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The Cash Balance Controversy Revisited: Age Discrimination and Fidelity to Statutory Text

Edward A. Zelinsky
Benjamin N. Cardozo School of Law, zelinsky@yu.edu

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THE CASH BALANCE CONTROVERSY REVISITED: AGE DISCRIMINATION AND FIDELITY TO STATUTORY TEXT

*Edward A. Zelinsky**

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I. INTRODUCTION

In a recent article in the *Virginia Tax Review*,[1] I explored the controversy surrounding cash balance pension plans. I anticipated that my analysis would please none of the partisans in this debate. As a matter of law, I concluded, the typical cash balance plan violates the statutory prohibitions on age-based reductions in the rate at which participants accrue their benefits. However, as a matter of policy, there is no sound reason to bar cash balance plans nor is there a logical basis for the resentment engendered by the conversion of traditional, annuity-providing defined benefit plans to the cash balance format since employers can legally achieve

* Edward A. Zelinsky is a Professor of Law at the Benjamin N. Cardozo School of Law of Yeshiva University.

[1] Edward A. Zelinsky, "The Cash Balance Controversy," 19 *Va. Tax Rev.* 683 (2000).

economically similar results by terminating their traditional pensions and replacing them with defined contribution arrangements. Indeed, I agree with the proponents of cash balance plans that such plans permit employers to remain within the defined benefit system rather than debark to the defined contribution universe; cash balance plans thus have a constructive role to play in providing retirement income.

As a matter of psychology, the resentment against cash balance conversions, deeply and sincerely held, largely stems from psychological expectations in the continuation of the *status quo*, rather than from any legal or logical entitlement to the perpetuation of existing pension coverage. While employers are well-advised to address those expectations as a matter of employee relations, I think it inadvisable to protect those expectations legislatively.

My prediction that this analysis would comfort none of the partisans has proved, if anything, to have been understated. Opponents of cash balance plans have invoked my statutory argument that such plans typically violate current age discrimination laws while ignoring my conclusions that, as a matter of policy, this result is troubling and that the statutes should be changed to permit cash balance plans.[2] Proponents of cash balance pensions have generally overlooked my positive comments about such pensions and have instead focused intense fire on my assessment that the relevant statutes, in their current form, declare many (perhaps most) cash balance plans to be age discriminatory.

Among these cash balance proponents, Richard C. Shea, Michael J. Francese and Robert S. Newman of Covington & Burling critique my interpretation of the pension age discrimination statutes.[3] Relying heavily on legislative intent

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[2] *See, e.g.*, AARP Urges Review of Cash Balance Plan Age Discrimination Issues, 2000 TNT 57-34 (March 23, 2000).

[3] Richard C. Shea, Michael J. Francese and Robert S. Newman, "Age Discrimination in Cash Balance Plans: Another View," 19 *Va. Tax Rev.* 763 (2000).

and history, Messrs. Shea, Francese and Newman contend that cash balance plans do not run afoul of the pension statutes barring age discrimination.

Much is at stake in the debate about the proper interpretation of current law. Statutes can be changed; indeed, Congress' proclivity to amend the tax law is an important reason courts should treat respectfully the literal terms of the Code. Nevertheless, in a controversy of this sort, tactical advantage redounds to the side defending the *status quo*, which must merely block legislative action. Accordingly, the statutory construction endorsed by the courts and the responsible administrators will influence the political dynamic surrounding cash balance pension plans since that construction will determine whether the defenders or the detractors of cash balance plans bear the burden of securing legislation to advance their program.

To clarify the issues in this debate,[4] I first summarize[5] the relevant statutes and revisit the application of these statutes in the cash balance setting. In this setting, any finding of age discrimination must necessarily be fact- and plan-specific; nevertheless, if we take the statutes seriously, it is reasonable to conclude that many, likely most, cash balance plans flunk the statutory prohibitions against age-based declines in the rate of benefit accrual.

In the second section of this article, I respond to the critique advanced by Messrs. Shea, Francese and Newman. At its most basic, Messrs. Shea, Francese and Newman brush aside the literal terminology of the pension age discrimination

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[4] Since this article is intended as a reply to Messrs. Shea, Francese and Newman, I confine my comments in the text to their analysis. However, in two instances, the Shea-Francese-Newman critique has undergirded additional criticisms of my conclusions. I briefly note and respond to these criticisms in footnotes 14 (pertaining to the critique of Mr. Lawrence J. Sher) and 29 (pertaining to the critique of Mr. Hubert V. Forcier). In footnote 40, I also respond briefly to the *Onan* decision of the U.S. District Court for the Southern District of Indiana.

