and Treasury guidance are correct readings of Congress's intent. ERISA Section 204(b)(1)(H) contains detailed rules for handling post-age-65 benefit accruals. Among these is the "offset" rule of ERISA Section 204(b)(1)(H)(iii) that governs benefits that are not in suspension (and for which payout of the benefit does not begin at normal retirement age). The offset rule states that the requirement for continued benefit accrual after age 65 during any plan year is satisfied "to the extent of any adjustment in the benefit payable under the plan during such plan year attributable to the delay in the distribution of benefits" after age 65.

If "benefit accrual," however, means growth in the age-65 accrued benefit, then for benefits earned in any year after age 65, the post-age-65 "benefit accrual" must itself include an actuarial "adjustment," because such adjustment would be required for any increment to the post-age-65 accrued benefit. Under the offset rule, this adjustment piece of the additional benefit accrual is treated as satisfied to the extent of the adjustment itself. This circular result is better avoided. It is avoided if "rate of benefit accrual" is not read to mean "rate of increment to the age-65 accrued benefit" but rather is read to mean something else. In

the case of benefits earned after age 65, that other meaning is the immediate annuity, rather than the age-65 annuity.

In short, "benefit accrual" under ERISA Section 204(b)(1)(H) cannot mean "increment to the age-65 accrued benefit," because by law, the latter is required to be actuarially increased after age 65, and the former is not. The two terms do not mean the same thing.

Again, cash balance critics have not refuted this statutory obstacle to their position. It has been pointed out by some critics that this particular pro-cash balance argument starts from the premise that the accrued benefit after age 65 must be actuarially increased. Critics have disagreed with the premise and argued that earned additions to the accrued benefit are not subject to any requirement for actuarial increase after age 65. In support, they cite Treasury Regulations Section 1.411(c)-1(f)(2) that states "no actuarial adjustment" to the IRC Section 411 "accrued benefit" is required on account of employment after normal retirement age. (The accrued benefit under IRC Section 411, of course, is the same as the "accrued benefit" under ERISA Section 2(23). By law, Treasury regulations govern the identical accrued benefit under both statutes.)[27]

We disagree. While Treasury Regulations Section 1.411(c)-1(f)(2) has never been withdrawn, it was superseded by OBRA's subsequent enactment. Specifically, ERISA Section 204(b)(1)(H)(iii)(I) allows an offset for post-age-65 benefit accruals by the actuarial adjustment of the accrued benefit required to adjust for delayed payout. Whatever the rule under prior law, OBRA 1986 generally compelled an actuarial adjustment in the post-age-65 accrued benefit, including the piece earned after age 65 (with statutory exceptions for benefits that commence at normal retirement age, and benefits in "suspension" as permitted by ERISA Section 204(b)(1)(H)(iii)).

Proposed and final regulations support our view. Proposed Treasury Regulations Section 1.411(c)-1(f)(2) (1988)—proposed to replace the regulation cited by cash balance critics—states "[e]xcept as permitted by (f)(1) of this section [relating to benefits in suspension], a defined benefit plan must make an actuarial adjustment to an accrued benefit the payment of which is deferred past normal retirement age." Proposed Treasury regulations governing ERISA Section 204(b)(1)(H) also clearly contemplate that, while each post-age-65 "benefit accrual" is not actuarially adjusted in the year first earned after age 65, this same "accrual"—once it becomes part of the "accrued benefit"—is actuarially increased in each subsequent year.[28] Final regulations under IRC Section 401(a)(9) state that the "accrued benefit" under IRC Section 411—and hence under ERISA—is generally required by IRC Section 411 to be increased "to reflect any delay in the payment of retirement benefits after normal retirement age."[29]

In short, the "benefit accrual" under ERISA Section 204(b)(1)(H) is not actuarially increased after age 65, while increments to the age-65

"accrued benefit" are required by law to be so increased. The two terms cannot mean the same thing.

CHANGE "RATE OF BENEFIT ACCRUAL" TO "BENEFIT ACCRUALS AFTER AGE 65"

The statute compels the conclusion that "rate of benefit accrual" cannot mean rate of growth in the age-65 accrued benefit. What then does it mean? As noted above, three federal district courts have decided that the rule applies only to benefit accruals earned after age 65, measured as the annuity commencing immediately in the year earned; that is, as the immediate annuity. We show here that this is the better reading of the statute. Before addressing the statute, however, we take a longish detour into legislative history to illustrate why Congress wanted to address the problem of post-age-65 benefit accruals. We then return to the statutory text to demonstrate why its preferred reading applies only to benefit accruals earned after age 65.

Legislative History and the Debate over Post-Age-65 Benefits

ADEA Section 4(a) was first enacted in 1967 to prohibit age-based discrimination in an employee's "compensation, terms, conditions or privileges of employment."[30] ADEA Section 4(f) states that ADEA did not prohibit a "bona fide employee benefit plan" such as a pension plan; this was not a "subterfuge" to evade ADEA's purpose.[31]

In 1979, the Department of Labor (DOL) issued final regulations on these provisions.[32] For our purposes, the 1979 regulation did two important things: First, it provided that under ADEA Section 4(f), a pension plan could satisfy ADEA on either an equal cost or equal benefit basis.[33] It thus restated a similar equal cost/equal benefit rule set forth in earlier 1969 regulations.[34] Second, the regulation let employers stop giving additional pension benefits to employees working beyond age 65.[35] The carve-out for post-age-65 benefits was necessary, according to the DOL, to conform ADEA with ERISA, allowing plans to halt additional pension accruals to employees who worked past age 65.[36]

Shortly thereafter, ADEA jurisdiction was transferred to the Equal Employment Opportunity Commission (EEOC), effective July 1, 1979.[37] The EEOC took two important stands with respect to the pension regulation it inherited from the Labor Department. The EEOC agreed that ADEA applied to pension benefits on an equal cost or equal benefit basis.[38] It disagreed, however, with the DOL's proposed carve-out for post-age-65 pension benefits. Calling the exemption contrary to law, the EEOC twice proposed guidance that would delete the post-age-65 exemption in the DOL's 1979 regulation.[39] The EEOC, however, did not follow up its proposed guidance

with published regulations. Thus, by the end of 1985, pension benefits before age 65 were (reasonably) indisputably subject to an equal cost or equal benefit standard; whether the law applied to post-age-65 pension benefits, however, remained in doubt.

