

Transition Provisions in Large Converted Cash Balance Pension Plans

Over one-fourth of all single employer defined benefit (DB) pension plan participants are now enrolled in plans with so-called cash balance formulas. Many people have raised concerns about whether cash balance plan conversions discriminate against older workers—especially long-service older workers—and deprive these workers of late-career benefits just as they were about to obtain them.

This study was commissioned to determine whether large employers which converted their pension plans to cash balance plans provided transition relief to older workers. The 25 largest cash balance plans (in terms of numbers of participants) were included in the analysis. Annual Form 5500 reports filed with the Department of Labor for 2003 are the best publicly available source of information on transition provisions. Analysis of the Form 5500 reports was followed up by telephone calls to representatives of all the plans to validate the information in the reports.

The 25 largest cash balance plans were all single-employer plans. They covered 9 percent of total participants in PBGC-insured single-employer plans and about 36 percent of total participants in single-employer cash balance plans. The total number of active participants in the 25 plans examined was 1.4 million.

The key finding of the study is that transition provisions are very common in large plans and were adopted by 23 of the 25 plans examined. The most common types of provisions were to grandfather

older workers under the prior plan formula or to grant older workers a benefit based on the greater of the prior or new formula.

In seven of the plans with transition provisions, all of the participants at the time of conversion were covered under the provision, while the remaining 16 plans specified a minimum age, service, or combination of age and service requirement for inclusion under the transition provision. Overall, roughly 45 percent of all prior plan participants in the plans were covered under some type of transition provision.

Comparison of transition provisions in plans converted prior to 1999 with those converted in more recent years shows two trends in eligibility requirements and the type of transition provision most likely to be adopted. First, there has been a movement to eliminate eligibility requirements for transition coverage. Nine of the ten pre-1999 plans with transition provisions imposed an age/service requirement for transition coverage. Of a total of 573 thousand active participants in the 10 plans, about 37 percent were eligible for transition coverage.

Among the 13 plans adding a cash balance feature in 1999 or later, only seven had such a requirement, with the remaining six plans grandfathering in all participants under the transition provision. About 55 percent of the total of 740,000 active participants in the 13 plans were covered under a transition provision.

Second, since 1999 there has been a trend toward a transition provision that grandfathers in participants under the prior

benefit formula. Fifty-four percent of plans converted in 1999 or later provided this transition provision type compared to 17 percent of pre-1999 converted plans. Conversely, a provision that provides eligible participants with the greater of the benefit accrued under the old or new formula is becoming less popular, with 31 percent of plans converted in 1999 or later adopting this provision type compared to 50 percent converted prior to 1999.

The findings of this report raise a number of important research and policy questions about cash balance conversions and the transition provisions available to older workers. There is a need to develop policies which ensure that cash balance plans prohibit age discrimination in benefits and comply with current laws governing the operation of DB plans. In addition, there is a need to extend to workers, at the time of their retirement, the option to choose the benefit calculated under the old formula or the benefit available under the new cash balance plan, whichever is greater.