



*Cash Balance Plan Update*

In a twenty-page decision issued on November 21, 2005, Judge LeGrome Davis dismissed an age discrimination claim against PNC's cash balance plan identical to the claim against IBM's cash balance plan that the Southern District of Illinois had sustained on July 31, 2003 *Register v. PNC Financial Services Group, Inc.*, No. 04-CV-6097 (E.D. Pa. Nov. 21, 2005). *PNC* is the best reasoned of the growing list of decisions that have rejected the assault on cash balance plans by Chief Judge Murphy in *Cooper v. IBM Personal Pension Plan*, 274 F. Supp. 2d 1010 (S.D. Ill. 2003). See, e.g., *Tootle v. ARINC, Inc.*, 222 F.R.D. 88, 93 (D. Md. 2004); *Eaton v. Onan Corp.*, 117 F. Supp. 2d 812 (S.D. Ind. 2000). See also *Campbell v. BankBoston, N.A.*, 327 F.3d 1, 9 (1st Cir. 2003) (detailing, but not resolving, dispute).

Both Judge Davis's *PNC* decision and Chief Judge Murphy's decision in *Cooper v. IBM Personal Pension Plan*, 274 F. Supp. 2d 1010 (S.D. Ill. 2003), arose in the context of a conversion from a traditional defined benefit plan to a cash balance plan. Both decisions considered whether a cash balance plan complies with ERISA § 204(b)(1)(H)'s directive that a defined benefit plan violates ERISA if, under the plan, "the employee's benefit accrual is ceased, or the rate of an employee's benefit accrual is reduced, because of the attainment of any age." Both decisions recognized, as Judge Davis stated, that "[t]he issue is whether the 'rate of an employee's benefit accrual' for a cash balance plan refers to the change in the form of an annuity that commences at age 65 or to the annual amount credited to the employee's cash balance account."

The analyses in the decisions differ dramatically. While *IBM* concluded that cash balance plans almost inherently violate ERISA § 204(b)(1)(B) by reducing the "rate of an employee's benefit accrual," when a participant's accrued benefit is expressed as a single life annuity commencing at normal retirement age (usually 65), Judge Davis concluded that the phrase "rate of an employee's benefit accrual" in ERISA § 204(b)(1)(H) "does not require that the rate be measured solely in terms of an annuity payable at normal retirement age." After noting that ERISA does not define "benefit accrual," Judge Davis in *PNC* rejected the *IBM* analysis in holding that "the rate of benefit accrual is determined by the change in the account balance" so that PNC's (and other) cash balance plans do not violate ERISA's age discrimination provisions.

In reaching his decision in *IBM*, Chief Judge Murphy adopted the proposition, first espoused by Professor Zelinsky, that cash balance plans, as customarily designed, inherently violate ERISA's benefit accrual rate age discrimination provisions because the rate of an



employee's benefit accrual must be determined solely in terms of a single life NRA annuity. Chief Judge Murphy, who purported to rely solely on the language of ERISA, ignored the previously decided *Eaton*, legislative history and the proposed regulations issued by Treasury. In the *IBM* opinion, Chief Judge Murphy even deleted from the ERISA definition of "accrued benefit," the concept of actuarial equivalence that ERISA's statutory definitions incorporate.

In declining to follow *IBM*, Judge Davis considered all preceding case law (even discounting some of the analysis in *Eaton* and *Tootle*), the language of ERISA § 204(b)(1)(H), its legislative history, and administrative interpretations by Treasury in both its 2002 proposed regulations and the 2005 and 2006 Revenue Proposals. Judge Davis concluded that the "secondary analysis" in *Eaton* was correct, *viz.*, "the accrual rate should be 'the change in the employee's cash balance account from one year to the next.'" *Eaton*, 117 F. Supp. 2d at 832-33."

A simple example demonstrates the difference in the analyses. Under the *PNC* analysis, a five-year employee first employed at age 25 at a fixed salary of \$20,000 has the same "accrued benefit" in a cash balance plan that provides service credits at 2% of salary and interest credits at the statutorily mandated discount rate as a five-year employee first employed at age 60 at the same fixed salary of \$20,000 because each has the same cash balance account,. Under Chief Judge Murphy's analysis in *IBM*, the accrued benefit for the younger employee when expressed as a single life annuity at normal retirement age of 65 is greater than that of the older employee so that the accrual rate is treated as having been reduced due to age, even though the accrued benefits expressed as single life annuities for the two employees are actuarially equivalent at any point in time.

The *PNC* decision is another piece of the ongoing puzzle as to the legal status of cash balance plans. Judge Davis's analysis in *PNC* is likely to influence, but may not be dispositive of, the pending Seventh Circuit *IBM* appeal in which briefing is still ongoing and a decision is (at least) months away. Indeed, *PNC* creates the likelihood that the Third Circuit will address the issues being presented in the *IBM* appeal, although most likely after the Seventh Circuit rules, with the possibility that there could be a split in the circuits, warranting intervention by the Supreme Court to resolve this dispute that has evaded legislative resolution to date.

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