To clear up the interagency dispute and clarify the law, legislators introduced bills amending ADEA to prohibit the cessation or reduction of pension benefit earnings "because of age." In the 99th Congress, for example, three such bills were introduced.[40] Floor statements accompanying all three bills stated that their sponsors' intentions were to respond to the exception for post-age-65 benefits in the DOL's ADEA regulations and the EEOC's objection.[41] All three bills also amended ERISA (and its mirror IRC provisions), to respond to the DOL's argument that its carve-out for post-age-65 pension benefits was required to conform ADEA to ERISA's provisions allowing employers to halt pension benefit accruals after age 65.[42] The three bills did not agree on how to reconcile the conflict between the two agencies with one approach leaning more to the carve-out position adopted by the DOL and one leaning more to the anti-carve-out position favored by the EEOC.

ERISA Section 204(b)(1)(H) in its current form was enacted as part of OBRA.[43] The OBRA Conference Committee Report said that the "purpose" of the legislation was to resolve the "disagreement" between the EEOC and the DOL about the application of ADEA to "benefit accruals and allocations."[44] As we have shown, the sole disagreement that legislators intended—or needed—to resolve was application of ADEA to post-age-65 benefit accruals. Consistent with our point, OBRA's legislative history uniformly reflects some legislators' apparent belief that ERISA Section 204(b)(1)(H) applied solely to post-age-65 benefit accruals. At all stages of the process—from the first introduced bills through legislators' deliberations on passage of the Conference Committee Report—documents show that legislators believed they were enacting legislation only to affect benefit accruals earned after age 65 and only to resolve the dispute about the prior law's application to benefit accruals earned after that age.[45]

What the Statute Says

Once it is read as a rule solely applicable to post-age-65 benefit accruals, the point of the statute becomes clearer: ERISA Section 204(b)(1)(H) is a legislative compromise governing the application of an old rule to post-age-65 benefit accruals. Hence the long and detailed rules governing post-age-65 benefits in "suspension" and those benefits not in suspension as well as the caption in mirror IRC Section 411(b)(1)(H).

If ERISA Section 204(b)(1)(H) applies only to benefit accruals after age 65, then what is the role of the carve-out for early retirement subsidies that by definition exist only before age 65? The carve-out is understandable as a meter-turning rule. If age 65 is the first year in

which the benefit accrual will be tested, then the baseline must be the benefit accrual measured at age 64—a year in which the subsidy will still have nonzero value. The carve-out for early retirement subsidies allows the value of the unsubsidized annuity measured at age 65 to be tested against the value of the subsidized annuity at age 64 without distortion by the subsidy.[46]

One OBRA provision is explicable only as a rule intended solely for post-age-65 benefit accruals. Recall that ERISA Section 204(b)(2) states that the rate of "allocations" (generally, employer contributions and forfeitures) to a defined contribution plan may not be reduced because of age. Its mirror provision IRC Section 411(b)(2) directs the Treasury to write special rules for "target benefit plans."[47] A target benefit plan is a defined contribution plan that mimics a defined benefit plan. Allocations are made so that the age-65 account balance will produce a target age-65 annuity. Allocations to a target benefit plan will generally be increased, not reduced, as the participant approaches age 65 (because increasingly larger allocations are necessary to yield the same age-65 benefit). For allocations to a target benefit plan before age 65, the special exception of IRC Section 411(b)(2) is thus not needed.

For allocations after age 65, however, a special exception is needed so that target benefit plans do not flunk the no-reduced-allocations rule of ERISA Section 204(b)(2). Consider two participants, one age 67 and one age 66. To yield the identical $100 life annuity for each, commencing immediately, a larger allocation must be made for the 66-year-old than for the 67-year-old (because of the 66-year-old's longer life expectancy). We see that if measured as identical immediate annuities, post-age-65 allocations to a target benefit plan would be reduced for each increase in the participant's age—a violation of ERISA Section 204(b)(2), unless a special exception applied. IRC Section 411(b)(2) contemplates that the Treasury produce just such an exception—an exception necessary only for post-age-65 allocations.[48]

We note parenthetically that the special exception for target benefit plans is necessary only if the post-age-65 allocations are measured as additions to the *immediate* annuity—that is, the annuity available to commence immediately in the year it is earned. Post-age-65 allocations would not be reduced if intended to yield identical additions to the annuity measured as the actuarial equivalent of the age-65 annuity. Rather, such allocations would remain level, and no special exception to the no-reduced-allocation rule would be required. The special rule for target benefit plans is needed only as—and indeed is explicable only as—a rule for post-age-65 allocations and only if Congress contemplated that benefit accruals after age 65 could be measured as the immediate annuity (the annuity available to commence immediately in the year of the allocation) and not solely as equal increments to the age-65 annuity. Post-age-65 allocations to a target benefit plan are thus like post-age-65 benefit accruals under a

defined benefit plan: in both cases, the statute requires us to conclude that they can be measured on the basis of the immediate annuity and not necessarily on the basis of the age-65 annuity.

In short, not only the general rule, but all the special exceptions of ERISA Section 204(b)(1)(H)—and even its companion provision adopted for defined contribution plans—can be explained entirely in terms of post-age-65 benefit accruals.

BENEFIT ACCRUALS BEFORE AGE 65

We have shown that the better reading of the statute is that it applies only to benefit accruals earned after age 65. This reading, however, is not necessary for the legality of cash balance pension plans. For the rest of this article, we assume provisionally that ERISA Section 204(b)(1)(H) applies to benefit accruals earned before age 65. We show that the statute compels the conclusion that these pre-age-65 benefit accruals can be measured on the basis of additions to the present value of the earliest annuity available under the plan. When measured on a present value basis, benefit accruals under a cash balance plan satisfy ERISA Section 204(b)(1)(H).

