Internal Revenue
bulletin

Bulletin No. 2010-48
November 29, 2010

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Notice 2010–75, page 781.

Credit for carbon dioxide sequestration, 2010 section 45Q inflation adjustment factor. The notice publishes the inflation adjustment factor for the credit for carbon dioxide (CO_2) sequestration under section 45Q of the Code for calendar year 2010. The amount of credit must be adjusted for inflation for taxable years beginning in a calendar year after 2009.

EMPLOYEE PLANS

T.D. 9505, page 755.

Final regulations under sections 411(a)(13) and 411(b)(5) of the Code, which were added by section 701(b) of the Pension Protection Act of 2006 (PPA '06), provide guidance concerning hybrid defined benefit pension plans, including cash balance plans. The regulations under section 411(a)(13) generally describe the plans that are treated as statutory hybrid plans and provide special benefit calculation and vesting rules with respect to those plans. The regulations under section 411(b)(5) provide rules for statutory hybrid plans to comply with age discrimination requirements, including rules governing design of and conversion to a statutory hybrid plan, and rules governing operation of those plans, including providing interest credits that do not exceed a market rate of return.

REG–132554–08, page 783.

Proposed regulations under sections 411(a)(13) and 411(b)(5) of the Code, as well as section 411(b)(1), provide additional guidance concerning hybrid defined benefit pension plans, including cash balance plans. In particular, these proposed regulations provide guidance as to the scope of relief under section 411(a)(13)(A), contain a special rule regarding the application of the 133 1/3 percent rule under section 411(b)(1)(B) to statutory hybrid plans that credit interest using a variable rate, provide an alternative method of satisfying the conversion protection requirements under section 411(b)(5)(B)(ii), and provide additional guidance with respect to the market rate of return rules under section 411(b)(5)(B)(i). A public hearing is scheduled for January 26, 2011.

ADMINISTRATIVE

Rev. Proc. 2010–41, page 781.

This procedure describes the procedures foreign persons and U.S. citizens without a social security number, due to conscientious religious objection, must follow to obtain a preparer tax identification number (PTIN) and provides temporary relief during the 2011 filing season for these individuals who experience delay in obtaining PTINs.

Finding Lists begin on page ii.
Index for July through November begins on page iv.

Department of the Treasury
Internal Revenue Service

The IRS Mission

Provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents are compiled semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The last Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the last Bulletin of each semiannual period.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 411.—Minimum Vesting Standards

26 CFR 1.411(a)(13)–1: Statutory hybrid plans.

T.D. 9505

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Hybrid Retirement Plans

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final Regulations.

SUMMARY: This document contains final regulations providing guidance relating to certain provisions of the Internal Revenue Code (Code) that apply to hybrid defined benefit pension plans. These regulations provide guidance on changes made by the Pension Protection Act of 2006, as amended by the Worker, Retiree, and Employer Recovery Act of 2008. These regulations affect sponsors, administrators, participants, and beneficiaries of hybrid defined benefit pension plans.

DATES: *Effective Date:* These regulations are effective on October 19, 2010.

Applicability Date: These regulations generally apply to plan years that begin on or after January 1, 2011. However, see the "**Effective/Applicability Dates**" section in this preamble for additional information regarding the applicability of these regulations.

FOR FURTHER INFORMATION CONTACT: Neil S. Sandhu, Lauson C. Green, or Linda S. F. Marshall at (202) 622–6090 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Income Tax Regulations (26 CFR part 1) under sections 411(a)(13) and 411(b)(5) of the Code. Generally, a defined benefit pension plan must satisfy the minimum vesting standards of section 411(a) and the accrual requirements of section 411(b) in order to be qualified under section 401(a) of the Code. Sections 411(a)(13) and 411(b)(5), which modify the minimum vesting standards of section 411(a) and the accrual requirements of section 411(b), were added to the Code by section 701(b) of the Pension Protection Act of 2006, Public Law 109–280 (120 Stat. 780 (2006)) (PPA '06). Sections 411(a)(13) and 411(b)(5), as well as certain effective date provisions related to these sections, were subsequently amended by the Worker, Retiree, and Employer Recovery Act of 2008, Public Law 110–458 (122 Stat. 5092 (2008)) (WRERA '08).

Section 411(a)(13)(A) provides that an applicable defined benefit plan (which is defined in section 411(a)(13)(C)) is not treated as failing to meet either (i) the requirements of section 411(a)(2) (subject to a special vesting rule in section 411(a)(13)(B) with respect to benefits derived from employer contributions) or (ii) the requirements of section 411(a)(11), 411(c), or 417(e), with respect to accrued benefits derived from employer contributions, merely because the present value of the accrued benefit (or any portion thereof) of any participant is, under the terms of the plan, equal to the amount expressed as the balance of a hypothetical account or as an accumulated percentage of the participant's final average compensation. Section 411(a)(13)(B) requires an applicable defined benefit plan to provide that an employee who has completed at least 3 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from employer contributions.

Under section 411(a)(13)(C)(i), an applicable defined benefit plan is defined as a defined benefit plan under which the accrued benefit (or any portion thereof) of a participant is calculated as the balance of a hypothetical account maintained for the participant or as an accumulated percentage of the participant's final average compensation. Under section 411(a)(13)(C)(ii), the Secretary of the Treasury is to issue regulations which include in the definition of an applicable defined benefit plan any defined benefit plan (or portion of such a plan) which has an effect similar to a plan described in section 411(a)(13)(C)(i).

Section 411(b)(1)(H)(i) provides that a defined benefit plan fails to comply with section 411(b) 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. Section 411(b)(5), which was added to the Code by section 701(b)(1) of PPA '06, provides additional rules related to section 411(b)(1)(H)(i). Section 411(b)(5)(A) generally provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) if a participant's accrued benefit, as determined as of any date under the terms of the plan, would be equal to or greater than that of any similarly situated, younger individual who is or could be a participant. For this purpose, section 411(b)(5)(A)(iv) provides that the accrued benefit may, under the terms of the plan, be expressed as an annuity payable at normal retirement age, the balance of a hypothetical account, or the current value of the accumulated percentage of the employee's final average compensation. Section 411(b)(5)(G) provides that, for purposes of section 411(b)(5), any reference to the accrued benefit of a participant refers to the participant's benefit accrued to date.

Section 411(b)(5)(B) imposes certain requirements on an applicable defined benefit plan in order for the plan to satisfy section 411(b)(1)(H). Section 411(b)(5)(B)(i) provides that such a plan is treated as failing to meet the requirements of section 411(b)(1)(H) if the terms of the plan provide for an interest credit (or an equivalent amount) for any plan year at a rate that is greater than a market rate of return. Under section 411(b)(5)(B)(i)(I), a plan is not treated as having an above- market rate merely because the plan provides for a reasonable minimum guaranteed rate of return or for a rate of return that is equal to the greater of a fixed or variable rate of return. Section 411(b)(5)(B)(i)(II) provides that an applicable defined benefit plan is treated as failing to meet the requirements of section 411(b)(1)(H) unless the plan provides that an interest credit (or an equivalent amount) of less than zero can in no event result in the account balance or similar amount being less than the aggregate amount of contributions credited to the account. Section 411(b)(5)(B)(i)(III) authorizes the Secretary of the Treasury to provide by regulation for rules governing the calculation of a market rate of return for purposes of section 411(b)(5)(B)(i)(I) and for permissible methods of crediting interest to the account (including fixed or variable interest rates) resulting in effective rates of return meeting the requirements of section 411(b)(5)(B)(i)(I).

Section 411(b)(5)(B)(ii), (iii), and (iv) contains additional requirements that apply if, after June 29, 2005, an applicable plan amendment is adopted. Section 411(b)(5)(B)(v)(I) defines an applicable plan amendment as an amendment to a defined benefit plan which has the effect of converting the plan to an applicable defined benefit plan. Under section 411(b)(5)(B)(ii), if, after June 29, 2005, an applicable plan amendment is adopted, the plan is treated as failing to meet the requirements of section 411(b)(1)(H) unless the requirements of section 411(b)(5)(B)(iii) are met with respect to each individual who was a participant in the plan immediately before the adoption of the amendment. Section 411(b)(5)(B)(iii) specifies that, subject to section 411(b)(5)(B)(iv), the requirements of section 411(b)(5)(B)(iii) are met with respect to any participant if the accrued benefit of the participant under the terms of the plan as in effect after the amendment is not less than the sum of: (I) the participant's accrued benefit for years of service before the effective date of the amendment, determined under the terms of the plan as in effect before the amendment; plus (II) the participant's accrued benefit for years of service after the effective date of the amendment, determined under the terms of the plan as in effect after the amendment. Section 411(b)(5)(B)(iv) provides that, for purposes of section 411(b)(5)(B)(iii)(I), the plan must credit the participant's account or similar amount with the amount of any early retirement benefit or retirement-type subsidy for the plan year in which the participant retires if, as of such time, the participant has met the age, years of service, and other requirements under the plan for entitlement to such benefit or subsidy.

Section 411(b)(5)(B)(v) sets forth certain provisions related to an applicable plan amendment. Section 411(b)(5)(B)(v)(II) provides that if the benefits under two or more defined benefit plans of an employer are coordinated in such a manner as to have the effect of adoption of an applicable plan amendment, the plan sponsor is treated as having adopted an applicable plan amendment as of the date the coordination begins. Section 411(b)(5)(B)(v)(III) directs the Secretary of the Treasury to issue regulations to prevent the avoidance of the purposes of section 411(b)(5)(B) through the use of two or more plan amendments rather than a single amendment.

Section 411(b)(5)(B)(vi) provides special rules for determining benefits upon termination of an applicable defined benefit plan. Under section 411(b)(5)(B)(vi)(I), an applicable defined benefit plan is not treated as satisfying the requirements of section 411(b)(5)(B)(i) (regarding permissible interest crediting rates) unless the plan provides that, upon plan termination, if the interest crediting rate under the plan is a variable rate, the rate of interest used to determine accrued benefits under the plan is equal to the average of the rates of interest used under the plan during the 5-year period ending on the termination date. In addition, under section 411(b)(5)(B)(vi)(II), the plan must provide that, upon plan termination, the interest rate and mortality table used to determine the amount of any benefit under the plan payable in the form of an annuity payable at normal retirement age is the rate and table specified under the plan for this purpose as of the termination date, except that if the interest rate is a variable rate, the rate used is the average of the rates used under the plan during the 5-year period ending on the termination date.

Section 411(b)(5)(C) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) solely because the plan provides offsets against benefits under the plan to the extent the offsets are otherwise allowable in applying the requirements of section 401(a). Section 411(b)(5)(D) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides a disparity in contributions or benefits with respect to which the requirements of section 401(l) (relating to permitted disparity for Social Security benefits and related matters) are met.

Section 411(b)(5)(E) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides for indexing of accrued benefits under the plan. Under section 411(b)(5)(E)(iii), indexing means the periodic adjustment of the accrued benefit by means of the application of a recognized investment index or methodology. Section 411(b)(5)(E)(ii) requires that, except in the case of a variable annuity, the indexing not result in a smaller benefit than the accrued benefit determined without regard to the indexing.

Section 701(a) of PPA '06 added provisions to the Employee Retirement Income Security Act of 1974, Public Law 93–406 (88 Stat. 829 (1974)) (ERISA), that are parallel to sections 411(a)(13) and 411(b)(5) of the Code. The guidance provided in these regulations with respect to the Code also applies for purposes of the parallel amendments to ERISA made by section 701(a) of PPA '06.[1]

Section 701(c) of PPA '06 added provisions to the Age Discrimination in Employment Act of 1967, Public Law 90–202 (81 Stat. 602 (1967)) (ADEA), that are parallel to section 411(b)(5) of the Code. Executive Order 12067 requires all Federal departments and agencies to advise and offer to consult with the Equal Employment Opportunity Commission (EEOC) during the development of any proposed rules, regulations, policies, procedures, or orders concerning equal employment opportunity. The Treasury Department and the IRS have consulted with the EEOC prior to the issuance of these regulations.

Section 701(d) of PPA '06 provides that nothing in the amendments made by section 701 should be construed to create an inference concerning the treatment of applicable defined benefit plans or conver-

[1] Under section 101 of Reorganization Plan No. 4 of 1978 (43 FR 47713), the Secretary of the Treasury has interpretive jurisdiction over the subject matter addressed by these regulations for purposes of ERISA, as well as the Code.

sions of plans into applicable defined benefit plans under section 411(b)(1)(H), or concerning the determination of whether an applicable defined benefit plan fails to meet the requirements of section 411(a)(2), 411(c), or 417(e), as in effect before such amendments, solely because the present value of the accrued benefit (or any portion thereof) of any participant is, under the terms of the plan, equal to the amount expressed as the balance of a hypothetical account or as an accumulated percentage of the participant's final average compensation.

Section 701(e) of PPA '06 sets forth the effective date provisions with respect to amendments made by section 701 of PPA '06. Section 701(e)(1) specifies that the amendments made by section 701 generally apply to periods beginning on or after June 29, 2005. Thus, the age discrimination safe harbors under section 411(b)(5)(A) and section 411(b)(5)(E) are effective for periods beginning on or after June 29, 2005. Section 701(e)(2) provides that the special present value rules of section 411(a)(13)(A) are effective for distributions made after August 17, 2006 (the date PPA '06 was enacted).

Under section 701(e) of PPA '06, the 3-year vesting rule under section 411(a)(13)(B) is generally effective for years beginning after December 31, 2007, for a plan in existence on June 29, 2005, while, pursuant to the amendments made by section 107(c) of WRERA '08, this vesting rule is generally effective for plan years ending on or after June 29, 2005, for a plan not in existence on June 29, 2005. The market rate of return limitation under section 411(b)(5)(B)(i) is generally effective for years beginning after December 31, 2007, for a plan in existence on June 29, 2005, while the limitation is generally effective for periods beginning on or after June 29, 2005, for a plan not in existence on June 29, 2005. Section 701(e)(4) of PPA '06 contains special effective date provisions for collectively bargained plans that modify these effective dates.

Under section 701(e)(5) of PPA '06, as amended by WRERA '08, sections 411(b)(5)(B)(ii), (iii), and (iv) apply to a conversion amendment that is adopted on or after, and takes effect on or after, June 29, 2005.

Under section 701(e)(6) of PPA '06, as added by WRERA '08, the 3-year vesting rule under section 411(a)(13)(B) does not apply to a participant who does not have an hour of service after the date the 3-year vesting rule would otherwise be effective.

Section 702 of PPA '06 provides for regulations to be prescribed by August 16, 2007, addressing the application of rules set forth in section 701 of PPA '06 where the conversion of a defined benefit pension plan into an applicable defined benefit plan is made with respect to a group of employees who become employees by reason of a merger, acquisition, or similar transaction.

Under section 1107 of PPA '06, a plan sponsor is permitted to delay adopting a plan amendment pursuant to statutory provisions under PPA '06 (or pursuant to any regulation issued under PPA '06) until the last day of the first plan year beginning on or after January 1, 2009 (January 1, 2011, in the case of governmental plans). As described in Rev. Proc. 2007–44, 2007–2 C.B 54), this amendment deadline applies to both interim and discretionary amendments that are made pursuant to PPA '06 statutory provisions or any regulation issued under PPA '06. See §601.601(d)(2)(ii)(*b*).

Section 1107 of PPA '06 also permits certain amendments to reduce or eliminate section 411(d)(6) protected benefits. Except to the extent permitted under section 1107 of PPA '06 (or under another statutory provision, including section 411(d)(6) and §§1.411(d)–3 and 1.411(d)–4), section 411(d)(6) prohibits a plan amendment that decreases a participant's accrued benefits or that has the effect of eliminating or reducing an early retirement benefit or retirement-type subsidy, or eliminating an optional form of benefit, with respect to benefits attributable to service before the amendment. However, an amendment that eliminates or decreases benefits that have not yet accrued does not violate section 411(d)(6), provided that the amendment is adopted and effective before the benefits accrue. If section 1107 of PPA '06 applies to an amendment of a plan, section 1107 provides that the plan does not fail to meet the requirements of section 411(d)(6) by reason of such amendment, except as provided by the Secretary of the Treasury.

Proposed regulations (EE–184–86) under sections 411(b)(1)(H) and 411(b)(2) were published by the Treasury Department and the IRS in the **Federal Register** on April 11, 1988 (53 FR 11876), as part of a package of regulations that also included proposed regulations under sections 410(a), 411(a)(2), 411(a)(8), and 411(c) (relating to the maximum age for participation, vesting, normal retirement age, and actuarial adjustments after normal retirement age, respectively).[2]

Notice 96–8, 1996–1 C.B. 359, see §601.601(d)(2)(ii)(*b*), described the application of sections 411 and 417(e) to a single-sum distribution under a cash balance plan where interest credits under the plan are frontloaded (that is, where the right to future interest credits with respect to an employee's hypothetical account balance is not conditioned upon future service and thus accrues at the same time that the benefits attributable to a hypothetical allocation to the account accrue). Under the analysis set forth in Notice 96–8, in order to comply with sections 411(a) and 417(e) in calculating the amount of a single-sum distribution under a cash balance plan, the balance of an employee's hypothetical account must be projected to normal retirement age and converted to an annuity under the terms of the plan, and then the employee must be paid at least the present value of the projected annuity, determined in accordance with section 417(e). Under that analysis, where a cash balance plan provides frontloaded interest credits using an interest rate that is higher than the section 417(e) applicable interest rate, payment of a single-sum distribution equal to the current hypothetical account balance as a complete distribution of the employee's accrued benefit may result in a violation of section 417(e) or a forfeiture in violation of section 411(a). In addition, Notice 96–8 proposed a safe harbor which provided that, if frontloaded interest cred-

[2] On December 11, 2002, the Treasury Department and the IRS issued proposed regulations regarding the age discrimination requirements of section 411(b)(1)(H) that specifically addressed cash balance plans as part of a package of regulations that also addressed section 401(a)(4) nondiscrimination cross-testing rules applicable to cash balance plans (67 FR 76123). The 2002 proposed regulations were intended to replace the 1988 proposed regulations. In Ann. 2003–22, 2003–1 C.B. 846), see §601.601(d)(2)(ii)(*b*), the Treasury Department and the IRS announced the withdrawal of the 2002 proposed regulations under section 401(a)(4), and in Ann. 2004–57, 2004–2 C.B. 15, see §601.601(d)(2)(ii)(*b*), the Treasury Department and the IRS announced the withdrawal of the 2002 proposed regulations relating to age discrimination.

its are provided under a plan at a rate no greater than the sum of identified standard indices and associated margins, no violation of section 411(a) or 417(e) would result if the employee's entire accrued benefit were to be distributed in the form of a single-sum distribution equal to the employee's hypothetical account balance, provided the plan uses appropriate annuity conversion factors. Since the issuance of Notice 96–8, four Federal appellate courts have followed the analysis set out in the Notice: *Esden v. Bank of Boston*, 229 F.3d 154 (2d Cir. 2000), *cert. dismissed*, 531 U.S. 1061 (2001); *West v. AK Steel Corp. Ret. Accumulation Pension Plan*, 484 F.3d 395 (6th Cir. 2007), *cert. denied*, 129 S. Ct. 895 (2009); *Berger v. Xerox Corp. Ret. Income Guarantee Plan*, 338 F.3d 755 (7th Cir. 2003), *reh'g and reh'g en banc denied*, No. 02–3674, 2003 U.S. App. LEXIS 19374 (7th Cir. Sept. 15, 2003); *Lyons v. Georgia-Pacific Salaried Employees Ret. Plan*, 221 F.3d 1235 (11th Cir. 2000), *cert. denied*, 532 U.S. 967 (2001).

Notice 2007–6, 2007–1 C.B. 272, see §601.601(d)(2)(ii)(*b*), provides transitional guidance with respect to certain requirements of sections 411(a)(13) and 411(b)(5) and section 701(b) of PPA '06. Notice 2007–6 includes certain special definitions, including: accumulated benefit, which is defined as a participant's benefit accrued to date under a plan; lump sum-based plan, which is defined as a defined benefit plan under the terms of which the accumulated benefit of a participant is expressed as the balance of a hypothetical account maintained for the participant or as the current value of the accumulated percentage of the participant's final average compensation; and statutory hybrid plan, which is defined as a lump sum-based plan or a plan which has an effect similar to a lump sum-based plan. Notice 2007–6 provides guidance on a number of issues, including a rule under which a plan that provides for indexed benefits described in section 411(b)(5)(E) is a statutory hybrid plan (because it has an effect similar to a lump sum-based plan), unless the plan either solely provides for post-retirement adjustment of the amounts payable to a participant or is a variable annuity plan under which the assumed interest rate used to determine adjustments is at least 5 percent. Notice 2007–6 provides a safe harbor for applying the rules set forth in section 701 of PPA '06 where the conversion of a defined benefit pension plan into an applicable defined benefit plan is made with respect to a group of employees who become employees by reason of a merger, acquisition, or similar transaction. This transitional guidance, along with the other guidance provided in Part III of Notice 2007–6, applies pending the issuance of further guidance and, thus, does not apply for periods to which these final regulations apply.

Proposed regulations (REG–104946–07, 2008–1 C.B. 596) under sections 411(a)(13) and 411(b)(5) (2007 proposed regulations) were published by the Treasury Department and the IRS in the **Federal Register** on December 28, 2007 (72 FR 73680). The Treasury Department and the IRS received written comments on the 2007 proposed regulations and a public hearing was held on June 6, 2008.

Announcement 2009–82, 2009–48 I.R.B. 720 and Notice 2009–97, 2009–52 I.R.B. 972, see §601.601(d)(2)(ii)(*b*), announced certain expected relief with respect to the requirements of section 411(b)(5). In particular, Announcement 2009–82 stated that the rules in the regulations specifying permissible market rates of return are not expected to go into effect before the first plan year that begins on or after January 1, 2011. In addition, Notice 2009–97 stated that, once final regulations under sections 411(a)(13) and 411(b)(5) are issued, it is expected that relief from the requirements of section 411(d)(6) will be granted for a plan amendment that eliminates or reduces a section 411(d)(6) protected benefit, provided that the amendment is adopted by the last day of the first plan year that begins on or after January 1, 2010, and the elimination or reduction is made only to the extent necessary to enable the plan to meet the requirements of section 411(b)(5).[3] Notice 2009–97 also extended the deadline for amending cash balance and other applicable defined benefit plans, within the meaning of section 411(a)(13)(C), to meet the requirements of section 411(a)(13) (other than section 411(a)(13)(A)) and section 411(b)(5), relating to vesting and other special rules applicable to these plans. Under Notice 2009–97, the deadline for these amendments is the last day of the first plan year that begins on or after January 1, 2010.

After consideration of the comments received in response to the 2007 proposed regulations, these final regulations generally adopt the provisions of the 2007 proposed regulations with certain modifications as described under the heading "Explanation of Provisions." In addition, the Treasury Department and the IRS are issuing proposed regulations (2010 proposed regulations) that address certain issues under sections 411(a)(13) and 411(b)(5) that have not been addressed in these final regulations (and that are generally indicated as "RESERVED" in these final regulations), and that also address a related issue under section 411(b)(1). The 2010 proposed regulations are being issued at the same time as these final regulations.

Explanation of Provisions

Overview

In general, these final regulations incorporate the transitional guidance provided under Notice 2007–6 as well as the provisions of the 2007 proposed regulations. The regulations adopt the terminology used in the proposed regulations (such as "statutory hybrid benefit formula" and "lump sum-based benefit formula") to take into account situations where plans provide more than one benefit formula. These regulations also provide additional guidance with respect to sections 411(a)(13) and 411(b)(5), taking into account comments received in response to the 2007 proposed regulations and also reflecting the enactment of WRERA '08.

I. *Section 411(a)(13): Applicable definitions, relief of section 411(a)(13)(A), and special vesting rules for applicable defined benefit plans*

A. *Definitions*

The regulations under section 411(a)(13) contain certain definitions that apply both for purposes of the regulations

[3] However, see footnote 6 in the preamble to the 2010 proposed regulations described in the next paragraph.

under section 411(a)(13) and the regulations under section 411(b)(5). Section 411(b)(5)(G) provides that, for purposes of section 411(b)(5), any reference to the accrued benefit means the benefit accrued to date. The final regulations refer to this as the "accumulated benefit", which is distinct from the participant's accrued benefit under section 411(a)(7) (an annuity beginning at normal retirement age that is actuarially equivalent to the participant's accumulated benefit). As in the 2007 proposed regulations, the regulations use the term "statutory hybrid plan" to refer to an applicable defined benefit plan described in section 411(a)(13)(C). Under the regulations, a statutory hybrid plan is a defined benefit plan that contains a statutory hybrid benefit formula, and a "statutory hybrid benefit formula" is a benefit formula that is either a lump sum-based benefit formula or a formula that has an effect similar to a lump sum-based benefit formula.

The regulations define a "lump sum-based benefit formula" as a benefit formula used to determine all or any part of a participant's accumulated benefit under which the accumulated benefit provided under the formula is expressed as the current balance of a hypothetical account maintained for the participant or as the current value of the accumulated percentage of the participant's final average compensation. The final regulations adopt the rules of the 2007 proposed regulations whereby the determination as to whether a benefit formula is a lump sum-based benefit formula is made based on how the accumulated benefit of a participant is expressed under the terms of the plan, and does not depend on whether the plan provides an optional form of benefit in the form of a single-sum payment. Similarly, a formula does not fail to be a lump sum-based benefit formula merely because the plan's terms state that the participant's accrued benefit is an annuity at normal retirement age that is actuarially equivalent to the balance of a hypothetical account maintained for the participant.

The preamble to the 2007 proposed regulations asked for comments on plan formulas that calculate benefits as the current value of an accumulated percentage of the participant's final average compensation (often referred to as "pension equity plans" or "PEPs"). Commenters indicated that some of these plans never credit interest, directly or indirectly, some explicitly credit interest after cessation of PEP accruals, and some do not credit interest explicitly but provide for specific amounts to be payable after cessation of accruals (both immediately and at future dates) based on actuarial equivalence using specified actuarial factors applied after cessation of accruals.

In response to these comments, the final regulations clarify that a benefit formula is expressed as the balance of a hypothetical account maintained for the participant if it is expressed as a current single-sum dollar amount. A lump sum-based benefit formula that credits interest is subject to the market rate of return rules, so that in any case in which a PEP formula provides for interest credits after cessation of PEP accruals, the interest credits are subject to the market rate of return rules.

The 2007 proposed regulations contained a rule whereby a benefit formula would not have been treated as a lump sum-based benefit formula with respect to a participant merely because the participant is entitled to a benefit that is not less than the benefit properly attributable to after-tax employee contributions. In response to comments received that this rule be broadened, the final regulations provide that the benefit properly attributable to after-tax employee contributions, rollover contributions, and other similar employee contributions is disregarded when determining whether a benefit formula is a lump sum-based benefit formula with respect to a participant. Thus, for example, a plan is not a statutory hybrid plan with a lump sum-based benefit formula with respect to a participant merely because the plan provides that the participant's benefit is equal to the sum-of or greater-of the benefit properly attributable to employee contributions and the benefit under a traditional defined benefit formula.

The regulations provide that a benefit is not properly attributable to employee contributions if such contributions are credited with interest at a rate that exceeds a reasonable rate of interest or if the conversion factors used to calculate the benefit based on such employee contributions are not actuarially reasonable. The regulations clarify that section 411(c) merely provides an example of an acceptable methodology for purposes of determining the benefit that is properly attributable to employee contributions.

The 2007 proposed regulations provided that a benefit formula under a defined benefit plan has an effect similar to a lump sum-based benefit formula if the formula provides that a participant's accumulated benefit payable at normal retirement age (or at benefit commencement, if later) is expressed as a benefit that includes periodic adjustments (including a formula that provides for indexed benefits described in section 411(b)(5)(E)) that are reasonably expected to result in a smaller annual benefit at normal retirement age (or at benefit commencement, if later) for the participant, when compared to a similarly situated, younger individual who is or could be a participant in the plan. A number of commenters suggested that the rule in the 2007 proposed regulations was too broad generally and also suggested that certain types of plans, such as plans described in section 411(b)(5)(E), be exempted entirely. However, the Treasury Department and the IRS believe that a key purpose of sections 411(a)(13) and 411(b)(5) is to address defined benefit plan formulas where younger participants receive a larger annual benefit at normal retirement age when compared to similarly situated, older participants. Therefore, the final regulations do not significantly narrow the definition of a benefit formula that has an effect similar to a lump sum-based benefit formula.

The regulations clarify that a benefit formula under a defined benefit plan has an effect similar to a lump sum-based benefit formula if the formula provides that a participant's accumulated benefit is expressed as a benefit that includes adjustments (including a formula that provides for indexed benefits described in section 411(b)(5)(E)) for a future period and the total dollar amount of the adjustments is reasonably expected to be smaller for the participant, when compared to a similarly situated, younger individual who is or could be a participant in the plan. Thus, a formula that provides that a participant's accumulated benefit is expressed as a benefit that includes the right to periodic adjustments is treated as having an effect similar to a lump sum-based benefit formula based on a comparison of the expected total dollar amount of the adjustments through benefit commencement, rather than the expected total accumulated benefit after application of these adjustments.

As in the 2007 proposed regulations, the regulations provide that a benefit formula under a plan has an effect similar to a lump sum-based benefit formula where the right to future adjustments accrues at the same time as the benefit that is subject to those adjustments. In addition, the regulations provide that a benefit formula that does not include adjustments is nevertheless treated as a formula with an effect similar to a lump sum-based benefit formula where benefits are adjusted pursuant to a pattern of repeated plan amendments and the total dollar amount of those adjustments is reasonably expected to be smaller for the participant than for any similarly situated, younger individual who is or could be a participant. See §1.411(d)–4, A–1(c)(1).

Like the 2007 proposed regulations, the regulations provide that certain benefits are disregarded when determining whether a benefit formula has an effect similar to a lump sum-based benefit formula. For example, the regulations provide that, for purposes of determining whether a benefit formula has an effect similar to a lump sum-based benefit formula, indexing that applies to adjust benefits after the annuity starting date (for example, cost-of-living increases) is disregarded. In addition, benefits properly attributable to certain employee contributions that are disregarded for purposes of determining whether a participant is treated as having a lump-sum based benefit formula are also disregarded for purposes of determining whether a formula has an effect similar to a lump sum-based benefit formula.

The regulations include an example that illustrates that a defined benefit formula is not treated as a statutory hybrid benefit formula merely because the formula provides for actuarial increases after normal retirement age. This is because actuarial increases after normal retirement age do not provide smaller adjustments for older participants when compared to similarly situated, younger participants.

The 2007 proposed regulations provided that variable annuity benefit formulas with assumed interest rates (sometimes referred to as "hurdle rates") of at least 5 percent are not treated as having an effect similar to a lump sum-based benefit formula. A number of commenters requested that the regulations extend this rule to variable annuity plans with lower hurdle rates. However, plans with lower hurdle rates are more likely to provide positive adjustments for future periods than plans with higher hurdle rates and, as a result, younger participants are more likely to receive a meaningfully larger total dollar amount of adjustments than older participants under these plans. The Treasury Department and the IRS are concerned that exempting these plans would mean that participants would lose the protections afforded to participants in statutory hybrid plans (including 3-year vesting and conversion protection). Therefore, the final regulations retain the rule whereby adjustments under a variable annuity do not have an effect similar to a lump sum-based benefit formula if the assumed interest rate used to determine the adjustments is 5 percent or higher. Such an annuity does not have an effect similar to a lump sum-based benefit formula even if post-annuity starting date adjustments are made using a specified assumed interest rate that is less than 5 percent.

B. *Relief under section 411(a)(13)(A)*

The regulations reflect new section 411(a)(13)(A) by providing that a statutory hybrid plan is not treated as failing to meet the requirements of section 411(a)(2), or, with respect to the participant's accrued benefit derived from employer contributions, the requirements of sections 411(a)(11), 411(c), or 417(e), merely because the plan provides that the present value of benefits as determined under a lump sum-based benefit formula is equal to the then-current balance of the hypothetical account maintained for the participant or the then-current value of the accumulated percentage of the participant's final average compensation under that formula. However, section 411(a)(13) does not alter the definition of the accrued benefit under section 411(a)(7)(A) (which generally defines the participant's accrued benefit as the annual benefit commencing at normal retirement age), nor does it alter the definition of the normal retirement benefit under section 411(a)(9) (which generally defines the participant's normal retirement benefit as the benefit under the plan commencing at normal retirement age).

Section 411(a)(13)(A) applies only with respect to a benefit provided under a lump sum-based benefit formula. A statutory hybrid plan that provides benefits under a benefit formula that is a statutory hybrid benefit formula other than a lump sum-based benefit formula (such as a plan that provides for indexing as described in section 411(b)(5)(E)) must comply with the present value rules of section 417(e) with respect to an optional form of benefit that is subject to the requirements of section 417(e).