[5] This first section is indeed a summary; more extensive analysis and examples can be found in my article.

statutes to reach results with which, as a matter of policy, I largely agree but which, as a matter of statutory interpretation, do not constitute a compelling construction of the statutes as they exist today. Messrs. Shea, Francese and Newman's invocation of legislative intent and history is unpersuasive in light of the constraining language of the relevant statutes.

The final section summarizes my conclusions. Our system of tax and pension laws cannot function without fidelity towards statutory texts, fidelity which frequently entails the acceptance of outcomes with which the reader disagrees as a matter of policy. Ultimately, a system of statutory law requires us to take statutes seriously. And taking the pension age discrimination statutes seriously leads to the conclusion that many, likely most, cash balance plans violate such statutes.

II. THE STATUTES

In essentially[6] identical terms, the Internal Revenue Code ("the Code"), the Employee Retirement Income Security Act of 1974 ("ERISA") and the Age Discrimination in Employment Act ("ADEA") preclude age discrimination in pensions. The relevant statutory provisions are specific and propound two separate rules for defined benefit and defined contribution arrangements. In the defined contribution setting, a plan is nondiscriminatory as to age[7] if "under the plan, allocations to

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[6] The heading to Code Section 411(b)(1)(H) reads "Continued Accrual Beyond Normal Retirement Age." No such heading accompanies the ERISA and ADEA counterparts nor does any such heading accompany the Code, ERISA or ADEA provisions relative to defined contribution plans and age discrimination. As I discuss *infra*, Messrs. Shea, Francese and Newman (correctly, in my judgment) ignore this heading while the *Onan* Court (incorrectly, in my judgment) makes much of it. See note 40, *infra*.

[7] The pension provisions relative to age discrimination, providing separate rules for defined benefit and defined contribution plans, stand in contrast to the provisions prohibiting discrimination in favor of highly compensated employees.

the employee's account are not ceased, and the rate at which amounts are allocated to the employee's account is not reduced, because of the attainment of any age."[8]

A defined benefit plan, on the other hand, is deemed discriminatory as to age if "under the plan, an employee's benefit accrual is ceased, or the rate of an employee's benefit accrual is reduced, because of the attainment of any age."[9]

Thus, the statutory test for age discrimination in the defined contribution setting focuses upon the employer's inputs to the plan ("allocations to the employee's account") and mandates that the employer's contributions for each employee not decrease with age. On the other hand, in the defined benefit context, the statutes focus upon outputs ("an employee's benefit accrual") and decree that age discrimination exists if "the rate of an employee's benefit accrual is reduced" because of age.

While designed to mimic defined contribution plans, cash balance arrangements are defined benefit plans pursuant to which plans, and ultimately sponsoring employers, guarantee specified benefits. Thus, the relevant test for age discrimination in the cash balance context is the plan's output – "the rate of an employee's benefit accrual."

The Code and ERISA further specify that an employee's accrued benefit in a defined benefit plan is "an annual benefit commencing at normal retirement age."[10] Since cash balance plans delineate each employee's pension entitlement, not as

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In particular, Code Section 401(a)(4) is sufficiently flexible in its terminology to be read as authorizing cross-testing, i.e., testing defined benefit plans on the basis of contributions and testing defined contribution plans on the basis of projected benefits. *See* Edward A. Zelinsky, "Is Cross-Testing A Mistake? Cash Balance Plans, New Comparability Formulas, and the Incoherence of the Nondiscrimination Norm." 49 *Buffalo L. Rev*. XX (forthcoming 2001).

[8] Code Section 411(b)(2)(A). ERISA Section 204(b)(2)(A) and ADEA Section 4(i)(1)(B) are essentially the same.

[9] Code Section 411(b)(1)(H)(i). ERISA Section 204(b)(1)(H)(i) and ADEA Section 4(i)(1)(A) are essentially the same.

[10] Code Section 411(a)(7)(A)(i), ERISA Section 2(23)(A).

a traditional annuity, but as a notional account balance, to determine a cash balance participant's accrued benefit as such benefit is defined statutorily, it is necessary to convert the participant's *ersatz* account balance under the plan into a deferred annuity projected to start at normal retirement.

