ERISA Section 204(h) Comments

Executive Summary

Representatives of the Employee Benefits Committee met with the IRS in December 1992 to discuss possible government submissions. The IRS identified Section 204(h) as an area where assistance was needed. Section 204(h) of ERISA requires pre-notification to plan participants of a plan amendment causing a significant reduction in future benefit accrual rates under a qualified plan. Failure to follow the timing and procedures under Section 204(h) will cause (1) the plan amendment to be void ab initio, and (2) benefit accruals to continue at the prior level.

The Employee Benefits Committee formed a special volunteer task force chaired by Nick Damico and Gerry Cole to develop a set of comments for regulations being developed by IRS under Section 204(h) of ERISA.

The attached comments make the following major points:

- The application of the notice requirements should be narrowly construed to apply to a significant reduction in normal retirement benefits and contribution rates only.

- Consistent with the Davidson decision, notice should be required for any amendment that has the effect of significantly reducing the normal retirement benefit that would otherwise accrue regardless of whether the amendment, in form, changes the actual rate of accrual.

- A safe harbor should be created under which a plan change that does not result in a reduction of 20% or more in normal retirement benefits or contribution rates for any plan participant cannot be a "significant reduction." Reductions of 20% or more would be significant or insignificant depending on facts and circumstances.

- Only affected persons should be required to be given notices, and copies of plan amendments need not be furnished where the amendment is adequately described in the notice.

- In view of the confusion in the application of the rules to TRA '86 amendments, the deadline for notices required in connection with TRA '86 amendments should be extended to 15 days before the end of 1994 Plan Year, regardless of when the amendments were actually made.

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October 4, 1993

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Attention: E:EP
Room 6526

Re: <u>Regulations under ERISA Section 204(h)</u>

Dear Ms. Petschek:

Enclosed please find two copies of Comments prepared by the Taxation Section of the District of Columbia Bar regarding Treasury regulations to be issued under section 204(h) of ERISA. These comments (which are dated September 20, 1993) are being submitted in response to an informal suggestion by IRS to the Section's Employee Benefits Committee several months ago that comments on implementation of section 204(h) would be helpful to the IRS.

Representatives of the Employee Benefits Committee and the subcommittee which prepared these comments would be most pleased to meet with you and other appropriate IRS personnel to discuss these comments in further detail and to respond to any questions you may have. Please contact Seth Tievsky (Committee Chair) at 663-9538 to arrange this.

We appreciate the opportunity to submit these comments.

Sincerely yours,

Patricia G. Lewis
Chair, Taxation Section

cc: F. David Lake, Esq.
Seth Tievsky, Esq.
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TAXATION SECTION
OF THE DISTRICT OF COLUMBIA BAR

COMMENTS TO THE INTERNAL REVENUE SERVICE REGARDING REGULATIONS TO BE ISSUED UNDER SECTION 204(h) OF ERISA

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Subcommittee on Section 204(h)

September 20, 1993

x/ Principal Authors

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The views expressed herein represent only those of the Taxation Section of the District of Columbia Bar and not those of the Bar or of its Board of Governors.

**COMMENTS TO THE INTERNAL REVENUE SERVICE
REGARDING REGULATIONS TO BE ISSUED UNDER
SECTION 204(h) OF ERISA**

These comments are in response to an informal request by the Internal Revenue Service (IRS) to the Employee Benefits Committee of the D.C. Bar's Taxation Section to make recommendations to the IRS regarding implementation of the requirements of section 204(h) of the Employee Retirement Income Security Act of 1974, as amended (ERISA). 29 USC Section 1054(h). The comments were prepared by a volunteer subcommittee of the Employee Benefits Committee of the Taxation Section of the D.C. Bar and is divided into four basic areas, as follows:

1. Background of section 204(h)
2. Plans and events covered
3. Notice requirements
4. Transitional problems

I. BACKGROUND

A. Enactment

Section 204(h) of ERISA was enacted as part of the Single-Employer Pension Plan Amendments Act of 1986 (SEPPAA) which was included in the Consolidated Omnibus Budget Reconciliation Act of 1985.[1] As enacted, section 204(h) provides:

> A plan ... may not be amended so as to provide for a significant reduction in the rate of future benefit accrual, unless, after adoption of the plan amendment and not less than 15 days before the effective date of the plan amendment, the plan administrator provides a written notice, setting forth the plan amendment and its effective date, to
>
> (1) each participant in the plan,
> (2) each beneficiary who is an alternate payee ... under an applicable qualified domestic relations order..., and
> (3) each employee organization representing participants in the plan ....

