



**SUMMARY:** This document contains proposed regulations that provide guidance on calculation of an employee's accrued benefit derived from the employee's contributions to a qualified defined benefit pension plan. These regulations are issued to reflect changes to the applicable law made by the Omnibus Budget Reconciliation Act of 1987 (OBRA '87) and the Omnibus Budget Reconciliation Act of 1989 (OBRA '89). OBRA '87 and OBRA '89 amended the law to change the accumulation of employee contributions and the conversion of those accumulated contributions to employee-derived accrued benefits.

**DATES:** Written comments and requests for a public hearing must be received by March 21, 1996.

**ADDRESSES:** Send submissions to: CC:DOM:CORP:R (EE-35-95), Room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R (EE-35-95), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC.

**FOR FURTHER INFORMATION CONTACT:** Concerning the regulations, Janet A. Laufer, (202) 622-4606, concerning submissions, Michael Slaughter, (202) 622-7190 (not toll-free numbers).

**SUPPLEMENTARY INFORMATION:**

*Background*

This document contains proposed amendments to regulations containing rules for computing an employee's accrued benefit derived from the employee's contributions to a qualified defined benefit pension plan. The proposed amendments reflect changes made to section 411(c)(2) by the Omnibus Budget Reconciliation Act of 1987, Public Law 100-203 (OBRA '87), and the Omnibus Budget Reconciliation Act of 1989, Public Law 101-239 (OBRA '89). OBRA '87 and OBRA '89 changed the interest rates used to accumulate an employee's contributions to normal retirement age. OBRA '89 also changed the manner in which the accumulated contributions

are converted to an annual benefit payable at normal retirement age, and removed a limitation on the employee-derived accrued benefit contained in prior law.

Section 411(c)(1) provides that an employee's accrued benefit derived from employer contributions as of any applicable date is the excess, if any, of the accrued benefit for the employee as of that date over the accrued benefit derived from contributions made by the employee as of that date. Section 411(c)(2)(B) provides that in the case of a defined benefit plan, the accrued benefit derived from contributions made by an employee as of any applicable date is the amount equal to the employee's contributions accumulated to normal retirement age using the interest rate(s) specified in section 411(c)(2)(C), expressed as an actuarially equivalent annual benefit commencing at normal retirement age using an interest rate which would be used by the plan under section 417(e)(3), as of the determination date. If the employee-derived accrued benefit is determined with respect to a benefit other than an annual benefit in the form of a single life annuity (without ancillary benefits) commencing at normal retirement age, section 411(c)(3) requires that the employee-derived accrued benefit be the actuarial equivalent of the benefit determined under section 411(c)(2).

Under section 411(c)(2)(C)(iii)(I), effective for plan years beginning after December 31, 1987, the interest rate used to accumulate an employee's contributions until the determination date is 120 percent of the Federal mid-term rate under section 1274 of the Internal Revenue Code (Code). For the period between the determination date and normal retirement age, section 411(c)(2)(C)(iii)(II) provides that the interest rate used to accumulate an employee's contributions is the interest rate which would be used under the plan under section 417(e)(3) as of the determination date. As noted above, section 411(c)(2)(B) provides that the interest rate which would be used under the plan under section 417(e)(3) as of the determination date also applies for purposes of converting the accumulated contributions to an annual benefit commencing at normal retirement age. The Retirement Protection Act of 1994, Public Law 103-465 (RPA '94) amended section 417(e) to change the applicable interest rate

---

**Notice of Proposed Rulemaking**

**Allocation of Accrued Benefits Between Employer and Employee Contributions**

**EE-35-95**

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Notice of proposed rule-making.

under section 417(e)(3) and to specify the applicable mortality table under that section. Examples contained in §1.411(c)-1(c)(6) of these proposed regulations reflect a plan that has been amended to comply with the interest rate and mortality table specifications enacted in RPA '94.

### *Explanation of Provisions*

#### 1. Conversion calculation

Prior to OBRA '89, section 411(c)-(2)(B) specified that the conversion factor to be used for purposes of computing the employee-derived accrued benefit was 10 percent for a straight life annuity commencing at normal retirement age of 65 (*i.e.*, multiply the accumulated contributions by .10), and that for other normal retirement ages the conversion factor was to be determined in accordance with regulations prescribed by the Secretary. Section 1.411(c)-1(c)(2) of the existing regulations provides that for normal retirement ages other than age 65, the conversion factor shall be the factor as determined by the Commissioner.