Such conversion reveals that, as a cash balance participant gets older, the same dollar contribution to the plan for her purchases less in annuity terms since there is less time for that contribution to accrue investment earnings before retirement and the commencement of previously deferred annuity payments. In defined contribution terms, cash balance plans are not age discriminatory since hypothetical contributions (i.e., inputs) for employees typically do not decrease with age. However, cash balance plans are defined benefit arrangements which, as a statutory matter, measure for age discrimination in terms of outputs, i.e., the annuity purchased as of normal retirement. In such annuity terms, the same dollar contribution each year purchases successively smaller amounts at retirement as the participant ages and thus has one less year for the contribution to accumulate investment earnings prior to payout at normal retirement.

Placing these arithmetic realities against the language of the statutes, each year, as an employee gets older, the same dollar contribution results in a reduced rate of benefit accrual since the employee's incremental accrued benefit – measured, per the statutes, as a deferred annuity to commence at retirement – declines as the employee successively attains later ages and thus gets closer to retirement. By the same token, the same cash balance contribution for two employees of different ages produces for the older employee a smaller accrued benefit measured as the projected annuity to be purchased with that contribution at normal retirement.

Cash balance pensions can avoid this problem by annually increasing theoretical contributions as the participant ages, thereby keeping stable the annuity value of those contributions. In practice, however, I am skeptical that many

cash balance pensions utilize this or any similar formula.[11] Nevertheless, this possibility highlights the fact- and plan-specific nature of the age discrimination inquiry in the cash balance context.

III. THE EMPIRE STRIKES BACK

A. *The Rate of Benefit Accrual*

In their critique published simultaneously with my article, Messrs. Shea, Francese and Newman take issue with my statutory analysis. In particular, they argue that my understanding of the statutory language (specifically, my reading of the statutes as requiring the determination of the rate of benefit accrual by converting cash balance allocations into deferred annuities starting at normal retirement) violates Congress' intent when it adopted the pension age discrimination statutes.[12] The "rate of benefit accrual," Messrs. Shea, Francese and Newman maintain, is undefined statutorily, opening the door to legislative intent to define that term, intent largely to be discerned from legislative history.[13] Finally, by focusing the inquiry upon benefit

[11] In theory, a cash balance plan might in practice achieve an equivalent result even with a single contribution rate. If every employee's salary increases each year enough so that that single rate produces steadily increasing allocations for every employee, the annuity value of each year's allocation can stay stable or increase. As I have observed, the issue is ultimately fact- and plan-specific. I am, however, skeptical that, in practice, this possibility saves many cash balance plans, particularly in an era of relatively stable wages.

[12] *See, e.g.*, Shea, Francese and Newman, *supra* note 3, at 768 ("Congress intended the 1986 Age Act to govern the rate of benefit accrual after normal retirement age"), 769 ("More problematic, however, is the fact that, when applied to accruals after normal retirement age, Professor Zelinsky's method produces results that are the exact opposite of what Congress intended"), 773 ("A method that actually produces the result Congress intended has something to recommend it.").

[13] *Id.* at 767. ("The truth of the matter, however, is that the term 'rate of benefit accrual' is nowhere defined in the age discrimination statutes.") The analysis advanced by Professor Forman and Attorney Nixon is similar. *See* Jonathan Barry Forman and Amy Nixon, "Cash Balance Pension Plan Conversions," 25

accruals after the attainment of normal retirement age, Messrs. Shea, Francese and Newman produce outcomes using my analysis which outcomes they allege are inconsistent with Congress' intent. The mismatch between these outcomes and Congress' intent, they claim, further discredits my statutory analysis that the rate of benefit accrual is properly determined in the cash balance context by converting theoretical contributions to projected annuities.[14]

Okla. City U. L. Rev. 379 (2000) at 421-22.

[14] Due to space constraints, Messrs. Shea, Francese and Newman do not address in detail the controversy surrounding wear away provisions. Since this was not a major topic for Messrs. Shea, Francese and Newman, I will not address it in detail here.