This notice requirement applies to defined benefit plans and to individual account plans subject to minimum funding requirements (<u>i.e.</u>, money-purchase plans). ERISA section 204(h)(2).

B. Legislative History

The provisions of SEPPAA generally relate to the single-employer plan termination insurance provisions under Title IV of ERISA which fall under the auspices of the Pension Benefit Guaranty Corporation (PBGC). The revisions to Title IV enacted as part of SEPPAA were the product of several years of effort on the part of Congress, the affected agencies and various interest groups and were intended to ensure a viable termination insurance program.

As ultimately enacted, the SEPPAA amendments reflect various provisions that arose out of two bills, H.R. 3128[2] and H.R. 3500,[3] and the amendments to those bills offered in the Senate. As noted in the conference report to SEPPAA,[4] discussing prior law, plans could be amended to freeze accruals or to freeze other factors used to calculate benefits without providing any notice to participants. H.R. 3500 included a provision that an amendment freezing accruals would not be effective unless affected parties (as defined in the bill) were given notice of the amendment after its adoption and at least 60 days prior to the effective date of the freeze. Consistent with the overall focus of SEPPAA on plan terminations, the proposed notice requirement was limited to complete freezing of accruals and included the PBGC in the list of affected parties to whom notice must be given. Neither H.R. 3128 nor the Senate amendments offered to H.R. 3500 and H.R. 3128 included any provisions affecting prior law. The conference report to SEPPAA does note that the proposals in one of the Senate amendments regarding plan terminations covered similar situations.

While the language of the original bills coupled with the focus of SEPPAA on plan terminations suggests that the original intent was to require notice in the event of a complete cessation of benefit accruals, including a plan termination, the provision was broadened in conference. The notice requirement was expanded to cover situations involving any "significant reduction" in the

rate of future accruals and no longer required notice to the PBGC. In addition, the time period for providing the notice was reduced from 60 days before the effective date of any amendment, to 15 days before the effective date.[5] There is no discussion in the conference report nor are there any statements in the legislative history that offer any explanation of the basis for this expansion of the scope of the 204(h) requirement or the basis for the timing requirements.

The lack of significant commentary on the language ultimately adopted by the conference committee makes it difficult to ascertain the actual intent behind the notice requirement. More particularly, it is equally difficult to discern the objectives of the substantive requirements of the notice and the need for the precise timing requirements. Unlike notices required in other circumstances (e.g., a notice of intent to terminate), the recipients of a proper 204(h) notice have no ability to stop the implementation of the amendment nor do they have any statutory basis for even commenting on the changes. The timing required for giving notice does not appear to be directed at enabling the recipients to take any action regarding the notice because the notice is not effective unless given after the adoption of the amendment. Similarly, the fact that the plan administrator must give only 15 days notice before the amendment becomes effective would not appear to allow for sufficient time for the recipients of the notice to take any action regarding the amendment. As a result, while the original proposal for a 60-day notice of a complete freeze of accruals was consistent with the other notice requirements regarding terminations which were enacted by SEPPAA, the current 204(h) requirement appears to be designed simply as an informational notice.

C. Interpretive Case Law

There have been only two reported cases of which we are aware involving disputes over the application of the 204(h)

notice requirement. They illustrate the potential problems and dramatic consequences which may flow from this requirement and the need for specific guidance.