As above, we take a short detour into legislative history to explore the possible origin of Congress's willingness to let benefit accruals be tested on the basis of the present value of the annuity available under the plan. Again, however, the ultimate goal of our analysis is to prove that this conclusion follows decisively from the statutory text. After our brief review of legislative history, we return to the statute, and we show that benefit accruals under a cash balance plan satisfy ERISA Section 204(b)(1)(H), because the statute itself says they do.

Legislative History and the Puzzling Preservation of Old Law

One strong reading of the legislative history is that legislators believed that benefit accruals earned before age 65 were not governed at all by ERISA Section 204(b)(1)(H) and were subject solely to ERISA's rules already governing "accrued benefits." These rules include the anti-backloading rule of ERISA Sections 204(b)(1)(A), (B), and (C) and the rule under ERISA Section 204(b)(1)(G) that the participant's accrued benefit may not be reduced because of increasing age and service. This reading is consistent with the position that ERISA Section 204(b)(1)(H) applies only to benefit accruals earned after age 65. It is also consistent with other pieces of legislative history. For example, Congresswoman Roukema stated that "pension plans [conforming] with the *existing benefit accrual rules* under ERISA and the Internal Revenue Code are considered to meet the new requirements."[49] Congressman Jeffords stated that pre-age-65 benefit accruals satisfy the new rules "if they also conform to the benefit accrual rules described

in [S]ection 204 of ERISA and [S]ection 411(b) of the Internal Revenue Code."[50] The Conference Committee Report similarly stated that pre-age-65 accruals are not subject to the new rules "in cases in which a plan satisfies the normal benefit accrual requirements."[51] In short, legislative history makes a strong case that benefit accruals earned after age 65 are governed by OBRA's new age discrimination rules and before age 65 by the pre-OBRA rules already in place under ERISA.

We are now, however, provisionally assuming that OBRA's age discrimination rules do apply before age 65. Given this assumption, what did lawmakers mean by stating that new ERISA Section 204(b)(1)(H) applied the "existing" or "normal" benefit accrual rules to pre-age-65 benefit accruals? A plausible reading is that, by referring to the "existing" benefit accrual rules, lawmakers meant the age discrimination rules of ADEA Sections 4(a) and 4(f), and that these were somehow incorporated into the new statute.

In what instances were ADEA's rules then understood to apply? We have already shown that pension benefits were understood to satisfy ADEA on either an equal cost or equal benefits basis. The equal cost/equal benefit rule had the concurrence of both the EEOC and the DOL. Legislative history shows that the details of this agency guidance were generally familiar to legislators. And the equal cost/equal benefit rule was specifically assumed by some legislators to be included in the new ERISA Section 204(b)(1)(H). For example, Congressman Jeffords stated that under the new legislation, "factors other than age—such as plan cost" could be taken into account under the new rules.[52]

Oddly, while the concept of equal cost/equal benefit testing had been around for a while, neither the term "cost" nor "benefit" was well defined in the context of a pension plan. Early DOL guidance provided that a benefit's "cost" was not the employer's actual cost of providing the benefit but rather the average or actuarial cost of that benefit for a "similarly situated" group of employees.[53] In the context of a defined benefit plan, a benefit's "cost" as actuarially valued in this way is the same as its "present value." For example, to an employee, the best measure of the present value of an age-65 annuity is the cost of buying that same annuity from a commercial insurer.

The measurement of "benefit" was similarly poorly defined, especially in the context of defined benefit pension plans. One court held that the benefit under a defined benefit plan was measured for purposes of ADEA Sections 4(a) and 4(f) as the present value of that benefit.[54]

In short, legislative history provides considerable evidence that the "equal cost" prong of ADEA testing—and possibly even the "equal benefit" prong—could be measured as the present value of the benefit provided.[55]

What the Statute States

The statute on this point is more clear than the legislative history. For pre-age-65 benefit accruals, the "rate of benefit accrual" under

ERISA Section 204(b)(1)(H) is permitted to be measured as the *present value* of the annuity that would actually be paid under the plan if it commenced at the earliest time permitted under the terms of the plan. This reading is compelled by the statutory text.

The starting point of the analysis is this. To test whether the "rate of benefit accrual" decreases, one must first determine how "benefit accruals" are measured. One possible measuring rod is the age-65 annuity—the *Cooper* court's sole candidate.

A second possible measure is the "immediate" annuity—that is, the life annuity commencing immediately in the year the benefit accrual is earned. We have shown that the immediate annuity is one permitted measurement of post-age-65 benefit accruals. For pre-age-65 benefit accruals, however, the "immediate annuity" concept requires some fleshing out. For example, what is the "immediate annuity" for the benefit accrual earned by a 25-year-old participant in a plan where, regardless of the participant's age at termination of employment, annuity distributions are not permitted until age 65? One answer to this question has been supplied by Shea, Francese, and Newman in their 2000 *Virginia Tax Review* article, in which they argue that the immediate annuity is an appropriate measure of the "benefit accrual" under ERISA Section 204(b)(1)(H).[56] We do not pursue this particular argument, however, we refer the reader to the article for an excellent exposition of this position.

A third possible measure of the "benefit accrual" is the annuity that would actually be paid by the plan if it commenced at the earliest time allowed under the terms of the plan. We here shorthand this as the "earliest available annuity." For the benefit accrual earned by the 25-year-old in our above example, the earliest available annuity is the age-65 annuity, because age 65 is the earliest date the annuity could commence if he or she terminated employment in the year of the benefit accrual. For a benefit accrual earned by a 56-year-old participant in a plan where benefits may commence for terminated employees any time after age 55, the earliest available annuity is the annuity commencing immediately at age 56. That is the earliest date the annuity could commence if he or she terminated employment at age 56. The earliest available annuity in this example (in this case it is also the immediately available annuity) would be the age-65 annuity actuarially reduced to reflect the value of its earlier commencement date unless the 56-year-old were eligible for a subsidized early retirement benefit. In this case, the earliest available annuity would the subsidized annuity.

