

The Case of Working After Normal Retirement Age

Case Summary

Client works until age 72, which is beyond normal retirement age.

Client does not receive pension payment until he stops working.

Client asserts that due to *Central Laborers v. Heinz* (541 U.S. 739), he was entitled to pension payments starting at age 65, while still employed.

Issues:

- Was Client entitled to benefits at age 65 while he continued working?
- Was Client entitled to benefits on April 1 of the calendar year following the calendar year in which he attained age 70 ½ while he continued working?
- Was his benefit calculated correctly?

Case Timeline

- 1/1/1999 Employees reaching age 70 ½ after this date cannot commence benefit distribution until actually retires, per 2003 plan document
- 7/2/1999 The Plan mailed notice to Client advising that an employee cannot receive pension distribution if continue to work after age 65
- 7/10/1999 Client is age 65
- 1/10/2005 Client is age 70 ½
- 4/1/2006 Date that actuarial adjustment should begin
- 12/31/2006 Client's last day of work
- 1/1/2007 Client begins retirement

Benefit Distribution Rules

When must a plan begin paying pension distributions?

- Unless participant elects otherwise, a plan must begin paying benefits no later than the 60th day after the close of the plan year in which the later occurs: A) participant attains age 65 or Normal Retirement Age under the plan, or B) the participant's 10th anniversary of participation, or C) Participant terminated service. *IRC Section 401(a)(14)*
- Client in this case was still working at age 65, and per the plan document, pension payments will begin when participant is age 65 and separated from service.

What is the latest date a participant may take pension distribution?

- The required beginning date for distributions is, "April 1 of the calendar year following the later of (I) the calendar year in which the employee attains age 70 ½, or (II) the calendar year in which the employee retires." *IRC section 401(a)(9)(C); See Also, Treas. Reg. 1.401(a)(9)-2 A-2.*
- The Plan provides that, "An employee attaining age 70 ½ on or after January 1, 1999 will not commence monthly receipt of accrued benefits under this Plan until such employee actually retires."
- Client's date of birth is 7/10/1934 and he attained age 70 ½ on 1/10/2005, and retired on 12/31/2006. He began receiving his pension on 1/1/2007, which is before his required date of 4/1/2007, and was in compliance.

Exception to the required beginning date rule for 5% owners

- Client asserted that because he was paid a salary over \$90,000/year he was a Highly Compensated Employee (HCE), and as such, he would fall under an exception in the statute that requires plans to pay benefits in some cases where the participant is still working for the employer sponsoring the plan.
- The IRC provides an exception to the required beginning date rule for 5% owners of the sponsoring employer; the required beginning date is April 1 of the calendar year following the calendar year in which the employee attained age 70 ½, regardless of employment status. *IRC Section 401(a)(9)(C)(ii)(I)*. The Plan also provides for this exception.
- Client did meet the 2003 Plan definition of HCE, but neither the statute nor the Plan requires that employees compensated above a certain amount receive benefits while still working, and Client did not own 5% of the company.

Anti-cutback Rule and Related Issues

Permissible Elimination of the Age 70 ½ Distribution Option

- Client objects to the Plan's refusal to pay him a benefit at age 70 ½ while still employed. This was changed from a prior version of the plan. The 2003 Plan changed the rule so that participants attaining age 70 ½ after 1/1/1999 cannot receive benefits until actually retiring.
- Client argues that this amendment violates that anti-cutback rule of ERISA Section 204(g) and IRC Section 411(d)(6) as interpreted by the Supreme Court in *Central Laborers' v. Heinz*.
- The Small Business Job Protection Act of 1996 (SBJPA) changed the "required beginning date." SBJPA allows plans to wait until employees separate from service, regardless of the employee's age. The relevant SBJPA provision was effective for years beginning after December 31, 1996. *Public Law 104-188 Section 1404 (amended IRC Section 401(a)(9)(C))*.

The Anti-Cutback Rule

- The anti-cutback rule provides generally that an accrued benefit may not be decreased by an amendment of the plan. *IRC Section 411(d)(6)*.
- A plan amendment that eliminates an optional form of benefit will violate the rule to the extent the amendment applies to benefits accrued as to the effective date of the amendment. *IRC Section 411(d)(6)(B)*.
- However, the rule also authorizes the Treasury Secretary to issue regulations providing exceptions to the anti-cutback rule to allow elimination of an optional form of benefit. *IRC Section 411(d)(6)(B)*.
- The option to begin collecting benefits while still working after age 70 ½ was protected by the anti-cutback rule and could only be eliminated by a regulation issued by the Treasury Secretary under the authority granted to the Secretary by the IRC. *IRC Section 411(d)(6)(B)*.
- Pursuant to its authority under the anti-cutback rule and in response to the SBJPA, the Treasury issued regulations allowing plans to eliminate the optional form of benefit for in-service distributions post age 70 ½ provided the plan follow certain requirements with respect to timing of the effective date of the amendment.