In Davidson v. Canteen Corp.,[6] the employer sponsored a pension plan that provided benefits based on an employee's final average compensation. Compensation was originally defined to include annual W-2 pay. The plan's definition of compensation was amended to exclude compensation resulting from the exercise of stock options; however, no other change to the plan's benefit formula was made. No written notice of the amendment was provided to plan participants. The plaintiffs had exercised stock options after the effective date of the amendment, and when they subsequently retired, their benefits did not include any income earned as the result of the post-amendment exercise of the options. The sponsor argued that no change was made to the rate of future accruals because there was no change to the plan formula and the 204(h) notice requirement was therefore inapplicable. The Seventh Circuit rejected this argument and held that while the rate of accruals under the plan's formula was not changed, the change in the definition of compensation in fact acomplished the same result. The court also held that the fact that the amendment affected only a small number of participants and would reduce benefits only in limited circumstances did not obviate the need for the notice required by section 204(h).

While Canteen reflects the uncertainties in the scope of section 204(h), another Seventh Circuit decision, Production and Maintenance Employees' Local 504 v. Roadmaster Corp.,[7] illustrates the potential problems in attempting to comply with the procedural requirements. In Roadmaster, the plan sponsor amended the plan to freeze benefit accruals. The effective date of the freeze was purported to be prior to the date that the board of directors formally adopted the amendment. The company mailed a notice of this change to the union and posted a notice for the employees. During the course of litigation, the company

attempted to cure the potential defects in the original notice by "clarifying" the original amendment to postpone the freeze until a date that was more than 15 days after the union had received notice and the notice to employees was posted. The court held that neither the original amendment nor the attempted "clarification" was effective as the result of the failure to give proper notice. With respect to the original amendment, the court noted that, because the amendment was effective retroactively, the notice was not given 15 days prior to the effective date as required by 204(h). Furthermore, the court held that the posting of the notice was insufficient to satisfy the requirement that each participant be given notice. The company's attempt to cure the initial defects by subsequently extending the accruals until after the notice had been given was likewise ineffective. The notice actually given did not set forth the effective date purportedly adopted by the clarification and, as with the first attempted amendment, the adoption date was in fact after the effective date. The court reasoned that participants were never given adequate notice that complied with the timing requirements - after adoption and before the effective date. As the result of the failure to give proper notice, the court concluded that the amendment to the plan freezing accruals was void ab initio.

D. Jurisdiction

Pursuant to Reorganization Plan Number 4 of 1978,[8] the authority of the Secretary of Labor to issue regulations and rulings under ERISA section 204 was transferred to the Secretary of the Treasury. To date, with the exception of the guidance issued in connection with plan amendments required by the Tax Reform Act of 1986 which are further discussed below, no formal guidance has been issued by the IRS regarding compliance with the 204(h) notice requirements.

II. Plans and Events Covered

A. Plans Covered

By its terms section 204(h) covers defined benefit and other plans subject to the minimum funding standards, *i.e.*, money purchase plans. This definition would appear to cover multiemployer as well as single employer defined benefit plans. Thus, there is no basis in the statutory language for excluding any plans in those categories (i.e., defined benefit and money-purchase plans). At the same time, there is no basis for expanding the categories of plans to which the section applies beyond defined benefit and money-purchase plans (e.g., profit-sharing, ESOP, 401(k) and stock bonus plans are not covered).

B. Events Covered

Section 204(h) applies to "a significant reduction in the rate of future benefit accrual." The issue is twofold: what is a reduction in the rate of future accruals and what is significant.

The initial question for the regulations being developed is whether to attempt to develop a specific definition of covered events or simply repeat the statutory definition without further elaboration. The subcommittee recommends that the IRS propose a specific definition. As more fully described below, the subcommittee recommends that IRS take the position that section 204(h) applies only to plan amendments that significantly reduce the rate at which a plan accrues the normal retirement benefit.