For all post-age-65 benefit accruals, the earliest available annuity under the plan is the same thing as the immediate annuity. This is because for an employee working past age 65, any benefit accruals earned after age 65 are permitted to commence immediately if the

participant terminates employment in the year of the benefit accrual. The earliest available annuity is the same thing as the immediate annuity in other cases as well, for example, in any plan that allows benefit payment to commence on an actuarially reduced basis immediately on termination of employment.

We have listed three ways of measuring the benefit accrual as an annuity: the age-65 annuity, the immediate annuity, and the earliest available annuity (which is same as the immediate annuity in some cases). A fourth possible measure is the *present value* of one of these annuities.

Here we demonstrate that the present value of the annuity—specifically, the present value of the earliest available annuity—must be one permitted way of measuring the "rate of benefit accrual." This conclusion is compelled by the statutory carve-out for early retirement subsidies under ERISA Section 204(b)(1)(H)(v).

The carve-out rule of Section 204(b)(1)(H)(v) states that in determining benefit accruals, "the subsidized portion of any early retirement benefit" may be "disregarded." Assume for the moment that ERISA Section 204(b)(1)(H) applies to pre-age-65 benefit accruals. Consider two employees, one age 60 and one age 63. Each earns an addition to the age-65 annuity of $10. Assume that both employees have met the age and service conditions for receiving a fully subsidized early retirement benefit under the plan. As the benefit accrual of each is fully subsidized, if either retired today, he or she would get the full $10 age-65 annuity, commencing immediately without actuarial reduction.

Why did Congress think that a carve-out for early retirement subsidies was necessary to make this "plain vanilla" subsidized benefit accrual pass ERISA Section 204(b)(1)(H)? As we have noted, no carve-out for subsidies is needed if "benefit accrual" is measured as the addition to the accrued benefit defined as the age-65 annuity. The subsidy, by definition, is not part of the accrued benefit. This point is illustrated in our example. For both the 60- and the 63-year-old, the addition to the accrued benefit expressed as the age-65 annuity is the same $10.

What if the benefit accrual is measured as the addition to the earliest available annuity—in this case, the $10 annuity that would commence immediately if the participant terminated employment? This could not be the right answer. For both the 60- and the 63-year-old, the addition to the earliest available annuity is the same dollar amount, namely, $10. No carve-out for early retirement subsidies is needed if "benefit accrual" is measured as the addition to the earliest available annuity.

We see that a carve-out is necessary only if Congress contemplated that the employer could test the earliest available annuity on a present value basis. The identical $10 life annuity available to commence immediately in our example has a longer expected duration for the 60-year-old than for the 63-year-old, and therefore a greater present value. Measured on a present value basis, the "rate of benefit accrual" is greater for the younger

employee than the older one in this case, solely because of age. The present value of the earliest available annuity in our example is the same for the 60-year-old as the 63-year- old only if the subsidy is "disregarded," as permitted by the carve-out rule. The carve-out for early retirement subsidies is needed if, and only if, Congress contemplated that employers could test the rate of benefit accrual on the basis of the present value of the earliest available annuity.

The earliest available annuity, as we have said, is the annuity that would actually be paid by the plan if it commenced at the earliest time permitted by the plan if the participant terminated employment in the year of the benefit accrual. In the case of the two participants eligible for subsidized early retirement in our above example, it is the annuity that would commence immediately if they accepted early retirement. In the case of the benefit accrual for, say, a 40-year-old participant in a plan that does not let benefits commence before age 65, it is the age-65 annuity. If this example is changed so that the plan lets benefits commence on a nonsubsidized basis immediately on termination of employment, it is the actuarially reduced age-40 annuity.

For this 40-year-old participant, of course, the present value of the actuarially reduced age-40 annuity is the same as the present value of the age-65 annuity.[57] For pre-age-65 benefit accruals, the present value of the earliest available annuity will always be the same as the present value of the age-65 annuity, except for accruals of subsidized early retirement benefits. In the case of a subsidized benefit accrual, the earliest available annuity is by definition the annuity that would commence immediately if the participant terminated employment (by definition, because the benefit subsidy does not begin to "accrue" until the first year the participant could elect to receive it by terminating employment). For this benefit accrual, the present value of the earliest available annuity is larger than the present value of the same benefit accrual paid as an age-65 annuity. The subsidized portion of the benefit accrual, however—measured as the present value of the increment to the earliest available annuity—shrinks to zero as the participant's age approaches age 65. Therefore there is the need for the carve-out for early retirement subsidies.[58]

In short, the "rate of benefit accrual" must be permitted to be measured as additions to the present value of the earliest available annuity under the plan, meaning the present value of the annuity that would be actually paid by the plan if it commenced at the earliest time permitted by the plan. If this way of measuring "benefit accrual" were not permitted, the statutory carve-out for subsidized benefit accruals would not be needed. The carve-out is supplied, however, showing that before age 65 the rate of benefit accrual is permitted to be measured as the present value of the addition to the earliest available annuity under the plan.

One more issue before we move on to the implications of our analysis for cash balance plans. We have seen that—assuming that

ERISA Section 204(b)(1)(H) applies to benefit accruals earned before age 65—the "rate of benefit accrual" for pre-age-65 benefit accruals can be measured as the present value of the addition to the earliest available annuity under the plan. For benefit accruals earned after age 65, however, we concluded that the statute (as well as legislative history and Treasury guidance) allows benefit accruals to be measured as additions to the face amount of this annuity, rather than to the present value of the annuity. For example, we considered a plan where the post-age-65 benefit accrual was an incremental life annuity of $10 per year, available to commence immediately in each of the years that the participant attained age 66, 67, and 68. This plan satisfied ERISA Section 204(b)(1)(H), even though the present value of the immediate $10 annuity commencing in any year after age 65 shrinks each year the participant ages.

