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National Association of Counties (NACo)
American Federation of Teachers (AFT)
United States Conference of Mayors (USCM)
Fraternal Order of Police (FOP)
International Brotherhood of Teamsters (IBT)
National League of Cities (NLC)
International Association of Fire Fighters (IAFF)
International City/County Management Association (ICMA)
National Education Association (NEA)
National Association of State Auditors Comptrollers and Treasurers (NASACT)
National Association of Police Organizations (NAPO)
National Association of State Treasurers (NAST)
Government Finance Officers Association (GFOA)
International Public Management Association for Human Resources (IPMA-HR)
National Association of State Retirement Administrators (NASRA)
National Conference on Public Employee Retirement Systems (NCPERS)
National Council on Teacher Retirement (NCTR)
National Association of Government Defined Contribution Administrators (NAGDCA)
National Public Employer Labor Relations Association (NPELRA)
National Conference of State Social Security Administrators (NCSSSA)
Service Employees International Union (SEIU)

February 21, 2008

The Honorable George Miller
Chairman, Committee on Education & Labor
U.S. House of Representatives
Washington, DC 20515

RE: Needed Technical Correction for Public Employee Pensions

Dear Mr. Chairman:

On behalf of the twenty-one national organizations listed above—representing state and local governments and officials, public employee unions, public retirement systems, and more than 20 million state and local government employees, retirees, and their beneficiaries—we are writing to request your assistance in making a needed technical correction to the Pension Protection Act (PPA) of 2006 to ensure restrictions aimed at issues in the ERISA plan setting do not impose benefit cuts on employees in governmental defined benefit plans. Specifically, we strongly support a needed statutory clarification to ensure rates of interest established by or in accordance with State or local laws are treated as permissible methods of crediting interest.

At issue is a requirement in the PPA stipulating that in order to comply with age discrimination laws the rate of interest used by a defined benefit plan can be **no greater** than a “market rate of return.” This cap is aimed at issues that arise under ERISA. In the public plan setting – where benefit protections and plan designs are quite different – the application of an interest rate cap would cut employee benefits, may actually conflict with State and local benefit guarantees, and also undermine efforts to preserve underlying defined benefit features.

Most governmental pension plans credit interest in some fashion, whether on refunds of contributions, deferred retirement option plans (DROPs), survivor benefits, or other optional forms of benefit common in public sector plans. These plan features are set through public law to achieve different objectives. In some cases, the structure was designed to protect public plan participants from the ravages of inflation or downside investment risk, in others to allow members to share in the investment gains of the plan. Many apply solely to optional ancillary provisions added to provide flexibility or accommodate the needs of short-service employees while safeguarding the traditional pension as the primary plan benefit. Nevertheless, State statutes and/or local ordinances guaranteeing numerous types of interest credit, including set, underlying or minimum rates of return, could be in excess of a new federal limitation in any particular year.

It is our understanding that PPA technical corrections legislation may soon be considered. We strongly urge your support of including a statutory clarification to ensure rates of interest guaranteed under State and local governmental plans are not in conflict with new federal requirements.

Attached is a one-page summary of the issue. If you have any questions or need additional information, please do not hesitate to contact the legislative representatives of our organizations:

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Impact of PPA's Interest Credit Limitations on Public Employee Plans

Restrictions in the Pension Protection Act (PPA) of 2006, Aimed at ERISA Plan Issues, Could Conflict with State and Local Government Employee Benefit Guarantees and Protections

Most Public DB Plans Credit Interest in Some Fashion. The current statutory definition of an “applicable defined benefit plan” subject to the limitations set forth in the PPA is being interpreted to cover numerous traditional DB plans with features and options that provide interest crediting. Treasury has indicated this would likely apply to long-standing public plan designs not subject to interest rate requirements under ERISA, as well as the vast majority of traditional public DB plans that credit interest on **refunds of contributions**, provide interest-bearing deferred retirement option plans (**DROPs**), **survivor benefits**, or other **optional forms of benefit** common in public sector plans that make these arrangements more attractive to public workers. These plan features have been adopted in open public legislative processes that included significant employee participation and in many cases were promoted by the employee groups themselves.

Cap on Interest Rates Could Conflict with State Guarantees and Efforts to Preserve Underlying Defined Benefit Features. The PPA stipulates that in order to comply with age discrimination laws the rate of interest used by an applicable defined benefit plan must be **no greater** than a “market rate of return.” State statutes and/or local ordinances guarantee numerous types of interest credit, including set, underlying or minimum rates of return that could be in excess of this new federal limitation in any particular year. State and local interest rate structures are set through public law to achieve different objectives. In some cases, the structure was designed to protect public plan participants from the ravages of inflation or downside investment risk, in others to allow members to share in the investment gains of the plan. Many apply solely to optional ancillary provisions added to provide flexibility or accommodate the needs of short-service employees while safeguarding the traditional pension as the primary plan benefit.

State and Local Protections Already Exist. State and local government constitutional, statutory, contractual and/or case law would generally prohibit conversions of traditional DB plans to cash balance or any other plan design, as most public employees are not only guaranteed what they have earned to date, but their future accruals are safeguarded as well. Such protections mean that any changes in the pension design are prospective only – applying solely to the way benefits will be provided to future employees.

Cross-Reference to Inapplicable Federal Laws Presents a Catch-22. Most of the cash balance and hybrid plan provisions of the PPA amend parts of the Internal Revenue Code (IRC) and ERISA from which governmental plans are exempt. The legislation’s modification to the Age Discrimination in Employment Act (ADEA), however, applies to private and public sector plans alike yet cross-references definitions in ERISA and parts of the IRC inapplicable to public sector plans. Because public plans are not subject to these cross-referenced sections of the Code and ERISA, Treasury's conforming regulations to these sections cannot make special accommodations for the specific designs and protections inherent in State and local government plans. Furthermore, since the Equal Employment Opportunity Commission (EEOC), which implements ADEA, is required by law to use the IRC definitions, this agency also cannot provide such relief. In short, even if Treasury or EEOC were to agree that a problem exists, neither agency appears to believe it has regulatory authority to deal with it.

Clarification Needed. The unique protections and plan designs inherent in State and local government retirement systems cannot be accommodated in regulations written for parts of the IRC and ERISA inapplicable to the public sector. A statutory clarification is needed to ensure rates of interest provided by State or local governmental plans in accordance with a statute, ordinance, administrative procedure, collective bargaining agreement or other public process, are treated as permissible methods of crediting interest under the PPA.