The penalty for failure to comply with the section in the few cases reported so far has been to require the employer to restore the prior plan provisions. Since a case under section 204(h) may be decided many years after the plan amendment, both the interests of participants and employers in certainty point in favor of specific guidelines. In this way, employers will be on notice of what plan amendments they must report, and hopefully, the courts will be dissuaded from developing a common law in this

area. Such judicial authorities -- given the vagueness of the statutory language -- will differ from jurisdiction to jurisdiction.

1. Types of Amendments Covered

The statutory language applies to only those amendments that reduce the rate of future accruals. Since ERISA's accrual rules apply only to the normal retirement benefit, the section should apply only to plan amendments that reduce the rate at which a plan accrues the normal retirement benefit. Thus, plan amendments that reduce early retirement subsidies for future accruals would not be covered. Similarly plan amendments that reduce the actuarial value of optional forms of benefit would not be covered under the section. Also, changes in the vesting schedule or the requirements for plan participation would not be covered because they do not change the amount of benefit persons will accrue after they become participants. To provide otherwise would go beyond the statutory language and unnecessarily increase administrative costs and uncertainty.

Rights to optional forms of benefit and early retirement subsidies are protected under section 411(d)(6) of the Internal Revenue Code (the Code) and notice of any changes in the treatment of future accruals with respect to optional forms or early retirement subsidies should be given participants in the summary of material modifications required under section 104(a)(1)(D) of ERISA. The ability of an employer to affect the future benefits of individuals who are not yet plan participants is limited by participation standards which severely limit the extent to which an employer may make an employee wait before becoming a participant. Thus, with respect to changes in the participation standard, one rationale for requiring notice -- the unfettered ability of an employer to determine the benefit formula -- is not present.

Although we recognize that these same arguments could be made regarding section 204(h) generally, the existence of these

other protections obviates the need to extend section 204(h) beyond the specific statutory language and argues strongly for a narrow interpretation of the provision. The legislative history also supports this view. Section 204(h) was first proposed as part of SEPPAA to prevent employers from totally freezing a plan without first notifying participants. Although Congress subsequently modified the language to include any significant reduction in the rate of accruals, the legislative history strongly implies that Congress intended to focus on events that were within the discretion of the employer. Accordingly, most changes that are made to comply with the Tax Reform Act of 1986 (TRA '86) should not be covered since they are not really discretionary. (In fact, the uncertainties of the 204(h) notice requirement in connection with TRA '86 amendments, we submit, necessitate a delay in the deadline for any 204(h) notice that may be required in connection with TRA '86 amendments to the end of the remedial amendment period (currently the end of the 1994 plan year). This proposal is discussed under IV. TRA '86 Issues, below.)

For these same reasons, we urge that the regulations specifically provide that no notice shall be required when non-discretionary mandated amendments result in a significant reduction in the rate of benefit accruals. Further, in other mandated benefit reduction situations (*i.e.*, where the plan sponsor is provided choices as to how to conform to required legislative or regulatory changes) the IRS should continue providing express guidance as to the applicability of section 204(h). See, for example, Q&A 18 of Notice 87-21[9] dealing with changes to Section 415 of the Internal Revenue Code.

The fact that the amendment applies only to reductions in the *rate* of accrual would also support an argument that changes in the definition of compensation or the computation of years of service that do not change the basic accrual formula are not within the scope of the section. The subcommittee recommends,

however, that any change that has the effect of significantly reducing the normal retirement benefit that would otherwise accrue after the date of the amendment should be covered. Employers should not be free to do indirectly that which they may not do directly. For example: It matters little whether the multiplier for accruals is changed from 1.5% of pay to 1% of pay or the definition of compensation is changed from regular earnings to two-thirds of regular earnings. These changes should be treated as reductions in the rate of accruals.

Although this approach would literally cover changes in the number of hours necessary to earn service credits, the rule should not apply to a change from the hours method to the broader elapsed time method of calculating service credits, or vice versa, since a change in the method of determining hours of service is not normally associated with, nor does it substantially effect, the benefit formula. Similarly, changes in equivalencies (e.g., to hours worked) should not be considered to cause a reduction in the rate of accrual of benefits.