The regulations do not provide guidance as to how section 411(a)(13)(A) applies with respect to payments that are not made in the form of a single-sum distribution of the hypothetical account balance or accumulated percentage of final average compensation, such as payments made in the form of an annuity. That issue is being addressed in the 2010 proposed regulations.

C. *Special vesting rules for applicable defined benefit plans*

Pursuant to section 411(a)(13)(B), the regulations provide that, in the case of a participant whose accrued benefit (or any portion thereof) under a defined benefit plan is determined under a statutory hybrid benefit formula, the plan is treated as failing to satisfy the requirements of section 411(a)(2) unless the plan provides that the participant has a nonforfeitable right to 100 percent of the participant's accrued benefit derived from employer contributions if the participant has 3 or more years of service. As in the 2007 proposed regulations, the final regulations provide that this requirement applies on a participant-by-participant basis and applies to the participant's entire benefit derived from employer contributions under a statutory hybrid plan (not just the portion of the participant's benefit that is determined under a statutory hybrid benefit formula). Furthermore, the regulations retain the rule under which, if a participant is entitled to the greater of two (or more) benefit amounts under a plan, where each amount is determined under a different benefit formula (including a benefit determined pursuant to an offset among formulas within the plan or a benefit determined as the greater of a protected benefit under section 411(d)(6) and another benefit amount), at least one of which is a benefit calculated under a statutory hybrid benefit formula, the 3-year vesting requirement applies to that participant's entire accrued benefit under the plan even if the participant's benefit under the statutory hybrid benefit formula is ultimately smaller than under the other formula.

The 2007 proposed regulations requested comments regarding the application of the 3-year vesting requirement to a floor plan that is not a statutory hybrid plan but that is part of a floor-offset arrangement with an independent plan that is a statutory hybrid plan. A number of commenters suggested that the 3-year vesting requirement should apply on a plan-by-plan basis, without regard to whether a plan is part of a floor-offset arrangement. In contrast, one commenter suggested that the 3-year vesting requirement should apply to both plans that are part of a floor-offset arrangement even if only one of the plans is a statutory hybrid plan, because the commenter felt that determining the amount of the offset in an arrangement involving plans with different vesting schedules would be inherently difficult. However, this concern is mitigated because, in the view of the Treasury Department and the IRS, a floor-offset arrangement where the benefit payable under a floor plan is reduced by the benefit payable under an independent plan is only permissible if the arrangement limits the offset to amounts that are vested under the independent plan.[4] Therefore, the regulations retain the rule whereby the 3-year vesting requirement is limited to plans that contain a statutory hybrid benefit formula and provide an example illustrating this rule with respect to a floor-offset arrangement where the benefit payable under a floor plan that does not include a statutory hybrid benefit formula is reduced by the vested accrued benefit payable under an independent plan that includes a statutory hybrid benefit formula.

II. *Section 411(b)(5): Safe harbor for age discrimination, conversion protection, and market rate of return limitation*

A. *Safe harbor for age discrimination*

The regulations reflect new section 411(b)(5)(A), which provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) with respect to certain benefit formulas if, as determined as of any date, a participant's accumulated benefit expressed under one of those formulas would not be less than any similarly situated, younger participant's accumulated benefit expressed under the same formula. A plan that does not satisfy this test is required to satisfy the general age discrimination rule of section 411(b)(1)(H)(i).

As in the 2007 proposed regulations, the regulations provide that the safe harbor standard under section 411(b)(5)(A) is available only where a participant's accumulated benefit under the terms of the plan is expressed as an annuity payable at normal retirement age (or current age, if later), the current balance of a hypothetical account, or the current value of the accumulated percentage of the employee's final average compensation. For this purpose, if the accumulated benefit of a participant is expressed as an annuity payable at normal retirement age (or current age, if later) under the plan terms, then the comparison of benefits is made using such an annuity. Similarly, if the accumulated benefit of a participant is expressed under the plan terms as the current balance of a hypothetical account or the current value of an accumulated percentage of the participant's final average compensation, then the comparison of benefits is made using the current balance of a hypothetical account or the current value of the accumulated percentage of the participant's final average compensation, respectively.

The regulations require a comparison of the accumulated benefit of each possible participant in the plan to the accumulated benefit of each other similarly situated, younger individual who is or could be a participant in the plan. For this purpose, as in the 2007 proposed regulations, the regulations provide that an individual is similarly situated to another individual if the individual is identical to that other individual in every respect that is relevant in determining a participant's benefit under the plan (including, but not limited to, period of service, compensation, position, date of hire, work history, and any other respect) except for age. In determining whether an individual is similarly situated to another individual, any characteristic that is relevant for determining benefits under the plan and that is based directly or indirectly on age is disregarded. For example, if a particular benefit formula applies to a participant on account of the participant's age, an individual to whom the benefit formula does not apply and who is identical to a participant in all respects other than age is similarly situated to the participant. By contrast, an individual is not similarly situated to a participant if a different benefit formula applies to the individual and the application of the different formula is based neither directly nor indirectly on age. For example, if the benefit formula under a plan is changed from one type to another for employees hired after the effective date of the change, employees hired after the relevant date would not be similarly situated with employees hired before that date because the benefit formula for new hires is not based directly nor indirectly on age.

The comparison of accumulated benefits is made without regard to any subsidized portion of any early retirement benefit that is included in a participant's accumulated benefit. For this purpose, the subsidized portion of an early retirement benefit is the retirement-type subsidy within the meaning of §1.411(d)–3(g)(6) that is contingent on a participant's severance from employment and commencement of benefits before normal retirement age.

In addition, like the 2007 proposed regulations, the regulations provide that the safe harbor is generally not available with respect to a participant if the benefit of any similarly situated, younger individual is expressed in a different form than the participant's benefit. Thus, for example, the safe harbor is not available for comparing the accumulated benefit of a participant expressed as an annuity at normal retirement age with the accumulated benefit of a similarly situated, younger participant

[4] See Rev. Rul. 76–259, 1976–2 C.B. 111, see §601.601(d)(2)(ii)(*b*).

expressed as the current balance of a hypothetical account.

Like the 2007 proposed regulations, the regulations generally permit a plan that provides the sum-of or the greater-of benefits that are expressed in two or more different forms of benefit to satisfy the safe harbor if the plan would separately satisfy the safe harbor for each separate form of benefit. For purposes of the safe harbor comparisons involving greater-of and sum-of benefit formulas, the 2007 proposed regulations contained a rule where a similarly situated, younger participant would be treated as having an accumulated benefit of zero under a benefit formula that does not apply to the participant. While the sum-of and greater-of provisions are organized differently in these regulations, the regulations effectively retain this rule because sum-of and greater-of formulas are eligible for the safe harbor even where older participants receive benefits expressed in a different form than the benefits of similarly situated, younger participants, as long as younger participants are not entitled to benefits expressed in a different form than the benefits of similarly situated, older participants.

Several commenters requested that the regulations clarify that the safe harbor is also available to plans that allow older participants to choose, at the time a new statutory hybrid benefit formula goes into effect, whether to receive a benefit under the statutory hybrid benefit formula or under the pre-existing traditional defined benefit formula. In response to such comments, the regulations adopt similar rules as the sum-of and greater-of rules for plans that provide participants with the choice of benefits that are expressed in two or more different forms.

As part of the sum-of, greater-of, and choice-of rules, the regulations reflect the fact that the sum of benefits expressed in two or more forms is never less than the greater of the same benefits and that the greater of benefits expressed in two or more forms is never less than the choice of the same benefits. As a result, the regulations provide that in order for the safe harbor to be available with respect to a participant who is provided with the greater of benefits expressed in two or more different forms, the plan must not provide any similarly situated, younger participant with the sum of the same benefits. Similarly, the regulations provide that in order for the safe harbor to be available with respect to a participant who is provided with the choice of benefits expressed in two or more different forms, the plan must not provide any similarly situated, younger participant with either the sum of or the greater of the same benefits. In addition, in order for the safe harbor to be available, the plan cannot provide for any other relationship between benefits expressed in different forms other than sum-of, greater-of, or choice-of benefits.

The regulations reflect new section 411(b)(5)(C), which provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides offsets of benefits under the plan to the extent such offsets are allowable in applying the requirements under section 401 and the applicable requirements of ERISA and ADEA. The regulations incorporate the provisions of section 411(b)(5)(D) (relating to permitted disparity under section 401(l)) without providing additional guidance. These rules are unchanged from the 2007 proposed regulations.

The regulations contain a number of new examples that illustrate the application of the safe harbor under various fact patterns. One of these examples illustrates that the safe harbor is not satisfied in the case of a plan that contains a suspension of benefits provision that reduces or eliminates interest credits for participants who continue in service after normal retirement age.

The regulations also reflect new section 411(b)(5)(E), which provides for the disregard of certain indexing of benefits for purposes of the age discrimination rules of section 411(b)(1)(H). As in the 2007 proposed regulations, the regulations limit the disregard of indexing to formulas under defined benefit plans other than lump sum-based formulas. In addition, the regulations clarify that the disregard of indexing is limited to situations in which the extent of the indexing for a participant would not be less than the indexing applicable to a similarly situated, younger participant. Thus, the disregard of indexing is only available if the indexing is neither terminated nor reduced on account of the attainment of any age.

Section 411(b)(5)(E) requires that the indexing be accomplished by application of a recognized investment index or methodology. The 2007 proposed regulations limited a recognized investment index or methodology to an eligible cost-of-living index as described in §1.401(a)(9)–6, A–14(b), the rate of return on the aggregate assets of the plan, or the rate of return on the annuity contract for the employee issued by an insurance company licensed under the laws of a State. The final regulations expand the list of what constitutes a recognized index or methodology by treating any rate of return that satisfies the market rate of return rules under these regulations as a recognized index or methodology.

As under the 2007 proposed regulations, the section 411(b)(5)(E)(ii) protection against loss ("no-loss") requirement for an indexed plan (which requires that the indexing not result in a smaller accrued benefit than if no indexing had applied) is implemented under the final regulations by applying the "preservation of capital" rule of section 411(b)(5)(B)(i)(II) to indexed plans. (The preservation of capital rule is discussed in section II. C. of this preamble.) The final regulations clarify that variable annuity benefit formulas (as defined in the regulations) are exempt from the no-loss and preservation of capital rules.

B. *Conversion protection*

The regulations provide guidance on the new conversion protections under section 411(b)(5)(B)(ii), (iii), and (iv) which is similar to the 2007 proposed regulations. Under the regulations, a participant whose benefits are affected by a conversion amendment that was both adopted and effective on or after June 29, 2005, must generally be provided with a benefit after the conversion that is at least equal to the sum of the benefits accrued through the date of the conversion and benefits earned after the conversion, with no permitted interaction between these two portions. This assures participants that there will be no "wear-away" as a result of a conversion, both with respect to the participant's accrued benefits and any early retirement subsidy to which the participant is entitled based on the pre-conversion benefits.

The 2007 proposed regulations included an alternative mechanism under which a plan could provide for the establishment of an opening hypothetical account balance or opening accumulated percentage of the participant's final average compensation as part of the conversion and keep separate track of (1) the benefit attributable to the opening hypothetical account balance (including interest credits attributable thereto) or attributable to the opening accumulated percentage of the participant's final average compensation and (2) the benefit attributable to post-conversion service under the post-conversion benefit formula. Comments on this rule were favorable and it is retained under the final regulations. A variety of examples illustrating application of the alternative are included in the regulations. Under this alternative, when a participant commences benefits, it must be determined whether the benefit attributable to the opening hypothetical account or attributable to the opening accumulated percentage that is payable in the particular optional form of benefit selected is greater than or equal to the benefit accrued under the plan prior to the date of conversion and that was payable in the same generalized optional form of benefit (within the meaning of §1.411(d)–3(g)(8)) at the same annuity starting date. If the benefit attributable to the opening hypothetical account balance or opening accumulated percentage is greater, then the plan must provide that such benefit is paid in lieu of the pre-conversion benefit, in addition to the benefit attributable to post-conversion service under the post-conversion benefit formula. If the benefit attributable to the opening hypothetical account balance or opening accumulated percentage is less, then the plan must provide that such benefit will be increased sufficiently to provide the pre-conversion benefit, in addition to the benefit attributable to post-conversion service under the post-conversion benefit formula.

As in the 2007 proposed regulations, the final regulations provide under this alternative that, if an optional form of benefit is available on the annuity starting date with respect to the benefit attributable to the opening hypothetical account balance or opening accumulated percentage, but no optional form (such as a single-sum distribution) within the same generalized optional form of benefit was available at that annuity starting date under the terms of a plan as in effect immediately prior to the effective date of the conversion amendment, then the comparison must still be made by assuming that the pre-conversion plan had such an optional form of benefit.

The preamble to the 2007 proposed regulations asked for comments on another alternative means of satisfying the conversion requirements that would involve establishing an opening hypothetical account balance, but would not require a comparison of benefits at the annuity starting date if certain requirements are met. Comments on this alternative were favorable, but some commenters requested that the alternative only be available where there was sufficient protection to ensure that participants' benefits would not be less than would apply under the rules in the 2007 proposed regulations. While these final regulations do not permit this additional alternative, it is included in the 2010 proposed regulations.

The regulations also provide guidance that is unchanged from the 2007 proposed regulations on what constitutes a conversion amendment under section 411(b)(5)(B)(v). Under the final regulations, whether an amendment is a conversion amendment is determined on a participant-by-participant basis. The regulations provide that an amendment (including multiple amendments) is a conversion amendment with respect to a participant if it meets two criteria: (1) the amendment reduces or eliminates the benefits that, but for the amendment, the participant would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula and under which the participant was accruing benefits prior to the amendment; and (2) after the effective date of the amendment, all or a portion of the participant's benefit accruals under the plan are determined under a statutory hybrid benefit formula.

The regulations clarify that only amendments that reduce or eliminate accrued benefits described in section 411(a)(7), or retirement-type subsidies described in section 411(d)(6)(B)(i), that would otherwise accrue as a result of future service are treated as amendments that reduce or eliminate the participant's benefits that would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula. As under the 2007 proposed regulations, a plan is treated as having been amended for this purpose if, under the terms of the plan, a change in the conditions of a participant's employment results in a reduction or elimination of the benefits that the participant would have accrued in the future under a benefit formula that is not a statutory hybrid benefit formula (for example, a job transfer from an operating division covered by a non-statutory hybrid defined benefit plan to an operating division that is covered by a formula expressed as the balance of a hypothetical account). However, in the absence of coordination between the formulas, the special requirements for conversion amendments typically will be satisfied automatically.

A number of commenters recommended that the effective date of a conversion amendment generally be the date accruals begin under a statutory hybrid benefit formula, rather than the date that future accruals are reduced under the non-statutory hybrid benefit formula. Several commenters suggested that, if this recommendation was not implemented generally, it should nevertheless apply at the effective date of an amendment which provides participants with the greater of benefits under the prior formula and a statutory hybrid benefit formula for a period of time before benefit accruals cease under the prior formula, especially if the amendment applies to a subgroup of existing older, long service employees. However, some comments expressed concern that such a change in the proposed definition of the effective date of a conversion amendment would allow plans to delay the statutory anti-wearaway protections by adding a less valuable cash balance benefit for the grandfathered group at a date, even though "the effect of converting" (within the meaning of section 411(b)(5)(B)(v)(I)) their traditional benefit into a cash balance benefit would occur for them at the later date when their benefit accruals cease under the prior formula.

The Treasury Department and the IRS are concerned that the requested change in the proposed rule would circumvent a key purpose behind the conversion protection requirements by allowing for a delayed wear-away that would occur at the time accruals cease under the prior formula. For example, if a plan were generally converted to a cash balance plan, but the plan were to provide for some class of participants, such as participants who are age 55 or older, to receive the greater of accruals under the prior formula or the new cash balance formula for a period of 5 years, the change requested in the comments would define the effective date of the conversion amendment for all participants to be the date the cash balance formula went into effect (rather than applying a participant by participant rule). As a result, 5 years after the cash balance formula went into effect, the hypothetical account balance for these older participants could provide benefits that are less than the frozen amount under the prior formula, a circumstance that would produce no additional accruals for some period of time after the end of the 5-year period. Therefore, the approach suggested by these comments would allow the type of wear-away the statute was intended to prevent. Accordingly, like the 2007 proposed regulations, the regulations adopt a rule whereby the effective date of a conversion amendment is, with respect to a participant, the date as of which the reduction occurs in the benefits that the participant would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula. In accordance with section 411(d)(6), the regulations provide that the date future benefit accruals are reduced cannot be earlier than the date of adoption of the conversion amendment.

The regulations provide rules, similar to those in the 2007 proposed regulations, prohibiting the avoidance of the conversion protections through the use of multiple plans or multiple employers. Under these rules, an employer is treated as having adopted a conversion amendment if the employer adopts an amendment under which a participant's benefits under a plan that is not a statutory hybrid plan are coordinated with a separate plan that is a statutory hybrid plan, such as through a reduction (offset) of the benefit under the plan that is not a statutory hybrid plan. In addition, if an employee's employer changes as a result of a merger, acquisition, or other transaction described in §1.410(b)–2(f), then the employee's old and new employers would be treated as a single employer for this purpose. Thus, for example, in an acquisition, if the buyer adopts an amendment to its statutory hybrid plan under which a participant's benefits under the seller's plan (that is not a statutory hybrid plan) are coordinated with benefits under the buyer's plan, such as through a reduction (offset) of the buyer's plan benefits, the seller and buyer would be treated as a single employer and as having adopted a conversion amendment. However, if there is no coordination between the plans, there is no conversion amendment.

The regulations retain the rule from the 2007 proposed regulations under which a conversion amendment also includes multiple amendments that result in a conversion amendment, even if the amendments would not be conversion amendments individually. If an amendment to provide a benefit under a statutory hybrid benefit formula is adopted within 3 years after adoption of an amendment to reduce benefits under a non-statutory hybrid benefit formula, then those amendments would be consolidated in determining whether a conversion amendment has been adopted. In the case of an amendment to provide a benefit under a statutory hybrid benefit formula that is adopted more than 3 years after adoption of an amendment to reduce non-statutory hybrid benefit formula benefits, there is a presumption that the amendments are not consolidated unless the facts and circumstances indicate that adoption of an amendment to provide a benefit under a statutory hybrid benefit formula was intended at the time of the reduction in the non-statutory hybrid benefit formula benefits.

A number of commenters expressed concern that the interaction between employee transfers and the conversion protection effective date provisions was unclear under the 2007 proposed regulations. In response to such comments, the regulations clarify that a conversion amendment must be both adopted on or after June 29, 2005, and be effective on or after June 29, 2005, in order for the conversion protection provisions to apply to such amendment. Therefore, if a transfer provision was adopted before June 29, 2005, an employee transfer is not treated as part of a conversion amendment to which the conversion protection provisions apply, even if the transfer occurs on or after June 29, 2005.

C. *Market rate of return limitation*

The regulations reflect the rule in section 411(b)(5)(B)(i)(I) under which a statutory hybrid plan is treated as failing to satisfy section 411(b)(1)(H) if it provides an interest crediting rate with respect to benefits determined under a statutory hybrid benefit formula that is in excess of a market rate of return. Several commenters suggested that the definition of interest crediting rate in the 2007 proposed regulations be revised to exclude not only adjustments conditioned on current service but also adjustments made as a result of past and imputed service as well as ad hoc adjustments. In response to the comments, the regulations expand the exclusions from the definition of interest credit to also exclude adjustments made as a result of imputed service, as well as certain one-time adjustments.

The final regulations provide that an interest credit generally means any increase or decrease for a period to a participant's accumulated benefit under a statutory hybrid benefit formula, under the terms of the plan at the beginning of the period, that is calculated by applying a rate of interest or rate of return (including a rate of increase or decrease under an index) to the participant's accumulated benefit (or a portion thereof) as of the beginning of the period, to the extent the increase or decrease is not conditioned on current service and is not made on account of imputed service; as well as any other increase for a period to a participant's accumulated benefit under a statutory hybrid benefit formula, under the terms of the plan at the beginning of the period, to the extent the increase is not conditioned on current service and is not made on account of imputed service.

Under the regulations, notwithstanding the general rule described in the previous paragraph, an increase to a participant's accumulated benefit is not treated as an interest credit to the extent the increase is made as a result of a plan amendment providing for a one-time adjustment to the participant's accumulated benefit. However, a pattern of repeated plan amendments each of which provides for a one-time adjustment to a participant's accumulated benefit will cause such adjustments to be treated as provided on a permanent basis under the terms of the plan.

The interest crediting rate for a period with respect to a participant generally equals the total amount of interest credits for the period divided by the participant's accumulated benefit at the beginning of the period.

Under the regulations, a principal credit means any increase to a participant's accumulated benefit under a statutory hybrid benefit formula that is not an interest credit. As a result, a principal credit includes an increase to a participant's accumulated benefit to the extent the increase is conditioned on current service or made on account of imputed service. Thus, for example, even if the plan denominates an increase to a hypothetical account balance as an interest credit, the increase is treated as a principal credit to the extent the increase is conditioned on current service. Similarly, a principal credit includes an increase to the current value of an accumulated percentage of the participant's final average compensation. For indexed benefits, a principal credit includes an increase to the participant's accrued benefit other than an increase provided by indexing. In addition, pursuant to the rule set forth earlier, a principal credit generally includes an increase to a participant's accumulated benefit to the extent the increase is made as a result of a plan amendment providing for a one-time adjustment to the participant's accumulated benefit. Thus, for example, a principal credit includes an opening hypothetical account balance or opening accumulated percentage of the participant's final average compensation.

Consistent with the requirement under §1.401–1(b)(1)(i) that a pension plan provide definitely determinable benefits, a plan that credits interest must specify how the plan determines interest credits and must specify how and when interest credits are credited. Under the regulations, a plan must determine the plan's interest crediting rate that will apply for each plan year (or portion of a plan year) using one of two permitted methods — either using the applicable periodic interest crediting rate that applies over the current period or, for certain rates, using the rate that applied in a specified lookback month with respect to a stability period. For this purpose, the plan's lookback month and stability period must satisfy the rules for selecting the lookback month and stability period under §1.417(e)–1(d)(4). However, the stability period and lookback month need not be the same as those used under the plan for purposes of section 417(e)(3).

In addition, the regulations require interest credits under a plan to be provided on an annual or more frequent periodic basis and also require interest credits for each period to be credited as of the end of the period. If, under a plan, interest is credited more frequently than annually (for example, daily, monthly or quarterly) based on one of the permissible annual interest rates, then the plan does not provide an above market rate of return if the periodic interest credits are provided under an interest crediting rate that is no greater than a *pro rata* portion of the applicable annual interest crediting rate. However, the regulations provide a special rule whereby a plan that credits interest daily based on one of these annual rates may credit interest at a rate which is 1/360$^{\text{th}}$ of the applicable annual rate (instead of 1/365$^{\text{th}}$) without violating the general rule of the preceding sentence. In addition, the regulations provide that interest credits based on one of these annual rates are not treated as creating an effective rate of return in excess of a market rate of return merely because an otherwise permissible interest crediting rate for a plan year is compounded more frequently than annually. Thus, for example, if a plan's terms provide for interest to be credited monthly and for the interest crediting rate to be equal to the interest rate on long-term investment grade corporate bonds and the applicable annual rate on these bonds for the plan year is 6 percent, then the accumulated benefit at the beginning of each month could be increased as a result of interest credits by as much as 0.5 percent per month during the plan year without resulting in an interest crediting rate that is in excess of a market rate of return. These rules are similar to those in the 2007 proposed regulations.

The 2007 proposed regulations provided that an interest crediting rate is not in excess of a market rate of return if it is always less than a particular interest crediting rate that meets the market rate of return limitation. A number of commenters suggested that this rule be revised to clarify that rates that may sometimes equal but are never greater than another permissible rate are also permissible. In response to these comments, the final regulations provide that an interest crediting rate is not in excess of a market rate of return if it can never be in excess of a particular rate that meets the market rate of return limitation. Thus, a rate that is a percentage (no greater than 100 percent) of a particular rate that meets the market rate of return limitation is not in excess of a market rate of return and a rate that is a fixed amount less than a particular rate that meets the market rate of return limitation is also not in excess of a market rate of return. Similarly, an interest crediting rate is not in excess of a market rate of return if it always equals the lesser of two or more rates where at least one of the rates meets the market rate of return limitation.

In addition, the regulations clarify that a statutory hybrid plan does not provide an effective interest crediting rate that is in excess of a market rate of return merely because the plan determines an interest credit by applying different rates to different predetermined portions of the accumulated benefit, provided each rate would separately satisfy the market rate of return limitations if the rate applied to the entire accumulated benefit. Thus, under this rule, statutory hybrid plans may, in effect, provide participants with rates that are a blend of two or more rates and may also apply different rates to portions of the benefit attributable to different principal credits. However, as in the 2007 proposed regulations, the final regulations provide that interest credits that are determined by applying the greater of two or more rates generally exceed a market rate of return except under certain limited circumstances.

The regulations provide that an interest crediting rate for a plan year is not in excess of a market rate of return if it is based on the rate of interest provided under one of several specified indices. Like the 2007 proposed regulations, these rates include the rate of interest on long-term investment grade corporate bonds (as described in section 412(b)(5)(B)(ii)(II) prior to amendment by PPA '06 for plan years beginning before January 1, 2008, and the third segment rate used under section 430(h) for subsequent plan years), the interest rate on 30-year Treasury securities, the interest rates on shorter term Treasuries with the associated margins that were safe harbor rates described in Notice 96–8, as well as certain cost-of-living indices. Several commenters on the 2007 proposed regulations suggested that this list be expanded to also include all of the interest rates permissible under section 417(e). The Treasury Department and the IRS agree with this suggestion and, as a result, the regulations expand the list of safe-harbor rates to include the first and second segment rates, as defined in either section 417(e) or 430(h) and whether calculated with or without regard to the transition rules of section 417(e)(3) or 430(h)(2)(G).

The regulations provide that an interest crediting rate based on a specified index must be adjusted on at least an annual basis. These rates are market yields to maturity on outstanding bonds and, as a result, these rates do not reflect defaults nor do these rates reflect the change in the market value of an outstanding bond as a result of future changes in the interest rate environment or in a bond issuer's risk profile. Because the interest rate does not reflect the change in the market value of an outstanding bond when an issuer becomes higher risk or the bond goes into default, the bonds have been limited to investment grade bonds in the top three quality levels where the risk of default is relatively small.

The regulations also set forth certain interest crediting rates that satisfy the statutory market rate of return requirement but that are not safe harbor rates. The regulations provide that, in the case of indexed benefits as described in section 411(b)(5)(E), an interest crediting rate equal to the actual rate of return on the aggregate assets of the plan, including both positive returns and negative returns, is not in excess of a market rate of return if the plan's assets are diversified so as to minimize the volatility of returns. The regulations further provide that this requirement that plan assets be diversified so as to minimize the volatility of returns does not require greater diversification than is required under section 404(a)(1)(C) of Title I of the Employee Retirement Income Security Act of 1974, Public Law 93–406 (88 Stat. 829 (1974)) with respect to defined benefit pension plans. Furthermore, the regulations provide that the rate of return on the annuity contract for the employee issued by an insurance company licensed under the laws of a State is not in excess of a market rate of return, subject to an anti-abuse rule. The 2010 proposed regulations provide that certain additional interest crediting rates satisfy the market rate of return limitation.

The regulations reflect the preservation of capital rule in section 411(b)(5)(B)(i)(II) that requires a statutory hybrid plan to provide that interest credits will not result in a hypothetical account balance (or similar amount) being less than the aggregate amount of the hypothetical allocations. Under the 2007 proposed regulations, this requirement applied at the participant's annuity starting date. In addition, the 2007 proposed regulations provided that the combination of this preservation of capital protection with a rate of return that otherwise satisfies the market rate of return limitation will not result in an effective interest crediting rate that is in excess of a market rate of return. Responses to these rules were favorable and they are retained in these regulations. Hypothetical allocations are referred to as principal credits in the regulations, as described earlier in this preamble. The regulations clarify that the preservation of capital requirement applies to all principal credits that were credited under the plan as of the annuity starting date, including principal credits that were credited before the statutory effective date of the preservation of capital requirement under section 411(b)(5)(b)(i)(II).

These regulations do not address section 411(b)(5)(B)(vi), which requires that a plan's provisions reflect special rules applicable upon plan termination. These plan termination rules are addressed in the 2010 proposed regulations.

Section 123 of WRERA '08 amended ADEA to provide that, in the case of a governmental plan that is described in the first sentence of section 414(d) of the Code,[5] a rate of return or a method of crediting interest established pursuant to any provision of Federal, State, or local law is treated as a market rate of return for certain purposes under ADEA as long as such rate or method does not violate any other requirement of ADEA. No changes have been made to these regulations as a result of section 123 of WRERA '08 because that provision does not amend the Internal Revenue Code.

III. *Section 411(d)(6): Changes in a plan's interest crediting rate*

The 2007 proposed regulations provided that, to the extent that benefits have accrued under the terms of a statutory hybrid plan that entitle the participant to future interest credits, an amendment to the plan to change the interest crediting rate for such interest credits violates section 411(d)(6) if the revised rate under any circumstances could result in a lower interest crediting rate as of any date after the applicable amendment date of the amendment changing the interest crediting rate. Several commenters on the 2007 proposed regulations requested clarification of this rule. In particular, one commenter noted that there are several circumstances in which an amendment that results in a lower interest credit for a particular period after amendment than would have been provided for the same period under the old rate may not result in a reduction under section 411(d)(6), such as where the plan's aggregate interest credits after the applicable amendment date but before the period at issue exceeded the interest credits that would have been provided under the old rate or where the plan was also amended to increase benefits under other provisions, such as providing for larger principal credits than were provided before the change in interest crediting rates.

In response to these comments, the regulations clarify that the right to interest credits in the future that are not conditioned on future service constitutes a section 411(d)(6) protected benefit. Thus, to the extent that benefits have accrued under the terms of a statutory hybrid plan that entitle the participant to future interest credits, an amendment to the plan to change the interest crediting rate must comply with section 411(d)(6) if the revised rate under any circumstances could result in interest credits that are smaller as of any date after the applicable amendment date of the plan amendment than the interest credits that would have been provided without regard to the amendment.

The regulations retain the rule in the 2007 proposed regulations under which a plan is not treated as providing smaller interest credits in the future for purposes of section 411(d)(6) merely because of an

[5] A governmental plan in the first sentence of section 414(d) means a plan that is established and maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by an agency or instrumentality of any of the foregoing.

amendment that changes the plan's interest crediting rate with respect to future interest credits from one of the safe harbor market rates of interest (for example, a rate based on an eligible cost-of-living index or a rate based on Treasury bonds with the margins specified in the regulations) to the rate of interest on long-term investment grade corporate bonds (the third segment rate under section 417(e) or 430(h)), if certain requirements are satisfied. Under this rule, the change in the interest crediting rates would not result in a reduction in accrued benefits in violation of section 411(d)(6) because it is expected that an interest crediting rate that equals the third segment rate would not provide smaller interest credits as of any date after the applicable amendment date than the prior safe harbor interest crediting rate, except in rare and unusual circumstances. This special rule is only available if the change applies to interest credits to be credited after the effective date of the amendment, the effective date of the amendment is at least 30 days after adoption and, on the effective date of the amendment, the new interest crediting rate is not lower than the interest crediting rate that would have applied in the absence of the amendment.

The 2010 proposed regulations provide additional guidance with respect to the market rate of return requirements where a plan is amended to change its interest crediting rate in the absence of the application of a special rule under section 411(d)(6). In such a case, in order to satisfy section 411(d)(6), a participant's benefit can never be less than the pre-amendment benefit increased for periods after the amendment using the pre-amendment interest crediting rate, thereby effectively requiring a minimum interest crediting rate.

Effective/Applicability Dates

The regulations reflect the statutory effective dates set forth in section 701(e) of PPA '06. Pursuant to section 701(e)(1) of PPA '06, the amendments made by section 701 of PPA '06 are generally effective for periods beginning on or after June 29, 2005. However, sections 701(e)(2) through 701(e)(6) of PPA '06, as amended by WRERA '08, set forth a number of special effective/applicability date rules that are described earlier in the Background section of the preamble of these regulations.

In addition, these regulations reflect the delayed effective date for collectively bargained plans as set forth in section 701(e)(4) of PPA '06. This rule delays the effective date for section 411(b)(5)(B)(i) with respect to a collectively bargained plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified on or before August 17, 2006.

