

May 12, 2000

HAND DELIVERED

CC:DOM:CORP:R (Notice 2000-14)
Courier's Desk
Internal Revenue Service
1111 Constitution Avenue NW
Washington, DC 20224

Re: Securities Industry Association Comments on IRS Notice 2000-14

On behalf of the Securities Industry Association (SIA), this letter responds to the request for comment contained in IRS Notice 2000-14 (the Notice) regarding the application of the requirements of Internal Revenue Code section 401(a)(4)¹ and the regulations thereunder (the section 401(a)(4) regulations) to so-called new comparability plans. The SIA is the securities industry trade association, representing the business interests of more than 700 securities firms in North America, most of which provide services with respect to retirement plans that could be affected by a reopening of the section 401(a)(4) regulations.

At the outset, it is important to note that the section 401(a)(4) regulations are only one component of a comprehensive and intertwined series of nondiscrimination regulations that were the product of nearly a decade of notice, comment, issuance, and reissuance. In fact, from the first consideration of the nondiscrimination regulations following changes made by the Tax Reform Act of 1986 until the issuance of final regulations in 1993, the various components of the nondiscrimination regulations were the subject of constant study, deliberation and revision.

The comprehensive package of nondiscrimination regulations that evolved from that lengthy deliberative process, including in particular the decision to permit cross-testing, was based on the basic premise that a consistent reading of the Code section 401(a)(4) requirements across all types of retirement plans is warranted based on the statutory language. As drafted, the nondiscrimination regulations are logical and

¹ Unless otherwise indicated, all section references are to the Internal Revenue Code of 1986 (the Code), as amended.

effective and operating as envisioned. Those regulations treat defined benefit and defined contribution plans comparably and ensure that retirement benefits are provided to a cross-section of the workforce.

On the whole, the nondiscrimination regulations evidence thoughtful deliberation by policymakers, including many members of Congress, in conjunction with the active input of all stakeholders in the process. In this regard, it should be noted that Congress has been aware of, and has considered, the issues raised in Notice 2000-14. In 1994, Congress specifically rejected legislative proposals that would have restricted cross-testing. Significantly, in response to the complete package of final regulations (and Congressional rejection of legislative proposals to change those rules), *every retirement plan* in America was reevaluated and amended an expensive and time-consuming process that was not, for the most part, completed until 1995.

For these basic reasons, we strongly urge you to proceed cautiously before considering any amendment to the nondiscrimination regulations. Even consideration of another change to the nondiscrimination regulations could have a chilling effect on retirement plan adoption and maintenance. *Absent compelling evidence of broad-based and actual abuse, no action should be taken.* To the extent isolated examples of untoward disparities in benefits exist, other avenues of challenge should be explored before the nondiscrimination regulations are reopened.

To date, no showing of systemic and serious abuse has been made. Hypothetical examples (or even isolated actual plans) that posit potentially large disparities between high-paid and low-paid contributions in a given year are not sufficient to justify reopening the section 401(a)(4) regulations. This is particularly true in light of the lengthy consideration of the package of nondiscrimination regulations, and the substantial disruption and instability that would be caused by changing the section 401(a)(4) regulations.

If, however, the nondiscrimination regulations are re-opened, we strongly urge that any reconsideration be subject to the same notice, comment, and issuance procedures as the original regulations. Anything less would risk that the proposed changes would be more sweeping than the perceived problems that the changes are purported to address. This would cause severe disruption and potential disqualification of retirement plans that were not intended to be affected and could cause some employers to terminate their plans.

This potential for an overly broad revision of the section 401(a)(4) regulations can be seen in the proposal for change contained in the Notice. The Notice posits a typical new comparability plan with very high allocation rates for the highly compensated employees and with allocation rates of only 3 percent for nonhighly compensated employees. A possible approach for addressing the problem of these so-called new comparability plans is then posited in the Notice an approach that could potentially

affect *all* defined contribution plans that cross-test or that might cross-test in the future. Specifically, the Notice proposes that the right to receive *each rate* of nonelective employer contributions must be currently and effectively available on a nondiscriminatory basis. Realizing that this blanket general rule is overly broad, the Notice then posits that, subject to certain conditions (which are unspecified), differences in attained age or service could be disregarded in determining if contribution rates are currently available. The Notice then states that generic age-weighted or service-based plans . . . and certain other appropriate plan designs would be permitted. There is no discussion of other appropriate plan designs.

One practice utilized today is where an employer provides different contribution rates for employees of different divisions based on competitive market pressures. While those plans would pass the rules in effect today when cross-tested, they might not pass the test proposed in the Notice.

Similarly, it is not unusual for employers that are modifying the terms of a retirement plan to allow older employees who are close to retirement (or all existing employees) to remain under the old benefit formula. Providing this type of benefit for a subset of the workforce is generally permitted as long as the benefits do not discriminate in favor of highly compensated employees. These transition benefits could not, however, satisfy the new standard that would be established by the Notice because they are not based on attained age or service e.g., new hires could not grow into the benefits.

While these are only a few of the examples of the unintended consequences that will arise if the section 401(a)(4) regulations are reopened, they have one thing in common. Despite the fact that the benefits are established for a legitimate business purpose and have none of the characteristics of new comparability plans, they would nonetheless be disrupted.

The experience of our member firms suggests that many small plan sponsors are using the opportunities made available by cross testing employer contributions to expand the benefits provided to their employees. This includes starting qualified retirement programs where none existed previously or increasing the level of employer contributions in existing qualified retirement programs. Some plan sponsors have also taken the opportunity to add 401(k) features to their existing profit sharing plans. This incentive to add 401(k) features to existing profit sharing plans, expanding the benefits provided to their employees, is especially true in cases where the existing qualified retirement plans were top heavy. In these cases, concerns regarding required employer contributions were mitigated by the cross testing. Significant changes to the 401(a)(4) regulations will inhibit plan sponsors ability and desire to expand the benefits to their employees.

Many retirement plan sponsors, particularly small employers, are already having a difficult time meeting the administrative expenses of maintaining a retirement plan without having to deal with unwarranted

Internal Revenue Service
May 12, 2000
Page 4

regulatory changes that will necessitate further revisions to existing retirement plans. For some of these employers, the added burden of yet another new regulatory requirement could force plan abandonment. For others, including the vast majority of plans that do not in any way resemble the hypothetical new comparability plan described in the Notice, any change in the rules could still require a costly review and potential reevaluation of plan terms.

For all these reasons, we urge you to carefully consider whether any change in the section 401(a)(4) regulations is justified at this time. We appreciate your consideration of our views. If you have any questions or would like to further discuss these comments, please contact Liz A. Liess at 202-326-5353.

Sincerely,

Maryanne Elias, Chair
Retirement Products & Estate Planning Committee