Rev. Rul. 76-47 (1976-1 C.B. 109) sets forth in tabular form the conversion factors to be used for determining the accrued benefit derived from employee contributions when the normal retirement age under the plan is other than age 65 or when the normal form of benefit is other than a single life annuity (without ancillary benefits). Rev. Rul. 76-47 further provides that where no standard factor is available, a conversion factor must be determined using an interest rate of 5 percent and the UP-1984 mortality table (without age setback).

OBRA '89 deleted the ten percent conversion factor in section 411(c)-(2)(B) and replaced it with the requirement that the accumulated contributions at normal retirement age be expressed as an annual benefit commencing at normal retirement age using an interest rate which would be used under the plan under section 417(e)(3) (as of the determination date). This change was effective retroactively to the effective date of the OBRA '87 provision relating to section 411(c)(2)(C) (the first day of the first plan year beginning after December 31, 1987).

To reflect the OBRA '89 amendments, these proposed regulations de-

fine *appropriate conversion factor* with respect to an accrued benefit expressed in the form of an annual benefit that is nondecreasing for the life of the participant as the present value of an annuity in the form of that annual benefit commencing at normal retirement age at a rate of \$1 per year. This amount is to be computed using the interest rate and mortality table which would be used under the plan under section 417(e)(3) and §1.417(e)-1T. To reflect the post-OBRA '89 conversion factor definition and to conform to common actuarial practice, these proposed regulations would change the *multiplied by* language in §1.411(c)-1(c)(1) to *divided by*.

#### 2. Accumulated contributions

As added by the Employee Retirement Income Security Act of 1974 (ERISA), section 411(c)(2)(C) provided that employee contributions were to be accumulated using a standard interest rate of 5 percent for years beginning on or after the effective date of that section. OBRA '87 changed the interest rate under section 411(c)(2)(C) to 120 percent of the applicable Federal mid-term rate under section 1274 for plan years after 1987. OBRA '89 again amended section 411(c)(2)(C) to provide that 120 percent of the applicable Federal mid-term rate under section 1274 is to be used for accumulating contributions only up to the *determination date*. For the period from the determination date to normal retirement age, the interest rate which would be used under the plan under section 417(e)(3) (as of the determination date) must be used for accumulating contributions for the period from the determination date to normal retirement age. Accordingly, these proposed regulations would amend paragraph (3) of §1.411(c)-1(c) to reflect those rates. As stated above, RPA '94 amended section 417(e)(3) to change the applicable interest rate. See §1.417(e)-1T.

#### 3. Determination date

Section 1.411(c)-1(c)(5)(i) defines the term determination date for purposes of section 411(c)(2)(C)(iii), in a case in which a participant will receive his or her entire accrued benefit derived from employee contributions in any one of the following forms (described in paragraph (c)(5)(ii)): an

annuity that is substantially nonincreasing, substantially nonincreasing installment payments for a fixed number of years, or a single sum distribution. In such a case, the term determination date means the date on which distribution of such benefit commences. For this purpose, an annuity that is nonincreasing except for automatic increases to reflect increases in the consumer price index is considered to be an annuity that is substantially nonincreasing.

Thus, for example, for purposes of section 411(c)(2)(C)(iii), in the case of a distribution of the employee's entire accrued benefit (or the employee's entire employee-derived accrued benefit) in the form of a nonincreasing single life annuity payable commencing either at normal retirement age or at early retirement age, the determination date is the date the annuity commences. Similarly, in the case of a single sum distribution of accumulated employee contributions (*i.e.*, employee contributions plus interest computed at or above the section 411(c) required rates) upon termination of employment with a deferred annuity benefit derived solely from employer contributions, the determination date is the date of distribution of the single sum of accumulated employee contributions.

Alternatively, the plan may provide that the determination date is the annuity starting date, as defined in §1.401(a)-20, Q&A-10.

Under §1.411(c)-1(c)(5)(iii) of these regulations, where a participant will receive a distribution that is not described in paragraph (c)(5)(i), the determination date will be as provided by the Commissioner.