I would, however, respond in this footnote to an extension of the Shea-Francese-Newman analysis advanced in a presentation to the ERISA Industry Committee (ERIC) by Lawrence J. Sher of Price WaterhouseCoopers LLP. In large measure, Mr. Sher attacked my analysis in the terms asserted by Messrs. Shea, Francese and Newman, i.e., by resort to legislative intent. However, one aspect of Mr. Sher's argument expanded this critique and thus requires response. In particular, Mr. Sher presented a wear-away example which, he claimed, negates my argument that wear-away provisions can, indeed often do, violate the pension age discrimination statutes as those statutes exist today. The example presented by Mr. Sher was as follows:

Wear-Away Period

Opening bal: PV prior accrued benefit at 8% interest
current final average pay = $50,000

(5% pay increases; 6% 30 yr. T-Bond rate and interest credits in all years)

Age at Transition	Years of Service at Transition		
	5	15	25
35	1 year	3 years	
40	2 years	4 years	
45	2 years	5 years	8 years
50	2 years	6 years	10 years
55	2 years	7 years	11 years
60	2 years	6 years	7 years
65	1 year	2 years	2 years

As I have stressed, in the cash balance context, any finding of age discrimination is necessarily fact- and plan-specific. It is thus not surprising that an actuary of Mr. Sher's skill can create an example in which the terms of the plan interact with the characteristics of the workforce to minimize the impact of age, i.e., the first column of this chart, an example in which all of the employees affected by the wear away have worked for the employer for five years.

What is surprising is Mr. Sher's suggestion that the other two columns also eliminate the impact of age in the wear away context. In the middle column, all affected employees have worked for the employer for fifteen years upon conversion to the cash balance method with wear away. In this example, as employees age from thirty-five to fifty-five, the wear-away period steadily elongates in lockstep with age: a thirty-five year old has a three year period during which he accrues no new pension benefits because his entitlement under the new cash balance plan is catching up to his entitlement under the traditional pension formula; a forty year old, in contrast, has a four year period of no net accrual; a forty-five year old's wear away period is five years; at age fifty, the wear away period is six years; at age fifty-five, it is seven years.

Messrs. Shea, Francese and Newman do not dispute the basic arithmetic prior to normal retirement: holding everything else constant, the same dollar allocated to an older employee's cash balance account produces a smaller annuity at normal retirement than the same contribution for a younger employee with more time for his contribution to accrue investment income until retirement. This math, for Messrs. Shea, Francese and Newman, is irrelevant in light of Congress' intent in adopting the age discrimination rules for pensions.

At its core, the methodology deployed by Messrs. Shea, Francese and Newman brushes the statute aside rather than engage the statutory text in any serious way. With the statutory text pushed aside, Messrs. Shea, Francese and Newman discern as authoritative legislative intent which felicitously corresponds with their policy preferences.

It is important to distinguish the manner in which Messrs. Shea, Francese and Newman invoke legislative intent extratextually from concern with statutory purpose, concern consistent with (and often an important part of) a serious engagement with statutory text. A serious reader of any text, particularly a legal text, will think about the purpose of the text he confronts. In contrast, Messrs. Shea, Francese and Newman use legislative intent as a device for avoiding confrontation with the statutory text and purport to find outside that text subjective legislative intent which they exalt as the definitive statement of the law.

I confess that I have trouble viewing this pattern as age neutral.

The results in the third column are similar: as employees with twenty-five years of service age from forty-five to fifty-five, the wear away period increases from eight, then to ten and finally to eleven years. In short, in this example, a fifty-five year old employee has a wear away period over one-third longer than the wear away period for his forty-five year old co-worker. The only variable explaining this difference is age.

I have elsewhere outlined my skepticism of appeals to extratextual legislative intent to overcome the terminology of intricate and technical statutes like our tax and pension laws.[15] Taxation and pensions are quintessentially statutory matters, properly overseen by politically accountable decisionmakers who speak through their statutory pronouncements. When the literal terminology of the statutes enacted by these decisionmakers is displaced in the name of extratextual intent, the law becomes less accountable and less predictable. The intent discovered typically corresponds with the policy preferences of the discoverer. Rarely do those discerning legislative intent acknowledge the conflicting interests and policies often embodied in legislative compromise, conflicts which belie any comfortable notion that the legislature acts with a single, coherent intent. The tax and pension laws (unlike historic texts) are recently adopted, frequently revised, and drafted with the assistance of technically-sophisticated experts; if the courts get it wrong, Congress can (and often does) correct them.

All of these factors leave me dubious in the pension and tax contexts of arguments, like Messrs. Shea, Francese and Newman's, which, instead of engaging statutory text, appeal to extratextual assessments of legislative intent. A serious commitment to statutory law requires that we exhaust the text-based possibilities before resorting to extratextual considerations.