The 2007 proposed regulations included a rule for determining whether a plan was collectively bargained if a collective bargaining agreement applies to some, but not all, of the plan participants. Under that rule, a plan would be considered a collectively bargained plan if at least 25 percent of the participants in the plan are members of collective bargaining units for which the benefit levels under the plan are specified under the collective bargaining agreement. The same proposed rule was included in proposed regulations under section 436 (REG–113891–07, 2007–1 C.B. 821 [72 FR 50544]) and, in response to comments, this rule was modified in final regulations under section 436 (T.D. 9467, 2009–2 I.R.B. 760 [74 FR 53004]). Rather than repeat the rule, these regulations incorporate by reference the rule under the final section 436 regulations.

These regulations generally apply to plan years that begin on or after January 1, 2011. However, §1.411(b)(5)–1(d)(1)(iii), (d)(1)(vi), and (d)(6)(i), which provide that the regulations set forth the exclusive list of interest crediting rates and combinations of interest crediting rates that satisfy the market rate of return requirement under section 411(b)(5), apply to plan years that begin on or after January 1, 2012. For plan years that begin before January 1, 2012, statutory hybrid plans may utilize a rate that is permissible under these final regulations or the 2010 proposed regulations for purposes of satisfying the statutory market rate of return requirement. In addition, certain paragraphs which are reserved in these regulations (at §1.411(a)(13)–1(b)(2), (b)(3), and (b)(4) and §1.411(b)(5)–1(c)(3)(iii), (d)(1)(iv)(D), (d)(2)(ii), (d)(4)(iv), (d)(5)(iv), (d)(6)(ii), (d)(6)(iii), (e)(2), (e)(3)(iii), and (e)(4)) are addressed in proposed regulations that are being published at the same time as these regulations and those paragraphs are proposed to apply to plan years that begin on or after January 1, 2012.

The regulations provide that a benefit formula is not treated as having an effect similar to a lump sum-based benefit formula with respect to a participant who does not have an hour of service after the regulatory effective date. In addition, the regulations provide that, with respect to a conversion amendment, where the effective date of the conversion amendment (as defined in the regulations) is on or after the statutory effective date, the conversion protection requirements in the regulations apply only to a participant who has an hour of service on or after the regulatory effective date. As a result, participants who have an hour of service on or after the regulatory effective date must be provided with the minimum benefit required under the regulations beginning as of the effective date of a conversion amendment (as defined in the regulations), even if the effective date of the conversion amendment is before the regulatory effective date.

For periods after the statutory effective date and before the regulatory effective date, the relief of sections 411(a)(13) and 411(b)(5) applies and the requirements of sections 411(a)(13) and 411(b)(5) must be satisfied. During the periods set forth in the preceding sentence, a plan is permitted to rely on the provisions of these regulations for purposes of applying the relief and satisfying the requirements of sections 411(a)(13) and 411(b)(5). Further, for periods after the statutory effective date and before the regulatory effective date, a plan is permitted to rely on the provisions of the 2010 proposed regulations, the 2007 proposed regulations, and Notice 2007–6 for purposes of applying the relief and satisfying the requirements of sections 411(a)(13) and 411(b)(5).

These regulations should not be construed to create any inference concerning the applicable law prior to the effective dates of sections 411(a)(13) and 411(b)(5). See also section 701(d) of PPA '06. In addition, these regulations should not be construed to create any inference concerning sections 411(a)(13) and 411(b)(5) prior to the effective date of the regulations.

Special Analyses

It has been determined that these regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these final regulations and, because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, the proposed regulations preceding these final regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal authors of these regulations are Neil S. Sandhu, Lauson C. Green, and Linda S. F. Marshall, Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and the Treasury Department participated in the development of these regulations.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding the following entries:

Authority: 26 U.S.C. 7805 * * *

Section 1.411(a)(13)–1 also issued under 26 U.S.C. 411(a)(13).

Section 1.411(b)(5)–1 also issued under 26 U.S.C. 411(b)(5).

* * * * *

Par. 2. Section 1.411(a)(13)–1 is added to read as follows:

§1.411(a)(13)-1 Statutory hybrid plans.

(a) *In general.* This section sets forth certain rules that apply to statutory hybrid plans under section 411(a)(13). Paragraph (b) of this section describes special rules for certain statutory hybrid plans that determine benefits under a lump sum-based benefit formula. Paragraph (c) of this section describes the vesting requirement for statutory hybrid plans. Paragraphs (d) and (e) of this section contain definitions and effective/applicability dates, respectively.

(b) *Calculation of benefit by reference to hypothetical account balance or accumulated percentage*—(1) *Payment of a current balance or current value under a lump sum-based benefit formula.* Pursuant to section 411(a)(13)(A), a statutory hybrid plan that determines any portion of a participant's benefits under a lump sum-based benefit formula is not treated as failing to meet the following requirements solely because, with respect to benefits determined under that formula, the present value of those benefits is, under the terms of the plan, equal to the then-current balance of the hypothetical account maintained for the participant or to the then-current value of the accumulated percentage of the participant's final average compensation under that formula—

(i) Section 411(a)(2); or

(ii) With respect to the participant's accrued benefit derived from employer contributions, section 411(a)(11), 411(c), or 417(e).

(2) *Requirements that lump sum-based benefit formula must satisfy to obtain relief.* [Reserved].

(3) *Alternative forms of distribution under a lump sum-based benefit formula.* [Reserved].

(4) *Rules of application.* [Reserved].

(c) *Three-year vesting requirement*—(1) *In general.* Pursuant to section 411(a)(13)(B), if any portion of the participant's accrued benefit under a defined benefit plan is determined under a statutory hybrid benefit formula, the plan is treated as failing to satisfy the requirements of section 411(a)(2) unless the plan provides that the participant has a nonforfeitable right to 100 percent of the participant's accrued benefit if the participant has three or more years of service. Thus, this 3-year vesting requirement applies with respect to the entire accrued benefit of a participant under a defined benefit plan even if only a portion of the participant's accrued benefit under the plan is determined under a statutory hybrid benefit formula. Similarly, if the participant's accrued benefit under a defined benefit plan is, under the plan's terms, the larger of two (or more) benefit amounts, where each amount is determined under a different benefit formula (including a benefit determined pursuant to an offset among formulas within the plan or a benefit determined as the greater of a protected benefit under section 411(d)(6) and another benefit amount) and at least one of those formulas is a statutory hybrid benefit formula, the participant's entire accrued benefit under the defined benefit plan is subject to the 3-year vesting rule of section 411(a)(13)(B) and this paragraph (c). The rule described in the preceding sentence applies even if the larger benefit is ultimately the benefit determined under a formula that is not a statutory hybrid benefit formula.

(2) *Examples.* The provisions of this paragraph (c) are illustrated by the following examples:

Example 1. Employer M sponsors Plan X, a defined benefit plan under which each participant's accrued benefit is equal to the sum of the benefit provided under two benefit formulas. The first benefit formula is a statutory hybrid benefit formula, and the second formula is not. Because a portion of each participant's accrued benefit provided under Plan X is determined under a statutory hybrid benefit formula, the 3-year vesting requirement described in paragraph (c)(1) of this section applies to each participant's entire accrued benefit provided under Plan X.

Example 2. The facts are the same as in *Example 1*, except that the benefit formulas described in *Example 1* only apply to participants for service performed in Division A of Employer M and a different benefit formula applies to participants for service performed in Division B of Employer M. Pursuant to the terms of Plan X, the accrued benefit of a participant attributable to service performed in Division B is based on a benefit formula that is not a statutory hybrid benefit formula. Therefore, the 3-year vesting requirement described in paragraph (c)(1) of this section does not apply to a participant with an accrued benefit under Plan X if the participant's benefit is solely attributable to service performed in Division B.

Example 3. Employer N sponsors defined benefit Plan Y, an independent plan that provides benefits based solely on a lump sum-based benefit formula, and defined benefit Plan Z, which provides benefits based on a formula which is not a statutory hybrid benefit formula, but which is a floor plan that provides for the benefits payable to a participant under Plan Z to be reduced by the amount of the vested accrued benefit payable under Plan Y. The formula under Plan Y is a statutory hybrid benefit formula. Accordingly, Plan Y is subject to the 3-year vesting requirement described in paragraph (c)(1) of this section. The formula provided under Plan Z, even taking into account the offset for vested accrued benefits under Plan Y, is not a statutory hybrid benefit formula. Therefore, Plan Z is not subject to the 3-year vesting requirement in paragraph (c)(1) of this section.

(d) *Definitions*—(1) *In general*. The definitions in this paragraph (d) apply for purposes of this section.

(2) *Accumulated benefit*. A participant's accumulated benefit at any date means the participant's benefit, as expressed under the terms of the plan, accrued to that date. For this purpose, if a participant's benefit is expressed under the terms of the plan as the current balance of a hypothetical account or the current value of an accumulated percentage of the participant's final average compensation, the participant's accumulated benefit is expressed in that manner regardless of how the plan defines the participant's accrued benefit. Thus, for example, the accumulated benefit of a participant may be expressed under the terms of the plan as either the current balance of a hypothetical account or the current value of an accumulated percentage of the participant's final average compensation, even if the plan defines the participant's accrued benefit as an annuity beginning at normal retirement age that is actuarially equivalent to that balance or value.

(3) *Lump sum-based benefit formula*—(i) *In general*. A lump sum-based benefit formula means a benefit formula used to determine all or any part of a participant's accumulated benefit under a defined benefit plan under which the accumulated benefit provided under the formula is expressed as the current balance of a hypothetical account maintained for the participant or as the current value of an accumulated percentage of the participant's final average compensation. A benefit formula is expressed as the current balance of a hypothetical account maintained for the participant if it is expressed as a current single-sum dollar amount. Whether a benefit formula is a lump sum-based benefit formula is determined based on how the accumulated benefit of a participant is expressed under the terms of the plan, and does not depend on whether the plan provides an optional form of benefit in the form of a single-sum payment.

(ii) *Exception for employee contributions*. For purposes of the definition of a lump sum-based benefit formula in paragraph (d)(3)(i) of this section, the benefit properly attributable to after-tax employee contributions, rollover contributions from eligible retirement plans under section 402(c)(8), and other similar employee contributions (such as repayments of distributions pursuant to section 411(a)(7)(C) and employee contributions that are pickup contributions pursuant to section 414(h)(2)) is disregarded. However, a benefit is not properly attributable to contributions described in this paragraph (d)(3)(ii) if the contributions are credited with interest at a rate that exceeds a reasonable rate of interest or if the conversion factors used to calculate such benefit are not actuarially reasonable. See section 411(c) for an example of a calculation of a benefit that is properly attributable to employee contributions.

(4) *Statutory hybrid benefit formula*—(i) *In general*. A statutory hybrid benefit formula means a benefit formula that is either a lump sum-based benefit formula or a formula that is not a lump sum-based benefit formula but that has an effect similar to a lump sum-based benefit formula.

(ii) *Effect similar to a lump sum-based benefit formula*—(A) *In general*. Except as provided in paragraphs (d)(4)(ii)(B) through (D) of this section, a benefit formula under a defined benefit plan that is not a lump sum-based benefit formula has an effect similar to a lump sum-based benefit formula if the formula provides that a participant's accumulated benefit is expressed as a benefit that includes the right to adjustments (including a formula that provides for indexed benefits under §1.411(b)(5)–1(b)(2)) for a future period and the total dollar amount of those adjustments is reasonably expected to be smaller for the participant than for a similarly situated, younger individual (within the meaning of §1.411(b)(5)–1(b)(5)) who is or could be a participant in the plan. A benefit formula that does not include adjustments for any future period is treated as a formula with an effect similar to a lump sum-based benefit formula if the formula would be described in the preceding sentence except for the fact that the adjustments are provided pursuant to a pattern of repeated plan amendments. See §1.411(d)–4, A–1(c)(1).

(B) *Exception for post-retirement benefit adjustments*. Post-annuity starting date adjustments in the amount payable to a participant (such as cost-of-living increases) are disregarded in determining whether a benefit formula under a defined benefit plan has an effect similar to a lump sum-based benefit formula.

(C) *Exception for certain variable annuity benefit formulas*. If the assumed interest rate used for purposes of the adjustment of amounts payable to a participant under a variable annuity benefit formula is 5 percent or higher, then the variable annuity benefit formula is not treated as being reasonably expected to provide a smaller total dollar amount of future adjustments for the participant than for a similarly situated, younger individual who is or could be a participant in the plan, and thus such a variable annuity benefit formula does not have an effect similar to a lump sum-based benefit formula.

(D) *Exception for employee contributions*. Benefits that are disregarded under paragraph (d)(3)(ii) of this section (benefits properly attributable to certain employee contributions) are also disregarded for purposes of determining whether a benefit formula has an effect similar to a lump sum-based benefit formula.

(5) *Statutory hybrid plan*. A statutory hybrid plan means a defined benefit plan that contains a statutory hybrid benefit formula.

(6) *Variable annuity benefit formula*. A variable annuity benefit formula means any benefit formula under a defined benefit plan which provides that the amount payable is periodically adjusted by reference to the difference between the rate of return on plan assets (or specified market indices) and a specified assumed interest rate.

(e) *Effective/applicability date*—(1) *Statutory effective/applicability date*—(i) *In general*. Except as provided in paragraphs (e)(1)(ii) and (e)(1)(iii) of this section, section 411(a)(13) applies for periods beginning on or after June 29, 2005.

(ii) *Calculation of benefits*. Section 411(a)(13)(A) applies to distributions made after August 17, 2006.

(iii) *Vesting*—(A) *Plans in existence on June 29, 2005*—(*1*) *General rule*. In the case of a plan that is in existence on June 29, 2005 (regardless of whether the plan is a statutory hybrid plan on that date), section 411(a)(13)(B) applies to plan years that begin on or after January 1, 2008.

(*2*) *Exception for plan sponsor election*. See §1.411(b)(5)–1(f)(1)(iii)(A)(*2*) for a special election for early application of section 411(a)(13)(B).

(B) *Plans not in existence on June 29, 2005*. In the case of a plan not in existence on June 29, 2005, section 411(a)(13)(B) applies to plan years that end on or after June 29, 2005.

(C) *Collectively bargained plans*. Notwithstanding paragraphs (e)(1)(iii)(A) and (B) of this section, in the case of a collectively bargained plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified on or before August 17, 2006, the requirements of section 411(a)(13)(B) do not apply to plan years that begin before the earlier of—

(*1*) The later of—

(*i*) The date on which the last of those collective bargaining agreements terminates (determined without regard to any extension thereof on or after August 17, 2006); or

(*ii*) January 1, 2008; or

(*2*) January 1, 2010.

(D) *Treatment of plans with both collectively bargained and non-collectively bargained employees*. In the case of a plan with respect to which a collective bargaining agreement applies to some, but not all, of the plan participants, the plan is considered a collectively bargained plan for purposes of paragraph (e)(1)(iii)(C) of this section if it is considered a collectively bargained plan under the rules of §1.436–1(a)(5)(ii)(B).

(E) *Hour of service required*. Section 411(a)(13)(B) does not apply to a participant who does not have an hour of service after section 411(a)(13)(B) would otherwise apply to the participant under the rules of paragraph (e)(1)(iii)(A), (B), or (C) of this section.

(2) *Effective/applicability date of regulations*—(i) *In general*. Except as provided in paragraph (e)(2)(ii) of this section, this section applies to plan years that begin on or after January 1, 2011. For the periods after the statutory effective date set forth in paragraph (e)(1) of this section and before the regulatory effective date set forth in the preceding sentence, the relief of section 411(a)(13)(A) applies and the 3-year vesting requirement of section 411(a)(13)(B) must be satisfied. During these periods, a plan is permitted to rely on the provisions of this section for purposes of applying the relief of section 411(a)(13)(A) and satisfying the requirements of section 411(a)(13)(B).

(ii) *Special effective date*. [Reserved].

(iii) *Hour of service required*. A benefit formula is not treated as having an effect similar to a lump sum-based benefit formula under paragraph (d)(4)(ii) of this section with respect to a participant who does not have an hour of service after the regulatory effective date set forth in paragraph (e)(2)(i) of this section.

Par. 3. Section 1.411(b)(5)–1 is added to read as follows:

§1.411(b)(5)–1 Reduction in rate of benefit accrual under a defined benefit plan.

(a) *In general*—(1) *Organization of regulation*. This section sets forth certain rules for determining whether a reduction occurs in the rate of benefit accrual under a defined benefit plan because of the attainment of any age for purposes of section 411(b)(1)(H)(i). Paragraph (b) of this section describes safe harbors for certain plan designs (including statutory hybrid plans) that are deemed to satisfy the age discrimination rules under section 411(b)(1)(H). Paragraph (c) of this section describes rules relating to statutory hybrid plan conversion amendments. Paragraph (d) of this section describes rules restricting interest credits (or equivalent amounts) under a statutory hybrid plan to a market rate of return. Paragraph (e) of this section contains additional rules related to market rates of return. Paragraph (f) of this section contains effective/applicability dates.

(2) *Definitions*. The definitions of accumulated benefit, lump sum-based benefit formula, statutory hybrid benefit formula, statutory hybrid plan, and variable annuity benefit formula in §1.411(a)(13)–1(d) apply for purposes of this section.

(b) *Safe harbors for certain plan designs*—(1) *Accumulated benefit testing*—(i) *In general*. Pursuant to section 411(b)(5)(A), and subject to paragraph (b)(1)(ii) of this section, a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) with respect to an individual who is or could be a participant if, as of any date, the accumulated benefit of the individual would not be less than the accumulated benefit of any similarly situated, younger individual who is or could be a participant. Thus, this test involves a comparison of the accumulated benefit of an individual who is or could be a participant in the plan with the accumulated benefit of each similarly situated, younger individual who is or could be a participant in the plan. See paragraph (b)(5) of this section for rules regarding whether a younger individual who is or could be a participant is similarly situated to a participant. The comparison described in this paragraph (b)(1)(i) is based on any of one the following benefit measures, each of which is referred to as a *safe-harbor formula measure*:

(A) The annuity payable at normal retirement age (or current age, if later) if the accumulated benefit of the participant under the terms of the plan is an annuity payable at normal retirement age (or current age, if later).

(B) The current balance of a hypothetical account maintained for the participant if the accumulated benefit of the participant under the terms of the plan is a balance of a hypothetical account.

(C) The current value of an accumulated percentage of the participant's final average compensation if the accumulated benefit of the participant under the terms of the plan is an accumulated percentage of final average compensation.

(ii) *Benefit formulas for comparison*—(A) *In general*. Except as provided in paragraphs (b)(1)(ii)(B), (C), and (D) of this section, the safe harbor provided by section 411(b)(5)(A) and paragraph (b)(1)(i) of this section is available only with respect to an individual if the individual's accumulated benefit under the plan is expressed in terms of only one safe-harbor formula measure and no similarly situated, younger individual who is or could be a participant has an accumulated benefit that is expressed in terms of any measure other than that same safe-harbor formula measure. Thus, for example, if a plan provides that the accumulated benefit of participants who are age 55 or over is expressed under the terms of the plan as a life annuity payable at normal retirement age (or current age if later) as described in paragraph (b)(1)(i)(A) of this section and the plan provides that the accumulated benefit of participants who are younger than age 55 is expressed as the current balance of a hypothetical account as described in paragraph (b)(1)(i)(B) of this section, then the safe harbor described in section

411(b)(5)(A) and paragraph (b)(1)(i) of this section does not apply to individuals who are or could be participants who are age 55 or over.

(B) *Sum-of benefit formulas*. If a plan provides that a participant's accumulated benefit is expressed as the sum of benefits determined in terms of two or more benefit formulas, each of which is expressed in terms of a different safe-harbor formula measure, then the plan is deemed to satisfy paragraph (b)(1)(i) of this section with respect to an individual who is or could be a participant, provided that the plan satisfies the comparison described in paragraph (b)(1)(i) of this section separately for benefits determined in terms of each safe-harbor formula measure and no accumulated benefit of a similarly situated, younger individual who is or could be a participant is expressed other than as—

(*1*) The sum of benefits under two or more benefit formulas, each of which is expressed in terms of one of those same safe-harbor formula measures as is used for the participant's "sum-of" benefit;

(*2*) The greater of benefits under two or more benefit formulas, each of which is expressed in terms of any one of those same safe-harbor formula measures;

(*3*) The choice of benefits under two or more benefit formulas, each of which is expressed in terms of any one of those same safe-harbor formula measures; or

(*4*) A benefit that is determined in terms of only one of those same safe-harbor formula measures.

(C) *Greater-of benefit formulas*. If a plan provides that a participant's accumulated benefit is expressed as the greater of benefits under two or more benefit formulas, each of which is determined in terms of a different safe-harbor formula measure, then the plan is deemed to satisfy paragraph (b)(1)(i) of this section with respect to an individual who is or could be a participant, provided that the plan satisfies the comparison described in paragraph (b)(1)(i) of this section separately for benefits determined in terms of each safe-harbor formula measure and no accumulated benefit of a similarly situated, younger individual who is or could be a participant is expressed other than as—

(*1*) The greater of benefits determined under two or more benefit formulas, each of which is expressed in terms of one of those same safe-harbor formula measures as is used for the participant's "greater-of" benefit;

(*2*) The choice of benefits determined under two or more benefit formulas, each of which is expressed in terms of one of those same safe-harbor formula measures; or

(*3*) A benefit that is determined in terms of only one of those same safe-harbor formula measures.

(D) *Choice-of benefit formulas*. If a plan provides that a participant's accumulated benefit is determined pursuant to a choice by the participant between benefits determined in terms of two or more different safe-harbor formula measures, then the plan is deemed to satisfy paragraph (b)(1)(i) of this section with respect to an individual who is or could be a participant, provided that the plan satisfies the comparison described in paragraph (b)(1)(i) of this section separately for benefits determined in terms of each safe-harbor formula measure and no accumulated benefit of a similarly situated, younger individual who is or could be a participant is expressed other than as—

(*1*) The choice of benefits determined under two or more benefit formulas, each of which is expressed in terms of one of those same safe-harbor formula measures as is used for the participant's "choice-of" benefit; or

(*2*) A benefit that is determined in terms of only one of those same safe-harbor formula measures.

(iii) *Disregard of certain subsidized benefits*. For purposes of paragraph (b)(1)(i) of this section, any subsidized portion of any early retirement benefit that is included in a participant's accumulated benefit is disregarded. For this purpose, the subsidized portion of an early retirement benefit is the retirement-type subsidy within the meaning of §1.411(d)–3(g)(6) that is contingent on a participant's severance from employment and commencement of benefits before normal retirement age.

(iv) *Examples*. The provisions of this paragraph (b)(1) are illustrated by the following examples:

Example 1. (i) *Facts relating to formulas described in paragraph (b)(1)(i)(A) of this section*. Employer X maintains a defined benefit plan that provides a straight life annuity payable commencing at normal retirement age (which is age 65) equal to 1 percent of the participant's highest 3 consecutive years' compensation times years of service and provides for suspension of benefits as permitted under section 411(a)(3)(B). In the case of a participant whose service continues after normal retirement age, the amount payable is the greater of (i) the benefit payable at normal retirement age, and for each year thereafter, actuarially increased to account for delayed commencement and (ii) the retirement benefit determined under the formula at the date the employee's service ceases (calculated by including years of service and increases in compensation after normal retirement age).

(ii) *Conclusion*. Under these facts, the plan formula is a formula described in paragraph (b)(1)(i)(A) of this section. The formula is not a statutory hybrid benefit formula merely because the plan formula includes a benefit that is based on the participant's benefit at normal retirement age (and each year thereafter) that is actuarially increased for commencement after attainment of normal retirement age. In addition, the plan formula would satisfy the comparison under paragraph (b)(1)(i) of this section for each individual who is or could be a participant because, as of any date (including any date after normal retirement age), the accumulated benefit of the individual would not be less than the accumulated benefit of any similarly situated, younger individual who is or could be a participant.

Example 2. (i) *Facts relating to formulas described in paragraph (b)(1)(i)(B) of this section*. Employer Y maintains a defined benefit plan that expresses each participant's accumulated benefit as the balance of a hypothetical account. Under the formula, the hypothetical account balance of each participant is credited monthly with interest at a specified rate and the hypothetical account balance of each employee who is a participant is also credited with a pay credit under the plan equal to 7 percent of the participant's compensation for the month.

(ii) *Conclusion*. The plan formula is a lump sum-based benefit formula described in paragraph (b)(1)(i)(B) of this section and the formula would satisfy the comparison under paragraph (b)(1)(i) of this section for each individual who is or could be a participant because, as of any date, the hypothetical account balance of the individual would not be less than the hypothetical account balance of any similarly situated, younger individual who is or could be a participant.

Example 3. (i) *Facts where plan suspends interest credits after normal retirement age*. The facts are the same as in *Example 2* except that the plan provides for suspension of benefits as permitted under section 411(a)(3)(B). Pursuant to the plan's suspension of benefits provision, the plan provides for interest credits to cease during service after normal retirement age or for the amount of the interest credits during this service to be reduced to reflect principal credits credited.

(ii) *Conclusion*. The plan does not satisfy the safe harbor in paragraph (b)(1)(i) of this section. Applying the rule of paragraph (b)(1)(i) of this section, the plan formula would fail to satisfy the safe harbor comparison under paragraph (b)(1)(i) of this section with respect to an individual whose benefits have been suspended because, as of any date after attainment of normal retirement age, the hypothetical account balance of this individual would be less than the hypothetical account balance of one or more similarly situated individuals who have not attained normal retirement age.

Example 4. (i) *Facts providing greater-of benefits as described in paragraph (b)(1)(ii)(C) of this section*. Employer Z sponsors a defined benefit plan that provides an accumulated benefit expressed as a straight life annuity commencing at the plan's normal retirement age (age 65), based on a percentage of average annual compensation times the participant's years of service. On November 2, 2011, the plan is amended effective as of January 1, 2012, to provide participants who have attained age 55 by January 1, 2012, with a benefit that is the greater of the benefit under the average annual compensation formula and a benefit that is based on the balance of a hypothetical account, which provides for annual pay credits of a specified percentage of the participant's compensation and annual interest credits based on the third segment rate.

(ii) *Conclusion where plan provides greater-of benefits to older participants*. The plan satisfies the safe harbor of paragraph (b)(1)(i) of this section with respect to all individuals who are or could be participants. Pursuant to the rules of paragraph (b)(1)(ii)(C) of this section, the plan satisfies the safe harbor with respect to individuals who have attained age 55 by January 1, 2012, because (A) with respect to the benefit described in paragraph (b)(1)(i)(A) of this section (the benefit based on average annual compensation, disregarding the benefit based on the balance of a hypothetical account), the accumulated benefit for any individual who is or could be a participant and who is at least age 55 on January 1, 2012, would in no event be less than the accumulated benefit for a similarly situated, younger individual who is or could be participant and who has not yet attained age 55 by January 1, 2012, (B) with respect to the benefit described in paragraph (b)(1)(i)(B) of this section (the benefit based on the balance of a hypothetical account, disregarding the benefit based on average annual compensation), the accumulated benefit for any individual who is or could be a participant and who is at least age 55 on January 1, 2012, would in no event be less than the accumulated benefit for a similarly situated, younger individual who is or could be a participant and who has not yet attained age 55 by January 1, 2012, and (C) the benefit of any individual who is or could be a participant who has not yet attained age 55 by January 1, 2012, is only expressed as an annuity payable at normal retirement age as described in paragraph (b)(1)(i)(A) of this section, and this safe-harbor formula measure applies also to participants who have attained age 55 by January 1, 2012. Furthermore, the plan satisfies the safe harbor with respect to individuals who have not yet attained age 55 by January 1, 2012, because the benefit of these individuals satisfies the general rule of paragraph (b)(1)(ii)(A) of this section.

(iii) *Conclusion where plan provides greater-of benefits only to younger participants*. If, instead of the facts in paragraph (i) of this *Example 4*, the plan had been amended to provide only participants who have not yet attained age 55 by January 1, 2012, with a benefit that is the greater of the benefit under the average annual compensation formula and a benefit that is based on the balance of a hypothetical account then, the safe harbor would not be satisfied with respect to individuals who have attained age 55 by January 1, 2012. Under paragraph (b)(1)(ii)(A) of this section, except as provided in paragraphs (b)(1)(ii)(B), (C), and (D) of this section, the safe harbor of paragraph (b)(1)(i) of this section is available only with respect to individuals over age 55, whose benefit is expressed in terms of only one safe-harbor formula measure, if no similarly situated, younger individual has an accumulated benefit that is expressed in terms of any measure other than that same safe-harbor formula measure. This is not the case under these facts. The greater-of rule of paragraph (b)(1)(ii)(C) of this section would not apply to individuals who have attained age 55 because the accumulated benefits of these individuals is not equal to the greater of benefits under two or more benefit formulas.

Example 5. (i) *Facts where plan provides choice-of benefits to older participants*. The facts are the same as in paragraph (i) of *Example 4*, except that for service after December 31, 2011, the amendment permits participants who have attained age 55 by January 1, 2012, to choose between benefits under the average annual compensation benefit formula or benefits under the hypothetical account balance formula (but, if a participant chooses the hypothetical account balance formula, his or her benefit under the plan is in no event to be less than the benefit determined under the average annual compensation benefit formula for service before January 1, 2012), while other participants receive benefits solely under the hypothetical account balance formula (but individuals who are participants on December 31, 2011, are in no event to receive less than the benefit determined under the average annual compensation benefit formula for service before January 1, 2012).

(ii) *Conclusion where plan provides choice to older participants*. The plan satisfies the safe harbor with respect to all individuals who are or could be participants. Pursuant to the rule of paragraph (b)(1)(ii)(D) of this section, the plan satisfies the safe harbor of paragraph (b)(1)(i) of this section with respect to individuals who have attained age 55 by January 1, 2012, and, pursuant to the rule of paragraph (b)(1)(ii)(A), the plan satisfies the safe harbor with respect to individuals who have not yet attained 55 by January 1, 2012.

(iii) *Conclusion where plan provides choice-of benefits to older workers and greater-of benefits to younger participants*. If, in addition to the facts in paragraph (i) of this *Example 5*, the plan were also to provide participants who had not yet attained age 55 by January 1, 2012, the greater of the benefits under the average annual compensation benefit formula or the benefits under the hypothetical account balance formula, then pursuant to the rules of paragraph (b)(1)(ii)(A) and (D) of this section, the safe harbor would not be satisfied with respect to participants who have attained age 55 by January 1, 2012.

(2) *Indexed benefits*—(i) *In general*. Except as provided in paragraph (b)(2)(iii) of this section, pursuant to section 411(b)(5)(E) and this paragraph (b)(2)(i), a defined benefit plan is not treated as failing to meet the requirements of section 411(b)(1)(H) with respect to a participant solely because a benefit formula (other than a lump sum-based benefit formula) under the plan provides for the periodic adjustment of the participant's accrued benefit under the plan by means of the application of a recognized index or methodology. For purpose of the preceding sentence, a rate that does not exceed a market rate of return, as defined in paragraph (d) of this section, is deemed to be a recognized index or methodology. However, such a plan must satisfy the qualification requirements otherwise applicable to statutory hybrid plans, including the requirements of §1.411(a)(13)–1(c) (relating to minimum vesting standards) and paragraph (c) of this section (relating to plan conversion amendments).

(ii) *Similarly situated participant test*. Paragraph (b)(2)(i) of this section does not apply unless the aggregate adjustments made to a participant's accrued benefit under the plan (determined as a percentage of the unadjusted accrued benefit) in a period would not be less than the aggregate adjustments for any similarly situated, younger participant. This test requires a comparison, for each period, of the aggregate adjustments for each individual who is or could be a participant in the plan for the period with the aggregate adjustments of each other similarly situated, younger individual who is or could be a participant in the plan for that period. See paragraph (b)(5) of this section for rules regarding whether each younger individual who is or could be a participant is similarly situated to a participant.

(iii) *Protection against loss*—(A) *In general*. Paragraph (b)(2)(i) of this section does not apply unless the plan satisfies section 411(b)(5)(E)(ii) and paragraph (d)(2) of this section (relating to preservation of capital).

(B) *Exception for variable annuity benefit formulas*. The requirement to satisfy section 411(b)(5)(B)(i)(II), as set forth in paragraph (d)(2) of this section, as well as section 411(b)(5)(E)(ii), as set forth in this paragraph (b)(2)(iii), does not apply in the case of a benefit provided under a variable annuity benefit formula as defined in §1.411(a)(13)–1(d)(6).

(3) *Certain offsets permitted*. A plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides offsets against benefits under the plan to the extent the offsets are allowable in applying the requirements of section 401(a) and the applicable requirements of the Employee Retire-

ment Income Security Act of 1974, Public Law 93–406 (88 Stat. 829 (1974)), and the Age Discrimination in Employment Act of 1967, Public Law 90–202 (81 Stat. 602 (1967)).

(4) *Permitted disparities in plan contributions or benefits*. A plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides a disparity in contributions or benefits with respect to which the requirements of section 401(l) are met.