2. Definition of Significant Reduction

The adjective "significant" does not occur often in ERISA, and there is no agreed threshold for what constitutes a "significant" event. We are unaware of any instance under ERISA in which the term "significant" is used in conjunction with the concept of the rate of something.

One option is to not define significant reduction and allow the courts to develop this concept under the common law. The few cases reported thus far have had little trouble in determining that an amendment that has a very substantial effect on future accruals, even for a small number of participants, is significant. These determinations were not based on any objective citeria. The reported cases have not, however, needed to explore carefully the limits of what constitutes a significant reduction. Again, because of the desire for certainty and the fact that the concept of a rate of accrual is already measured

under the accrual rules, we believe that the regulation should establish a safe harbor for what does not constitute a "significant reduction in the rate of future benefit accruals."

The term significant implies something not necessarily as large as 50% and, obviously, something more than zero. Within that range, reasonable people can differ on what is a significant reduction in the rate of accruals. We are not suggesting that the IRS determine by regulation specifically, in each instance, when a reduction will be deemed significant. However, we do suggest that the IRS should prescribe a threshold, or safe harbor, under which the amendment may be conclusively presumed to be insignificant, so that courts, participants, and employers may know for certain that such an amendment that reduces the rate of future accruals is not significant.

In this regard, rulings and cases under section 411(d)(3) of the Internal Revenue Code can provide some guidance. The IRS rulings provide that a partial termination occurs if there is a significant reduction in the number of participants. Those rulings and cases have generally held that a reduction of more than 25% is significant, and a reduction of less than 15% is not significant. Moreover, the instructions to the IRS Form 5310 (Question 13c) require the employer or plan administrator to explain why any reduction in participants of 20% or more would not constitute a partial termination.

3. <u>Safe Harbor</u>

Given all of the above, we suggest providing a safe harbor so that a plan amendment, or series of plan amendments over the course of two plan years, that is not reasonably expected to reduce the annual rate of accrual of the normal retirement benefit of any participant that would otherwise accrue after the effective date of the amendment by 20% or more is not covered by the section. A facts and circumstances standard would apply if the reduction were 20% or more.

Under this standard, if the change involves only the plan benefit formula, it should be relatively easy to determine whether or not future benefit accruals would be reduced by 20% or more. If other factors such as the definition of compensation are involved, the regulations should not require the plan actuaries or consultants to determine future benefit accruals for each participant. Rather, the plan administrator should be permitted to rely on sample demonstrations (e.g., at various compensation and service levels) prepared by the plan's actuaries or consultants in determing whether or not the safe harbor would apply.

This standard could be applied to cash balance plans that change the guaranteed interest rate by estimating the effect of the change on the projected cash balance at normal retirement age under the former and new guaranteed rate of interest. For a money-purchase plan, the regulation would not apply to reductions in the percent of contributions or percent of compensation on which those contributions are based, of less than 20%. For example, if the plan amendment decreased contributions from 10% of earnings to 8.25% of earnings without changing the definition of earnings, it would fall within the safe harbor. However, if the plan also changed the definition of earnings to reduce the earnings taken into account for any participant, it might not qualify for the safe harbor.

In the case of a target benefit plan, the determination should be based on the effect of any changes on the targeted normal retirement benefit.

For changes of 20% or more, we recommend that the regulation provide that whether the change is significant be based on all the facts and circumstances. These would include the percentage of participants affected[10] and the expected aggregate effect of the change on the normal retirement benefit that would otherwise accrue. Thus, failure to meet the safe harbor would not automatically require the notice.

III. Mechanics of the Notice

The overriding goal regarding the mechanics of the 204(h) notice should be to educate affected participants while minimizing the resulting administrative burden. The goal of the 204(h) notice can be met without requiring plan administrators to engage in unnecessary and/or duplicative efforts. Given (a) the range of communication methods available to plan sponsors and (b) the diversity of benefit reductions that arguably fall under the section, a standard of reasonableness under the facts and circumstances should be established.[11] More specific guidance should be provided with regard to who receives the notice, its format and content, the method of delivery, multiple notice requirements and the timing of the notice.