#### 4. Elimination of limitation on employee-derived accrued benefit

Prior to OBRA '89, section 411(c)(2)(E) of the Code limited the accrued benefit derived from employee contributions to the greater of (1) the employee's accrued benefit under the plan, or (2) the sum of the employee's mandatory contributions, without interest. Section 7881(m)(1)(C) of OBRA '89 deleted that provision. Section 7881(m)(1)(D) of OBRA '89 added section 411(a)(7)(D) to the Code, which provides that the accrued benefit of an employee shall not be less than the amount determined under section 411(c)(2)(B) with respect to the

employee's accumulated contributions. Accordingly, these proposed regulations delete the rule included in §1.411(c)-1(d) of the existing regulations, which reflects the pre-OBRA '89 rule.

5. Delegation of authority

Section 1.411(c)-1(d) of these proposed regulations provides that the Commissioner may prescribe additional guidance on calculating the accrued benefit derived from employer or employee contributions under a defined benefit plan.

Effective Date

These amendments are proposed to be effective for plan years beginning on or after January 1, 1997. For example, assume that under a plan the employee's date of termination of employment is treated as the determination date, and distribution of the employee's entire employee-derived accrued benefit (as determined under the terms of the plan then in effect) occurs or commences prior to the first day of the plan year beginning in 1997. In that case, with respect to interest credits under section 411(c)(2)(C)(iii) for plan years beginning after 1987, the Service will not treat the plan as having failed to satisfy the requirements of section 411(c), nor will it require that additional amounts be credited in the calculation of the employee-derived accrued benefit in order to satisfy the requirements of section 411(c) after final regulations become effective, merely because the date the employee's employment terminated was treated as the determination date, provided that interest is credited in accordance with section 411(c)(2)(C)(iii)(I) for the period before the date the employee terminated employment and in accordance with section 411(c)(2)(C)(iii)(II) thereafter.

Once amendments to the regulations under §1.411(c)-1 are adopted in final form, the Service will obsolete or modify Rev. Rul. 76-47, Rev. Rul. 78-202 (1978-2 C.B. 124) and Rev. Rul. 89-60 (1989-1 C.B. 113) as necessary or appropriate.

Taxpayers may rely on these proposed regulations for guidance pending the issuance of final regulations.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a

significant regulatory action as defined in EO 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) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying. A public hearing may be scheduled if requested in writing by a person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the hearing will be published in the Federal Register.

Drafting Information

The principal author of these regulations is Janet A. Laufer, Office of the Associate Chief Counsel (Employee Benefits and Exempt Organizations). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

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(c)-1 is amended by:

- 1. Revising paragraphs (c)(1), (c)(2), (c)(3), (c)(5) and (c)(6).
2. Revising paragraph (d).
3. Adding paragraph (g).

The additions and revisions read as follows:

§1.411(c)-1 Allocation of accrued benefits between employer and employee contributions.

\* \* \* \* \*

(c) Accrued benefit derived from mandatory employee contributions to a defined benefit plan—(1) General Rule. In the case of a defined benefit plan (as defined in section 414(j)), the accrued benefit derived from contributions made by an employee under the plan as of any applicable date in the form of an annual benefit commencing at normal retirement age and nondecreasing for the life of the participant is equal to the amount of the employee's accumulated contributions (determined under paragraph (c)(3) of this section) divided by the appropriate conversion factor with respect to that form of benefit (determined under paragraph (c)(2) of this section). Paragraph (e) of this section provides rules for actuarial adjustments where the benefit is to be determined in a form other than the form described in this paragraph (c)(1).

(2) Appropriate conversion factor. For purposes of this paragraph, with respect to a form of annual benefit commencing at normal retirement age described in paragraph (c)(1), the term appropriate conversion factor means the present value of an annuity in the form of that annual benefit commencing at normal retirement age at a rate of \$1 per year, computed using an interest rate and mortality table which would be used under the plan under section 417(e)(3) and §1.417(e)-1T (as of the determination date).