(5) *Definition of similarly situated*. For purposes of paragraphs (b)(1) and (b)(2) of this section, an individual is similarly situated to another individual if the individual is identical to that other individual in every respect that is relevant in determining a participant's benefit under the plan (including period of service, compensation, position, date of hire, work history, and any other respect) except for age. In determining whether an individual is similarly situated to another individual, any characteristic that is relevant for determining benefits under the plan and that is based directly or indirectly on age is disregarded. For example, if a particular benefit formula applies to a participant on account of the participant's age, an individual to whom the benefit formula does not apply and who is identical to the participant in all other respects is similarly situated to the participant. By contrast, an individual is not similarly situated to a participant if a different benefit formula applies to the individual and the application of the different formula is not based directly or indirectly on age.

(c) *Special rules for plan conversion amendments*—(1) *In general*. Pursuant to section 411(b)(5)(B)(ii), (iii), and (iv), if there is a conversion amendment within the meaning of paragraph (c)(4) of this section with respect to a defined benefit plan, then the plan is treated as failing to meet the requirements of section 411(b)(1)(H) unless the plan, after the amendment, satisfies the requirements of paragraph (c)(2) of this section.

(2) *Separate calculation of post-conversion benefit*—(i) *In general*. A statutory hybrid plan satisfies the requirements of this paragraph (c)(2) if the plan provides that, in the case of an individual who was a participant in the plan immediately before the date of adoption of the conversion amendment, the participant's benefit at any subsequent annuity starting date is not less than the sum of—

(A) The participant's section 411(d)(6) protected benefit (as defined in §1.411(d)–3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the conversion amendment; and

(B) The participant's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the conversion amendment.

(ii) *Rules of application*. For purposes of this paragraph (c)(2), except as provided in paragraph (c)(3) of this section, the benefits under paragraphs (c)(2)(i)(A) and (c)(2)(i)(B) of this section must each be determined in the same manner as if they were provided under separate plans that are independent of each other (for example, without any benefit offsets), and, except to the extent permitted under §1.411(d)–3 or §1.411(d)–4 (or other applicable law), each optional form of payment provided under the terms of the plan with respect to a participant's section 411(d)(6) protected benefit as in effect before the conversion amendment must be available thereafter to the extent of the plan's benefits for service prior to the effective date of the conversion amendment.

(3) *Establishment of opening hypothetical account balance or opening accumulated percentage*—(i) *In general*. Provided that the requirements of paragraph (c)(3)(ii) or (c)(3)(iii) of this section are satisfied, a statutory hybrid plan under which an opening hypothetical account balance or opening accumulated percentage of the participant's final average compensation is established as of the effective date of the conversion amendment does not fail to satisfy the requirements of paragraph (c)(2) of this section merely because benefits attributable to that opening hypothetical account balance or opening accumulated percentage (that is, benefits that are not described in paragraph (c)(2)(i)(B) of this section) are substituted for benefits described in paragraph (c)(2)(i)(A) of this section.

(ii) *Comparison of benefits at annuity starting date*—(A) *Testing requirement*. The requirements of this paragraph (c)(3)(ii) are satisfied with respect to an optional form of benefit payable at an annuity starting date only if the plan provides that the amount of the benefit payable in that optional form under the lump sum-based benefit formula that is attributable to the opening hypothetical account balance or opening accumulated percentage as described in paragraph (c)(3)(i) of this section is not less than the benefit under the comparable optional form of benefit under paragraph (c)(2)(i)(A) of this section. To satisfy this requirement, if the benefit under the optional form attributable to the opening hypothetical account balance or opening accumulated percentage is less than the benefit under the comparable optional form of benefit described in paragraph (c)(2)(i)(A) of this section, then the benefit attributable to the opening hypothetical account balance or opening accumulated percentage must be increased to the extent necessary to provide the minimum benefit described in this paragraph (c)(3)(ii). Thus, if a plan is using the option under this paragraph (c)(3)(ii) to satisfy paragraph (c)(2) of this section with respect to a participant, the participant must receive a benefit equal to not less than the sum of—

(*1*) The benefit described in paragraph (c)(2)(i)(B) of this section; and

(*2*) The greater of—

(*i*) The benefit attributable to the opening hypothetical account balance or attributable to the opening accumulated percentage of the participant's final average compensation as described in this paragraph (c)(3)(ii); or

(*ii*) The benefit described in paragraph (c)(2)(i)(A) of this section.

(B) *Comparable optional form of benefit*. If there was an optional form of benefit within the same generalized optional form of benefit (within the meaning of §1.411(d)–3(g)(8)) that would have been available to the participant at that annuity starting date under the terms of the plan as in effect immediately before the effective date of the conversion amendment, then that optional form of benefit is the comparable optional form of benefit.

(C) *Special rule for new post-conversion optional forms of benefit*. If an optional form of benefit is available on the annuity starting date with respect to the benefit attributable to the opening hypothetical account balance or opening accumulated percentage, but no optional form within the same generalized optional form of benefit (within the meaning of §1.411(d)–3(g)(8)) was available at that annuity starting date under the terms of the plan as in effect immediately prior to the effective date of the conversion amendment, then, for purposes of this paragraph (c)(3)(ii), the plan is treated as if such an optional form of benefit were available immediately prior to the effective date of the conversion amendment for purposes of this paragraph (c)(3)(ii). Thus, for example, if a single-sum optional form of payment is not available under the plan terms applicable to the accrued benefit described in paragraph (c)(2)(i)(A) of this section, but a single-sum optional form of payment is available with respect to the benefit attributable to the opening hypothetical account balance or opening accumulated percentage as of the annuity starting date, then, for purposes of this paragraph (c)(3)(ii), the plan is treated as if a single sum (which satisfies the requirements of section 417(e)(3)) were available under the terms of the plan as in effect immediately prior to the effective date of the conversion amendment.

(iii) *Comparison of benefits at effective date of conversion amendment*. [Reserved].

(4) *Conversion amendment*—(i) *In general*. An amendment is a conversion amendment that is subject to the requirements of this paragraph (c) with respect to a participant if—

(A) The amendment reduces or eliminates the benefits that, but for the amendment, the participant would have accrued after the effective date of the amendment under a benefit formula that is not a statutory hybrid benefit formula (and under which the participant was accruing benefits prior to the amendment); and

(B) After the effective date of the amendment, all or a portion of the participant's benefit accruals under the plan are determined under a statutory hybrid benefit formula.

(ii) *Rules of application*—(A) *In general*. Paragraphs (c)(4)(iii), (iv), and (v) of this section describe special rules that treat certain arrangements as conversion amendments. The rules described in those paragraphs apply both separately and in combination. Thus, for example, in an acquisition described in §1.410(b)–2(f), if the buyer adopts an amendment under which a participant's benefits under the seller's plan that is not a statutory hybrid plan are coordinated with a separate plan of the buyer that is a statutory hybrid plan, such as through an offset of the participant's benefit under the buyer's plan by the participant's benefit under the seller's plan, the seller and buyer are treated as a single employer under paragraph (c)(4)(iv) of this section and they are treated as having adopted a conversion amendment under paragraph (c)(4)(iii) of this section. However, pursuant to paragraph (c)(4)(iii) of this section, if there is no coordination between the two plans, there is no conversion amendment.

(B) *Covered amendments*. Only amendments that eliminate or reduce accrued benefits described in section 411(a)(7), or a retirement-type subsidy described in section 411(d)(6)(B)(i), that would otherwise accrue as a result of future service are treated as amendments described in paragraph (c)(4)(i)(A) of this section.

(C) *Operation of plan terms treated as covered amendment*. If, under the terms of a plan, a change in the conditions of a participant's employment results in a reduction of the participant's benefits that would have accrued in the future under a benefit formula that is not a statutory hybrid benefit formula, the plan is treated for purposes of this paragraph (c)(4) as if such plan terms constitute an amendment that reduces the participant's benefits that would have accrued after the effective date of the change under a benefit formula that is not a statutory hybrid benefit formula. Thus, for example, if a participant transfers from an operating division that is covered by a non-statutory hybrid benefit formula to an operating division that is covered by a statutory hybrid benefit formula, there has been a conversion amendment and the effective date of the conversion amendment is the date of the transfer. For purposes of applying the effective date rule of paragraph (f)(1)(ii) of this section, the date that the relevant plan terms were adopted is treated as the adoption date of the amendment.

(iii) *Multiple plans*. An employer is treated as having adopted a conversion amendment if the employer adopts an amendment under which a participant's benefits under a plan that is not a statutory hybrid plan are coordinated with a separate plan that is a statutory hybrid plan, such as through a reduction (offset) of the benefit under the plan that is not a statutory hybrid plan.

(iv) *Multiple employers*. If the employer of an employee changes as a result of a transaction described in §1.410(b)–2(f), then the two employers are treated as a single employer for purposes of this paragraph (c)(4).

(v) *Multiple amendments*—(A) *In general*—(*1*) *General rule*. For purposes of this paragraph (c)(4), a conversion amendment includes multiple amendments that result in a conversion amendment even if the amendments are not conversion amendments individually. For example, an employer is treated as having adopted a conversion amendment if the employer first adopts an amendment described in paragraph (c)(4)(i)(A) of this section and, at a later date, adopts an amendment that adds a benefit under a statutory hybrid benefit formula as described in paragraph (c)(4)(i)(B) of this section, if they are consolidated under paragraph (c)(4)(v)(A)(*2*) of this section.

(*2*) *Delay between plan amendments*. In determining whether a conversion amendment has been adopted, an amendment to provide a benefit under a statutory hybrid benefit formula is consolidated with a prior amendment to reduce non-statutory hybrid benefit formula benefits if the amendment providing benefits under a statutory hybrid benefit formula is adopted within three years after adoption of the amendment reducing non-statutory hybrid benefit formula benefits. Thus, the later adoption of the statutory hybrid benefit formula will cause the earlier amendment to be treated as part of a conversion amendment. In the case of an amendment to provide a benefit under a statutory hybrid benefit formula that is adopted more than three years after adoption of an amendment to reduce benefits under a non-statutory hybrid benefit formula, there is a presumption that the amendments are not consolidated unless the facts and circumstances indicate that adoption of the amendment to provide a benefit under a statutory hybrid benefit formula was intended at the time of reduction in the non-statutory hybrid benefit formula.

(B) *Multiple conversion amendments*. If an employer adopts multiple amendments reducing benefits described in paragraph (c)(4)(i)(A) of this section, each amendment is treated as a separate conversion amendment, provided that paragraph (c)(4)(i)(B) of this section is applicable at the time of the amendment (taking into account the rules of this paragraph (c)(4)).

(vi) *Effective date of a conversion amendment*. The effective date of a conversion amendment is, with respect to a participant, the date as of which the reduction of the participant's benefits described in paragraph (c)(4)(i)(A) of this section occurs. In accordance with section 411(d)(6), the date of a reduction of those benefits cannot be earlier than the date of adoption of the conversion amendment.

(5) *Examples*. The following examples illustrate the application of this paragraph (c):

Example 1. (i) *Facts where plan does not establish opening hypothetical account balance for participants and participant elects life annuity at normal retirement age*. Employer N sponsors Plan E, a defined benefit plan that provides an accumulated benefit, payable as a straight life annuity commencing at age 65 (which is Plan E's normal retirement age), based on a percentage of highest average compensation times the participant's years of service. Plan E permits any participant who has had a severance from employment to elect payment in the following optional forms of benefit (with spousal consent if applicable), with any payment not made in a straight life annuity converted to an equivalent form based on reasonable actuarial assumptions: a straight life annuity; and a 50 percent, 75 percent, or 100 percent joint and survivor annuity. The payment of benefits may commence at any time after attainment of age 55, with an actuarial reduction if the commencement is before normal retirement age. In addition, the plan offers a single-sum payment after attainment of age 55 equal to the present value of the normal retirement benefit using the applicable interest rate and mortality table under section 417(e)(3) in effect under the terms of the plan on the annuity starting date.

(ii) *Facts relating to the conversion amendment*. On January 1, 2012, Plan E is amended to eliminate future accruals under the highest average compensation benefit formula and to base future benefit accruals under a hypothetical account balance formula. For service on or after January 1, 2012, each participant's hypothetical account balance is credited monthly with a pay credit equal to a specified percentage of the participant's compensation during the month and also with interest based on the third segment rate described in section 430(h)(2)(C)(iii). With respect to benefits under the hypothetical account balance attributable to service on and after January 1, 2012, a participant is permitted to elect (with spousal consent if applicable) payment in the same generalized optional forms of benefit (even though different actuarial factors apply) as under the terms of the plan in effect before January 1, 2012, and also as a single-sum distribution. The plan provides for the benefit attributable to service before January 1, 2012, to be determined under the terms of the plan as in effect immediately before the effective date of the amendment, and the benefit attributable to service on and after January 1, 2012, to be determined separately, under the terms of the plan as in effect after the effective date of the amendment, with neither benefit offsetting the other in any manner. Thus, each participant's benefit is equal to the sum of the benefit attributable to service before January 1, 2012 (to be determined under the terms of the plan as in effect immediately before the effective date of the amendment), plus the benefit attributable to the participant's hypothetical account balance.

(iii) *Facts relating to an affected participant*. Participant A is age 62 on January 1, 2012. On December 31, 2011, A's benefit for years of service before January 1, 2012, payable as a straight life annuity commencing at A's normal retirement age (age 65), which is January 1, 2015, is $1,000 per month. On January 1, 2015, when Participant A has a severance from employment, the then-current hypothetical account balance, with pay credits and interest from January 1, 2012, to January 1, 2015, is $11,000. Using the conversion factors applicable under the plan on January 1, 2015, that balance is equivalent to a straight life annuity of $100 per month commencing on January 1, 2015. This benefit is in addition to the benefit attributable to service before January 1, 2012. Participant A elects (with spousal consent) a straight life annuity of $1,100 per month commencing January 1, 2015.

(iv) *Conclusion*. Participant A's benefit satisfies the requirements of paragraph (c) of this section because Participant A's benefit is not less than the sum of Participant A's section 411(d)(6) protected benefit (as defined in §1.411(d)–3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment, and Participant A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 2. (i) *Facts involving plan's establishment of opening hypothetical account balance and payment of pre-conversion accumulated benefit in life annuity at normal retirement age*. Except as indicated in this *Example 2*, the facts are the same as the facts under paragraph (i) of *Example 1*.

(ii) *Facts relating to the conversion amendment*. On January 1, 2012, Plan E is amended to eliminate future accruals under the highest average compensation benefit formula and to provide future benefit accruals under a hypothetical account balance formula. An opening hypothetical account balance is established for each participant, and, under the plan's terms, that balance is equal to the present value of the participant's accumulated benefit on December 31, 2011 (payable as a straight life annuity at normal retirement age or immediately, if later), using the applicable interest rate and applicable mortality table under section 417(e)(3) on January 1, 2012. Under Plan E, the account based on this opening hypothetical account balance is maintained as a separate account from the account for accruals on or after January 1, 2012. The hypothetical account balance maintained for each participant for accruals on or after January 1, 2012, is credited monthly with a pay credit equal to a specified percentage of the participant's compensation during the month. A participant's hypothetical account balance (including both of the separate accounts) is credited monthly with interest based on the third segment rate described in section 430(h)(2)(C)(iii).

(iii) *Facts relating to optional forms of benefit*. Following severance from employment and attainment of age 55, a participant is permitted to elect (with spousal consent if applicable) payment in the same generalized optional forms of benefit as under the plan in effect prior to January 1, 2012, with the amount payable calculated based on the hypothetical account balance on the annuity starting date and the applicable interest rate and applicable mortality table on the annuity starting date. The single-sum distribution is equal to the hypothetical account balance.

(iv) *Facts relating to conversion protection*. The plan provides that, as of a participant's annuity starting date, the plan will determine whether the benefit attributable to the opening hypothetical account payable in the particular optional form of benefit selected is equal to or greater than the benefit accrued under the plan through the date of conversion and payable in the same generalized optional form of benefit with the same annuity starting date. If the benefit attributable to the opening hypothetical account balance is equal to or greater than the pre-conversion benefit, the plan provides that such benefit is paid in lieu of the pre-conversion benefit, together with the benefit attributable to post-conversion pay-based principal credits. If the benefit attributable to the opening hypothetical account balance is less than the pre-conversion benefit, the plan provides that such benefit is increased sufficiently to provide the pre-conversion benefit, together with the benefit attributable to post-conversion pay-based principal credits.

(v) *Facts relating to an affected participant*. On January 1, 2012, the opening hypothetical account balance established for Participant A is $80,000, which is the present value of Participant A's straight life annuity of $1,000 per month commencing at January 1, 2015, using the applicable interest rate and applicable mortality table under section 417(e)(3) in effect on January 1, 2012. On January 1, 2012, the applicable interest rate for Participant A is equivalent to a level rate of 5.5 percent. Thereafter, Participant A's hypothetical account balance for subsequent accruals is credited monthly with a pay credit equal to a specified percentage of the participant's compensation during the month. In addition, Participant A's hypothetical account balance (including both of the separate accounts) is credited monthly with interest based on the third segment rate described in section 430(h)(2)(C)(iii).

(vi) *Facts relating to calculation of the participant's benefit*. Participant A has a severance from employment on January 1, 2015 at age 65, and elects (with spousal consent) a straight life annuity commencing January 1, 2015. On January 1, 2015, the opening hypothetical account balance, with interest credits from January 1, 2012, to January 1, 2015, has become $95,000, which, using the conversion factors under the plan on January 1, 2015, is equivalent to a straight life annuity of $1,005 per month commencing on January 1, 2015 (which is greater than the $1,000 a month payable at age 65 under the terms of the plan in effect before January 1, 2012). This benefit is in addition to the benefit determined using the hypothetical account balance for service after January 1, 2012.

(vii) *Conclusion*. The benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant A because A's benefit is not less than the sum of (A) the greater of Participant A's benefits attributable to the opening hypothetical account balance and A's section 411(d)(6) protected benefit (as defined in §1.411(d)–3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment, and (B) Participant A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 3. (i) *Facts involving a subsequent decrease in interest rates*. The facts are the same as in *Example 2*, except that, because of a decrease in bond rates after January 1, 2012, and before January 1, 2015, the rate of interest credited in that period averages less than 5.5 percent, and, on January 1, 2015, the effective applicable interest rate under section 417(e)(3) under the plan's terms is 4.7 percent. As a result, Participant A's opening hypothetical account balance plus attributable interest credits has increased to only $87,000 on January 1, 2015, and, using the conversion factors under the plan on January 1, 2015, is equivalent to a straight life annuity commencing on January 1, 2015, of $775 per month. Under the terms of Plan E, the benefit attributable to A's opening account balance is increased so that A's straight life annuity commencing on January 1, 2015, is $1,000 per month. This benefit is in addition to the benefit attributable to the hypothetical account balance for service after January 1, 2012.

(ii) *Conclusion*. The benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant A because A's benefit is not less than the sum of—

(A) The greater of A's benefits attributable to the opening hypothetical account balance and A's section 411(d)(6) protected benefit (as defined in §1.411(d)–3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment; and

(B) A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 4. (i) *Facts involving payment of a subsidized early retirement benefit*. The facts are the same as in *Example 2*, except that under the terms of Plan E on December 31, 2011, a participant who retires before age 65 and after age 55 with 30 years of service has only a 3 percent per year actuarial reduction. Participant A has a severance from employment on January 1, 2013, when A is age 63 and has 30 years of service. On January 1, 2013, A's opening hypothetical account balance, with interest from January 1, 2012, to January 1, 2013, has become $86,000, which, using the conversion factors under the plan (as amended) on January 1, 2013, is equivalent to a straight life annuity commencing on January 1, 2013, of $850 per month.

(ii) *Facts relating to calculation of the participant's benefit*. Under the terms of Plan E on December 31, 2011, Participant A is entitled to a straight life annuity commencing on January 1, 2013, equal to at least $940 per month ($1,000 reduced by 3 percent for each of the 2 years that A's benefits commence before normal retirement age). Under the terms of Plan E, the benefit attributable to A's opening account balance is increased so that A is entitled to a straight life annuity of $940 per month commencing on January 1, 2015. This benefit is in addition to the benefit determined using the hypothetical account balance for service after January 1, 2012.

(iii) *Conclusion*. The benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant A because A's benefit is not less than the sum of—

(A) The greater of Participant A's benefits attributable to the opening hypothetical account balance (increased by attributable interest credits) and A's section 411(d)(6) protected benefit (as defined in §1.411(d)–3(g)(14)) with respect to service before the effective date of the conversion amendment, determined under the terms of the plan as in effect immediately before the effective date of the amendment; and

(B) Participant A's section 411(d)(6) protected benefit with respect to service on and after the effective date of the conversion amendment, determined under the terms of the plan as in effect after the effective date of the amendment.

Example 5. (i) *Facts involving addition of a single-sum payment option*. The facts are the same as in *Example 2*, except that, before January 1, 2012, Plan E did not offer payment in a single-sum distribution for amounts in excess of $5,000. Plan E, as amended on January 1, 2012, offers payment in any of the available annuity distribution forms commencing at any time following severance from employment as were provided under Plan E before January 1, 2012. In addition, Plan E, as amended on January 1, 2012, offers payment in the form of a single sum attributable to service before January 1, 2012, which is the greater of the opening hypothetical account balance (increased by attributable interest credits) or a single-sum distribution of the straight life annuity payable at age 65 using the same actuarial factors as are used for mandatory cashouts for amounts equal to $5,000 or less under the terms of the plan on December 31, 2011. Participant B is age 40 on January 1, 2012, and B's opening hypothetical account balance (increased by attributable interest credits) is $33,000 (which is the present value, using the conversion factors under the plan (as amended) on January 1, 2012, of Participant B's straight life annuity of $1,000 per month commencing at January 1, 2037, which is when B will be age 65). Participant B has a severance from employment on January 1, 2015, and elects (with spousal consent) an immediate single-sum distribution. Participant B's opening hypothetical account balance (increased by attributable interest) on January 1, 2015, is $45,000. The present value, on January 1, 2015, of Participant B's benefit of $1,000 per month, commencing immediately using the actuarial factors for mandatory cashouts under the terms of the plan on December 31, 2011, would result in a single-sum payment of $44,750. Participant B is paid a single-sum distribution equal to the sum of $45,000 plus an amount equal to B's January 1, 2015, hypothetical account balance for benefit accruals for service after January 1, 2012.

(ii) *Conclusion*. Because, under Plan E, Participant B is entitled to the sum of—

(A) The greater of the $45,000 opening hypothetical account balance (increased by attributable interest credits) and $44,750 (present value of the benefit with respect to service prior to January 1, 2012, using the actuarial factors for mandatory cashout distributions under the terms of the plan on December 31, 2011); and

(B) An amount equal to B's hypothetical account balance for benefit accruals for service after January 1, 2012, the benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant B. If Participant B's hypothetical account balance under Plan E was instead less than $44,750 on January 1, 2015, Participant B would be entitled to a single-sum payment equal to the sum of $44,750 and an amount equal to B's hypothetical account balance for benefit accruals for service after January 1, 2012.

Example 6. (i) *Facts involving addition of new annuity optional form of benefit*. The facts are the same as in *Example 2*, except that, after December 31, 2011, and before January 1, 2015, Plan E is amended to offer payment in a 5-, 10-, or 15-year term certain and life annuity, using the same actuarial assumptions that apply for other optional forms of distribution. When Participant A has a severance from employment on January 1, 2015, A elects (with spousal consent) a 5-year term certain and life annuity commencing immediately equal to $935 per month. Application of the same actuarial assumptions to Participant A's benefit of $1,000 per month (under Plan E as in effect on December 31, 2011), commencing immediately on January 1, 2015, would result in a 5-year term certain and life annuity commencing immediately equal to $955 per month. Under the terms of Plan E, the benefit attributable to A's opening account balance is increased so that, using the conversion factors under the plan (as amended) on January 1, 2015, A's opening hypothetical account balance (increased by attributable interest credits) produces a 5-year term certain and life annuity commencing immediately equal to $955 per month commencing on January 1, 2015. This benefit is in addition to the benefit determined using the January 1, 2015, hypothetical account balance for service after January 1, 2012.

(ii) *Conclusion*. This benefit satisfies the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant A.

Example 7. (i) *Facts involving addition of distribution option before age 55*. The facts are the same as in *Example 5*, except that Participant B (age 43) elects (with spousal consent) a straight life annuity commencing immediately on January 1, 2015. Under Plan E, the straight life annuity attributable to Participant B's opening hypothetical account balance at age 43 is $221 per month. Application of the same actuarial assumptions to Participant B's benefit of $1,000 per month commencing at age 65 (under Plan E as in effect on December 31, 2011) would result in a straight life annuity commencing immediately on January 1, 2015, equal to $219 per month.

(ii) *Conclusion.* Because, under its terms, Plan E provides that Participant B is entitled to an amount not less than the present value (using the same actuarial assumptions as apply on January 1, 2015, in converting the $45,000 hypothetical account balance attributable to the opening hypothetical account balance to the $221 straight life annuity) of Participant B's straight life annuity of $1,000 per month commencing at age 65, and the $221 straight life annuity is in addition to the benefit accruals for service after January 1, 2012, payment of the $221 monthly annuity would satisfy the requirements of paragraph (c)(3)(ii)(A) of this section with respect to Participant B.

(d) *Market rate of return*—(1) *In general*—(i) *Basic test*. Subject to the rules of paragraph (e) of this section, a statutory hybrid plan satisfies the requirements of section 411(b)(1)(H) and this paragraph (d) only if, for any plan year, the interest crediting rate with respect to benefits determined under a statutory hybrid benefit formula is not greater than a market rate of return.

(ii) *Definitions relating to market rate of return*—(A) *Interest credit*. Subject to other rules in this paragraph (d), an interest credit for purposes of this paragraph (d) and section 411(b)(5)(B) means the following adjustments to a participant's accumulated benefit under a statutory hybrid benefit formula, to the extent not conditioned on current service and not made on account of imputed service (as defined in §1.401(a)(4)–11(d)(3)(ii)(B))—

(*1*) Any increase or decrease for a period, under the terms of the plan at the beginning of the period, that is calculated by applying a rate of interest or rate of return (including a rate of increase or decrease under an index) to the participant's accumulated benefit (or a portion thereof) as of the beginning of the period; and

(*2*) Any other increase for a period, under the terms of the plan at the beginning of the period.

(B) *Treatment of plan amendments*. An increase to a participant's accumulated benefit is not treated as an interest credit to the extent the increase is made as a result of a plan amendment providing for a one-time adjustment to the participant's accumulated benefit. However, a pattern of repeated plan amendments each of which provides for a one-time adjustment to a participant's accumulated benefit will cause such adjustments to be treated as provided on a permanent basis under the terms of the plan. See §1.411(d)–4, A–1(c)(1).

(C) *Interest crediting rate*. Except as otherwise provided in this paragraph (d), the interest crediting rate, or effective rate of return, for a period with respect to a participant equals the total amount of interest credits for the period divided by the participant's accumulated benefit at the beginning of the period.

(D) *Principal credit*. For purposes of this paragraph (d), a principal credit means any increase to a participant's accumulated benefit under a statutory hybrid benefit formula that is not an interest credit. Thus, for example, a principal credit includes an increase to a participant's accumulated benefit to the extent the increase is conditioned on current service or made on account of imputed service. As a result, a principal credit includes an increase to the value of an accumulated percentage of the participant's final average compensation. For indexed benefits described in paragraph (b)(2) of this section, a principal credit includes an increase to the participant's accrued benefit other than an increase provided by indexing. In addition, pursuant to the rule in paragraph (d)(1)(ii)(B) of this section, a principal credit generally includes an increase to a participant's accumulated benefit to the extent the increase is made as a result of a plan amendment providing for a one-time adjustment to the participant's accumulated benefit. As a result, a principal credit includes an opening hypothetical account balance or opening accumulated percentage of the participant's final average compensation, as described in paragraph (c)(3) of this section.

(iii) *Market rate of return for single rates*. Except as is otherwise provided in this paragraph (d)(1), an interest crediting rate is not in excess of a market rate of return only if the plan terms provide that the interest credit for each plan year is determined using one of the following specified interest crediting rates:

(A) The interest rate on long-term investment grade corporate bonds (as described in paragraph (d)(3) of this section).

(B) An interest rate that, under paragraph (d)(4) of this section, is deemed to be not in excess of the interest rate described in paragraph (d)(3) of this section.

(C) A rate of return that, under paragraph (d)(5) of this section, is not in excess of a market rate of return.

(iv) *Timing and other rules related to interest crediting rate*—(A) *In general*. A plan that provides interest credits must specify how the plan determines interest credits and must specify how and when interest credits are credited. The plan must specify the method for determining interest credits in accordance with the requirements of paragraph (d)(1)(iv)(B) of this section, the frequency of interest crediting in accordance with the requirements of paragraph (d)(1)(iv)(C) of this section, and the treatment of interest credits on distributed amounts, as well as other debits and credits during the period, in accordance with the rules of paragraph (d)(1)(iv)(D) of this section. See paragraph (e) of this section for additional rules that apply to changes in the interest crediting rate.

(B) *Methods to determine interest credits*. A plan that is using any specified interest crediting rate can determine interest credits for each current interest crediting period based on the effective periodic interest crediting rate that applies over the period. Alternatively, a plan that is using one of the interest crediting rates described in paragraph (d)(3) or (d)(4) of this section can determine interest credits for a stability period based on the interest crediting rate for a specified lookback month with respect to that stability period. For purposes of the preceding sentence, the stability period and lookback month must satisfy the rules for selecting the stability period and lookback month under §1.417(e)–1(d)(4), although the interest crediting rate can be any one of the rates in paragraph (d)(3) or (d)(4) of this section and the stability period and lookback month need not be the same as those used under the plan for purposes of section 417(e)(3).

(C) *Frequency of interest crediting*. Interest credits under a plan must be provided on an annual or more frequent periodic basis and interest credits for each interest crediting period must be credited as of the end of the period. If a plan provides for the crediting of interest more frequently than annually (for example, daily, monthly or quarterly) based on one of the annual interest rates described in paragraph (d)(3) or (d)(4) of this section, then the plan generally provides an above market rate of return unless each periodic interest credit is determined using an interest crediting rate that is no greater than a *pro rata* portion of the applicable annual interest crediting rate. However, a plan that credits interest daily based on one of the annual interest rates described in paragraph (d)(3) or (d)(4) of this section is not treated as providing an above market rate of return merely because the plan determines each daily interest credit using a daily interest crediting rate that is 1/360 of the applicable annual interest crediting rate. In addition, interest credits determined, under the terms of a plan, based on one of the annual interest rates described in paragraph (d)(3) or (d)(4) of this section are not treated as creating an effective rate of return that is in excess of a market rate of return merely because an otherwise permissible interest crediting rate for a plan year is compounded more frequently than annually. Thus, for example, if a plan's terms provide for interest to be credited monthly and for the interest crediting rate to be equal to the interest rate on long-term investment grade corporate bonds (as described in paragraph (d)(3) of this section) and the applicable annual rate on these bonds for the plan year is 6 percent, then the accumulated benefit at the beginning of each month could be increased as a result of interest credits by as much as 0.5 percent per month during the plan year without resulting in an interest crediting rate that is in excess of a market rate of return.

(D) *Debits and credits during the interest crediting period*. [Reserved].

(v) *Lesser rates*. An interest crediting rate is not in excess of a market rate of return if the rate can never be in excess of a particular rate that is described in paragraph (d)(1)(iii) of this section. Thus, for example, an interest crediting rate that always equals the rate described in paragraph (d)(3) of this section minus 200 basis points is not in excess of a market rate of return because it can never be in excess of the rate described in paragraph (d)(3) of this section. Similarly, an interest crediting rate that always equals the lesser of the yield on 30-year Treasury bonds and a fixed 6 percent interest rate is not in excess of a market rate of return because it can never be in excess of the yield on 30-year Treasury bonds.

(vi) *Greater-of rates*. If a statutory hybrid plan determines an interest credit by applying the greater of 2 or more different rates to the accumulated benefit, the effective interest crediting rate is not in excess of a market rate of return only if each of the different rates would separately satisfy the requirements of this paragraph (d) and the requirements of paragraph (d)(6) of this section are also satisfied.

(vii) *Blended rates*. A statutory hybrid plan does not provide an effective interest crediting rate that is in excess of a market rate of return merely because the plan determines an interest credit by applying different rates to different predetermined portions of the accumulated benefit, provided each rate would separately satisfy the requirements of this paragraph (d) if the rate applied to the entire accumulated benefit.

(2) *Preservation of capital requirement*—(i) *General rule*. A statutory hybrid plan satisfies the requirements of section 411(b)(1)(H) only if the plan provides that the participant's benefit under the statutory hybrid benefit formula determined as of the participant's annuity starting date is no less than the benefit based on the sum of all principal credits (as described in paragraph (d)(1)(ii)(D) of this section) credited under the plan to the participant as of that date (including principal credits that were credited before the applicable statutory effective date of paragraph (f)(1) of this section).