A. Who Receives the Notice

Section 204(h) broadly defines the recipient group as participants, alternate payees under a qualified domestic relations order ("QDRO"), and employee organization representatives. As discussed above, section 204(h) appears to cover certain benefits available to a limited number of participants at the time of the plan amendment's effective date. In certain instances, it would be unnecessarily burdensome for plan sponsors to notify persons who are not reasonably expected to be adversely affected by the amendment at the time of its effective date. In this regard, the regulations should provide that a plan administrator need not provide the notice to participants, former participants or alternate payees falling into any of the following categories:

1) active participants accruing benefits under the plan who, in the reasonable opinion of the plan administrator as of the date the plan amendment is adopted, will not incur a significant reduction in the rate of benefit accrual because of the plan amendment;

2) active participants accruing benefits under a formula that will not be affected by the plan amendment;
3) alternate payees whose benefit rights under a QDRO will not be affected by the plan amendment;
4) former participants with vested deferred benefits, the amount of which will not be affected by the plan amendment; and
5) employee organizations representing only participants in any of the above categories.

These provisions would strengthen the 204(h) notice requirement by focusing delivery of the notice on those actually affected while limiting unnecessary production of notices for parties not reasonably expected to be affected directly by the plan amendment. This approach also avoids confusing or alarming unaffected parties. The regulations should provide explicit examples of situations where the above-listed exceptions would be available.

In providing notice under section 204(h), plan administrators should have reasonable protection from missing incoming plan participants. Therefore, the regulations should provide that when notice is given at least within 15 days before and within 60 days of the effective date of the plan amendment, the plan administrator is not required to notify plan participants who commence participation between the date notice is given and the amendment's effective date.

B. Format and Content of the Notice

Section 204(h) provides that the notice be (a) written and (b) set forth the plan amendment and its effective date. The possible benefit reductions covered under section 204(h) can require descriptions of varying lengths. Under some interpretations, actual reproduction and dissemination of the plan amendment may be the only manner of complying with section 204(h). In other cases a brief synopsis of the amendment could

suffice. In fact, in some cases, dissemination of the plan amendment by itself may not be adequate since the average plan participant might not be able to comprehend it. Accordingly, given the (a) varying demographics of participant groups and (b) changing technology available for employee benefit communications, the regulations should broadly define the available formats and content of the notice. The regulations should allow any format that is designed in a manner calculated to be understood by the average affected plan participant. In addition, the regulations should clarify that different formats and language may be used with respect to different sub-groups of affected participants. Finally, the regulations should clarify that it is permissible, although not required, to attach to the notice the actual plan amendment itself.

The communication should be required to set forth the effective date and expressly, by way of example or otherwise, indicate the general impact of the amendment on future benefit accruals. Regulations under section 204(h) should not require the plan administrator to detail all the circumstances which may cause significant reductions in the rate of benefit accrual or explain detailed aspects of the potential consequences.

In addition, the regulations should not require the notice to be set forth in a free-standing document. For example, if a notice of plan termination is issued during the notice period, all notification requirements could be satisfied in one communication.

C. Delivery of the Notice

Delivery requirements for the notice should allow for maximum administrative flexibility. The requirements of section 204(h) should be considered met so long as the plan administrator sends a communication to the affected parties' last known addresses or by a reasonable approximate method (e.g., desk drop; interoffice mail; posting). In certain cases, a written electronic transfer which is reasonably assumed to reach affected

participants should suffice so long as (a) each participant can produce a hard copy and (b) the plan administrator makes readily available a hard copy of the notice upon request.

In the event a notice is returned to sender address unknown, the notice should be deemed delivered.

D. Multiple Notices

Neither section 204(h) nor its legislative history requires the delivery of an express and distinct communication. In certain instances a separate 204(h) notice would be duplicative of other required notices. Accordingly, as briefly noted above, if a revised summary plan description, summary of material modifications, notice of intent to terminate, etc., otherwise meets the timing requirements of section 204(h) and adequately describes the benefit reduction, the requirements of section 204(h) should be considered met.