Why the different treatments permitted for post-age- and pre-age-65 benefit accruals? The answer is that ERISA Section 204(b)(1)(H) seems to be designed to accomplish this kind of result. The statute is on its face a legislative compromise among competing treatments of post-age-65 benefit accruals. It preserves pre-OBRA rules for benefits in "suspension." For nonsuspended benefits, it allows the plan to offset additional post-age-65 benefit accruals by the actuarial value of prior distributions, or, alternatively, by the actuarial adjustments required for the previously earned accrued benefit.[59] The measurement permitted for post-age-65 benefit accruals is part of this detailed regime specified solely for the treatment of benefit accruals earned after age 65. The statute shows that Congress did not intend that benefit accruals earned before age 65 necessarily be treated under the same rules.

WHAT THIS MEANS FOR CASH BALANCE PLANS

It follows from our analysis that on the basis of the statute alone, *Cooper* was wrongly decided; the rate of benefit accrual under cash balance plans is not inherently age discriminatory under ERISA Section 204(b)(1)(H).

First, ERISA Section 204(b)(1)(H) is better read to apply only to benefit accruals earned after age 65. Under this preferred reading, it has no adverse impact on cash balance plans.

While this is the preferred reading of ERISA Section 204(b)(1)(H), it is not required for the legality of cash balance plans. Even assuming that ERISA Section 204(b)(1)(H) applies to benefit accruals earned before age 65, we have shown that these "benefit accruals" must be permitted to be measured in terms of the present value of the earliest available annuity or, more specifically, as the present value of the annuity that would actually be paid under the plan if it commenced at the earliest time permitted by the plan.

When measured as the present value of the earliest available annuity, pre-age-65 benefit accruals under a cash balance plan satisfy ERISA Section 204(b)(1)(H). Return to our first example in this article. Each of two employees, ages 35 and 55, is granted a pay credit of $100 to his or her cash balance account. Assume the plan does not permit payouts until age 65. Measured as the addition to the age-65 annuity, the benefit accrual is larger for the 35-year-old ($43) than for the 55-year-old ($16). Measured, however, as the present value of the age-65 annuity, when the discount rate is the interest crediting rate used in the plan, the benefit accrual for both employees is the same $100. The rate of benefit accrual is the same for both and satisfies ERISA Section 204(b)(1)(H).

The result, of course, does not change if the plan allows earlier payouts, because (absent benefit subsidies, which we do not assume here) the present value of the earliest available annuity is always the same as the present value of the age-65 annuity. The pre-age-65 benefit accrual under a cash balance plan always satisfies ERISA Section 204(b)(1)(h) when measured as the present value of the earliest available annuity, as the statute allows us to do.

Moreover, when looking at the present value testing permitted under ERISA Section 204(b)(1)(H), the account balance approach of *Eaton* and *Tootle* is supported and explained. In a cash balance plan, the present value of providing the yearly addition to a participant's age-65 benefit is the annual pay credit.[60] In an individual account plan, such as a 401(k) plan, the present value of providing each addition to a participant's benefit is the annual "allocation" to the account balance.[61] In such a plan, the same allocation will produce a smaller age-65 benefit for an older participant than for a younger one, because the account balance has less time to grow to reach its age-65 value. Similarly, in a cash balance plan, the identical pay credit yields a smaller increment to the age-65 benefit for the older participant than for the younger, but its present value is the same—this is all that ERISA Section 204(b)(1)(H) requires.

One more point about the present value testing permitted by ERISA Section 204(b)(1)(H). We have shown this conclusion follows decisively from the statute. It has the added virtue, however, of being consistent with the legislative history of ADEA, and specifically, the present value concept that was always lurking underneath the equal cost, and even the equal benefit, prongs of traditional ADEA testing concepts. By allowing pre-age-65 benefit accruals to be tested on the basis of the present value of the earliest available annuity under the plan, OBRA gave some definitive mathematical shape to a concept that was hitherto extant, but arguably rather loosely defined in the context of pension benefit accruals.

CONCLUSION

The *Eaton* and *Tootle* courts held that cash balance plans did not violate ERISA Section 204(b)(1)(H). They reasoned that ERISA Section

204(b)(1)(H) does not apply to benefit accruals earned before age 65. In the alternative, they reasoned that, even if ERISA Section 204(b)(1)(H) applied to benefit accruals earned before age 65, it applies to the benefit accrual as expressed under the plan—that is, as the pay credit added to the participant's account balance. We have shown that the statute is consistent with both conclusions.

First, we have shown that "rate of benefit accrual" under ERISA Section 204(b)(1)(H) cannot be measured solely as additions to the age-65 accrued benefit, and that the arguments of cash balance critics have not adequately taken into account this obstacle to their own position. Second, we have shown that the better reading of ERISA Section 204(b)(1)(H) is that it applies only to benefit accruals earned after age 65. Third, even assuming that the statute applies to benefit accruals earned before age 65, we have shown that the "rate of benefit accrual" before age 65 must be permitted to be measured in terms of the present value of the life annuity that would actually be paid by the plan if it commenced at the earliest time allowed by the plan. This is the only possible reading of the statute and, more specifically, the only way to explain why Congress believed it was necessary to enact a carve-out for subsidized early retirement annuities in order that they could pass ERISA Section 204(b)(1)(H).

When measured as the present value of the earliest available annuity under the plan, benefit accruals under a cash balance plan satisfy ERISA Section 204(b)(1)(H). On the basis of the statute alone, we are compelled to conclude that the cash balance critics are wrong, that *Cooper* was wrongly decided, and that cash balance plans are not illegally age discriminatory under ERISA Section 204(b)(1)(H).

NOTES

1. Edward A. Zelinsky, "The Cash Balance Controversy," 19 Va. Tax Rev. 683 (2000); Edward A. Zelinsky, "The Cash Balance Controversy Revisited: Age Discrimination and Fidelity to Statutory Text," 20 *Va. Tax Rev.* 557 (2001); Norman Stein, "A Controversy Over Age in an Age of Cash Balance Controversy," 14 *Benefits Law Journal* 33 (2001). *See also Cooper v. IBM Personal Pension Plan,* 274 F. Supp. 2d 1010, 1022 (S.D. Ill. 2003) ("There may be policy reasons why Congress should specifically authorize [cash balance formulas] in the context of defined benefit plans. But the narrow question here is whether the 1999 Plan comports with the literal and unambiguous provisions of ERISA § 204(b)(1)(H), and it does not.")