Anti-Cutback and the Plan

- Plans can lawfully eliminate the option if the amendment is adopted no later than the last day of the first plan year beginning on or after 1/1/2000, and the amendment is limited to employees attaining age 70 ½ after 1998. *Treas. Reg. Section 1.411(d)-4 (A-10)*.
- The 2003 Plan provides that employees attaining age 70 ½ on or after 1/1/1999 would not commence benefit distribution until the employees actually retired.
- Client attained age 70 ½ on 1/10/2005, after the effective date of the amendment.

Central Laborers' v. Heinz (541 U.S. 739)

- In *Heinz*, the Supreme Court held that the plan amendment violated the anti-cutback rule because it had the effect of eliminating a subsidized early retirement benefit that was earned by service before the amendment was passed.
- Client's case deals with the elimination of an optional form of benefit.
- The anti-cutback rule allows the Treasury to issue regulations allowing plans to adopt amendments eliminating optional forms of benefit. *IRC Section 411(d)(6)(B)*.
- *Heinz* speaks only to the limited issue of reduction of subsidized early retirement benefits and does not apply to Client's issues.

The Benefit Calculation

The Claim

- Client asserts that he is entitled to an actuarial adjustment on all accrued benefits for lost earnings from age 65 through 1/1/2007 when he retired from employment.

Age 65 to April 1 following attainment of age 70 ½

- ERISA prohibits a pension plan from stopping an employee's benefit accrual because of attainment of any age. *ERISA Section 204(b)(1)(H)(i)*. The Plan complies with this ERISA provision, client did receive benefit accruals after age 65.
- ERISA permits benefits being suspended when the participant remains employed. *ERISA Section 203(a)(3)(B)(i)*.
- Labor regulations require that participants be notified of the suspension by personal delivery or first class mail, and participants must be notified of procedures for seeking review of the plan's decision (can be via SPD). *29 CFR Section 2530.203-3(a)(4)*.
- If a participant is properly notified, the Plan is not required to actuarially adjust any benefits not paid during the suspension period of age 65 to April 1 of the calendar year following the calendar year of attaining age 70 ½. *Treas. Reg. Section 1.401(a)(9)-6 (A-9)*.
- Although Client could not remember receiving notification of benefit suspension after age 65, the Plan was able to show the generic notification letter sent out as standard operating procedure in this situation and had documented that such a letter was sent to client on 7/2/1999, the month that client reached age 65. Therefore, no actuarial adjustment is due for the time period between age 65 and April 1 following attainment of age 70 ½.

April 1 following the attainment of age 70 ½ until actual retirement

- The IRC requires that for participants who retire after the calendar year in which they attain age 70 ½, the accrued benefit shall be actuarially increased to take into account the period after April 1 of the year after age 70 ½, in which the employee was not receiving any benefits. *IRC Section 401(a)(9)(C)(iii)*.
- Client attained age 70 ½ on 1/10/2005 and retired on 1/1/2007, so suspended benefits between 4/1/2006 and 1/1/2007 must be actuarially adjusted.

Amount of Actuarial Increase Required

- Treasury regulations require that the actuarial increase must be no less than:
 - (1) the actuarial equivalent of the employee's retirement benefits that would have been payable as of the date the actuarial increase must commence;
 - (2) plus the actuarial equivalent of any additional benefits accrued after that date;
 - (3) reduced by the actuarial equivalent of any distributions made with respect to the employee's retirement benefits after that date. *26 CFR Section 1.401(a)(9)-6(A-8).*

Client's Benefit

- Under the plan, Client is paid the greater of the following:
 - (1) the accrued benefit as of 4/1/2006, actuarially increased through 12/31/2006;
 - (2) the accrued benefit as of 12/31/2006.

The greater benefit was (1).

The Plan was in violation of both ERISA and the Code because the benefit originally paid to Client did not include BOTH:

- (a) Accruals earned between April of the year after Client turned 70 ½ (4/1/2006) and the date Client actually retired (1/1/2007), and
- (b) Upward actuarial adjustment on those additional accruals.

Taken together, this resulted in a benefit claim for an additional \$85.62 per month.