(ii) *Application to multiple annuity starting dates*. [Reserved].

(iii) *Exception for variable annuity benefit formulas*. See paragraph (b)(2)(iii)(B) of this section for an exception to this paragraph (d)(2).

(3) *Long-term investment grade corporate bonds*. For purposes of this paragraph (d), the rate of interest on long-term investment grade corporate bonds means the third segment rate described in section 417(e)(3)(D) or 430(h)(2)(C)(iii) (determined with or without regard to the transition rules of section 417(e)(3)(D)(ii) or 430(h)(2)(G)). However, for plan years beginning prior to January 1, 2008, the rate of interest on long-term investment grade corporate bonds means the rate described in section 412(b)(5)(B)(ii)(II) prior to amendment by the Pension Protection Act of 2006, Public Law 109–280 (120 Stat. 780) (PPA '06).

(4) *Safe harbor rates of interest*—(i) *In general*. This paragraph (d)(4) identifies interest rates that are deemed to be not in excess of the interest rate described in paragraph (d)(3) of this section. The Commissioner may, in guidance of general applicability, specify additional interest crediting rates that are deemed to be not in excess of the rate described in paragraph (d)(3) of this section. See §601.601(d)(2)(ii)(*b*).

(ii) *Rates based on bonds with margins*—(A) *In general*. An interest crediting rate is deemed to be not in excess of the interest rate described in paragraph (d)(3) of this section if the rate is equal to the sum of any of the following rates of interest for bonds and the associated margin for that interest rate:

Interest Rate Bond Index	**Associated Margin**
The discount rate on 3-month Treasury Bills	175 basis points
The discount rate on 12-month or shorter Treasury Bills	150 basis points
The yield on 1-year Treasury Constant Maturities	100 basis points
The yield on 3-year or shorter Treasury bonds	50 basis points
The yield on 7-year or shorter Treasury bonds	25 basis points
The yield on 30-year or shorter Treasury bonds	0 basis points
The first segment rate	0 basis points
The second segment rate	0 basis points

(B) *Rule of application*. For purposes of this paragraph (d)(4), the first and second segment rates mean the first and second segment rates described in section 417(e)(3)(D) or 430(h)(2)(C), determined with or without regard to the transition rules of section 417(e)(3)(D)(ii) or 430(h)(2)(G).

(iii) *Eligible cost-of-living indices*. An interest crediting rate is deemed to be not in excess of the interest rate described in paragraph (d)(3) of this section if the rate is adjusted no less frequently than annually and is equal to the rate of increase with respect to an eligible cost-of-living index described in §1.401(a)(9)–6, A–14(b), except that, for purposes of this paragraph (d)(4)(iii), the eligible cost-of-living index described in §1.401(a)(9)–6, A–14(b)(2) is increased by 300 basis points.

(iv) *Fixed rate of interest*. [Reserved].

(5) *Other rates of return*—(i) *General rule*. This paragraph (d)(5) sets forth additional methods for determining an interest crediting rate that is not in excess of a market rate of return.

(ii) *Actual rate of return on plan assets*. In the case of indexed benefits described in paragraph (b)(2) of this section, an interest crediting rate equal to the actual rate of return on the aggregate assets of the plan, including both positive returns and negative returns, is not in excess of a market rate of return if the plan's assets are diversified so as to minimize the volatility of returns. This requirement that plan assets be diversified so as to minimize the volatility of returns does not require greater diversification than is required under section 404(a)(1)(C) of Title I of the Employee Retirement Income Security Act of 1974, Public Law 93–406 (88 Stat. 829 (1974)) with respect to defined benefit pension plans.

(iii) *Annuity contract rates*. The rate of return on the annuity contract for the employee issued by an insurance company licensed under the laws of a State is not in excess of a market rate of return. However, this paragraph (d)(5)(iii) does not apply if the Commissioner determines that the annuity contract has been structured to provide an interest crediting rate that is in excess of a market rate of return.

(iv) *Rate of return on certain RICs*. [Reserved].

(6) *Combinations of rates of return*—(i) *In general*. A plan that determines interest credits based, in whole or in part, on the greater of two or more different interest crediting rates provides an effective interest crediting rate in excess of a market rate of return unless the combination of rates is described in paragraph (d)(6)(ii), (d)(6)(iii), (e)(3)(iii), or (e)(4) of this section. However, a plan is not treated as providing the greater of two or more interest crediting rates merely because the plan satisfies the requirements of paragraph (d)(2) of this section. In addition, a plan is not treated as providing the greater of two or more interest crediting rates merely because a rate of return described in paragraph (d)(5)(iii) of this section is itself based on the greater of two or more rates.

(ii) *Annual or more frequent floor applied to bond-based rates*. [Reserved].

(iii) *Cumulative floor applied to equity-based or bond-based rates*. [Reserved].

(e) *Other rules regarding market rates of return*—(1) *In general*. This paragraph (e) sets forth additional rules regarding the application of the market rate of return requirement with respect to benefits determined under a statutory hybrid benefit formula.

(2) *Plan termination*. [Reserved].

(3) *Rules relating to section 411(d)(6)*—(i) *General rule*. The right to interest credits in the future that are not conditioned on future service constitutes a section 411(d)(6) protected benefit (as defined in §1.411(d)–3(g)(14)). Thus, to the extent that benefits have accrued under the terms of a statutory hybrid plan that entitle the participant to future interest credits, an amendment to the plan to change the interest crediting rate must satisfy section 411(d)(6) if the revised rate under any circumstances could result in interest credits that are smaller as of any date after the applicable amendment date (within the meaning of §1.411(d)–3(g)(4)) than the interest credits that would be provided without regard to the amendment. For additional rules, see §1.411(d)–3(b). Paragraphs (e)(3)(ii) and (e)(3)(iii) of this section set forth special rules that apply regarding the interaction of section 411(d)(6) and changes to a plan's interest crediting rate. The Commissioner may, in guidance of general applicability, prescribe additional rules regarding the interaction of section 411(d)(6) and section 411(b)(5), including changes to a plan's interest crediting rate. See §601.601(d)(2)(ii)(*b*).

(ii) *Adoption of long-term investment grade corporate bond rate*. For purposes of applying section 411(d)(6) and this paragraph (e) to an amendment to change to the interest crediting rate described in paragraph (d)(3) of this section, a plan is not treated as providing interest credits that are smaller as of any date after the applicable amendment date than the interest credits that would be provided using an interest crediting rate described in paragraph (d)(4) of this section merely because the plan credits interest after the applicable amendment date using the interest crediting rate described in paragraph (d)(3) of this section, provided—

(A) The amendment only applies to interest credits to be credited after the effective date of the amendment;

(B) The effective date of the amendment is at least 30 days after adoption of the amendment; and

(C) On the effective date of the amendment, the new interest crediting rate is not lower than the interest crediting rate that would have applied in the absence of the amendment.

(iii) *Coordination of section 411(d)(6) and market rate of return limitation*. [Reserved].

(4) *Actuarial increases after normal retirement age*. [Reserved].

(f) *Effective/applicability date*—(1) *Statutory effective/applicability dates*—(i) *In general*. Except as provided in paragraph (f)(1)(iii) of this section, section 411(b)(5) applies for periods beginning on or after June 29, 2005.

(ii) *Conversion amendments*. The requirements of section 411(b)(5)(B)(ii), 411(b)(5)(B)(iii), and 411(b)(5)(B)(iv) apply to a conversion amendment (as defined in paragraph (c)(4) of this section) that both is adopted on or after June 29, 2005, and takes effect on or after June 29, 2005.

(iii) *Market rate of return*—(A) *Plans in existence on June 29, 2005*—(*1*) *In general*. In the case of a plan that was in existence on June 29, 2005 (regardless of whether the plan was a statutory hybrid plan on that date), section 411(b)(5)(B)(i) applies to plan years that begin on or after January 1, 2008.

(*2*) *Exception for plan sponsor election*. Notwithstanding paragraph (f)(1)(iii)(A)(*1*) of this section, a plan sponsor of a plan that was in existence on June 29, 2005 (regardless of whether the plan was a statutory hybrid plan on that date) may elect to have the requirements of section 411(a)(13)(B) and section 411(b)(5)(B)(i) apply for any period on or after June 29, 2005, and before the first plan year beginning after December 31, 2007. In accordance with section 1107 of the PPA '06, an employer is permitted to adopt an amendment to make this election as late as the last day of the first plan year that begins on or after January 1, 2009 (January 1, 2011, in the case of a governmental plan as defined in section 414(d)) if the plan operates in accordance with the election.

(B) *Plans not in existence on June 29, 2005*. In the case of a plan not in existence on June 29, 2005, section 411(b)(5)(B)(i) applies to the plan on and after the later of June 29, 2005, and the date the plan becomes a statutory hybrid plan.

(iv) *Collectively bargained plans*—(A) *In general*. Notwithstanding paragraph (f)(1)(iii) of this section, in the case of a collectively bargained plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified on or before August 17, 2006, the requirements of section 411(b)(5)(B)(i) do not apply to plan years that begin before the earlier of—

(*1*) The later of—

(*i*) The date on which the last of those collective bargaining agreements terminates (determined without regard to any extension thereof on or after August 17, 2006); or

(*ii*) January 1, 2008; or

(*2*) January 1, 2010.

(B) *Treatment of plans with both collectively bargained and non-collectively bargained employees*. In the case of a plan with respect to which a collective bargaining agreement applies to some, but not all, of the plan participants, the plan is considered a collectively bargained plan for purposes of this paragraph (f)(1)(iv) if it is considered a collectively bargained plan under the rules of §1.436–1(a)(5)(ii)(B).

(2) *Effective/applicability date of regulations*—(i) *In general*—(A) *General effective date*. Except as provided in paragraph (f)(2)(i)(B) of this section, this section applies to plan years that begin on or after January 1, 2011.

(B) *Special effective date*. Paragraphs (d)(1)(iii), (d)(1)(vi), and (d)(6)(i) of this section apply to plan years that begin on or after January 1, 2012.

(ii) *Conversion amendments*. With respect to a conversion amendment (within the meaning of paragraph (c)(4) of this section), where the effective date of the conversion amendment (as defined in paragraph (c)(4)(vi) of this section) is on or after the statutory effective date set forth in paragraph (f)(1)(ii) of this section, the requirements of paragraph (c)(2) of this section apply only to a participant who has an hour of service on or after the regulatory effective date set forth in paragraph (f)(2)(i) of this section.

(iii) *Reliance before regulatory effective date*. For the periods after the statutory effective date set forth in paragraph (f)(1) of this section and before the regulatory effective date set forth in paragraph (f)(2)(i) of this section, the safe harbor and other relief of section 411(b)(5) applies and the market rate of return and other requirements of section 411(b)(5) must be satisfied. During these periods, a plan is permitted to rely on the provisions of this section for purposes of applying the relief and satisfying the requirements of section 411(b)(5).

Steven T. Miller,
Deputy Commissioner for Services and Enforcement.

Approved September 17, 2010.

Michael F. Mundaca,
Assistant Secretary of the Treasury for Tax Policy.

(Filed by the Office of the Federal Register on October 18, 2010, 8:45 a.m., and published in the issue of the Federal Register for October 19, 2010, 75 F.R. 64123)

Part III. Administrative, Procedural, and Miscellaneous

Credit for Carbon Dioxide Sequestration 2010 Section 45Q Inflation Adjustment Factor

Notice 2010–75

SECTION 1. PURPOSE

This notice publishes the inflation adjustment factor for the credit for carbon dioxide (CO_2) sequestration under § 45Q of the Internal Revenue Code (§ 45Q credit) for calendar year 2010. The inflation adjustment factor is used to determine the amount of the credit allowable under § 45Q. The calendar year 2010 inflation-adjusted credit applies to the amount of qualified CO_2 captured by a taxpayer at a qualified facility and disposed of in secure geological storage.

SECTION 2. BACKGROUND

Section 45Q(a)(1) allows a credit of $20 per metric ton of qualified CO_2 that is captured by the taxpayer at a qualified facility, disposed of by the taxpayer in secure geological storage, and not used by the taxpayer as a tertiary injectant. Section 45Q(a)(2) allows a credit of $10 per metric ton of qualified CO_2 that is captured by the taxpayer at a qualified facility, used by the taxpayer as a tertiary injectant in a qualified enhanced oil or natural gas recovery project (EOR project), and disposed of by the taxpayer in secure geological storage.

Section 45Q(b)(1) defines the term "qualified carbon dioxide" as CO_2 captured from an industrial source that would otherwise be released into the atmosphere as industrial emission of greenhouse gas (GHG), and that is measured at the source of capture and verified at the point of disposal or injection. Qualified CO_2 includes the initial deposit of captured CO_2 used as a tertiary injectant but does not include CO_2 that is re-captured, recycled, or otherwise re-injected as part of the enhanced oil and natural gas recovery process.

Section 45Q(c) defines the term "qualified facility" as an industrial facility that is owned by the taxpayer, where carbon capture equipment is placed in service, and where at least 500,000 metric tons of CO_2 is captured during the taxable year.

Section 45Q(d)(2) provides that the Secretary, in consultation with the Administrator of the Environmental Protection Agency (EPA), the Secretary of Energy, and the Secretary of the Interior, shall establish regulations for determining adequate security measures for the geological storage of CO_2 under paragraph (1)(B) or (2)(C) of subsection (a) such that the CO_2 does not escape into the atmosphere. See section 5 of Notice 2009–83, 2009–44 I.R.B. 588, for procedures regarding secure geological storage.

Section 45Q(d)(5) allows the § 45Q credit to the person that captures and physically or contractually ensures the disposal of or the use as a tertiary injectant of the qualified CO_2, except to the extent provided in regulations prescribed by the Secretary.

Under § 45Q(d)(7), for taxable years beginning in a calendar year after 2009, the dollar amount contained in § 45Q(a) must be adjusted for inflation by multiplying such dollar amount by the inflation adjustment factor for such calendar year determined under § 43(b)(3)(B), determined by substituting "2008" for "1990."

Section 43(b)(3)(B) defines "inflation adjustment factor" as, with respect to any calendar year, a fraction the numerator of which is the GNP implicit price deflator for the preceding calendar year and the denominator of which is the GNP implicit price deflator for 1990. For purposes of § 45Q(d)(7), with respect to 2010 calendar year, the inflation adjustment factor is a fraction the numerator of which is the GNP implicit price deflator for 2009 (109.764) and the denominator of which is the GNP implicit price deflator for 2008 (108.486).

Section 45Q(e) provides that the § 45Q credit will apply with respect to qualified CO_2 before the end of the calendar year in which the Secretary, in consultation with the EPA, certifies that 75,000,000 metric tons of qualified CO_2 have been taken into account in accordance with § 45Q(a).

SECTION 3. INFLATION ADJUSTMENT FACTOR

The inflation adjustment factor for calendar year 2010 is 1.0118. The 45Q credit for calendar year 2010 is $20.24 per metric ton of qualified CO_2 under § 45Q(a)(1) and $10.12 per metric ton of qualified CO_2 under § 45Q(a)(2).

SECTION 4. DRAFTING INFORMATION

The principal author of this notice is Jennifer C. Bernardini of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this notice, contact Jennifer C. Bernardini at (202) 622–3110 (not a toll-free call).

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26 CFR 601.601: Rules and regulations.
(Also Part I, §§ 6109; 1.6109–2.)

Rev. Proc. 2010–41

SECTION 1. PURPOSE

The purpose of this revenue procedure is to (1) describe the procedures foreign persons and U.S. citizens without a social security number due to conscientious religious objection must follow to obtain a preparer tax identification number (PTIN) and (2) provide temporary relief during the 2011 filing season for these individuals who experience delay in obtaining PTINs.

SECTION 2. BACKGROUND

On September 30, 2010, the Treasury Department and the IRS published final regulations in the **Federal Register**, T.D. 9501, 2010–46 I.R.B. 651 [75 FR 60309], requiring paid tax return preparers who prepare all or substantially all of a tax return or claim for refund to register with the IRS to obtain PTINs. The IRS also announced that the online PTIN application system and paper application, Form W-12, *IRS Paid Preparer Tax Identification Number (PTIN) Application*, are available for tax return preparers to apply for a PTIN.

Both the online system and the Form W-12 generally require an individual to submit a valid social security number to obtain a PTIN. The IRS recognizes, however, that some tax return preparers required to obtain a PTIN may not have a social security number. In particular, a foreign person (who, for example, may prepare returns for United States taxpayers living in a foreign country) may not have a social security number and may not be eligible to obtain one. Similarly, a U.S. citizen may not have a social security number due to a conscientious religious objection to applying for and receiving a social security number.

SECTION 3. SCOPE

This revenue procedure supplements the final regulations under section 1.6109–2, which require a paid tax return preparer to register with the IRS and obtain a PTIN, by providing a mechanism by which a foreign person and a U.S. citizen without a social security number due to conscientious religious objection may obtain a PTIN. For purposes of this revenue procedure, a foreign person is an individual who does not have, and is not eligible to obtain, a social security number and is neither a citizen of the United States nor a resident alien of the United States as defined in section 7701(b)(1)(A). For purposes of this revenue procedure, a U.S. citizen without a social security number due to conscientious religious objection is a member of a recognized religious group. A recognized religious group is a religious group conscientiously opposed to its members applying for, and receiving, social security numbers that has existed continuously since December 31, 1950. Section 4 of this revenue procedure only applies to tax return preparers who are foreign persons or U.S. citizens without a social security number due to conscientious religious objection. Section 5 of this revenue procedure only applies to tax return preparers who are foreign persons or U.S. citizens without a social security number due to conscientious religious objection during the 2011 filing season.

SECTION 4. GENERAL PTIN PROCEDURES FOR TAX RETURN PREPARERS WHO ARE FOREIGN PERSONS OR U.S. CITIZENS WITHOUT A SOCIAL SECURITY NUMBER DUE TO CONSCIENTIOUS RELIGIOUS OBJECTION

Tax return preparers who are foreign persons or U.S. citizens without a social security number due to conscientious religious objection may apply for a PTIN using a two-part process. Both parts of the process must be completed before a PTIN will be issued. To obtain a PTIN, a tax return preparer who is a foreign person or a U.S. citizen without a social security number due to conscientious religious objection first must complete either the online PTIN application or the paper Form W-12. Second, a foreign person must provide a completed Form 8946, *PTIN Supplemental Application for Foreign Persons Without a Social Security Number,* which is a paper form. A U.S. citizen without a social security number due to conscientious religious objection must provide a completed Form 8945, *PTIN Supplemental Application for U.S. Citizens Without a Social Security Number Due To Conscientious Religious Objection*, which is a paper form. Additional documentation must be submitted with the Forms 8945 and 8946, as required by the instructions to the forms. Forms W-12, 8945 and 8946 and the accompanying instructions are available on *http://www.IRS.gov.*

SECTION 5. RELIEF FOR 2011 FILING SEASON

The IRS expects tax return preparers who are foreign persons or U.S. citizens without a social security number due to conscientious religious objection to apply for PTINs as soon as reasonably possible. The IRS recognizes, however, that the two-step application process for these individuals may take substantially more time to complete than the application process available for tax return preparers with social security numbers. In some cases, circumstances outside of the control of the foreign person or U.S. citizen without a social security number due to conscientious religious objection may delay the ability to submit a timely, complete application. For example, it may be difficult for these tax return preparers to obtain the additional documentation required to complete the Forms 8945 or 8946.

Accordingly, for purposes of the 2011 filing season, tax return preparers who are foreign persons or U.S. citizens without a social security number due to conscientious religious objection will be considered to have complied with the requirement to obtain a PTIN set forth in the final regulations under section 1.6109–2 if they complete the online application or submit a completed paper Form W-12 by the later of (1) January 31, 2011, or (2) 10 days after the first day on which they prepare all or substantially all of a U.S. tax return for compensation, and they submit a completed PTIN supplemental application, Form 8945 or Form 8946, including any required additional documentation, within 60 days after the completion of the online application or submission of the paper Form W-12. The applicable PTIN user fee must be submitted with the online application or paper Form W-12. Tax return preparers who are foreign persons or U.S. citizens without a social security number due to conscientious religious objection who have not obtained a PTIN but are considered to be in compliance with section 6109 under this revenue procedure may prepare and sign U.S. tax returns and claims for refund as a paid tax return preparer without furnishing a PTIN or other identifying number for returns prepared on or before October 31, 2011.

SECTION 6. EFFECTIVE DATES

This revenue procedure is effective October 26, 2010. Section 5 of this revenue procedure will be obsolete after October 31, 2011.

SECTION 7. DRAFTING INFORMATION

The principal author of this revenue procedure is Matthew D. Lucey of the Office of Associate Chief Counsel (Procedure & Administration). For further information regarding this revenue procedure, contact Matthew D. Lucey at (202) 622–4940 (not a toll-free call).

Part IV. Items of General Interest

Notice of Proposed Rulemaking and Notice of Public Hearing

Additional Rules Regarding Hybrid Retirement Plans

REG–132554–08

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations providing guidance relating to certain provisions of the Internal Revenue Code (Code) that apply to hybrid defined benefit pension plans. These regulations would provide guidance on changes made by the Pension Protection Act of 2006, as amended by the Worker, Retiree, and Employer Recovery Act of 2008. These regulations would affect sponsors, administrators, participants, and beneficiaries of hybrid defined benefit pension plans. This document also provides a notice of a public hearing on these proposed regulations.

DATES: Written or electronic comments must be received by Wednesday, January 12, 2011. Outlines of topics to be discussed at the public hearing scheduled for Wednesday, January 26, 2011, at 10 a.m. must be received by Friday, January 14, 2011.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–132554–08), Room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG–132554–08), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically, via the Federal eRulemaking Portal at *http://www.regulations.gov* (IRS REG–132554–08). The public hearing will be held in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Neil S. Sandhu, Lauson C. Green, or Linda S. F. Marshall at (202) 622–6090; concerning submissions of comments, the hearing, and/or being placed on the building access list to attend the hearing, Regina Johnson, at (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Income Tax Regulations (26 CFR part 1) under sections 411(a)(13), 411(b)(1), and 411(b)(5) of the Code. Generally, a defined benefit pension plan must satisfy the minimum vesting standards of section 411(a) and the accrual requirements of section 411(b) in order to be qualified under section 401(a) of the Code. Sections 411(a)(13) and 411(b)(5), which modify the minimum vesting standards of section 411(a) and the accrual requirements of section 411(b), were added to the Code by section 701(b) of the Pension Protection Act of 2006, Public Law 109–280 (120 Stat. 780 (2006)) (PPA '06). Sections 411(a)(13) and 411(b)(5), as well as certain effective date provisions related to these sections, were subsequently amended by the Worker, Retiree, and Employer Recovery Act of 2008, Public Law 110–458 (122 Stat. 5092 (2008)) (WRERA '08).

Section 411(a)(13)(A) provides that an applicable defined benefit plan (which is defined in section 411(a)(13)(C)) is not treated as failing to meet either (i) the requirements of section 411(a)(2) (subject to a special vesting rule in section 411(a)(13)(B) with respect to benefits derived from employer contributions) or (ii) the requirements of section 411(a)(11), 411(c), or 417(e), with respect to accrued benefits derived from employer contributions, merely because the present value of the accrued benefit (or any portion thereof) of any participant is, under the terms of the plan, equal to the amount expressed as the balance of a hypothetical account or as an accumulated percentage of the participant's final average compensation. Section 411(a)(13)(B) requires an applicable defined benefit plan to provide that an employee who has completed at least 3 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from employer contributions.

Under section 411(a)(13)(C)(i), an applicable defined benefit plan is defined as a defined benefit plan under which the accrued benefit (or any portion thereof) of a participant is calculated as the balance of a hypothetical account maintained for the participant or as an accumulated percentage of the participant's final average compensation. Under section 411(a)(13)(C)(ii), the Secretary of the Treasury is to issue regulations which include in the definition of an applicable defined benefit plan any defined benefit plan (or portion of such a plan) which has an effect similar to a plan described in section 411(a)(13)(C)(i).

Section 411(a) requires that a defined benefit plan satisfy the requirements of section 411(b)(1). Section 411(b)(1) provides that a defined benefit plan must satisfy one of the three accrual rules of section 411(b)(1)(A), (B), and (C) with respect to benefits accruing under the plan. The three accrual rules are the 3 percent method of section 411(b)(1)(A), the 133$^1/_3$ percent rule of section 411(b)(1)(B), and the fractional rule of section 411(b)(1)(C).

Section 411(b)(1)(B) provides that a defined benefit plan satisfies the requirements of the 133$^1/_3$ percent rule for a particular plan year if, under the plan, the accrued benefit payable at the normal retirement age is equal to the normal retirement benefit, and the annual rate at which any individual who is or could be a participant can accrue the retirement benefits payable at normal retirement age under the plan for any later plan year is not more than 133$^1/_3$ percent of the annual rate at which the individual can accrue benefits for any plan year beginning on or after such particular plan year and before such later plan year.

For purposes of applying the 133$^1/_3$ percent rule, section 411(b)(1)(B)(i) provides that any amendment to the plan which is in effect for the current year is treated as in effect for all other plan years. Section 411(b)(1)(B)(ii) provides that any change in an accrual rate which does not apply to any individual who is or could be a participant in the current plan year is disregarded. Section 411(b)(1)(B)(iii) provides that the fact that benefits under the plan may be payable to certain participants before normal retirement age is disregarded. Section 411(b)(1)(B)(iv) provides that social security benefits and all other relevant factors used to compute benefits are treated as remaining constant as of the current plan year for all years after the current year.

Section 411(b)(1)(H)(i) provides that a defined benefit plan fails to comply with section 411(b) 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. Section 411(b)(5), which was added to the Code by section 701(b)(1) of PPA '06, provides additional rules related to section 411(b)(1)(H)(i). Section 411(b)(5)(A) generally provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) if a participant's accrued benefit, as determined as of any date under the terms of the plan, would be equal to or greater than that of any similarly situated, younger individual who is or could be a participant. For this purpose, section 411(b)(5)(A)(iv) provides that the accrued benefit may, under the terms of the plan, be expressed as an annuity payable at normal retirement age, the balance of a hypothetical account, or the current value of the accumulated percentage of the employee's final average compensation. Section 411(b)(5)(G) provides that, for purposes of section 411(b)(5), any reference to the accrued benefit of a participant refers to the participant's benefit accrued to date.

Section 411(b)(5)(B) imposes certain requirements on an applicable defined benefit plan in order for the plan to satisfy section 411(b)(1)(H). Section 411(b)(5)(B)(i) provides that such a plan is treated as failing to meet the requirements of section 411(b)(1)(H) if the terms of the plan provide for an interest credit (or an equivalent amount) for any plan year at a rate that is greater than a market rate of return. Under section 411(b)(5)(B)(i)(I), a plan is not treated as having an above-market rate merely because the plan provides for a reasonable minimum guaranteed rate of return or for a rate of return that is equal to the greater of a fixed or variable rate of return. Section 411(b)(5)(B)(i)(II) provides that an applicable defined benefit plan is treated as failing to meet the requirements of section 411(b)(1)(H) unless the plan provides that an interest credit (or an equivalent amount) of less than zero can in no event result in the account balance or similar amount being less than the aggregate amount of contributions credited to the account. Section 411(b)(5)(B)(i)(III) authorizes the Secretary of the Treasury to provide by regulation for rules governing the calculation of a market rate of return for purposes of section 411(b)(5)(B)(i)(I) and for permissible methods of crediting interest to the account (including fixed or variable interest rates) resulting in effective rates of return meeting the requirements of section 411(b)(5)(B)(i)(I).

Sections 411(b)(5)(B)(ii), 411(b)(5)(B)(iii), and 411(b)(5)(B)(iv) contain additional requirements that apply if, after June 29, 2005, an applicable plan amendment is adopted. Section 411(b)(5)(B)(v)(I) defines an applicable plan amendment as an amendment to a defined benefit plan which has the effect of converting the plan to an applicable defined benefit plan. Under section 411(b)(5)(B)(ii), if, after June 29, 2005, an applicable plan amendment is adopted, the plan is treated as failing to meet the requirements of section 411(b)(1)(H) unless the requirements of section 411(b)(5)(B)(iii) are met with respect to each individual who was a participant in the plan immediately before the adoption of the amendment. Section 411(b)(5)(B)(iii) specifies that, subject to section 411(b)(5)(B)(iv), the requirements of section 411(b)(5)(B)(iii) are met with respect to any participant if the accrued benefit of the participant under the terms of the plan as in effect after the amendment is not less than the sum of: (I) the participant's accrued benefit for years of service before the effective date of the amendment, determined under the terms of the plan as in effect before the amendment; plus (II) the participant's accrued benefit for years of service after the effective date of the amendment, determined under the terms of the plan as in effect after the amendment. Section 411(b)(5)(B)(iv) provides that, for purposes of section 411(b)(5)(B)(iii)(I), the plan must credit the participant's account or similar amount with the amount of any early retirement benefit or retirement-type subsidy for the plan year in which the participant retires if, as of such time, the participant has met the age, years of service, and other requirements under the plan for entitlement to such benefit or subsidy.

Section 411(b)(5)(B)(v) sets forth certain provisions related to an applicable plan amendment. Section 411(b)(5)(B)(v)(II) provides that if the benefits under two or more defined benefit plans of an employer are coordinated in such a manner as to have the effect of adoption of an applicable plan amendment, the plan sponsor is treated as having adopted an applicable plan amendment as of the date the coordination begins. Section 411(b)(5)(B)(v)(III) directs the Secretary of the Treasury to issue regulations to prevent the avoidance of the purposes of section 411(b)(5)(B) through the use of two or more plan amendments rather than a single amendment.

Section 411(b)(5)(B)(vi) provides special rules for determining benefits upon termination of an applicable defined benefit plan. Under section 411(b)(5)(B)(vi)(I), an applicable defined benefit plan is not treated as satisfying the requirements of section 411(b)(5)(B)(i) (regarding permissible interest crediting rates) unless the plan provides that, upon plan termination, if the interest crediting rate under the plan is a variable rate, the rate of interest used to determine accrued benefits under the plan is equal to the average of the rates of interest used under the plan during the 5-year period ending on the termination date. In addition, under section 411(b)(5)(B)(vi)(II), the plan must provide that, upon plan termination, the interest rate and mortality table used to determine the amount of any benefit under the plan payable in the form of an annuity payable at normal retirement age is the rate and table specified under the plan for this purpose as of the termination date, except that if the interest rate is a variable rate, the rate used is the average of the rates used under the plan during the 5-year period ending on the termination date.

Section 411(b)(5)(C) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H)(i) solely because the plan provides offsets against benefits under the plan to the extent the offsets are otherwise allowable in applying the requirements of section 401(a). Section 411(b)(5)(D) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides a disparity in contributions or benefits with respect to which the requirements of section 401(l) (relating to permitted disparity for Social Security benefits and related matters) are met.

Section 411(b)(5)(E) provides that a plan is not treated as failing to meet the requirements of section 411(b)(1)(H) solely because the plan provides for indexing of accrued benefits under the plan. Under section 411(b)(5)(E)(iii), indexing means the periodic adjustment of the accrued benefit by means of the application of a recognized investment index or methodology. Section 411(b)(5)(E)(ii) requires that, except in the case of a variable annuity, the indexing not result in a smaller benefit than the accrued benefit determined without regard to the indexing.

Section 701(a) of PPA '06 added provisions to the Employee Retirement Income Security Act of 1974, Public Law 93–406 (88 Stat. 829 (1974)) (ERISA), that are parallel to sections 411(a)(13) and 411(b)(5) of the Code. The guidance provided in these regulations with respect to sections 411(a)(13) and 411(b)(5) of the Code would also apply for purposes of the parallel amendments to ERISA made by section 701(a) of PPA '06, and the guidance provided in these regulations with respect to section 411(b)(1) of the Code would also apply for purposes of section 204(b)(1) of ERISA.[1]

Section 701(c) of PPA '06 added provisions to the Age Discrimination in Employment Act of 1967, Public Law 90–202 (81 Stat. 602 (1967)), that are parallel to section 411(b)(5) of the Code. Executive Order 12067 requires all Federal departments and agencies to advise and offer to consult with the Equal Employment Opportunity Commission (EEOC) during the development of any proposed rules, regulations, policies, procedures, or orders concerning equal employment opportunity. The Treasury Department and the IRS have consulted with the EEOC prior to the issuance of these regulations.

Section 701(d) of PPA '06 provides that nothing in the amendments made by section 701 should be construed to create an inference concerning the treatment of applicable defined benefit plans or conversions of plans into applicable defined benefit plans under section 411(b)(1)(H), or concerning the determination of whether an applicable defined benefit plan fails to meet the requirements of section 411(a)(2), 411(c), or 417(e), as in effect before such amendments, solely because the present value of the accrued benefit (or any portion thereof) of any participant is, under the terms of the plan, equal to the amount expressed as the balance of a hypothetical account or as an accumulated percentage of the participant's final average compensation.