(3) Accumulated contributions. For purposes of section 411(c) and this section, the term accumulated contributions means the total of—

(i) All mandatory contributions made by the employee (determined under paragraph (c)(4) of this section);

(ii) Interest (if any) on such contributions, computed at the rate provided by the plan to the end of the last plan year to which section 411(a)(2) does not apply (by reason of the applicable effective dates);

(iii) Interest on the sum of the amounts determined under paragraphs (c)(3)(i) and (ii) of this section compounded annually at the rate of 5 percent per annum from the beginning of the first plan year to which section 411(a)(2) applies (by reason of the applicable effective date) to the beginning of the first plan year beginning after December 31, 1987;

(iv) Interest on the sum of the amounts determined under paragraphs (c)(3)(i) through (iii) of this section compounded annually at 120 percent of the Federal mid-term rate(s) (as in effect under section 1274(d) of the Internal Revenue Code for the first month of a plan year) for the period beginning with the first plan year beginning after December 31, 1987 and ending on the determination date; and

(v) Interest on the sum of the amounts determined under paragraphs (c)(3)(i) through (iv) of this section compounded annually, using an interest rate which would be used under the plan under section 417(e)(3) and §1.417(e)-1T (as of the determination date), from the determination date to the date on which the employee would attain normal retirement age.

\* \* \* \* \*

(5) *Determination date*—(i) For purposes of section 411(c) and this section, in a case in which a participant will receive his or her entire accrued benefit derived from employee contributions in any one of the forms described in paragraph (c)(5)(ii), the term *determination date* means the date on which distribution of such benefit commences. Alternatively, in such a case, the plan may provide that the determination date is the annuity starting date with respect to that benefit, as defined in §1.401(a)-20, Q&A-10.

(ii) Paragraph (c)(5)(i) applies to the following forms: an annuity that is substantially nonincreasing (e.g., an annuity that is nonincreasing except for automatic increases to reflect increases in the consumer price index), substantially nonincreasing installment payments for a fixed number of years, or a single sum distribution.

(iii) In a case in which a participant will receive a distribution that is not described in paragraph (c)(5)(i), the determination date will be as provided by the Commissioner.

(6) *Examples.*

(i) *Facts.* (A) In the following examples, Employer X maintains a qualified defined benefit

plan that required mandatory employee contributions for 1987 and prior years, but not for years after 1987. The plan year is the calendar year. The plan provides for a normal retirement age of 65 and for 100 percent vesting in the employer-derived portion of a participant's accrued benefit after 5 years of service.

(B) The terms of the plan provide that the normal form of benefit is a level monthly amount commencing at normal retirement age and payable for the life of the participant. A plan participant who elects not to receive benefits in the form of the qualified joint and survivor annuity provided by the plan may elect to receive a single-sum distribution of the present value of his or her accrued benefit upon termination of employment.

(C) As of January 1, 1995, the plan was amended to provide that, for purposes of computing actuarially equivalent benefits, the single sum is calculated using the unisex version of the 1983 GAM mortality table (as provided in Revenue Ruling 95-6 (1995-1 C.B. 80)), and interest at the rate equal to the annual rate of interest on 30-year Treasury securities for the first calendar month preceding the first day of the plan year during which the annuity starting date occurs.

(D) Under the plan, employee contributions are accumulated at 3 percent interest for plan years beginning before 1976, 5 percent interest for plan years beginning after 1975 and before 1988, and interest at 120 percent of the Federal mid-term rate (as in effect under section 1274(d) for the first month of the plan year) for plan years beginning after 1987 until the determination date. Under the plan, the determination date is defined as the annuity starting date. For the period from the determination date until the date on which the employee attains normal retirement age, interest is credited at the interest rate which would be used under the plan under section 417(e)(3) as of the determination date.

(E) A, an unmarried participant, terminates employment with X on January 1, 1997 at age 56 with 15 years of service. As of December 31, 1987, A's total accumulated mandatory employee contributions to the plan, including interest compounded annually at 5 percent for plan years beginning after 1975 and before 1988, equaled \$3,021. A receives his or her accrued benefit in the form of an annual single life annuity commencing at normal retirement age. A's annuity starting date is January 1, 2006, and therefore the determination date is January 1, 2006.

(ii) *Annuity at Normal Retirement Age—Determination of Employee-Derived and Total Plan Vested Accrued Benefit.*

*Example 1.*

For purposes of this example, it is assumed that A's total accrued benefit under the plan in the normal form of benefit commencing at normal retirement age is \$2,949 per year. A's benefit, as of January 1, 2006, would be determined as follows:

(1) Determine A's total accrued benefit in the form of an annual single life annuity commencing at normal retirement age under the plan's formula (\$2,949 per year payable at age 65).