2. 29 U.S.C. § 1054(b)(1)(H)(i).

3. 29 U.S.C. § 623(i)(1); 26 U.S.C. § 411(b)(1)(H)(i).

4. *See Eaton,* 117 F. Supp. 2d at 822–823; Conf. Rep. No. 1012, 99th Cong. 2d Sess. 378–379 (Oct. 17, 1986).

5. IRC § 411(b)(2); ERISA § 204(b)(2); ADEA § 4(i)(1)(B).

6. ERISA Section 3(24) defines "normal retirement age" as the normal retirement age determined under the plan, but no later than the later of age 65 or the fifth anniver-

sary of the participant's commencement of participation in the plan. Our simplification thus ignores that the statute allows—and in some instances compels—normal retirement age to be expressed in ways other than age 65. The principal result of this simplification is that our analysis does not address cash balance plans that express the normal retirement age for each employee as the age that is five years after the employee's participation commencement date, as permitted by ERISA. In addition, of course, if a plan uses a specified age other than age 65 as its normal retirement age, that age should be read instead of "age 65."

7. Assuming a 5 percent interest rate and an annuity factor of 10.

8. *Cooper v. IBM Personal Pension Plan,* 274 F. Supp. 2d at 1021.

9. *Eaton v. Onan Corp.,* 117 F. Supp. 2d at 827–829; *Tootle v. ARINC, Inc.,* 2004 U.S. Dist. LEXIS 10629, at *15–16; *Engers v. AT&T Corp.,* No. 98-3660, letter op. at 8–11.

10. *Eaton v. Onan Corp.,* 117 F. Supp. 2d at 832–833; *see also Tootle v. ARINC, Inc.,* 2004 U.S. Dist. LEXIS 10629, at *16–18 (adopting a similar approach).

11. As noted above, our discussion does not include those cash balance plans that define "normal retirement age" as five years after the participant commences participation in the plan.

12. Kevin P. O'Brien and Rosina B. Barker, "Do Cash Balance Plans Violate the ADEA?" 13 *Benefits Law Journal* 75 (2000); Richard C. Shea, Michael J. Francese, and Robert S. Newman, "Age Discrimination in Cash Balance Plans: Another View," 19 *Va. Tax Rev.* 763 (2000); *See also, e.g.,* Memorandum in Support of Defendants' Motion for Partial Summary Judgment on Plaintiffs' Age Discrimination Claim with Respect to IBM's Cash Balance Formula, *Cooper v. the IBM Personal Pension Plan,* United States District Court, Southern District of Illinois, Civil Action No. 99-829 GPM, Sept. 12, 2002 ("Cooper Defendants Br. 9/12/02").

13. *See, e.g., Rusello v. United States,* 464 U.S. 16, 23 (1983) (when Congress includes limitations in one subsection of the statute but not another, we are required to conclude that limiting language not intended to apply to subsection where omitted).

14. *Cooper* at 1022.

15. *See In re Gulf Pension Litig.,* 764 F. Supp. 1149, 1176–1177 (S.D. Tex. 1991) (references in IRC § 411(d)(3) to "benefits accrued" and in Treas. Reg. § 1.411(d)-2(b)(2) to "future benefit accruals" are not the same as the term "accrued benefit," and courts will not assume that differences in wording were "drafting oversights").

16. Richard C. Shea, Michael J. Francese, and Robert S. Newman, "Age Discrimination in Cash Balance Plans: Another View," 19 *Va. Tax Rev.* 763 (2000).

17. ERISA § 203(a)(1).

18. Treas. Reg. § 1.411(a)-7(a)(1) (flush language) ("For purposes of this subparagraph [defining "accrued benefit"] a subsidized early retirement benefit which is provided by a plan is not taken into account, except to the extent of determining the normal retirement benefit under the plan."); H. Rep. No. 779, 93d Cong. 2d Sess. 59 (Feb. 1974); H. Rep. No. 1280, 93d Cong. 2d Sess. 273 (Aug. 1974) ("Also, the accrued benefit does not include the value of the right to receive early retirement benefits, or the value of social security supplements or other benefits under the plan which are not continued for any employee after he has attained normal retirement age."); *Atkins v. Northwest Airlines, Inc.,* 967 F.2d 1197, 1201 (8th Cir. 1998); *De Nobel v. Vitro Corporation,* 885 F.2d 1180, 1194 (4th Cir. 1989); *American Stores Co. v. American Stores Co. Retirement Plan,* 928 F.2d 986, 990 (10th Cir. 1991); *Ashenbaugh v.*

Crucible, Inc., 1975 Salaried Retirement Plan, 854 F.2d 1516 (3d Cir. 1988), cert. denied, 490 U.S. 1105 (1989); *Bencivenga v. Western Pennsylvania Teamsters and Employers Pension Fund,* 763 F.2d 574 (3d Cir. 1985); *Tilly v. Mead Corp.,* 927 F.2d 756 (4th Cir. 1991). *See McBarron v. S&T Industries, Inc.,* 771 F.2d 94 (6th Cir. 1985). *Contra Amato v. Western Union International, Inc.,* 773 F.2d 1402 (2d Cir. 1985), *cert. dismissed,* 474 U.S. 1113 (1986).

19. ERISA § 204(c)(3).

20. *Amato v. Western Union International, Inc.,* 773 F.2d 1402, 1412 (2d Cir. 1985).

21. *Id*. ("Thus the prohibition of IRC § 411(d)(6) against decreasing accrued benefits is to be applied broadly to bar not only provisions "directly" affecting computation of accrued benefits (which neither 26 C.F.R. § 1.411(d)-3(b) (1984) nor Rev. Rul. 81-12 purports to enumerate) but also those "indirectly" doing so, such as changes affecting actuarial factors for determining early retirement benefits. Even if there were doubts about the IRS's interpretation, it would be entitled to enforcement.")