E. Timing of the Notice

Section 204(h) requires notice be provided after the adoption of the amendment and not less than 15 days before the effective date. The regulations should provide that the amendment will be considered as adopted on the date the plan sponsor completes corporate governance activities it deems necessary to set forth the parameters of the changes. Because of the possible delays in setting out the technical language, it should be possible to give notice after the corporation has set the policy, even if the actual plan amendment is not in final executed form. Thus, the regulations should provide that the plan amendment itself need not be completed and executed if all approval steps have taken place.

If notice is not timely given, the employer should have the option of applying the plan amendment as of a date which is at least 15 days after the notice is given. In other words, corrective amendments, effective as of a date that is at least 15 days after a notice is given, should be permitted.

IV. TRA '86 Issues

The application of section 204(h) to TRA '86 amendments presents special problems. A short review of the IRS pronouncements on the 204(h) notice requirements, made as part of its major TRA '86 announcements, notices and procedures issued to date, may be helpful.

First, in IRS Notice 88-131, the IRS announced methods for plans not yet amended for TRA '86 to "freeze" accruals to avoid violating the section 411(d)(6) requirements. In other words, the IRS quickly recognized that to meet the new TRA '86 requirements, the flexibility to provide some cutback in benefits for some participants was critical, since many of the new rules (particularly the section 401(a)(4) requirements) would not be in place before the 1989 effective date.

IRS Notice 88-131 provided four model amendments to deal with the above-described problem. The first three model amendments dealt with freezing of benefits for some or all of the plan participants. Model Amendment #4 dealt with plan termination. IRS Notice 88-131 specifically stated that the 204(h) notice was not required in connection with Model Amendments 1-3, although it also stated that a 204(h) notice may be required in connection with the TRA '86 permanent amendments that were to replace the model amendment at a later time -- if such later amendments significantly reduced future benefit accruals.

The position taken by the IRS in Notice 88-131 actually involved a significant policy decision to the effect that 204(h) notices required in connection with TRA '86 could be given after the amendment's effective date. (As discussed above, section 204(h) requires that the 204(h) notice be given before the amendment's effective date.) Consequently, the IRS recognized early on that TRA '86 amendments required special administrative relief as to 204(h) notices.

IRS Notice 88-131 also logically provided that if Model Amendment #4 was used to effectuate a plan termination a 204(h) notice was required. Model Amendment #4, which initially had to be adopted by May 31, 1989, allowed for the termination of a plan in 1989 without the 1989 TRA '86 amendments if the benefit accruals of the highly compensated employees were frozen as of the end of 1988. Later, in IRS Notice 89-92,[12] the IRS extended the latest termination date under Model Amendment #4 to December 31, 1989, provided the model amendment was adopted and the 204(h) notice given by December 16, 1989.

At this point, the IRS appeared to be developing a reasonable overall approach to the 204(h) notice requirements to the effect that the 204(h) notice had to be given in connection with a plan termination, but otherwise as to TRA '86 amendments, could be delayed until a permanent method of complying with the new TRA '86 requirements had been worked out. However, the consistent delays in promulgating final substantive rules, the need for employers to make changes unconnected with TRA '86, and a confusing approach to extending the deadlines for adoption of some of the model amendments all combined to obfuscate the application of the 204(h) notice requirements. This situation was further compounded by the lack of regulations under section 204(h) as to how, or to whom, the notice should be given, and when a significant reduction in future benefit accruals might occur (other than by reason of a plan termination).

Against this background, the IRS issued Rev. Proc. 89-65,[13] extending the expiration date of Model Amendment #3 in all cases to the end of the 1990 plan year -- and beyond the end of the 1990 plan year if a 204(h) notice was given by 12/31/90. Similarly, IRS Notice 90-73[14] provided that Model Amendment #2 could not be extended beyond the 1991 plan year unless a 204(h) notice was given no later than 15 days before the beginning of the 1992 plan year.