(2) Determine A's accumulated contributions with interest to January 1, 1997. As of December 31, 1987, A's accumulated contributions with interest under the plan provisions were \$3,021. A's employee contributions are accumulated

from December 31, 1987 to January 1, 1997 using 120 percent of the Federal mid-term rate under section 1274(d). This rate is 10.61 percent for 1988, 11.11 percent for 1989, 9.57 percent for 1990, 9.78 percent for 1991, 8.10 percent for 1992, 7.63 percent for 1993, 6.40 percent for 1994, and 9.54 percent for 1995. It is assumed for purposes of this example that 120 percent of the Federal mid-term rate is 7.00 percent for each year between 1996 and 2006, and that the 30-year Treasury rate for December 2005 is 8.00 percent. Thus, A's contributions accumulated to January 1, 1997, equal \$6,480.

(3) Determine A's accumulated contributions with interest to normal retirement age (January 1, 2006) using, for the 1996 plan year and for years until normal retirement age, 120 percent of the Federal mid-term rate under section 1274(d), which is assumed to be 7.00 percent (\$11,913).

(4) Determine the accrued annual annuity benefit derived from A's contributions by dividing A's accumulated contributions determined in paragraph (3) of this *Example 1* by the plan's appropriate conversion factor. The plan's appropriate conversion factor at age 65 is 9.196, and the accrued benefit derived from A's contributions would be  $\$11,913 / 9.196 = \$1,295$ .

(5) Determine the accrued benefit derived from employer contributions as the excess, if any, of the employee's accrued benefit under the plan over the accrued benefit derived from employee contributions ( $\$2,949 - \$1,295 = \$1,654$  per year).

(6) Determine the vested percentage of the accrued benefit derived from employer contributions under the plan's vesting schedule (100 percent).

(7) Determine the vested accrued benefit derived from employer contributions by multiplying the accrued benefit derived from employer contributions by the vested percentage ( $\$1,654 \times 100 \text{ percent} = \$1,654$  per year).

(8) Determine A's vested accrued benefit in the form of an annual single life annuity commencing at normal retirement age by adding the accrued benefit derived from employee contributions and the vested accrued benefit derived from employer contributions, the sum of paragraphs (4) and (7) of this *Example 1* ( $\$1,295 + \$1,654 = \$2,949$  per year).

*Example 2.*

This example assumes the same facts as *Example 1* except that A's total accrued benefit under the plan in the normal form of benefit commencing at normal retirement age is \$1,000 per year. A's benefit, as of January 1, 2006, would be determined as follows:

(1) Determine A's total accrued benefit in the form of an annual single life annuity commencing at normal retirement age under the plan's formula (\$1,000 per year payable at age 65).

(2) Determine A's accumulated contributions with interest to January 1, 1997 (\$6,480 from paragraph 2 of *Example 1*).

(3) Determine A's accumulated contributions with interest to normal retirement age (January 1, 2006) (\$11,913 from paragraph 3 of *Example 1*).

(4) Determine the accrued annual annuity benefit derived from A's contributions by dividing A's accumulated contributions determined in paragraph (3) of this *Example 2* by the plan's appropriate conversion factor (\$1,295 from paragraph 4 of *Example 1*).

(5) Determine the accrued benefit derived from employer contributions as the excess, if

any, of the employee's accrued benefit under the plan over the accrued benefit derived from employee contributions. Because the accrued benefit derived from employee contributions (\$1,295) is greater than the employee's accrued benefit under the plan (\$1,000), the accrued benefit derived from employer contributions is zero, and A's vested accrued benefit in the form of an annual single life annuity commencing at normal retirement age is \$1,295 per year.

(d) *Delegation to Commissioner.* The Commissioner may prescribe additional guidance on calculating the accrued benefit derived from employee contributions under a defined benefit plan through publication in the Internal Revenue Bulletin of revenue rulings, notices, or other documents (see §601.601(d)(2) of this chapter).

(e) \* \* \*

(f) \* \* \*

(g) *Effective date.* Paragraphs (c)(1), (c)(2), (c)(3), (c)(5), (c)(6) and (d) of this section are effective for plan years beginning on or after January 1, 1997.

Margaret Milner Richardson,  
*Commissioner of  
Internal Revenue.*

(Filed by the Office of the Federal Register on December 21, 1995, 8:45 a.m., and published in the issue of the Federal Register for December 22, 1995, 60 F.R. 66532)