22. Under ERISA Section 204(g)(B), as amended by the Retirement Equity Act of 1984, a plan amendment cutting back early retirement subsidies is "treated as" reducing accrued benefits. The "treated as" would be unnecessary if subsidies were "accrued benefits" for that or any other section of the Internal Revenue Code.

23. *See, e.g.,* Shea, Francese, and Newman (2000); Cooper Defendants Br. 9/12/02.

24. The dollar figures are illustrative and are not actuarially determined.

25. *Eaton v. Onan Corp.,* 117 F. Supp. 2d at 830.

26. *See* Prop. Treas. Reg. § 1.411(b)-2(b)(3)(iv), Example (5). The example shows that the initial "accrual" in each year is earned under the plan's stated formula and is not actuarially increased as would be expected of an increment to the "accrued benefit." After it becomes part of the accrued benefit, however, the accrual is subject to the same actuarial increases as all other parts of the accrued benefit in years thereafter. Under ERISA § 3002(c), Treasury guidance governing the IRC's accrued benefit under IRC § 411 applies to the ERISA accrued benefit under ERISA § 204.

27. ERISA § 3002(c).

28. Prop. Treas. Reg. § 1.411(b)-2(b)(3)(iv), Example (5).

29. Treas. Reg. § 1.401(a)(9)-6, Q&A-9. IRC § 401(a)(9)(C)(iii) requires an actuarial increase for benefits that commence after age 70½. According to Treas. Reg. § 1.401(a)(9)-6, Q&A-9, the actuarial increase required under IRC § 401(a)(9) is different from the one required by IRC § 411 (and ERISA § 204) only in that the IRC § 411 increase is subject to the exception for benefits in suspension, and the IRC § 401(a)(9) increase is not.

30. Age Discrimination in Employment Act of 1967 (ADEA), Pub. L. No. 90-202, 81 Stat. 602.

31. In 1978 Congress amended ADEA § 4(f) to reverse the Supreme Court's decision in *United Airlines v. McMann,* 434 U.S. 192 (1977), and clarify that ADEA § 4(f) did not permit a benefit plan to promote involuntary age-based retirement. Age Discrimination in Employment Act of 1978, Pub. L. No. 95-256, 92 Stat 189. This amendment is not relevant to our discussion.

32. Interpretive Bulletin on Employee Benefit Plans in Final Form, 44 Fed. Reg. 30648 (May 25, 1979). These were adopted by the Equal Employment Opportunity Commission (EEOC) when it assumed jurisdiction. 44 Fed Reg. 37974 (June 29, 1979).

The regulations were originally located at 29 C.F.R. § 860.120 but have since been redesignated by the EEOC as 29 C.F.R. § 1625.10.

33. 29 C.F.R § 860.120(a) (1979) stated that "A [retirement or pension plan] will be considered in compliance with the statute where the actual amount of payment made *or cost incurred* on behalf of an older worker is equal to that made or incurred on behalf of a younger worker *even though the older worker may thereby receive a lesser amount* of pension or retirement benefits." [Emphasis supplied].

34. 29 C.F.R. § 860.120 (1969) stated that "[a] retirement, pension, or insurance plan will be considered in compliance with the statute where the actual amount of payment made, or cost incurred, on behalf of an older worker is equal to that made or incurred on behalf of a younger worker, even though the older worker may thereby receive a lesser amount of pension or retirement benefits, or insurance coverage."

35. For example, for participants who had reached normal retirement age, defined benefit plans could cease crediting service for benefit accrual purposes, decline to provide actuarial increases for delayed payout stemming from delayed retirement, and ignore salary increases and benefit enhancements under the plan. Defined contribution plans could cease continued contributions. 29 C.F.R. § 860.120(f)(1)(iv) (1979).

36. For a summary of the DOL's position on this point, see, e.g., EEOC Proposed Partial Rescission of Interpretive Bulletin, *reprinted* at BNA Pension Reporter No. 107, X-1-10 (June 30, 1980).

37. Reorganization Plan No. 1 of 1978, 43 Fed. Reg. 19807 (May 9, 1978).

38. EEOC Proposed Partial Rescission of Interpretive Bulletin, *reprinted* at 12 BNA Pension Reporter 389 (Mar. 11, 1985), which stated "The Commission therefore proposes to modify the existing interpretation to reflect the principle that a retirement pension or insurance plan will be considered in compliance with the statute where the actual amount of payment made or cost incurred in behalf of an older worker is equal to that made or incurred in behalf of a younger worker *even though the older worker thereby may receive a lesser amount of pension or retirement benefits or insurance coverage."* [Emphasis supplied].

39. EEOC Proposed Partial Rescission of Interpretive Bulletin, *reprinted* at 12 BNA Pension Reporter 389 (Mar. 11, 1985). EEOC Proposed Partial Rescission of Interpretive Bulletin, *reprinted* at BNA Pension Reporter No 107, X-1 - 10 (June 30, 1980).

40. S. 2 introduced by Senator Cranston, H.R. 2712 by Congressman Biaggi, and S. 1427 by Senator Grassley.

41. Senator Cranston stated that he introduced S. 2 because of DOL regulations allowing employers to stop pension contributions after age 65. He further stated that he supported the EEOC's "stated intention" to revise this rule, but that "in the meantime, however, I have included in my legislation provisions which would overturn the existing rule." 131 Cong. Rec. S. 572 (Jan. 24, 1985). In his floor statement to H.R. 2712, Congressman Biaggi stated that its purpose was to overturn Labor Department regulations which allow the "denial of pension contributions for workers over age 65." 131 Cong. Rec. E 2671 (June 11, 1985).

42. For example, in his floor statement to S. 1437, Senator Grassley stated that the bill's purpose was to respond to the EEOC's announced (but still nonfinal) decision to rescind DOL regulations allowing employers to cease benefit accruals after age 65. He explained that his bill was necessary because, under the EEOC's proposed revision, ADEA would conflict with ERISA, which would "continue to permit pension plans to halt accrual at age 65." 131 Cong. Rec. S 9429 (July 11, 1985).