First of all, these approaches appeared to conflict with the IRS's position in IRS Notice 88-131 that the 204(h) notice could be delayed until the permanent TRA '86 amendments were made. Moreover, some employers would want to extend Model Amendment #3 beyond the 1990 plan year, others would not, and a third group would replace Model Amendment #3 with an interim amendment which might or might not involve a significant reduction in the future accrual of benefits. Similar options were available with respect to Model Amendment #2. These possibilities further clouded the issue of whether a 204(h) notice was required.

On a broader scale, the delay in announcing final TRA '86 substantive rules has led employers to concentrate on deadlines for *adopting* amendments, rather than advising employees that their actions might result in a cutback of some benefits. In other words, even if the 204(h) rules had been clear, compliance would be spotty during the TRA '86 transitional period. At the same time, if a decision were made to terminate the plan because of the new requirements, the need to provide a 204(h) notice should have been obvious.

In essence, we submit that the approach initially taken in Notice 88-131 was essentially correct -- restricting standard 204(h) notices to plan terminations, and delaying 204(h) notice requirements that might apply in connection with TRA '86 amendments to a later date. The imposition of 204(h) notice requirements in 1990 and 1991 in connection with extensions of Model Amendments #2 and #3 detracted from that approach. Moreover, employers have had their hands full in keeping up with TRA '86 requirements, without focusing on the requirements of section 204(h), the rules for which have yet to be announced.

Given the above situation, we submit that a general relief program should be announced, hopefully in connection with proposed or final regulations under section 204(h). We propose that IRS should allow any 204(h) notice requirements that might have arisen in connection with plan amendments dealing with TRA

'86 to be met by a 204(h) notice given no later than 15 days before the end of the final remedial amendment period (*e.g.*, currently by no later than 15 days before the end of the 1994 plan year) -- **regardless of when the TRA '86 amendments are actually made, including the situation where such amendments were made before the end of the 1994 Plan Year, but no 204(h) notice was given or an ineffective 204(h) notice was given.** Of course, the relief would not apply to a plan termination, or to a significant reduction in future benefit accruals unconnected with TRA '86. However, a good faith transitional rule would appear desirable in these situations pending final regulations.

Obviously, in considering the comments set forth above and in developing the regulations, questions not addressed above will arise. Members of the special subcommittee of the Employee Benefits Committee of the D.C. Bar Taxation Section which initially prepared the above comments, along with designated officers of the Employee Benefits Committee, are agreeable to working with the IRS in the development of proposed and final regulations under section 204(h) -- particularly in connection with the comments made above.

ENDNOTES

1. Consolidated Omnibus Budget Reconciliation Act of 1985, Title XI, Pub. L. No. 99-272, 100 Stat. 82 (1986).

2. H.R. 3128, 99th Cong. 2d Sess. (1986).

3. H.R. 3500, 99th Cong. 2d Sess. (1986).

4. Joint Explanatory Statement of the Conference Committee on H.R. 3128, December 19, 1985.

5. Id.

6. Davidson v. Canteen Corp., 957 F.2d 1404 (7th Cir., 1992).

7. Production and Maintenance Employees' Local 504 v. Roadmaster Corp., 954 F. 2d 1397 (7th Cir., 1992).

8. Reorg. Plan No. 4 of 1978, 1978 U.S. Code Cong. & Ad. News (95 Stat.) 9814.

9. IRS Notice 87-21, 1987-1 C.B. 458.

10. Contrary to the Roadmaster case, we feel that a change only affecting a few participants, even if major, need not necessarily be covered by 204(h).

11. Indeed, the Service should consider providing an exception to the harsh results of a strict application of section 204(h) where the employer has made a good faith effort to comply with the notice requirements.

12. Rev. Proc. 89-92, 1989-2 C.B. 410.

13. Rev. Proc. 89-65, 1989-2 C.B. 786.

14. IRS Notice 90-73, 1990-2 C.B. 353.