Section 701(e) of PPA '06 sets forth the effective date provisions with respect to amendments made by section 701 of PPA '06. Section 701(e)(1) specifies that the amendments made by section 701 generally apply to periods beginning on or after June 29, 2005. Thus, the age discrimination safe harbors under section 411(b)(5)(A) and section 411(b)(5)(E) are effective for periods beginning on or after June 29, 2005. Section 701(e)(2) provides that the special present value rules of section 411(a)(13)(A) are effective for distributions made after August 17, 2006 (the date PPA '06 was enacted).

Under section 701(e) of PPA '06, the 3-year vesting rule under section 411(a)(13)(B) is generally effective for years beginning after December 31, 2007, for a plan in existence on June 29, 2005, while, pursuant to the amendments made by section 107(c) of WRERA '08, the rule is generally effective for plan years ending on or after June 29, 2005, for a plan not in existence on June 29, 2005. The market rate of return limitation under section 411(b)(5)(B)(i) is generally effective for years beginning after December 31, 2007, for a plan in existence on June 29, 2005, while the limitation is generally effective for periods beginning on or after June 29, 2005, for a plan not in existence on June 29, 2005. Section 701(e)(4) of PPA '06 contains special effective date provisions for collectively bargained plans that modify these effective dates.

Under section 701(e)(5) of PPA '06, as amended by WRERA '08, sections 411(b)(5)(B)(ii), (iii), and (iv) apply to a conversion amendment that is adopted on or after, and takes effect on or after, June 29, 2005.

Under section 701(e)(6) of PPA '06, as added by WRERA '08, the 3-year vesting rule under section 411(a)(13)(B) does not apply to a participant who does not have an hour of service after the date the 3-year vesting rule would otherwise be effective.

Section 702 of PPA '06 provides for regulations to be prescribed by August 16, 2007, addressing the application of rules set forth in section 701 of PPA '06 where the conversion of a defined benefit pension plan into an applicable defined benefit plan is made with respect to a group of employees who become employees by reason of a merger, acquisition, or similar transaction.

Under section 1107 of PPA '06, a plan sponsor is permitted to delay adopting a plan amendment pursuant to statutory provisions under PPA '06 (or pursuant to any regulation issued under PPA '06) until the last day of the first plan year beginning on or after January 1, 2009 (January 1, 2011, in the case of governmental plans). As described in Rev. Proc. 2007–44, 2007–2 C.B. 54, this amendment deadline applies to both interim and discretionary amendments that are made pursuant to PPA '06 statutory provisions or any regulation issued under PPA '06. See §601.601(d)(2)(ii)(*b*).

Section 1107 of PPA '06 also permits certain amendments to reduce or eliminate section 411(d)(6) protected benefits. Except to the extent permitted under section 1107 of PPA '06 (or under another statutory provision, including section 411(d)(6) and §§1.411(d)–3 and 1.411(d)–4), section 411(d)(6) prohibits a plan amendment that decreases a participant's accrued benefits or that has the effect of eliminating or reducing an early retirement benefit or retirement-type subsidy, or eliminating an optional form of benefit, with respect to benefits attributable to service before the amendment. However, an amendment that eliminates or decreases benefits that have

[1] Under section 101 of Reorganization Plan No. 4 of 1978 (43 FR 47713), the Secretary of the Treasury has interpretive jurisdiction over the subject matter addressed by these regulations for purposes of ERISA, as well as the Code.

not yet accrued does not violate section 411(d)(6), provided that the amendment is adopted and effective before the benefits accrue. If section 1107 of PPA '06 applies to an amendment of a plan, section 1107 provides that the plan does not fail to meet the requirements of section 411(d)(6) by reason of such amendment, except as provided by the Secretary of the Treasury.

Section 1.411(b)–1(a)(1) of the Treasury Regulations provides that a defined benefit plan is not a qualified plan unless the method provided by the plan for determining accrued benefits satisfies at least one of the alternative methods in §1.411(b)–1(b) for determining accrued benefits with respect to all active participants under the plan. Section 1.411(b)–1(b)(2)(i) provides that a defined benefit plan satisfies the 133$\frac{1}{3}$ percent rule of section 411(b)(1)(B) for a particular plan year if (A) under the plan the accrued benefit payable at the normal retirement age (determined under the plan) is equal to the normal retirement benefit (determined under the plan), and (B) the annual rate at which any individual who is or could be a participant can accrue the retirement benefits payable at normal retirement age under the plan for any later plan year cannot be more than 133$\frac{1}{3}$ percent of the annual rate at which the participant can accrue benefits for any plan year beginning on or after such particular plan year and before such later plan year. Section 1.411(b)–1(b)(2)(ii)(A) through (D) sets forth a series of rules that correspond to the rules of section 411(b)(1)(B)(i) through (iv). Section 1.411(b)–1(b)(2)(ii)(D) provides that, for purposes of the 133$\frac{1}{3}$ percent rule, for any plan year, social security benefits and all relevant factors used to compute benefits, *e.g.*, consumer price index, are treated as remaining constant as of the beginning of the current plan year for all subsequent plan years.

Proposed regulations (EE–184–86) under sections 411(b)(1)(H) and 411(b)(2) were published by the Treasury Department and the IRS in the **Federal Register** on April 11, 1988 (53 FR 11876), as part of a package of regulations that also included proposed regulations under sections 410(a), 411(a)(2), 411(a)(8), and 411(c) (relating to the maximum age for participation, vesting, normal retirement age, and actuarial adjustments after normal retirement age, respectively).[2]

Notice 96–8, 1996–1 C.B. 359, see §601.601(d)(2)(ii)(*b*), described the application of sections 411 and 417(e)(3) to a single-sum distribution under a cash balance plan where interest credits under the plan are frontloaded (that is, where future interest credits to an employee's hypothetical account balance are not conditioned upon future service and thus accrue at the same time that the benefits attributable to a hypothetical allocation to the account accrue). Under the analysis set forth in Notice 96–8, in order to comply with sections 411(a) and 417(e)(3) in calculating the amount of a single-sum distribution under a cash balance plan, the balance of an employee's hypothetical account must be projected to normal retirement age and converted to an annuity under the terms of the plan, and then the employee must be paid at least the present value of the projected annuity, determined in accordance with section 417(e). Under that analysis, where a cash balance plan provides frontloaded interest credits using an interest rate that is higher than the section 417(e) applicable interest rate, payment of a single-sum distribution equal to the current hypothetical account balance as a complete distribution of the employee's accrued benefit may result in a violation of the minimum present value requirements of section 417(e) or a forfeiture in violation of section 411(a). In addition, Notice 96–8 proposed a safe harbor which provided that, if frontloaded interest credits are provided under a plan at a rate no greater than the sum of identified standard indices and associated margins, no violation of section 411(a) or 417(e) would result if the employee's entire accrued benefit were to be distributed in the form of a single-sum distribution equal to the employee's hypothetical account balance, provided the plan uses appropriate annuity conversion factors. Since the issuance of Notice 96–8, four Federal appellate courts have followed the analysis set out in the notice: *Esden v. Bank of Boston*, 229 F.3d 154 (2d Cir. 2000), *cert. dismissed*, 531 U.S. 1061 (2001); *West v. AK Steel Corp. Ret. Accumulation Pension Plan*, 484 F.3d 395 (6th Cir. 2007), *cert. denied*, 129 S. Ct. 895 (2009); *Berger v. Xerox Corp. Ret. Income Guarantee Plan*, 338 F.3d 755 (7th Cir. 2003), *reh'g and reh'g en banc denied*, No. 02–3674, 2003 U.S. App. LEXIS 19374 (7th Cir. Sept. 15, 2003); *Lyons v. Georgia-Pacific Salaried Employees Ret. Plan*, 221 F.3d 1235 (11th Cir. 2000), *cert. denied*, 532 U.S. 967 (2001).

Notice 2007–6, 2007–1 C.B. 272, see §601.601(d)(2)(ii)(*b*), provides transitional guidance with respect to certain requirements of sections 411(a)(13) and 411(b)(5) and section 701(b) of PPA '06. Notice 2007–6 includes certain special definitions, including: accumulated benefit, which is defined as a participant's benefit accrued to date under a plan; lump sum-based plan, which is defined as a defined benefit plan under the terms of which the accumulated benefit of a participant is expressed as the balance of a hypothetical account maintained for the participant or as the current value of the accumulated percentage of the participant's final average compensation; and statutory hybrid plan, which is defined as a lump sum-based plan or a plan which has an effect similar to a lump sum-based plan. Notice 2007–6 provides guidance on a number of issues, including a rule under which a plan that provides for indexed benefits described in section 411(b)(5)(E) is a statutory hybrid plan (because it has an effect similar to a lump sum-based plan), unless the plan either solely provides for post-retirement adjustment of the amounts payable to a participant or is a variable annuity plan under which the assumed interest rate used to determine adjustments is at least 5 percent. Notice 2007–6 provides a safe harbor for applying the rules set forth in section 701 of PPA '06 where the conversion of a defined benefit pension plan into an applicable defined benefit plan is made with respect to a group of employees who become employees by reason of a merger, acquisition, or similar

[2] On December 11, 2002, the Treasury Department and the IRS issued proposed regulations regarding the age discrimination requirements of section 411(b)(1)(H) that specifically addressed cash balance plans as part of a package of regulations that also addressed section 401(a)(4) nondiscrimination cross-testing rules applicable to cash balance plans (67 FR 76123). The 2002 proposed regulations were intended to replace the 1988 proposed regulations. In Ann. 2003–22, 2003–1 C.B. 847, see §601.601(d)(2)(ii)(*b*), the Treasury Department and the IRS announced the withdrawal of the 2002 proposed regulations under section 401(a)(4), and in Ann. 2004–57, 2004–2 C.B. 15, see §601.601(d)(2)(ii)(*b*), the Treasury Department and the IRS announced the withdrawal of the 2002 proposed regulations relating to age discrimination.

transaction. This transitional guidance, along with the other guidance provided in Part III of Notice 2007–6, applies pending the issuance of further guidance and, thus, does not apply for periods to which the 2010 final regulations (as described later in this preamble) apply.

Proposed regulations (REG–104946–07, 2008–1 C.B. 596) under sections 411(a)(13) and 411(b)(5) (2007 proposed regulations) were published by the Treasury Department and the IRS in the **Federal Register** on December 28, 2007 (72 FR 73680). The Treasury Department and the IRS received written comments on the 2007 proposed regulations and a public hearing was held on June 6, 2008.

Proposed regulations (REG–100464–08, 2008–2 C.B. 313) under section 411(b)(1)(B) (2008 proposed backloading regulations) were published by the Treasury Department and the IRS in the **Federal Register** on June 18, 2008 (73 FR 34665). The 2008 proposed backloading regulations would provide guidance on the application of the accrual rule for defined benefit plans under section 411(b)(1)(B) in cases where plan benefits are determined on the basis of the greatest of two or more separate formulas. The Treasury Department and the IRS received written comments on the 2008 proposed backloading regulations and a public hearing was held on October 15, 2008.

Announcement 2009–82, 2009–2 C.B. 720, and Notice 2009–97, 2009–2 C.B. 972, announced certain expected relief with respect to the requirements of section 411(b)(5). In particular, Announcement 2009–82 stated that the rules in the regulations specifying permissible market rates of return are not expected to go into effect before the first plan year that begins on or after January 1, 2011. In addition, Notice 2009–97 stated that, once final regulations under sections 411(a)(13) and 411(b)(5) are issued, it is expected that relief from the requirements of section 411(d)(6) will be granted for a plan amendment that eliminates or reduces a section 411(d)(6) protected benefit, provided that the amendment is adopted by the last day of the first plan year that begins on or after January 1, 2010, and the elimination or reduction is made only to the extent necessary to enable the plan to meet the requirements of section 411(b)(5).[3] Notice 2009–97 also extended the deadline for amending cash balance and other applicable defined benefit plans, within the meaning of section 411(a)(13)(C), to meet the requirements of section 411(a)(13) (other than section 411(a)(13)(A)) and section 411(b)(5), relating to vesting and other special rules applicable to these plans. Under Notice 2009–97, the deadline for these amendments is the last day of the first plan year that begins on or after January 1, 2010.

Final regulations (2010 final regulations) under sections 411(a)(13) and 411(b)(5) are being issued at the same time as these proposed regulations. The 2010 final regulations adopt most of the provisions of the 2007 proposed regulations, with certain modifications, and also reserve a number of sections relating to issues that are not addressed in those final regulations. These reserved issues relate to the scope of relief provided under section 411(a)(13)(A), a potential alternative method of satisfying the conversion protection requirements, additional rules with respect to the market rate of return requirement, and the application of the special plan termination rules. These proposed regulations generally address these issues, as well as an issue under section 411(b)(1).

Explanation of Provisions

Overview

In general, these proposed regulations would provide guidance with respect to certain issues under sections 411(a)(13) and 411(b)(5) that are not addressed in the 2010 final regulations, as well as an issue under section 411(b)(1) for hybrid defined benefit plans that adjust benefits using a variable rate.

I. *Section 411(a)(13): Scope of relief of section 411(a)(13)(A)*

A. *The 2010 final regulations*

The 2010 final regulations define a lump sum-based benefit formula as a benefit formula used to determine all or any part of a participant's accumulated benefit under which the accumulated benefit provided under the formula is expressed as the current balance of a hypothetical account maintained for the participant or as the current value of an accumulated percentage of the participant's final average compensation. The 2010 final regulations provide that the relief of section 411(a)(13)(A) applies to the benefits determined under a lump sum-based benefit formula.

B. *Limitations on the relief of section 411(a)(13)(A)*

The proposed regulations would provide that the relief of section 411(a)(13)(A) does not apply with respect to the benefits determined under a lump sum-based benefit formula unless certain requirements are satisfied. In particular, the proposed regulations would provide that the relief does not apply unless, at all times on or before normal retirement age, the then-current hypothetical account balance or the then-current accumulated percentage of the participant's final average compensation is not less than the present value, determined using reasonable actuarial assumptions, of the portion of the participant's accrued benefit that is determined under the lump sum-based benefit formula. However, the plan would be deemed to satisfy this requirement for periods before normal retirement age if, upon attainment of normal retirement age, the then-current balance of the hypothetical account or the then-current value of the accumulated percentage of the participant's final average compensation is actuarially equivalent (using reasonable actuarial assumptions) to the portion of the participant's accrued benefit that is determined under the lump sum-based benefit formula. Thus, for periods before normal retirement age, a statutory hybrid plan with a lump sum-based benefit formula that meets the requirements of the preceding sentence need not project interest credits to normal retirement age and discount the resulting accrued benefit back in order to apply the relief of section 411(a)(13)(A) with respect to the benefit determined under the lump sum-based benefit formula.

In addition, the proposed regulations would provide that the relief of section 411(a)(13)(A) does not apply unless, as of

[3] However, see footnote 6 in Section IV.C of this preamble.

each annuity starting date after normal retirement age, the then-current balance of the hypothetical account or the then-current value of the accumulated percentage of the participant's final average compensation satisfies the requirements of section 411(a)(2) or would satisfy those requirements but for the fact that the plan suspends benefits in accordance with section 411(a)(3)(B). Thus, for example, a plan that expresses the accumulated benefit as the balance of a hypothetical account and that does not comply with the suspension of benefit rules may have difficulty obtaining the relief of section 411(a)(13)(A) if, after normal retirement age, the plan credits interest at such a low rate that the adjustments provided by the interest credits, together with any principal credits, are insufficient to provide any required actuarial increases.

The proposed regulations would also provide that the relief of section 411(a)(13)(A) does not apply unless the balance of the hypothetical account or the accumulated percentage of the participant's final average compensation may not be reduced except as a result of one of the specified reasons set forth in the regulations. Under the proposed regulations, reductions would only be permissible as a result of: (1) benefit payments, (2) qualified domestic relations orders under section 414(p), (3) forfeitures that are permitted under section 411(a) (such as charges for providing a qualified preretirement survivor annuity), (4) amendments that are permitted under section 411(d)(6), and (5) adjustments resulting from the application of interest credits (under the rules of §1.411(b)(5)–1) that are negative for a period, for plans that express the accumulated benefit as the balance of a hypothetical account.

C. *Application of section 411(a)(13)(A) to distributions other than single sums*

The proposed regulations would provide that the relief under section 411(a)(13)(A) (with respect to the requirements of sections 411(a)(2), 411(c), and 417(e)) extends to certain other forms of benefit under a lump sum-based benefit formula, in addition to a single-sum payment of the entire benefit. In particular, the proposed regulations would clarify that the relief provided under section 411(a)(13)(A) extends to an optional form of benefit that is currently payable with respect to a lump sum-based benefit formula if, under the terms of the plan, the optional form of benefit is determined as of the annuity starting date as the actuarial equivalent, determined using reasonable actuarial assumptions, of the then-current balance of the hypothetical account or the then-current value of an accumulated percentage of the participant's final average compensation.

In addition, the proposed regulations would create a special rule that provides that the relief under section 411(a)(13)(A) also extends to an optional form of benefit that is not subject to the minimum present value requirements of section 417(e) and that is currently payable with respect to a lump sum-based benefit formula if, under the terms of the plan, this optional form of benefit is determined as of the annuity starting date as the actuarial equivalent (using reasonable actuarial assumptions) of the optional form of benefit that: (1) commences as of the same annuity starting date; (2) is payable in the same generalized optional form (within the meaning of §1.411(d)–3(g)(8)) as the accrued benefit; and (3) is the actuarial equivalent (using reasonable actuarial assumptions) of the then-current balance of the hypothetical account maintained for the participant or the then-current value of an accumulated percentage of the participant's final average compensation. This special rule would facilitate the payment of an immediate annuity, such as a joint and survivor annuity or life annuity with period certain, that is calculated as the actuarial equivalent of the form of payment of the accrued benefit under the plan, such as an immediately payable straight life annuity.

Finally, the proposed regulations would provide that the relief under section 411(a)(13)(A) applies on a proportionate basis to a payment of a portion of the benefit under a lump sum-based benefit formula that is not paid in the form of an annuity, such as a payment of a specified dollar amount or percentage of the then-current balance of a hypothetical account maintained for the participant or then-current value of an accumulated percentage of the participant's final average compensation. Thus, for example, if a plan that expresses the participant's entire accumulated benefit as the balance of a hypothetical account distributes 40 percent of the participant's then-current hypothetical account balance, the plan is treated as satisfying the requirements of section 411(a) and the minimum present value rules of section 417(e) with respect to 40 percent of the participant's then-current accrued benefit.

D. *Application of section 411(a)(13)(A) to plans with multiple formulas*

The proposed regulations would clarify that the relief provided under section 411(a)(13)(A) does not apply to any portion of the participant's benefit that is determined under a formula that is not a lump sum-based benefit formula. Thus, for example, where the participant's accrued benefit equals the greater of the benefit under a hypothetical account formula and the benefit under a traditional defined benefit formula, a single-sum payment of the participant's entire benefit must equal the greater of the then-current balance of the hypothetical account and the present value, determined in accordance with section 417(e), of the benefit under the traditional defined benefit formula. On the other hand, where the plan provides an accrued benefit equal to the sum of the benefit under a hypothetical account formula plus the excess of the benefit under a traditional defined benefit formula over the benefit under the hypothetical account formula, a single-sum payment of the participant's entire benefit must equal the then-current balance of the hypothetical account plus the excess of the present value, determined in accordance with section 417(e), of the benefit under the traditional defined benefit formula over the present value, determined in accordance with section 417(e), of the benefit under the hypothetical account formula. See the request for comments under the heading "**Comments and Public Hearing**" on the issue of determining the present value of a benefit determined, in part, based on the benefit under a lump sum-based benefit formula.

E. *Application of section 411(a)(13)(A) to pension equity plans*

The preamble to the 2007 proposed regulations asked for comments on plan formulas that calculate benefits as the current value of an accumulated percentage of the participant's final average compensation (often referred to as "pension equity plans" or "PEPs"). Commenters indicated that some of these plans never credit interest, directly or indirectly, some explicitly credit interest after cessation of PEP accruals, and some do not credit interest explicitly but provide for specific amounts to be payable after cessation of PEP accruals (both immediately and at future dates) based on actuarial equivalence using specified actuarial factors applied upon cessation of PEP accruals.

The 2010 final regulations clarify that a formula is expressed as the balance of a hypothetical account maintained for the participant if it is expressed as a current single-sum dollar amount. Thus, a PEP formula that credits interest after cessation of PEP accruals is considered a formula that is expressed as the balance of a hypothetical account after cessation of PEP accruals. As a result, such a formula is a lump sum-based benefit formula that is subject to the rules of section 411(a)(13)(A) set forth earlier in this preamble, as those rules are applied to PEP formulas during the period of PEP accruals and as those rules are applied to hypothetical account balance formulas after cessation of PEP accruals.

Under these proposed regulations, any other PEP formula (including those that do not credit interest, directly or indirectly, and those that offer actuarially equivalent forms of payment using specified actuarial factors applied after cessation of PEP accruals) would also be subject to the rules of section 411(a)(13)(A), as explained earlier in this preamble. Thus, for example, a PEP that does not explicitly credit interest but, instead, calculates the annuity benefit commencing at future ages as the actuarial equivalent of the PEP value as of cessation of PEP accruals would be eligible for the relief of section 411(a)(13)(A) with respect to the PEP value as of every period before cessation of PEP accruals. In addition, since the accrued benefit is calculated as an annuity commencing at normal retirement age that is actuarially equivalent to the PEP value as of cessation of PEP accruals, the relief described above that applies to annuities that are calculated as the actuarial equivalent of the then-current PEP value would not apply.

II. *Section 411(b)(1): Special rule with respect to statutory hybrid plans*

Under the regulations with respect to the $133\frac{1}{3}$ percent rule of section 411(b)(1)(B), for any plan year, social security benefits and all relevant factors used to compute benefits, *e.g.*, consumer price index, are treated as remaining constant as of the beginning of the current plan year for all subsequent plan years. A number of commenters on both the 2007 proposed regulations and the 2008 proposed backloading regulations expressed concern that this rule might effectively preclude statutory hybrid plans from using an interest crediting rate that is a variable rate that could potentially be negative in a year, such as an equity-based rate. This is because, if a plan treated an interest crediting rate that was negative as remaining constant in all future years for purposes of the backloading test of section 411(b)(1)(B), a principal credit (such as a pay credit) that accrues in a later year would result in a greater benefit accrual than an otherwise identical principal credit that accrues in an earlier year because the principal credit that accrues later is credited with negative interest credits for fewer years. Thus, these commenters were concerned that a plan that uses a variable rate could fail the backloading rules of section 411(b)(1) even where both the pay crediting and interest crediting formulas do not vary over time.

In response to these comments, the proposed regulations contain a special rule regarding the application of the $133\frac{1}{3}$ percent rule of section 411(b)(1)(B) to a statutory hybrid plan that adjusts benefits using a variable interest crediting rate that can potentially be negative in any given year. Under this proposed rule, a plan that determines any portion of the participant's accrued benefit pursuant to a statutory hybrid benefit formula (as defined in §1.411(a)(13)–1(d)(4)) that utilizes an interest crediting rate described in §1.411(b)(5)–1(d) that is a variable rate that was less than zero for the prior plan year would not be treated as failing to satisfy the requirements of the $133\frac{1}{3}$ percent rule for the current plan year merely because the section 411(b)(1)(B) backloading calculation is performed assuming that the variable rate is zero for the current plan year and all future plan years.

III. *Section 411(b)(5): Special conversion protection rule and additional rules with respect to the market rate of return limitation*

A. *Comparison at effective date of conversion amendment*

In accordance with the requirements of section 411(b)(5)(B)(ii), the 2010 final regulations provide that a participant whose benefits are affected by a conversion amendment generally must be provided with a benefit after the conversion that is at least equal to the sum of benefits accrued through the date of conversion and benefits earned after the conversion, with no permitted interaction between the two portions. The 2010 final regulations provide for an alternative method of satisfying the conversion protection requirements where an opening hypothetical account balance or opening accumulated percentage of the participant's final average compensation is established at the time of the conversion and the plan provides for separate calculation of (1) the benefit attributable to the opening hypothetical account balance (including interest credits attributable thereto) or attributable to the opening accumulated percentage of the participant's final average compensation and (2) the benefit attributable to post-conversion service under the post-conversion benefit formula. Under this alternative, the plan must provide that, when a participant commences benefits, the participant's benefit will be increased if the benefit attributable to the opening hypothetical account or opening accumulated percentage that is payable in the particular optional form of benefit selected is less than the benefit accrued under the plan prior to the date of conversion and that was payable in the same generalized optional form of benefit (within the meaning of §1.411(d)–3(g)(8)) at the same annuity starting date.

The preamble to the 2007 proposed regulations requested comments on another alternative method of satisfying the conversion protection requirements that would not require this comparison at the annuity starting date. In response to favorable comments related to this alternative, these proposed regulations would provide that certain plans may satisfy the conversion protection requirements of sections 411(b)(5)(B)(ii), 411(b)(5)(B)(iii), and

411(b)(5)(B)(iv) by establishing an opening hypothetical account balance without a subsequent comparison of benefits at the annuity starting date. While testing at the annuity starting date would not be required under this method, a number of requirements like those described in the preamble to the 2007 proposed regulations would need to be satisfied in order to ensure that the hypothetical account balance used to replicate the pre-conversion benefit (the opening hypothetical account balance and interest credits on that account balance) is reasonably expected in most, but not necessarily all, cases to provide a benefit at least as large as the pre-conversion benefit for all periods after the conversion amendment.

This alternative method would be limited to situations where an opening hypothetical account balance is established and would not be available where an opening accumulated percentage of the participant's final average compensation is established because these plans would be unable to reliably replicate the pre-conversion benefit. This is because the value of the opening accumulated percentage would only increase as a result of unpredictable increases in compensation for periods after the conversion amendment until cessation of PEP accruals, rather than by application of an annual interest crediting rate.

This alternative would only be available where the participant elects to receive payment in the form of a single-sum distribution equal to the sum of the then-current balance of the hypothetical account used to replicate the pre-conversion benefit and the benefit attributable to post-conversion service under the post-conversion benefit formula. Because of the limited availability of this alternative, plans will still need to separately keep track of the pre-conversion benefit in order to satisfy the conversion protection requirements for all forms of distribution other than a single-sum distribution. See the related request for comments in this preamble under the heading "**Comments and Public Hearing**."

Under this alternative, in order to satisfy the requirements of section 411(d)(6), the participant's benefit after the effective date of the conversion amendment must not be less than the participant's section 411(d)(6) protected benefit (as defined in §1.411(d)–3(g)(14)) with respect to service before the effective date of the conversion amendment (determined under the terms of the plan as in effect immediately before the effective date of the amendment). Also, the plan, as in effect immediately before the effective date of the conversion amendment, either must not have provided a single-sum payment option (for benefits that cannot be immediately distributed under section 411(a)(11)) or must have provided a single-sum payment option that was based solely on the present value of the benefit payable at normal retirement age (or at date of benefit commencement, if later) and which was not based on the present value of the benefit payable commencing at any date prior to normal retirement age. This condition ensures that the hypothetical account balance used to replicate the pre-conversion benefit does not result in a single-sum distribution that is less than would have been available under an early retirement subsidy under the pre-conversion formula.

Under this alternative method of satisfying the conversion protection requirements, the opening hypothetical account balance must be established in accordance with the rules under which this opening balance is not less than the present value, determined in accordance with section 417(e), of the accrued benefit immediately prior to the effective date of the conversion amendment. In addition, under this alternative, the interest crediting rate under the plan as of the effective date of the conversion amendment must be either the rate of interest on long-term investment grade corporate bonds (the third segment rate) or one of several specified safe harbor rates. Also, as of that date, the value of the index used to determine the interest crediting rate under the plan must be at least as great for every participant or beneficiary as the interest rate that was used to determine the opening hypothetical account balance. This requirement is satisfied, for example, if each participant's opening hypothetical account balance is determined using the applicable interest rate and applicable mortality table under section 417(e)(3), the interest crediting rate under the plan is the third segment rate, and, at the effective date of the conversion amendment, the third segment rate is the highest of the three segment rates. If, subsequent to the effective date of the conversion amendment, the interest crediting rate changes (whether by plan amendment or otherwise) with respect to a participant who was a participant at the time of the effective date of the conversion amendment from an interest crediting rate that is either the rate of interest on long-term investment grade corporate bonds or one of the specified safe harbor rates to a different interest crediting rate that is not in all cases at least as great as the prior interest crediting rate under the plan, then the new interest crediting rate does not apply to the existing hypothetical account balance as of the effective date of the change in interest crediting rates (or, if the plan created a subaccount consisting of the opening hypothetical account balance and interest credits on that subaccount, then the new interest crediting rate does not apply to the subaccount).

Finally, either the plan must provide a death benefit after the effective date of the conversion amendment which has a present value that is at all times at least equal to the then-current balance of the hypothetical account used to replicate the pre-conversion benefit or the plan must not have applied a pre-retirement mortality decrement in establishing the opening hypothetical account balance.

B. *Market rate of return*

The 2010 final regulations provide that a plan that credits interest must specify how the plan determines interest credits and must specify how and when interest credits are credited. In addition, the 2010 final regulations contain certain specific rules regarding the method and timing of interest credits, including a requirement that interest be credited at least annually.

The proposed regulations include a rule that would provide that a plan is not treated as failing to meet the interest crediting requirements merely because the plan does not provide for interest credits on amounts distributed prior to the end of the interest crediting period. Thus, if a plan credits its interest at periodic intervals, the plan would not be required to credit interest on amounts that were distributed between the dates on which interest under the plan is credited to the account balance.

Furthermore, the proposed regulations include a rule that would allow plans to credit interest taking into account increases or decreases to the participant's accumulated benefit that occur during the period. In particular, the rule would provide that a plan is not treated as failing to meet the market rate of return limitations merely because the plan calculates increases or decreases to the participant's accumulated benefit by applying a rate of interest or rate of return (including a rate of increase or decrease under an index) to the participant's adjusted accumulated benefit (or portion thereof) for the period. For this purpose, the participant's adjusted accumulated benefit equals the participant's accumulated benefit as of the beginning of the period, adjusted for debits and credits (other than interest credits) made to the accumulated benefit prior to the end of the interest crediting period, with appropriate weighting for those debits and credits based on their timing within the period. For plans that calculate increases or decreases to the participant's accumulated benefit by applying a rate of interest or rate of return to the participant's adjusted accumulated benefit (or portion thereof) for the period, interest credits include these increases and decreases, to the extent provided under the terms of the plan at the beginning of the period and to the extent not conditioned on current service and not made on account of imputed service, and the interest crediting rate with respect to a participant equals the total amount of interest credits for the period divided by the participant's adjusted accumulated benefit for the period.

The proposed regulations would provide that the preservation of capital requirement is applied only at an annuity starting date on which a distribution of the participant's entire benefit as of that date under the plan's statutory hybrid benefit formula commences. The proposed regulations would also provide special rules to ensure that prior distributions are taken into account in determining the guarantee provided by the preservation of capital requirement with respect to a current distribution to which the rule applies.

These proposed regulations would broaden the list of permitted interest crediting rates from those permitted under the 2010 final regulations. A number of commenters on the 2007 proposed regulations requested that the rate of return on plan assets be treated as a market rate of return for all types of statutory hybrid plans, and not just indexed plans. In response to these comments, the proposed regulations would permit the use of the rate of return on plan assets as a market rate of return for statutory hybrid plans generally if the plan's assets are diversified so as to minimize the volatility of returns. Like the 2010 final regulations, the proposed regulations would provide that this requirement that plan assets be diversified so as to minimize the volatility of returns does not require greater diversification than is required under section 404(a)(1)(C) of Title I of the Employee Retirement Income Security Act of 1974, Public Law 93–406 (88 Stat. 829 (1974)) with respect to defined benefit pension plans.

The preamble to the 2007 proposed regulations asked for comments about the possibility of allowing an interest credit to be determined by reference to a rate of return on a regulated investment company (RIC) described in section 851. The preamble focused on whether such an investment has sufficiently constrained volatility that the existence of the capital preservation rule would not result in an above market rate of return. In response to comments received on the 2007 proposed regulations, these proposed regulations would provide that an interest crediting rate is not in excess of a market rate of return if it is equal to the rate of return on a RIC, as defined in section 851, that is reasonably expected to be not significantly more volatile than the broad United States equities market or a similarly broad international equities market. For example, a RIC that has most of its assets invested in securities of issuers (including other RICs) concentrated in an industry sector or a country other than the United States, that uses leverage, or that has significant investment in derivative financial products, for the purpose of achieving returns that amplify the returns of an unleveraged investment, generally would not meet this requirement. Thus, a RIC that has most of its investments concentrated in the semiconductor industry or that uses leverage in order to provide a rate of return that is twice the rate of return on the Standard & Poor's 500 index (S&P 500) would not meet this requirement. On the other hand, a RIC whose investments track the rate of return on the S&P 500, a broad-based "small-cap" index (such as the Russell 2000 index), or a broad-based international equities index would meet this requirement. The requirement that the RIC's investments not be concentrated in an industry sector or a specific international country is intended to limit the volatility of the returns, as well as the risk inherent in non-diversified investments. Similarly, the requirement that the RIC not provide leveraged returns is intended both to ensure that rates provided by the RIC do not exceed an unleveraged market rate as well as to limit the volatility of the returns provided. Subject to these requirements, the proposed rule is intended to provide plan sponsors with greater flexibility in choosing an equity-based rate than would be provided if the regulations were to list particular equity-based rates that satisfy the market rate of return requirement.