43. Conf. Rep. No. 1012, 99th Cong. 2d Sess. 378 (Oct. 17, 1986). A measure similar to the Grassley bill was included in a floor amendment adopted by the Senate as part of the OBRA legislation it sent over to the House. *See* Amendment No. 2863 to S. 2706, adopted by voice vote, Sept. 19, 1986. 132 Cong. Rec. S 13176 (Sept. 19, 1986). According to the Conference Committee Report, the OBRA conferees agreed to the Senate provisions, with modifications.

44. Conf. Rep. No. 1012, 99th Cong. 2d Sess. 378 (Oct. 17, 1986) ("Disagreement exists as to whether and to what extent benefit accruals and allocations are required under ADEA, as currently in effect.")

45. Spreadsheets in front of the Members of the Conference Committee—that is, documents prepared by staff summarizing the differences between the House and Senate versions of the bill—described the provision as relating to "Benefit Accruals Beyond Normal Retirement Age." *See* Comparative Committee Print, Description of Provisions of H.R. 5300, as passed by the House and Senate, Sept. 1986, No. 62-594 O, U.S. Government Printing Office, at 256 (1986). The Conference Committee Report stated that the new rules were intended to apply only to post-age-65 accruals. See Conf. Rep. No. 1012, 99th Cong. 2d Sess. 379 (Oct. 17, 1986). (The new rules do not apply where "the plan satisfies the normal benefit accrual requirements for employees who have not attained normal retirement age.") Floor statements during the House's debate on the Conference Committee Report made by members of the Committee on Education and Labor—the principal committee of jurisdiction—show these members believed that ERISA § 204(b)(1)H) applied only to benefits earned after age 65. *See* statements of Representatives Clay, Roukema, and Jeffords, 132 Cong. Rec. H. 11437 (Oct. 17, 1986). The heading of the bill's amendment of the relevant provisions of ERISA and the IRC stated that the amendments affected only post-age-65 benefits. *See* H.R. 5300, "Section 9202, Benefit Accruals Beyond Normal Retirement Age," Conf. Rep. No. 1012, 99th Cong. 2d Sess. 106 (Oct. 17, 1986). The revenue estimates prepared by staff for the Senate pursuant to its vote on the bill (required by the "Gramm-Rudmann-Hollings" law then in effect) described the provision as "requiring employers to continue pension accrual for employees who work beyond the normal retirement age." *See* 132 Cong. Rec. S 16921.

46. We thus disagree with our own earlier position on this point, in which we assumed that the carve-out for early retirement subsidies forbade reading the statute to apply only to post-age-65 accruals.

47. IRC § 411(b)(2)(B) ("The Secretary shall provide by regulation for the application of the requirements of this paragraph to target benefit plans.")

48. This reading is required by the statute. It is also supported by the OBRA Conference Committee Report, which directs the Secretary of the Treasury to issue regulations providing for the "treatment of benefit accruals under a target benefit plan for employees who have attained normal retirement age…." Conf. Rep. No. 1012, 99th Cong. 2d Sess. 380 (October 17, 1986).

49. Statement of Cong. Roukema, 132 Cong. Rec. H 11437 (Oct. 17, 1986).

50. Statement of Cong. Jeffords, 132 Cong. Rec. H 11437 (Oct. 17, 1986).

51. Conf. Rep. No. 1012, 99th Cong. 2d Sess. 379 (Oct. 17, 1986).

52. 132 Cong. Rec. H 11437 (Oct. 17, 1986) [emphasis supplied].

53. 1979 guidance stated that the employer could measure the "cost" of benefits based on their average cost for a "larger group of similarly situated employees." The employer could not, however, use its own cost data if its own actual cost was "sig-

nificantly different" from actuarial average cost data. See Amendment to Interpretive Bulletin (29 C.F.R. § 860.120), 44 Fed. Reg. 30648, 30650 (May 25, 1979).

54. *Abenante v. Fulflex Inc.,* 701 F. Supp. 296 (D. R.I. 1988).

55. We should note that in 1989 the Supreme Court held that equal cost was not an exclusive defense under ADEA § 4(f). *Public Employees Retirement System of Ohio v. Betts,* 492 U.S. 158 (1989). The *Betts* decision is not relevant to our point. By 1989, Congress had already enacted ERISA § 204(b)(1)(H) and ADEA § 4(i) as free-standing and independent sections, with none of the "subterfuge" and other language of § 4(f) that led to the *Betts* decision. All that is relevant to our discussion is what Congress thought it was doing when it enacted these provisions in 1986.

56. Shea, Francese, and Newman (2000) at 772–774 and fns. 22–25.

57. ERISA § 204(c)(3) requires that the accrued benefit commencing before normal retirement age be the actuarial present value of the normal retirement age benefit.

58. Oddly, ERISA § 204(b)(2) provides the same exception for benefit subsidies in a defined contribution plan. The need for the carve-out is not readily apparent in the case of a defined contribution plan. This is because the early retirement subsidy in a defined benefit plan has meaning only for annuities commencing before age 65, and is defined as the incremental piece of this pre-age-65 annuity over the reduced pre-age-65 annuity that is the present value of the annuity commencing at age 65. In a defined contribution plan, where the accrued benefit is expressed as the age-65 annuity, the meaning of the "subsidy" is harder to fathom. Our best bet is that Congress intended the rule for defined contribution plans that express the benefit under the plan in terms of the age-65 annuity that would be paid under a defined benefit plan, such as target benefit plans. For such plans, the allocation to a participant who accepts subsidized early retirement may be age discriminatory. This is because the additional allocation necessary to fund the same "subsidy" would shrink as the participant's age approaches age 65 (for the same reason that the present value of the subsidized benefit accrual gets smaller as the participant's age approaches age 65). For such defined contribution plans, a carve-out from ERISA § 204(b)(2) is necessary so that additional allocation necessary to fund the enhanced pre-age-65 annuity does not run afoul of the statute.

59. ERISA § 204(b)(1)(H)(iii).

60. Interest credits, of course, are not part of the employer's cost, because they are "paid" for by the plan's investment earnings.

61. The allocation is the employer's contribution to the account (plus forfeitures if any). The effect of forfeitures is age-neutral and does not affect the analysis.

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