The preamble to the 2007 proposed regulations requested comments as to how to implement a rule that provides that interest credits are determined under the greater of two or more interest crediting rates without violating the market rate of return limitation. In response to such comments, these proposed regulations would provide that in certain limited circumstances a plan can provide interest credits based on the greater of two or more interest crediting rates without exceeding a market rate of return.

The Treasury Department and the IRS have modeled the historical distribution of rates of interest on long-term investment grade corporate bonds and have determined that those rates have only infrequently been lower than 4 percent and, when lower, were generally lower by small amounts and for limited durations. Therefore, the increase in the effective rate of return resulting from adding an annual 4 percent floor to one of these bond rates has historically been small enough that the effective rate of return is not in excess of a market rate of return. As a result, the proposed rules would provide that it is permissible for a plan to utilize an annual floor of 4 percent in conjunction with a permissible bond rate. Specifically, the proposed regulations would provide that a plan does not provide an interest crediting rate that is in excess of a market rate of return merely because the plan provides that the interest crediting rate for an interest crediting period equals the greater of the rate of interest on long-term investment grade corporate bonds (or one of the safe harbor rates that, under the regulations, are deemed not to be in excess of that rate) and an annual interest rate of 4 percent.

This rule permitting a plan to utilize an annual floor of 4 percent in conjunction with a permissible bond-based rate would also permit plans that credit interest more frequently than annually using a permissible bond-based rate to also utilize a periodic floor that is a *pro rata* portion of an annual 4 percent floor. Thus, plans that credit interest more frequently than annually could provide an effective annual floor that is greater than 4 percent, both due to the effect of compounding because the floor would be applied more frequently than annually and because the floor would be applied in any period that the bond-based rate was below the floor, even if the annual rate exceeded 4 percent for the plan year. However, given the nature of bond-based rates, including the serial correlation of rates from one period to the next, as well as the fact that 4 percent is not expected to exceed a permissible bond-based rate except infrequently, by small amounts, and for limited durations, in most instances a periodic floor that is based on a 4 percent annual floor will not provide a floor that is significantly different than an annual floor of 4 percent.

In contrast, because of the volatility of equity-based rates, adding an annual floor to an equity-based rate often provides a cumulative rate of return that far exceeds the rate of return provided by the equity-based rate without such floor. It should also be noted that commenters on the 2007 proposed regulations generally did not request that such an annual floor be permitted (perhaps in recognition that a minimum guaranteed annual return when applied to equity-based rates could have a significant impact on funding). Accordingly, the proposed regulations would not allow the use of an annual floor in conjunction with the rate of return on plan assets or on a permissible RIC.

On the other hand, if, instead of applying a floor on each year's rate of return, a cumulative floor is applied to an equity-based rate, the effective rate of return is not necessarily substantially greater than the rate of return provided without the floor. Specifically, the Treasury Department and the IRS have determined that, based on the modeling of long-term historical returns, a 3 percent floor that applies cumulatively (in the aggregate from the date of each principal credit until the annuity starting date, without a floor on the rate of return provided in any interim period) could be combined with any permissible rate (including a permissible equity-based rate), without increasing the effective rate of return to such an extent that the effective rate of return would be in excess of a market rate of return. As a result, the proposed rule would provide that a plan that determines interest credits using any particular interest crediting rate that satisfies the market rate of return limitation does not provide an effective interest crediting rate in excess of a market rate of return merely because the plan provides that the participant's benefit, as of the participant's annuity starting date, is equal to the greater of the benefit determined using the interest crediting rate and the benefit determined as if the plan had used a fixed annual interest crediting rate equal to 3 percent (or a rate not in excess of 3 percent) for principal credits in all years. This rule in the proposed regulations that allows for plans to utilize a cumulative floor of up to 3 percent would also allow plans some additional flexibility in design. Thus, for example, a plan that utilizes annual ceilings in conjunction with a permissible rate could also provide a cumulative floor of up to 3 percent.

Similar to the rules with respect to application of the preservation of capital requirement, the proposed regulations would provide that the determination of the guarantee provided by any cumulative floor with respect to the participant's benefit is made only at an annuity starting date on which a distribution of the participant's entire benefit as of that date under the plan's statutory hybrid benefit formula commences. The proposed regulations would also provide special rules to ensure that prior distributions are taken into account in determining whether the guarantee exceeds the benefit otherwise provided under the plan.

In addition to permitting certain fixed floors to be applied to variable rates, the proposed regulations would also permit a standalone fixed rate of interest to be used for interest crediting purposes. While the statutory language at section 411(b)(5)(B)(i)(I) does not explicitly reference a fixed interest crediting rate, the reference to "a reasonable minimum guaranteed rate of return" and the reference to "the greater of a fixed or variable rate of return" necessarily mean that some fixed rate must also be permissible. Further, the statutory language at section 411(b)(5)(B)(i)(III) specifically authorizes the Treasury Department to issue regulations permitting a fixed rate of interest under the rules relating to a market rate of return. However, reconciling a fixed interest crediting rate with the statutory requirement that an interest crediting rate "*for any plan year* shall be at a rate which is not greater than a market rate of return" [emphasis added] presents unique challenges because, by definition, fixed rates do not adjust with the market. As a result, the use of any fixed rate will result in an interest crediting rate that is above a then-current market rate of interest during any period in which the current market rate falls below the fixed rate.

In light of this fact, the Treasury Department and the IRS believe that, in order to satisfy the market rate of return requirement, any fixed interest crediting rate allowed under the rules must not be expected to exceed future market rates of interest, except infrequently, by small amounts, and for limited durations. Based on the historical modeling described above, the Treasury Department and the IRS have determined that a 5 percent fixed rate satisfies these criteria and that any higher fixed rate would result in an effective rate of return that is in excess of a market rate of return.

Specifically, the proposed rules would provide that an annual interest crediting rate of a fixed 5 percent is a safe harbor rate deemed to be not in excess of the rate of interest on long-term investment grade corporate bonds. As a result, an interest crediting rate of a fixed 5 percent would satisfy the market rate of return limitation. In addition, the special section 411(d)(6) rule set forth in the 2010 final regulations with respect to certain changes in interest crediting rates would apply to an interest crediting rate of a fixed 5 percent and, as a result, a plan amendment that changes the interest crediting rate under the plan to the third segment rate from a fixed 5 percent is deemed to satisfy the requirements of section 411(d)(6), provided certain requirements are met.

The 2010 final regulations provide that §§1.411(b)(5)–1(d)(1)(iii), 1.411(b)(5)–1(d)(1)(vi), and

1.411(b)(5)–1(d)(6), which provide that the regulations set forth the exclusive list of interest crediting rates and combinations of interest crediting rates that satisfy the market rate of return requirement under section 411(b)(5), apply to plan years that begin on or after January 1, 2012. For plan years that begin before January 1, 2012, statutory hybrid plans may utilize a rate that is permissible under the 2010 final regulations or these proposed regulations for purposes of satisfying the statutory market rate of return requirement.

C. *Plan termination*

The proposed regulations would provide guidance with respect to the application of the rules of section 411(b)(5)(B)(vi), which require special plan provisions relating to interest crediting rates and annuity conversion rates that apply when the plan is terminated. Under the proposed regulations, a statutory hybrid plan is treated as meeting the market rate of return requirements only if the terms of the plan satisfy the rules in the regulations relating to section 411(b)(5)(B)(vi). Title IV of ERISA also imposes special rules that apply when a single employer pension plan is terminated (including special rules relating to plan amendments). See regulations of the Pension Benefit Guaranty Corporation for additional rules that apply when a pension plan is terminated.

These proposed regulations reflect the statutory requirement that a plan provide that, if the interest crediting rate used to determine a participant's accumulated benefit (or a portion thereof) varied (that is, was not a constant fixed rate) during the 5-year period ending on the plan termination date, then the interest crediting rate used to determine the participant's accumulated benefit under the plan after the date of plan termination is equal to the average of the rates used under the plan during the 5-year period ending on the plan termination date. If the interest crediting rate used to determine a participant's accumulated benefit (or a portion thereof) was instead a single fixed rate for all periods during the 5-year period ending on the plan termination date, then the interest crediting rate used to determine the participant's accumulated benefit after the date of plan termination would be equal to that fixed rate.

Under this rule, the interest crediting rate used after plan termination would be based on the average of the rates that applied under the plan during the 5-year period preceding plan termination, without regard to whether this average rate exceeds then-current market rates of return (but, in determining the average rate, a rate would only be taken into account to the extent that the rate did not exceed a market rate of return when the rate actually applied). For purposes of this calculation, the proposed regulations would provide that, subject to certain other rules described in this preamble, the average of the rates used under the plan during the 5-year period ending on the termination date is determined with respect to a participant as the arithmetic average, expressed as an annual rate, of the applicable interest crediting rates that applied in the 5-year period. In determining this average, each interest crediting period for which the interest crediting date is within the 5-year period ending on the plan termination date would be taken into account, with interest crediting rates for periods that are less than a year in length adjusted and weighted proportionately. However, under this rule, if a period begins on or before the date that is 5 years before the termination date and ends within the 5-year period ending on the plan termination date, the period would be weighted as though the entire period were within the 5-year period ending on the plan termination date.

Section 411(b)(5)(B)(vi) does not explicitly provide rules with respect to plans that determine interest credits based on equity-based rates of return that may involve potential losses. Since the trailing 5-year average of an equity-based rate of return may have little, if any, correlation to the actual future equity-based rate of return, the Treasury Department and the IRS do not believe it is appropriate to provide that the trailing 5-year average of such rate of return be used to determine benefits after plan termination. In such cases, the Treasury Department and the IRS believe that it is appropriate to apply a bond-based rule instead. Thus, the proposed regulations would provide that, with respect to an interest crediting rate used to determine a participant's accumulated benefit for an interest crediting period during the 5-year period ending on the termination date that is not a fixed interest rate or a bond-based rate of interest (or is based on a variable rate that is not permissible under the regulations), the terms of the plan must provide that, for purposes of determining the average upon plan termination, the interest crediting rate for the interest crediting period is deemed to be equal to the third segment rate for the last calendar month ending before the beginning of the interest crediting period, as adjusted for any actual applicable floors and ceilings that applied to the rate of return in the period, but without regard to any reductions that applied to the rate of return in the period. Thus, for example, if the actual interest crediting rate in an interest crediting period was equal to the rate of return on plan assets, but not greater than 5 percent, then for purposes of determining the plan's average interest crediting rate, the interest crediting rate for that interest crediting period would be deemed to equal to the lesser of the applicable third segment rate for the period and 5 percent. However, if the actual interest crediting rate in an interest crediting period was equal to the rate of return on plan assets minus 200 basis points, then for purposes of determining the plan's average interest crediting rate, the interest crediting rate for that interest crediting period would be deemed to equal the third segment rate (not the third segment rate minus 200 basis points). See the request for comments in this preamble under the heading "**Comments and Public Hearing**" regarding the application of floors, ceilings, and reductions for purposes of the plan termination provisions when the third segment rate is substituted for an equity-based rate.

As provided in section 411(b)(5)(B)(i), the regulations require that the terms of the plan also provide that the interest rate and mortality table (including tabular adjustment factors) used on and after plan termination for purposes of determining the amount of any benefit under the plan payable in the form of an annuity (commencing at or after normal retirement age) be based on the interest rate and mortality table specified under the plan for that purpose as of the termination date, except that if the interest rate is a variable rate, the interest rate is instead based on the rules described in the preceding paragraphs of this preamble using a 5-year average.

A number of special rules apply for purposes of determining the interest crediting rate that applies after plan termination. In particular, for purposes of determining the average rate during the five-year period ending on plan termination, the interest crediting rate that applied for each interest crediting period is generally the ongoing interest crediting rate that was specified under the plan in that period, without regard to any section 411(d)(6) protected benefit using an old interest crediting rate. However, if, at the end of the last interest crediting period prior to plan termination, the participant's accumulated benefit is based on a section 411(d)(6) protected benefit that results from a prior amendment to change the rate of interest crediting applicable under the plan, then, for purposes of determining the average rate, the pre-amendment interest crediting rate is treated as having applied for each interest crediting period after the date of the interest crediting rate change. In addition, the proposed regulations would provide that if the plan determines a participant's interest credits in any interest crediting period by applying different rates to different predetermined portions of the accumulated benefit as permissible under the regulations, then the participant's interest crediting rate for the interest crediting period is assumed for purposes of the plan termination provisions to be the weighted average of the fixed interest rates, determined under the plan termination rules, that apply to each portion of the accumulated benefit.

Furthermore, to reduce the administrative burden and to determine the average rate for each participant based on 5 years of interest crediting data, if the plan provided for interest credits for any interest crediting period in which, pursuant to the terms of the plan, the individual was not eligible to receive interest credits (because the individual was not a participant or beneficiary in the relevant interest crediting period or otherwise), then, for purposes of determining the interest crediting rate that applies after plan termination, the individual is treated as though the individual received interest credits in that period using the interest crediting rate that applied in that period under the terms of the plan to determine the benefit of a similarly situated participant or beneficiary who was eligible to receive interest credits. However, if, under the terms of the plan, the individual was not eligible to receive any interest credits during the entire 5-year period ending on the plan termination date, then the rules fixing the interest crediting rate do not apply to determine the individual's benefit after plan termination.

The proposed regulations include examples to illustrate the application of these plan termination rules, including how these rules would apply where a plan bases its interest crediting rate on a weighted average of more than one rate, how these rules would apply where the plan's ongoing interest crediting rate is an equity-based rate of return, and how these rules would apply to a participant whose benefits are determined where the plan had switched interest crediting rates in the past and where the interest credit prior to termination was determined by applying the old rate to the benefit attributable to principal credits before the applicable amendment date.

D. *Special rule with respect to changes in interest crediting rates where plan provides section 411(d)(6) protection*

An inherent tension exists between the requirement not to reduce a participant's accrued benefit and the requirement that an interest crediting rate not be in excess of a market rate of return that makes changes in interest crediting rates difficult to implement for statutory hybrid plans in many circumstances. This is because, in order to satisfy section 411(d)(6), a participant's benefit can never be less than the pre-amendment benefit increased for periods after the amendment using the pre-amendment interest crediting rate, thereby effectively requiring a minimum interest crediting rate. In light of this tension, the proposed regulations would create a special market rate of return rule that applies in the case of an amendment to change the plan's interest crediting rate.

In particular, the proposed rule would provide that, in the case of an amendment to change a plan's interest crediting rate for periods after the applicable amendment date from one interest crediting rate (the old rate) that is not in excess of a market rate of return to another interest crediting rate (the new rate) that is not in excess of a market rate of return, the plan's effective interest crediting rate is not in excess of a market rate of return merely because the plan provides for the benefit of any participant who is benefiting under the plan on the applicable amendment date to never be less than what it would be if the old rate had continued but without taking into account any principal credits after the applicable amendment date. A pattern of repeated plan amendments each of which provides for a prospective change in the plan's interest crediting rate with respect to the benefit as of the applicable amendment date will be treated as resulting in the ongoing plan terms providing that the interest crediting rate equals the greater of each of the interest crediting rates, so that the special rule in the preceding sentence would not apply. See §1.411(d)–4, A–1(c)(1). Thus, in such cases the plan will be treated as providing a rate of return that is in excess of a market rate of return, unless the resulting greater-of rate satisfies the market rate of return rules.

E. *Special rule with respect to interest crediting rate after normal retirement age*

In coordination with the rules under section 411(a)(13)(A) (as described in section I of this preamble) that apply with respect to the benefit determined as of each annuity starting date after normal retirement age, the proposed regulations would provide that a statutory hybrid plan is not treated as providing an effective interest crediting rate that is in excess of a market rate of return merely because the plan provides that the participant's benefit, as of each annuity starting date after normal retirement age, is equal to the greater of the benefit determined using an interest crediting rate that is not otherwise in excess of a market rate of return and the benefit that satisfies the requirements of section 411(a)(2). Thus, for example, a cash balance plan would not be treated as providing an effective interest crediting rate in excess of a market rate of return merely because the plan credits interest after normal retirement age at a rate that is sufficient to provide any required actuarial increases.

IV. *Changes in interest crediting rates and Code section 411(d)(6)*

A. *Background*

An amendment to change a plan's interest crediting rate that only applies with respect to benefits that have not yet accrued (such as where the plan establishes a second hypothetical account balance for future principal credits to which a different interest crediting rate is applied) would not result in a reduction in accrued benefits attributable to service before the applicable amendment date and, therefore, such a change would not violate section 411(d)(6).[4] However, except to the extent permitted under section 1107 of PPA '06 or as otherwise described in section IV of this preamble, an amendment to change a plan's future interest crediting rate with respect to benefits that have already accrued (in other words, with respect to an existing account balance) must satisfy section 411(d)(6) if the change could result in interest credits that are smaller as of any date after the applicable amendment date than the interest credits that would be credited without regard to the amendment.[5]

B. *Special section 411(d)(6) rule with respect to changes in future interest crediting rates*

Under the 2010 final regulations, a plan is not treated as providing smaller interest credits after the applicable amendment date merely because the amendment changes the plan's future interest crediting rate with respect to benefits that have already accrued to the rate of interest on long-term investment grade corporate bonds (the third segment rate under section 430(h)(2)(C)(iii)) from one of the other bond-based safe harbor rates permitted under the 2010 final regulations (for example, a rate based on Treasury bonds with any of the margins specified in the regulations or an eligible cost-of-living index). However, the change is permitted only if: (1) the effective date of the amendment is at least 30 days after adoption, (2) the new interest crediting rate only applies to interest to be credited after the effective date of the amendment, and (3) on the effective date of the amendment, the new interest crediting rate is not lower than the interest crediting rate that would have applied in the absence of the amendment.

C. *Changes that would otherwise violate section 411(d)(6) but that are made to the extent necessary to satisfy section 411(b)(5)*

After these proposed regulations under sections 411(a)(13) and 411(b)(5) are issued as final regulations, it is expected that relief from the requirements of section 411(d)(6) will be granted for a plan amendment that eliminates or reduces a section 411(d)(6) protected benefit, provided that the amendment is adopted before those final regulations apply to the plan, and the elimination or reduction is made only to the extent necessary to enable the plan to meet the requirements of section 411(b)(5).[6] It is expected that this section 411(d)(6) relief will be available in the case of an amendment that reduces the future interest crediting rate with respect to benefits that have already accrued from a rate that is in excess of a market rate of return under the final market rate of return rules to the extent necessary to constitute a permissible rate under the final market rate of return rules. However, it is expected that this relief would not permit a plan with an interest crediting rate within the list of permitted rates under the final market rate of return rules to change to another permitted rate because the change would not be necessary to enable the plan to satisfy the requirements of section 411(b)(5). Similarly, it is expected that this relief would not permit a plan with an interest crediting rate that is impermissible under the final market rate of return rules to change to a permissible rate using less than the maximum permitted margin for that rate because the reduction would be more than necessary to enable the plan to satisfy the requirements of section 411(b)(5). For purposes of the preceding sentence, a rate without an associated margin is treated as having a maximum permitted margin of zero. See the request for comments, under the heading "**Comments and Public Hearing**" in this preamble, regarding limitations on the scope of this anticipated relief under §1.411(d)–4, A–2(b)(2)(i) because the relief must be limited to amendments that change a plan's interest crediting rate only to the extent necessary to enable the plan to satisfy the requirements of section 411(b)(5).

Proposed Effective/Applicability Dates

The specific rules that would be implemented under the proposed regulations generally would apply to plan years that begin on or after January 1, 2012. However, as stated in the preamble to the 2010 final regulations, a plan is permitted to rely on the provisions of these proposed regulations, as well as the 2010 final regulations, the 2007 proposed regulations, and Notice 2007–6, for purposes of satisfying the requirements of sections 411(a)(13) and 411(b)(5) for periods before the regulatory effective date.

Special Analyses

It has been determined that these proposed regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The Treasury Department and the IRS specifically request comments on the clarity of the proposed regulations and

[4] However, see section 204(h) of ERISA and section 4980F of the Code for notice requirements relating to amendments that provide for a significant reduction in the rate of future benefit accrual.

[5] Except to the extent permitted under section 411(d)(6) and §§1.411(d)–3 and 1.411(d)–4, another Code provision, or another statutory provision such as section 1107 of PPA '06, section 411(d)(6) prohibits a plan amendment that decreases a participant's accrued benefits or that has the effect of eliminating or reducing an early retirement benefit or retirement-type subsidy, or eliminating an optional form of benefit, with respect to benefits attributable to service before the amendment.

[6] Announcement 2009–82 and Notice 2009–97 stated that the IRS and the Treasury Department expected to provide such relief. While Notice 2009–97 indicated the relief would only apply if the amendment is adopted by the last day of the first plan year that begins on or after January 1, 2010, this preamble supersedes that applicability date to provide that it is expected that this relief would apply if the amendment is adopted before final regulations that finalize these proposed regulations apply to the plan.

how they may be made easier to understand.

In addition to comments on issues addressed in these proposed regulations, the Treasury Department and the IRS specifically request comments on the following issues:

- Should a defined benefit plan that expresses a participant's accumulated benefit as a current single-sum dollar amount and that does not provide for interest credits be excluded from the definition of a statutory hybrid plan?
- In the case of a statutory hybrid plan that credits interest using an interest crediting rate equal to the rate of return on a RIC, how does section 411(d)(6) apply if the underlying RIC subsequently ceases to exist?
- The proposed regulations permit certain fixed interest crediting rates (a fixed 5 percent rate for any year, the greater of 4 percent or certain bond-based indices for any year, and a cumulative minimum 3 percent annual rate). Comments regarding these specific proposed rules should take into account how any general legal standard for a market rate of return would be applied in different economic circumstances with variable interest rate markets, as well as the related ability that would generally be available under these proposed regulations at §1.411(b)(5)–1(e)(3)(iii) for the plan sponsor to change the crediting rate on an existing hypothetical account balance for active participants from one interest crediting rate to another, including the risk that whatever fixed rate is permitted might allow a plan's interest credits to exceed market rates of interest either frequently, by an amount that might be large, or for an extended duration. Commenters recommending any additional types of rates of return than those in these proposed regulations should justify how those rates meet a market rate of return, taking into account the minimum guarantee rules.
- Should a statutory hybrid plan be able to offer participants a menu of hypothetical investment options (including a life-cycle investment option, whereby participants are automatically transitioned incrementally at certain ages from a blended rate that is more heavily equity-weighted to a rate that is more heavily bond-weighted) and, if so, what plan qualification issues (*i.e.,* forfeiture, section 411(d)(6), market rate of return, and other section 411(b)(5) issues) arise under such a plan design? In particular, do the following events raise issues: (1) a participant elects to switch from one investment option to another; (2) a bond index or RIC underlying one of the investment options ceases to exist; (3) the plan is amended to eliminate an investment option; (4) a participant elects to switch from an investment option with a cumulative minimum to an investment option without a cumulative minimum (or *vice versa*); or (5) the plan is terminated and, pursuant to the special rules that apply upon plan termination, the interest crediting rate that applies to determine a participant's benefit after plan termination must be fixed?
- How does a statutory hybrid plan that provides benefits under a statutory hybrid benefit formula other than a lump sum-based benefit formula (such as a plan that provides for indexing as described in section 411(b)(5)(E)) — a plan to which section 411(a)(13)(A) does not apply — ensure compliance with the minimum present value rules of section 417(e)?
- How does a statutory hybrid plan determine the section 417(e) minimum present value of the participant's benefit where a portion of the benefit is determined based partly on the benefit under a lump sum-based benefit formula, although that portion is not determined under a lump sum-based benefit formula? For example, where a portion of the accrued benefit is equal to the excess of the benefit under a traditional defined benefit formula over the benefit under a hypothetical account formula, how is the present value of that portion of the accrued benefit determined?
- Should the proposed alternative method of satisfying the conversion protection requirements that does not require a comparison of benefits at the annuity starting date be broadened to apply to forms of distribution other than a single-sum distribution? If this rule should be broadened, what rules would ensure that the benefit attributable to the opening hypothetical account balance is not less than the benefit available under the same generalized optional form under the pre-conversion formula (which may include subsidized early retirement benefits and other retirement-type subsidies) consistent with the goal of having a simplified alternative?
- How does a statutory hybrid plan that uses a variable interest crediting rate that may potentially be negative satisfy the fractional rule of section 411(b)(1)(C) if the 133$^1/_3$ percent rule of section 411(b)(1)(B) is not satisfied?
- For purposes of the plan termination rules, should a floor, ceiling, or reduction that applied to an equity-based rate in an interest crediting period be treated as applying in the same manner to the third segment rate or is it appropriate for such an adjustment to be disregarded or otherwise modified for purposes of such rules?
- Under the relief to be provided pursuant to §1.411(d)–4, A–2(b)(2)(i), which authorizes amendments that reduce a section 411(d)(6) protected benefit only to the extent necessary to satisfy the requirements of section 411(b)(5), should a statutory hybrid plan with an interest crediting rate that is impermissible under the final market rate of return rules be permitted to be amended to change the future interest crediting rate with respect to benefits that have already accrued to any permissible rate using the maximum permitted margin for that rate or should that be dependent upon the reasons that the pre-amendment rate exceeded a market rate of return? Thus, for example, should a plan with an impermissible bond-based rate (without a fixed component) be permitted to switch to any permissible rate, bond-based or otherwise, using the maximum permitted margin for that rate? Should a plan with an impermissibly high standalone fixed rate be permitted to switch to the maximum rate of any type, should it be permitted to switch to the maximum permitted bond-based rate with the maximum permitted floor for that rate (the third segment rate with a fixed 4

percent floor), or must it switch to the maximum permitted standalone fixed rate (a fixed rate of 5 percent)? Should a plan with a permissible bond-based rate but with an impermissibly high fixed floor be permitted to switch to the maximum rate of any type, should it be permitted to retain the pre-amendment bond-based rate while reducing the floor to the maximum permitted floor for that rate (a fixed 4 percent floor), should it be permitted to switch to the maximum permitted standalone fixed rate (a fixed rate of 5 percent), or must it switch to the maximum permitted bond-based rate with the maximum permitted floor for that rate (the third segment rate with a fixed 4 percent floor)?

All comments will be available for public inspection and copying. A public hearing has been scheduled for Wednesday, January 26, 2011, beginning at 10 a.m. in the Auditorium, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the "**FOR FURTHER INFORMATION CONTACT**" section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit written or electronic comments by Wednesday, January 12, 2011, and an outline of topics to be discussed and the amount of time to be devoted to each topic (a signed original and eight (8) copies) by Friday, January 14, 2011. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal authors of these regulations are Neil S. Sandhu, Lauson C. Green, and Linda S. F. Marshall, Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and the Treasury Department participated in the development of these regulations.

* * * * *

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.411(a)(13)–1 is amended by revising paragraphs (b)(2), (b)(3), (b)(4), and (e)(2)(ii) to read as follows:

§1.411(a)(13)–1 Statutory hybrid plans.

* * * * *

(b) * * *

(2) *Requirements that lump sum-based benefit formula must satisfy to obtain relief*—(i) *In general*. The relief of paragraph (b)(1) of this section does not apply with respect to benefits determined under a lump sum-based benefit formula unless the requirements of paragraphs (b)(2)(ii) through (iv) of this section are satisfied.

(ii) *Benefit on or before normal retirement age*. A plan satisfies this paragraph (b)(2)(ii) only if, at all times on or before normal retirement age, the then-current balance of the hypothetical account or the then-current value of the accumulated percentage of the participant's final average compensation is not less than the present value, determined using reasonable actuarial assumptions, of the portion of the participant's accrued benefit that is determined under the lump sum-based benefit formula. However, a plan is deemed to satisfy the requirement in the preceding sentence for periods before normal retirement age if, upon attainment of normal retirement age, the then-current balance of the hypothetical account or the then-current value of the accumulated percentage of the participant's final average compensation is actuarially equivalent (using reasonable actuarial assumptions) to the portion of the participant's accrued benefit that is determined under the lump sum-based benefit formula.

(iii) *Benefit after normal retirement age*. A plan satisfies this paragraph (b)(2)(iii) only if, as of each annuity starting date after normal retirement age, the then-current balance of the hypothetical account or the then-current value of the accumulated percentage of the participant's final average compensation—

(A) Satisfies the requirements of section 411(a)(2); or

(B) Would satisfy the requirements of section 411(a)(2) but for the fact that the plan suspends benefits in accordance with section 411(a)(3)(B).

(iv) *Reductions limited*. A plan satisfies this paragraph (b)(2)(iv) only if the balance of the hypothetical account or accumulated percentage of the participant's final average compensation may not be reduced except as a result of—

(A) Benefit payments under paragraph (b)(3) of this section;

(B) Qualified domestic relations orders under section 414(p);

(C) Forfeitures that are permitted under section 411(a) (such as charges for providing a qualified preretirement survivor annuity);

(D) Amendments that are permitted under section 411(d)(6); or

(E) Adjustments resulting from the application of interest credits (under the rules of §1.411(b)(5)–1) that are negative for a period, for plans that express the accumulated benefit as the balance of a hypothetical account.

(3) *Alternative forms of distribution under a lump sum-based benefit formula*—(i) *Payment of current account balance or current value*. The relief of paragraph (b)(1) of this section applies with respect to a single-sum payment equal to the then-current balance of a hypothetical account maintained for the participant or the then-current value of an accumulated percentage of the participant's final average compensation.

(ii) *Payment of benefits that are actuarially equivalent to current account balance or current value*. With respect to the benefits under a lump sum-based benefit formula, the relief of paragraph (b)(1) of this section applies to an optional form of benefit that is determined as of the annuity starting date as the actuarial equivalent, using reasonable actuarial assumptions, of the then-current balance of a hypothetical account maintained for the participant or the then-current value of an accumulated percentage of the participant's final average compensation.

(iii) *Payment of benefits based on immediate annuity*. With respect to the benefits under a lump sum-based benefit formula, the relief of paragraph (b)(1) of this section applies to an optional form of benefit that is not subject to the minimum present value requirements of section 417(e) and that is determined under the plan as of the annuity starting date as the actuarial equivalent (using reasonable actuarial assumptions) of the optional form of benefit that—

(A) Commences as of the same annuity starting date;

(B) Is payable in the same generalized optional form (within the meaning of §1.411(d)–3(g)(8)) as the accrued benefit; and

(C) Is the actuarial equivalent (using reasonable actuarial assumptions) of the then-current balance of a hypothetical account maintained for the participant or the then-current value of an accumulated percentage of the participant's final average compensation.

(iv) *Payment of portion of current account balance or current value*. The relief of paragraph (b)(1) of this section applies on a proportionate basis to a payment of a portion of the benefit under a lump sum-based benefit formula that is not paid in a form otherwise described in this paragraph (b)(3), such as a payment of a specified dollar amount or percentage of the then-current balance of a hypothetical account maintained for the participant or then-current value of an accumulated percentage of the participant's final average compensation. Thus, for example, if a plan that expresses the participant's entire accumulated benefit as the balance of a hypothetical account distributes 40 percent of the participant's then-current hypothetical account balance in a single payment, the plan is treated as satisfying the requirements of section 411(a) and the minimum present value rules of section 417(e) with respect to 40 percent of the participant's then-current accrued benefit. See paragraph (b)(3)(ii) or (iii) of this section for relief applicable with respect to a distribution with respect to the remainder (60 percent) of the participant's accumulated benefit.

(v) *Conditions for applicability*. This paragraph (b)(3) applies to a payment of benefits under a lump sum-based benefit formula only if the requirements of paragraph (b)(2) of this section are also satisfied.

(4) *Rules of application*. The relief of paragraph (b)(1) of this section applies only to the portion of the participant's benefit that is determined under a lump sum-based benefit formula and does not apply to any portion of the participant's benefit that is determined under a formula that is not a lump sum-based benefit formula. Thus, the following rules apply:

(i) *Greater-of formulas*. Where the participant's accrued benefit equals the greater of the benefit under a lump sum-based benefit formula and the benefit under another formula, a single-sum payment of the participant's entire benefit must equal the greater of the then-current accumulated benefit under the lump sum-based benefit formula and the present value, determined in accordance with section 417(e), of the benefit under the other formula. Applying this rule where the non-lump sum-based benefit formula provides a benefit equal to a *pro rata* portion of the benefit determined by projecting a future hypothetical account balance (including future principal credits), a single-sum payment of the participant's entire benefit must equal the greater of the then-current balance of the hypothetical account and the present value, determined in accordance with section 417(e), of the *pro-rata* benefit determined by projecting the future hypothetical account balance.

(ii) *"Sum-of" formulas*. Where the accrued benefit equals the sum of the benefit under a lump sum-based benefit formula plus the excess of the benefit under another formula over the benefit under the lump sum-based benefit formula, a single-sum payment of the participant's entire benefit must equal the then-current accumulated benefit under the lump sum-based benefit formula plus the excess of the present value, determined in accordance with section 417(e), of the benefit under the other formula over the present value, determined in accordance with section 417(e), of the benefit under the lump sum-based benefit formula.

* * * * *

(e) * * *

(2) * * *

(ii) *Special effective date*. Paragraphs (b)(2), (b)(3), and (b)(4) of this section apply to plan years that begin on or after January 1, 2012.

* * * * *

Par. 3. Section 1.411(b)–1 is amended by adding paragraphs (b)(2)(ii)(G) and (b)(2)(ii)(H) to read as follows:

§1.411(b)–1 Accrued benefit requirements.

* * * * *

(b) * * *

(2) * * *

(ii) * * *

(G) *Special rule for multiple formulas*. [Reserved].

(H) *Variable interest crediting rate under a statutory hybrid benefit formula*. For plan years that begin on or after January 1, 2012, a plan that determines any portion of the participant's accrued benefit pursuant to a statutory hybrid benefit formula (as defined in §1.411(a)(13)–1(d)(4)) that utilizes an interest crediting rate described in §1.411(b)(5)–1(d) that is a variable rate that was less than zero for the prior plan year is not treated as failing to satisfy the requirements of paragraph (b)(2) of this section for the current plan year merely because the plan assumes for purposes of paragraph (b)(2) of this section that the variable rate is zero for the current plan year and all future plan years.

* * * * *

Par. 4. Section 1.411(b)(5)–1 is amended by:

1. Revising paragraph (c)(3)(iii).

2. Adding *Example 8* to paragraph (c)(5).

3. Revising paragraphs (d)(1)(iv)(D), (d)(2)(ii), (d)(4)(iv), (d)(5)(ii), (d)(5)(iv), (d)(6)(ii), (d)(6)(iii), (e)(2), (e)(3)(iii), (e)(4), and (f)(2)(i)(B).

The revisions and addition read as follows:

§1.411(b)(5)–1 Reduction in rate of benefit accrual under a defined benefit plan.

* * * * *

(c) * * *

(3) * * *

(iii) *Comparison of benefits at effective date of conversion amendment*—(A) *In general*. A plan satisfies the requirements of this paragraph (c)(3)(iii) with respect to a participant only if an opening hypothetical account balance is established to replicate the pre-conversion benefit and the requirements of paragraphs (c)(3)(iii)(B) through (c)(3)(iii)(G) of this section are each satisfied.

(B) *Single-sum payment*. At the annuity starting date, the participant elects to receive payment in the form of a single-sum distribution equal to the sum of the then-current balance of the hypothetical account used to replicate the pre-conversion benefit and the benefit attributable to post-conversion service under the post-conversion benefit formula.

(C) *Not less than pre-conversion benefit*. In accordance with section 411(d)(6), the aggregate benefit payable at the annuity starting date after the effective date of the conversion amendment is not less than the benefit described in paragraph (c)(2)(i)(A) of this section.

(D) *Form of pre-conversion benefit*. The plan, as in effect immediately prior to the effective date of the conversion amendment, either did not provide a single-sum payment option (for benefits that cannot be immediately distributed under section 411(a)(11)) or provided a single-sum payment option that was based solely on the present value of the benefit payable at normal retirement age (or at date of benefit commencement, if later), and which was not based on the present value of the benefit payable commencing at any date prior to normal retirement age.

(E) *Minimum opening account balance*. The plan provides for the opening hypothetical account balance under paragraph (c)(3)(i) of this section to be established in accordance with rules under which the amount of this opening balance will not be less than the present value, determined in accordance with section 417(e), of the participant's accrued benefit under the plan immediately prior to the effective date of the conversion amendment.

(F) *Interest credits*—(*1*) *Requirement as of effective date of conversion amendment.* As of the effective date of the conversion amendment, the interest crediting rate under the plan is an interest crediting rate described in paragraph (d)(3) or (d)(4) of this section. In addition, as of that date, the value of the index used to determine the interest crediting rate under the plan is at least as great for every participant or beneficiary as the interest rate that was used pursuant to paragraph (c)(3)(iii)(E) of this section to determine the opening hypothetical account balance. This requirement is satisfied, for example, if each participant's opening hypothetical account balance is determined using the applicable interest rate and applicable mortality table under section 417(e)(3), the interest crediting rate under the plan is the third segment rate, and, at the effective date of the conversion amendment, the third segment rate is the highest of the three segment rates.

(*2*) *Requirement for later interest crediting rate changes*. If, subsequent to the effective date of the conversion amendment, the interest crediting rate changes (whether by plan amendment or otherwise) with respect to a participant who was a participant at the time of the effective date of the conversion amendment from a particular interest crediting rate described in paragraph (d)(3) or (d)(4) of this section to a different interest crediting rate that is not in all cases at least as great as the prior interest crediting rate under the plan, then the new interest crediting rate does not apply to the existing hypothetical account balance as of the effective date of the change in interest crediting rates (or, if the plan created a subaccount consisting of the opening hypothetical account balance and interest credits on that subaccount, then the new interest crediting rate does not apply to the subaccount).

(G) *Death benefits*. The plan either—

(*1*) Provides a death benefit after the effective date of the conversion amendment which has a present value that is at all times at least equal to the then-current balance of the hypothetical account used to replicate the pre-conversion benefit; or

(*2*) Applied no pre-retirement mortality decrement in establishing the opening hypothetical account balance under paragraph (c)(3)(iii)(E) of this section.

* * * * *

(c) * * *

(5) * * *

Example 8. (i) *Facts where plan establishes opening hypothetical account balance under paragraph (c)(3)(iii) of this section.* Employer O sponsors Plan F, a defined benefit plan that provides an accumulated benefit, payable as a straight life annuity commencing at age 65 (which is Plan F's normal retirement age), based on a percentage of highest average compensation times the participant's years of service. Plan F permits any participant who has had a severance from employment to elect payment in the following optional forms of benefit (with spousal consent if applicable), with any payment not made in a straight life annuity converted to an equivalent form based on reasonable actuarial assumptions: a straight life annuity; and a 50 percent, 75 percent, or 100 percent joint and survivor annuity. The payment of benefits may commence at any time after attainment of age 55, with an actuarial reduction if the commencement is before normal retirement age. In addition, the plan offers a single-sum payment after attainment of age 55 equal to the present value of the normal retirement benefit using the applicable interest rate and mortality table under section 417(e)(3) in effect under the terms of the plan on the annuity starting date. (These facts are the same as those in paragraph (i) of *Example 1*.)

(ii) *Facts relating to the conversion amendment and establishment of opening balance*. On January 1, 2012, Plan F is amended to eliminate future accruals under the highest average compensation benefit formula and to base future benefit accruals on a hypothetical account balance. As of January 1, 2012, the plan establishes an opening hypothetical account balance for each individual who was a participant in the plan on December 31, 2011, equal to the present value of the participant's accumulated benefits, payable as a straight life annuity commencing at age 65, based on the actuarial assumptions then applicable under section 417(e)(3). New participants begin with a hypothetical account balance of zero on their date of participation. For service on or after January 1, 2012, each participant's hypothetical account balance is credited monthly with a pay credit equal to a specified percentage of the participant's compensation during the month and also with interest based on the third segment rate described in section 430(h)(2)(C)(iii). With respect to benefits under the hypothetical account balance, a participant is permitted to elect (with spousal consent) payment in the same generalized optional forms of benefit (even though different actuarial factors apply) as under the terms of the plan in effect before January 1, 2012, and also as a single-sum distribution. The plan provides that in no event will the benefit payable be less than the benefits attributable to service before January 1, 2012, to be determined under the terms of the plan as in effect immediately before the effective date of the amendment. In the event of death prior to the annuity starting date, the plan provides a death benefit equal to the hypothetical account balance (and allows a surviving spouse to elect payment in the form of an actuarially equivalent life annuity).

(iii) *Conclusion*. Plan F satisfies the requirements of paragraph (c)(3)(iii) of this section for participants who elect to receive payment in the form of a single-sum distribution equal to the hypothetical account balance in accordance with the requirements of paragraph (c)(3)(iii)(B) of this section for the following reasons. First, Plan F satisfies the requirements of paragraph (c)(3)(iii)(C) of this section because the benefit payable can never be less than the pre-conversion benefit, in accordance with the requirements of section 411(d)(6). Second, Plan F satisfies the requirements of paragraph (c)(3)(iii)(D) of this section because prior to conversion it provided for a single-sum payment option that was based solely on the present value of the benefit payable at normal retirement age. Third, Plan F satisfies the requirements of paragraph (c)(3)(iii)(E) of this section because the amount of the opening balance is not less than the present value of the participant's accrued benefit under the plan immediately prior to the effective date of the conversion amendment, as determined in accordance with section 417(e). Fourth, Plan F satisfies the requirements of paragraph (c)(3)(iii)(F) of this section because it provides for interest credits that are described in paragraph (d)(3) of this section on the opening balance and the interest credits are reasonably expected to be no lower than the interest rate used to determine the opening balance. This is the case because interest is credited at least annually after the effective date of the conversion amendment and the interest rate used to establish the opening balance (which is based on the first, second, and third segment rates described in section 430(h)(2)(C) referenced under section 417(e)(3)) is not greater than the interest rate applicable under the third segment rate described in section 430(h)(2)(C)(iii) which the plan uses to determine interest for all future periods after the effective date of the conversion amendment. Fifth, Plan F satisfies the requirements of paragraph (c)(3)(iii)(G) of this section because it provides a death benefit after the effective date of the conversion amendment which has a present value that is at all times at least equal to the hypothetical account balance at the date of death.

* * * * *

(d) * * *

(1) * * *

(iv) * * *

(D) *Debits and credits during the interest crediting period*. A plan is not treated as failing to meet the requirements of this paragraph (d) merely because the plan does not provide for interest credits on amounts distributed prior to the end of the interest crediting period. Furthermore, a plan is not treated as failing to meet the requirements of this paragraph (d) merely because the plan calculates increases or decreases to the participant's accumulated benefit by applying a rate of interest or rate of return (including a rate of increase or decrease under an index) to the participant's adjusted accumulated benefit (or portion thereof) for the period. For this purpose, the participant's adjusted accumulated benefit equals the participant's accumulated benefit as of the beginning of the period, adjusted for debits and credits (other than interest credits) made to the accumulated benefit prior to the end of the interest crediting period, with appropriate weighting for those debits and credits based on their timing within the period. For plans that calculate increases or decreases to the participant's accumulated benefit by applying a rate of interest or rate of return to the participant's adjusted accumulated benefit (or portion thereof) for the period, interest credits include these increases and decreases, to the extent provided under the terms of the plan at the beginning of the period and to the extent not conditioned on current service and not made on account of imputed service (as defined in §1.401(a)(4)–11(d)(3)(ii)(B)), and the interest crediting rate with respect to a participant equals the total amount of interest credits for the period divided by the participant's adjusted accumulated benefit for the period.

* * * * *

(2) * * *

(ii) *Application to multiple annuity starting dates*—(A) *In general*. Paragraph (d)(2)(i) of this section applies only at an annuity starting date, within the meaning of §1.401(a)–20, A–10(b), on which a distribution of the participant's entire benefit under the plan's statutory hybrid benefit formula as of that date commences. For a participant who has more than one annuity starting date, paragraph (d)(2)(ii)(B) of this section provides rules for the application of paragraph (d)(2)(i) of this section, taking into account prior distributions. If the comparison under paragraph (d)(2)(ii)(B) of this section results in the sum of principal credits exceeding the sum of the amounts described in paragraphs (d)(2)(ii)(B)(*1*) through (d)(2)(ii)(B)(*3*) of this section, then the participant's benefit to be distributed at the current annuity starting date is increased by an amount equal to the excess.

(B) *Comparison to reflect prior distributions*. For a participant who has more than one annuity starting date, the sum of all principal credits credited to the participant under the plan, as of the current annuity starting date, is compared to the sum of—

(*1*) The participant's benefit as of the current annuity starting date;

(*2*) The amount of the offset to the participant's benefit under the statutory hybrid benefit formula that is attributable to any prior distribution of the participant's benefit under that formula; and

(*3*) The amount of any increase to the participant's benefit as a result of the application of paragraph (d)(2)(i) of this section to a prior distribution.

* * * * *

(4) * * *

(iv) *Fixed rate of interest*. An annual interest crediting rate equal to a fixed 5 percent is deemed to be not in excess of the interest rate described in paragraph (d)(3) of this section.

* * * * *

(5) * * *

(ii) *Actual rate of return on plan assets*. An interest crediting rate equal to the actual rate of return on the aggregate assets of the plan, including both positive returns and negative returns, is not in excess of a market rate of return if the plan's assets are diversified so as to minimize the volatility of returns. This requirement that plan assets be diversified so as to minimize the volatility of returns does not require greater diversification than is required under section 404(a)(1)(C) of Title I of the Employee Retirement Income Security Act of 1974, Public Law 93–406 (88 Stat. 829 (1974)) with respect to defined benefit pension plans.

* * * * *

(iv) *Rate of return on certain RICs*. An interest crediting rate is not in excess of a market rate of return if it is equal to the rate of return on a regulated investment company (RIC), as defined in section 851, that is reasonably expected to be not significantly more volatile than the broad United States equities market or a similarly broad international equities market. For example, a RIC that has most of its assets invested in securities of issuers (including other RICs) concentrated in an industry sector or a country other than the United States, that uses leverage, or that has significant investment in derivative financial products, for the purpose of achieving returns that amplify the returns of an unleveraged investment, generally would not meet this requirement. Thus, a RIC that has most of its investments concentrated in the semiconductor industry or that uses leverage in order to provide a rate of return that is twice the rate of return on the Standard & Poor's 500 index (S&P 500) would not meet this requirement. On the other hand, a RIC whose investments track the rate of return on the S&P 500, a broad-based "small-cap" index (such as the Russell 2000 index), or a broad-based international equities index would meet this requirement.

* * * * *

(6) * * *

(ii) *Annual or more frequent floor applied to bond-based rates*. An interest crediting rate under a plan does not fail to be described in paragraph (d)(3) or (d)(4) of this section for an interest crediting period merely because the plan provides that the interest crediting rate for that interest crediting period equals the greater of—

(A) An interest crediting rate described in paragraph (d)(3) or (d)(4) of this section; and

(B) An annual interest rate of 4 percent (or a *pro rata* portion of an annual interest rate of 4 percent for plans that provide interest credits more frequently than annually).

(iii) *Cumulative floor applied to equity-based or bond-based rates*—(A) *In general*. A plan that determines interest credits under a statutory hybrid benefit formula using a particular interest crediting rate described in paragraph (d)(3), (d)(4), or (d)(5) of this section (or an interest crediting rate that can never be in excess of a particular interest crediting rate described in paragraph (d)(3), (d)(4), or (d)(5) of this section) does not provide an effective interest crediting rate in excess of a market rate of return merely because the plan provides that the participant's benefit under the statutory hybrid benefit formula determined as of the participant's annuity starting date is equal to the greater of—

(*1*) The benefit determined using the interest crediting rate; and

(*2*) The benefit determined as if the plan had used a fixed annual interest crediting rate equal to 3 percent (or a lower rate) for all principal credits that are made during the guarantee period (minimum guarantee amount).

(B) *Guarantee period defined*. The guarantee period is the prospective period which begins on the date on which the cumulative floor described in this paragraph (d)(6)(iii) begins to apply to the participant's benefit and which ends on the date on which that cumulative floor ceases to apply to the participant's benefit.

(C) *Application to multiple annuity starting dates*. The determination under paragraph (d)(6)(iii)(A) of this section is made only at an annuity starting date, within the meaning of §1.401(a)–20, A–10(b), on which a distribution of the participant's entire benefit under the plan's statutory hybrid benefit formula as of that date commences. For a participant who has more than one annuity starting date, paragraph (d)(6)(iii)(D) of this section provides rules for the application of paragraph (d)(6)(iii)(A) of this section, taking into account any prior distributions. If the comparison under paragraph (d)(6)(iii)(D) of this section results in the minimum guarantee amount exceeding the sum of the amounts described in paragraphs (d)(6)(iii)(D)(*1*) through (d)(6)(iii)(D)(*3*) of this section, then the participant's benefit to be distributed at the current annuity starting date is increased by an amount equal to the excess.

(D) *Comparison to reflect prior distributions*. For a participant who has more than one annuity starting date, the minimum guarantee amount (described in paragraph (d)(6)(iii)(A)(*2*) of this section), as of the current annuity starting date, is compared to the sum of—

(*1*) The participant's benefit, as of the current annuity starting date, to which a minimum guaranteed rate described in paragraph (d)(6)(iii)(A)(*2*) of this section applies;

(*2*) The amount of the offset to the participant's benefit under the statutory hybrid benefit formula that is attributable to any prior distribution of the participant's benefit under that formula and to which a minimum guaranteed rate described in paragraph (d)(6)(iii)(A)(*2*) of this section applied, together with interest at that minimum guaranteed rate annually from the prior annuity starting date to the current annuity starting date; and

(*3*) The amount of any increase to the participant's benefit as a result of the application of paragraph (d)(6)(iii)(A) of this section to any prior distribution, together with interest annually at the minimum guaranteed rate that applied to the prior distribution from the prior annuity starting date to the current annuity starting date.

(E) *Application to portion of participant's benefit*. A cumulative floor described in this paragraph (d)(6)(iii) may be applied to a portion of a participant's benefit, provided the requirements of this paragraph (d)(6)(iii) are satisfied with respect to that portion of the benefit. If a cumulative floor described in this paragraph (d)(6)(iii) applies to a portion of a participant's benefit, only the principal credits that are attributable to that portion of the participant's benefit are taken into account in determining the amount of the guarantee described in paragraph (d)(6)(iii)(A)(*2*) of this section.

* * * * *

(e) * * *

(2) *Plan termination*—(i) *In general*—(A) *Interest crediting rates*. If the interest crediting rate used to determine a participant's accumulated benefit (or a portion thereof) has been a variable rate during the interest crediting periods in the 5-year period ending on the plan termination date (including any case in which the rate was not the same fixed rate during all such periods), then a statutory hybrid plan is treated as meeting the requirements of section 411(b)(5)(B)(i) and paragraph (d)(1) of this section only if the terms of the plan satisfy the requirements of paragraph (e)(2)(ii) of this section. See regulations of the Pension Benefit Guaranty Corporation for additional rules that apply when a pension plan is terminated.

(B) *Annuity conversion factors*. A statutory hybrid plan is treated as meeting the requirements of section 411(b)(5)(B)(i) and paragraph (d)(1) of this section only if the terms of the plan provide that the interest rate and mortality table (including tabular adjustment factors) used on and after plan termination for purposes of determining the amount of any benefit under the plan payable in the form of an annuity commencing at or after normal retirement age are the interest rate and mortality table specified under the plan for that purpose as of the termination date, except that if the interest rate is a variable rate (as described in paragraph (e)(2)(i) of this section), then the interest rate for that purpose is determined pursuant to the rules of paragraph (e)(2)(ii) of this section.

(ii) *Interest crediting rates that are variable*—(A) *General rule*. Subject to the other rules in this paragraph (e)(2), a plan satisfies this paragraph (e)(2)(ii) only if the terms of the plan provide that, on the plan termination date, if the interest crediting rate used to determine a participant's accumulated benefit has been a variable rate as described in paragraph (e)(2)(i) of this section, then the interest crediting rate used to determine the participant's accumulated benefit under the plan after the date of plan termination is equal to the average of the interest crediting rates used under the plan during the 5-year period ending on the plan termination date. For this purpose, an interest crediting rate is used under the plan if the rate applied under the terms of the plan during an interest crediting period for which the interest crediting date is within the 5-year period ending on the plan termination date and the average is determined as the arithmetic average of the rates used, with each rate adjusted to reflect the length of the interest crediting period and the average rate expressed as an annual rate.

(B) *Variable interest crediting rates that are based on interest rates*. With respect to an interest crediting rate that was a variable interest rate described in paragraph (d)(3) or (d)(4) of this section (taking into account the rules of paragraph (d)(6)(ii) of this section), a variable interest rate that can never be in excess of a rate described in paragraph (d)(3) or (d)(4) of this section, or a fixed interest rate that has not been the same rate during the entire 5-year period ending on the plan termination date, the actual interest rate that applied under the plan for the interest crediting period is used for purposes of determining the average interest crediting rate. For this purpose, the rate that applied for the interest crediting period takes into account minimums, maximums, and other reductions that applied in the period, other than cumulative floors under paragraph (d)(6)(iii) of this section.

(C) *Variable interest crediting rates that are other rates of return*. With respect to any interest crediting rate not described in paragraph (e)(2)(ii)(B) of this section (that is, a variable rate described in paragraph (d)(5) of this section), the interest crediting rate that applied for the interest crediting period for purposes of determining the average interest crediting rate is deemed to be equal to the third segment rate under section 430(h)(2)(C)(iii) for the last calendar month ending before the beginning of the interest crediting period, as adjusted to account for any minimums or maximums that applied in the period (other than cumulative floors under paragraph (d)(6)(iii) of this section), but without regard to other reductions that applied in the period. Thus, for example, if the actual interest crediting rate in an interest crediting period was equal to the rate of return on plan assets, but not greater than 5 percent, then for purposes of determining the plan's average interest crediting rate, the interest crediting rate for that interest crediting period would be deemed to equal the lesser of the applicable third segment rate for the period and 5 percent. However, if the actual interest crediting rate in an interest crediting period was equal to the rate of return on plan assets minus 200 basis points, then for purposes of determining the plan's average interest crediting rate, the interest crediting rate for that interest crediting period would be deemed to equal the third segment rate.

(iii) *Rules of application*—(A) *Section 411(d)(6) protected benefits*. In general, for purposes of determining the average interest crediting rate under paragraph (e)(2)(ii) of this section, the interest crediting rate that applied for each interest crediting period is the ongoing interest crediting rate that was specified under the plan in that period, without regard to any section 411(d)(6) protected benefit using an interest crediting rate that applied under the plan prior to amendment. However, if, at the end of the last interest crediting period prior to plan termination, the participant's accumulated benefit is based on a section 411(d)(6) protected benefit that results from a prior amendment to change the rate of interest crediting applicable under the plan, then, for purposes of determining the average interest crediting rate under paragraph (e)(2)(ii) of this section, the pre-amendment interest crediting rate is treated as having applied for each interest crediting period after the date of the interest crediting rate change.

(B) *Weighted averages*. If the plan determines the interest credit in any interest crediting period by applying different rates to different predetermined portions of the accumulated benefit under paragraph (d)(1)(vii) of this section, then, for purposes of determining the average interest crediting rate under paragraph (e)(2)(ii) of this section, the interest crediting rate that applied for the interest crediting period is the weighted average of the relevant interest rates that apply, under the rules of paragraph (e)(2)(ii) of this section, to each portion of the accumulated benefit.

(C) *Participants with less than five years of interest credits upon plan termination*. If the plan provided for interest credits for any interest crediting period in which, pursuant to the terms of the plan, the individual was not eligible to receive interest credits (because the individual was not a participant or beneficiary in the relevant interest crediting period or otherwise), then, for purposes of determining the individual's average interest crediting rate under paragraph (e)(2)(ii) of this section, the individual is treated as though the individual received interest credits in that period using the interest crediting rate that applied in that period under the terms of the plan to a similarly situated participant or beneficiary who was eligible to receive interest credits. However, if, under the terms of the plan, the individual was not eligible to receive any interest credits during the entire 5-year period ending on the plan termination date, then the rules under paragraph (e)(2)(ii) do not apply to determine the individual's benefit after plan termination.

(iv) *Examples*. The following examples illustrate the rules of this paragraph (e)(2). In each case, it is assumed that the plan is terminated in a standard termination.

Example 1. (i) *Facts*. Plan A is a defined benefit plan with a calendar plan year that expresses each participant's accumulated benefit in the form of a hypothetical account balance to which principal credits are made at the end of each calendar quarter and to which interest is credited at the end of each calendar quarter based on the balance at the beginning of the quarter. Interest credits under Plan A are based on a rate of interest fixed at the beginning of each plan year equal to the third segment rate for the preceding December, except that the plan used the rate of interest on 30-year Treasury bonds (instead of the third segment rate) for plan years before 2012. The plan is terminated on March 3, 2016. The third segment rate credited under Plan A from January 1, 2012, through December 31, 2015, is assumed to be: 6 percent annually for each of the four quarters in 2015 (1.5 percent quarterly); 6.5 percent annually for each of the four quarters in 2014 (1.625 percent quarterly); 6 percent annually for each of the four quarters in 2013 (1.5 percent quarterly); and 5.5 percent annually for each of the four quarters in 2012 (1.375 percent quarterly). The rate of interest on 30-year Treasury bonds credited under Plan A for each of the four quarters in 2011 is assumed to be 4.4 percent annually (1.1 percent quarterly).

(ii) *Conclusion*. Pursuant to paragraph (e)(2)(ii)(B) of this section, the interest crediting rate used to determine accrued benefits under the plan on and after the date of plan termination is 5.68 percent. This is determined by calculating the average quarterly rate of 1.42 percent (the sum of 1.5 percent times 4, 1.625 times 4, 1.5 times 4, 1.375 times 4, and 1.1 percent times 4, divided by the 20 quarters that end in the 5-year period from March 4, 2011 to March 3, 2016) and multiplying such rate by 4 to determine the average annual rate.

Example 2. (i) *Facts*. The facts are the same as *Example 1*, except that Participant B commenced participation in Plan A on April 17, 2013.

(ii) *Conclusion*. Pursuant to paragraph (e)(2)(iii)(C) of this section, the interest crediting rate used to determine Participant B's accrued benefits under Plan A on and after the date of plan termination is 5.68 percent, which is the same rate that would have applied to Participant B if Participant B had participated in the plan during the 5-year period preceding the date of plan termination, as described in *Example 1*.

Example 3. (i) *Facts*. Plan C is a defined benefit plan with a calendar plan year that expresses each participant's accumulated benefit in the form of a hypothetical account balance to which principal credits are made at the end of each calendar year and to which interest is credited at the end of each calendar year based on the balance at the end of the preceding year. The plan is terminated on January 27, 2014. The plan's interest crediting rate for each calendar year during the entire 5-year period ending on the plan termination date is equal to (A) 50 percent of the greater of the rate of interest on 3-month Treasury Bills for the preceding December and an annual rate of 4 percent, plus (B) 50 percent of the rate of return on plan assets. The rate of interest on 3-month Treasury Bills credited under Plan C is assumed to be: 3.4 percent for 2013; 4 percent for 2012; 4.5 percent for 2011; 3.5 percent for 2010; and 4.2 percent for 2009. Each of these rates applied under Plan C for interest credited during this period for purposes of the interest credits described in clause (A) of this paragraph (i), except that the 4 percent minimum rate applied for 2013 and 2010. For purposes of the interest credits described in clause (B) of this paragraph (i), the rate of interest on the third segment rate in the prior years (based on the rate for the preceding December) is assumed to be: 6 percent for 2013; 6.5 percent for 2012; 6 percent for 2011; 5.5 percent for 2010; and 6 percent for 2009.

(ii) *Conclusion*. Pursuant to paragraph (e)(2)(ii) of this section, the interest crediting rate used to determine accrued benefits under the plan on and after the date of plan termination is 5.07 percent. This number is equal to the sum of 50 percent of 4.14 percent (which is the sum of 4 percent, 4 percent, 4.5 percent, 4 percent, and 4.2 percent, divided by 5), and 50 percent of 6 percent (which is the average third segment rate for the 5 interest crediting periods ending within the 5-year period).

Example 4. (i) *Facts*. The facts are the same as in *Example 3*, except that the plan had credited interest before January 1, 2012, using the rate of return on a RIC and was amended effective January 1, 2012, to base interest credits for all plan years after 2011 on the interest rate formula described in *Example 3*(i). In order to comply with section 411(d)(6), the plan provides that, for each participant or beneficiary who was a participant on December 31, 2011, the benefits at any date are based on either the ongoing hypothetical account balance on that date (which is based on the December 31, 2011 balance, with interest credited thereafter at the rate described in the first sentence of *Example 3*(i) and taking principal credits after 2011 into account) or a special hypothetical account balance (the pre–2012 balance) on that date, whichever balance is greater. For each participant, the pre–2012 balance is a hypothetical account balance equal to the participant's December 31, 2011, balance, with interest credited thereafter at the RIC rate of return, but with no principal credits after 2011. There are 10 participants for whom his or her pre–2012 balance exceeded his or her ongoing hypothetical account balance at the end of 2013.

(ii) *Conclusion*. Since Plan C credited interest prior to 2012 using the rate of return on a RIC (a rate not described in paragraph (d)(3) or (d)(4) of this section), for purposes of determining the average interest crediting rate upon plan termination, the interest crediting rate used to determine accrued benefits under Plan C for all participants during those periods (for the calendar years 2009, 2010, and 2011) is deemed to be equal to the third segment rate for the preceding December. In addition, since the pre–2012 balances exceeded the ongoing hypothetical account balance for 10 participants in the last interest crediting period prior to plan termination, for purposes of determining the average interest crediting rate upon plan termination, the interest crediting rate used to determine accrued benefits under Plan C for 2012 and 2013 for those participants is deemed to be equal to the third segment rate for the month of December preceding 2012 and the month of December preceding 2013, respectively. For all other participants, for purposes of determining the average interest crediting rate upon plan termination, the interest crediting rate used to determine accrued benefits under Plan C for 2012 and 2013 is based on the ongoing interest crediting rate (the formula described in *Example 3*).

(3) * * *

(iii) *Coordination of section 411(d)(6) and market rate of return limitation*—(A) *In general*. An amendment to a statutory hybrid plan that preserves a section 411(d)(6) protected benefit is subject to the rules under paragraph (d) of this section relating to market rate of return. However, in the case of an amendment to change a plan's interest crediting rate for periods after the applicable amendment date from one interest crediting rate (the old rate) that satisfies the requirements of paragraph (d) of this section to another interest crediting rate (the new rate) that satisfies the requirements of paragraph (d) of this section, the plan's effective interest crediting rate is not in excess of a market rate of return for purposes of paragraph (d) of this section merely because the plan provides for the benefit of any participant who is benefiting under the plan (within the meaning of §1.410(b)–3(a)) on the applicable amendment date to never be less than what it would be if the old rate had continued but without taking into account any principal credits (as defined in paragraph (d)(1)(ii)(D) of this section) after the applicable amendment date.

(B) *Multiple amendments*. A pattern of repeated plan amendments each of which provides for a prospective change in the plan's interest crediting rate with respect to the benefit as of the applicable amendment date will be treated as resulting in the ongoing plan terms providing that the interest crediting rate equals the greater of each of the interest crediting rates, so that the rule in paragraph (e)(3)(iii)(A) of this section would not apply. See §1.411(d)–4, A–1(c)(1).

(4) *Actuarial increases after normal retirement age*. A statutory hybrid plan is not treated as providing an effective interest crediting rate that is in excess of a market rate of return for purposes of paragraph (d) of this section merely because the plan provides that the participant's benefit, as of each annuity starting date after normal retirement age, is equal to the greater of—

(i) The benefit determined using an interest crediting rate that is not in excess of a market rate of return under paragraph (d) of this section; and

(ii) The benefit that satisfies the requirements of section 411(a)(2).

* * * * *

(f) * * *

(2) * * *

(i) * * *

(B) *Special effective date*. Paragraphs (c)(3)(iii), (d)(1)(iii), (d)(1)(iv)(D), (d)(1)(vi), (d)(2)(ii), (d)(4)(iv), (d)(5)(iv), (d)(6), (e)(2), (e)(3)(iii), and (e)(4) of this section apply to plan years that begin on or after January 1, 2012.

* * * * *

Steven T. Miller,
Deputy Commissioner for Services and Enforcement.

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Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in laws or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in a new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statement of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D. —Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z —Corporation.

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Key to Abbreviations:

Ann	Announcement
CD	Court Decision
DO	Delegation Order
EO	Executive Order
PL	Public Law
PTE	Prohibited Transaction Exemption
RP	Revenue Procedure
RR	Revenue Ruling
SPR	Statement of Procedural Rules
TC	Tax Convention
TD	Treasury Decision
TDO	Treasury Department Order

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