In a critical move, Messrs. Shea, Francese and Newman ground their appeal to legislative intent by observing that the pension age discrimination statutes do not define the term "rate of benefit accrual." The absence of such a definition,

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[15] Edward A. Zelinsky, "Text, Purpose, Capacity and *Albertson's*: A Response to Professor Geier," 2 *Fla. Tax. Rev.* 717 (1996); Edward A. Zelinsky, "*Albertson's*: Why Courts Shouldn't Override Clear Statutory Language," 66 TAX NOTES 1691 (1995).

they suggest, invites their extratextual inquiry into legislative intent.

I am not convinced. Statutory terms are undefined for many reasons: poor draftsmanship, legislative carelessness, the imperatives of political compromise, the desire to delegate interpretation to courts or administrators, the political need to legislate quickly.

However, most statutory terms are not defined since they need not be. Placed in proper context and read in a reasonable fashion, most statutory terms are undefined because the reader willing to engage the text (whether a judge, lawyer or administrator) can be reasonably confident what such terms mean.

In this setting, it is helpful to think of statutory terminology as falling into three categories: open-ended, bounding, and constraining. Some statutory language is so broad and open-ended as to provide a virtual invitation to the reader to supply much, perhaps most, of the content. The Code's provision relative to the deductibility of reasonable compensation is the classic example of such expansive terminology, an overture to the courts to fashion doctrine, free of any significant textual constraints.[16]

Other statutory text imposes significant boundaries while still leaving considerable territory within those boundaries. Confronted with such a statutory text, the reader's task is to make the statute as coherent and workable as possible within the textually-demarcated borders. ERISA's preemption provision is an example of such a bounding text.[17]

Yet other statutory language is highly constraining. Indeed, as a practical matter, statutes would be of little utility unless the bulk of statutory language fell into this

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[16] *See* Edward A. Zelinsky, "Reasonable Compensation: A Study in Doctrinal Obsolescence," *NYU 58th Institute on Federal Taxation – Employee Benefits and Executive Compensation* 2000 at 13-1.

[17] *See* Edward A. Zelinsky, "Travelers, Reasoned Textualism, and The New Jurisprudence of ERISA Preemption," 21 *Cardozo L. Rev*. 807 (1999).

third category. Taxpayers, for example, cannot be expected to discharge their tax obligations unless much of those obligations is fixed with reasonable clarity by the Code.

The "rate of benefit accrual," I suggest, comes within this third category: the statutes' drafters did not define this term because they did not need to. The statutes define an employee's accrued benefit under a defined benefit plan as a deferred annuity commencing at normal retirement. The most natural reading of the pension age discrimination provisions is that the rate of benefit accrual is the rate at which accrued benefits accrue – and accrued benefit is a defined term, specified as a projected annuity commencing at normal retirement.

If I am right that the term "rate of benefit accrual" is not problematic, there is no need to resort to extratextual legislative intent to determine what that term means in the cash balance context since a fair reading of the statutes themselves indicates the approach to be taken, i.e., to translate cash balance allocations into projected annuities starting at normal retirement and to measure the impact (if any) of age on such projected annuities. Thus, the failure to define the term "rate of benefit accrual" reflects not the need to resort to extratextual statements of legislative intent, but rather the ability of the statutes, confronted with a commitment to find coherent meaning, to yield such meaning.

I am, moreover, skeptical of the invocation of legislative history to override highly specific statutory language. There may be merit to such history when statutory terminology is ambiguous or nondirective.[18] However, Messrs. Shea, Francese and Newman's invocation of legislative history to transcend constraining statutory terminology recalls Justice Scalia's observation that citation to legislative history is like

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[18] For a more extensive exploration of the propriety of legislative history, see William N. Eskeridge, Jr., "The Circumstances of Politics and the Application of Statutes," 100 *Colum L. Rev.* 558 (2000).

"entering a crowded cocktail party and looking over the heads of the guests for one's friends."[19] The metaphor is a particularly apt description of the approach embraced by Messrs. Shea, Francese and Newman: peering over the statutes to find friendly faces in the legislative history.

As part of their resort to such history, Messrs. Shea, Francese and Newman highlight the possibility that an employee might work after normal retirement age and Congress' concern to protect such an employee from age discrimination.[20] Messrs. Shea, Francese and Newman carefully avoid portraying Congress as intending to outlaw pension age discrimination *only* after normal retirement – the statutory language is otherwise and proscribes age discrimination in retirement plans at "any age." However, Messrs. Shea, Francese and Newman seek to shift the focus to the period after normal retirement and, after making such a shift, take from the legislative history an example of flat benefit accruals ($10 of annuity income for each month of additional service), an example, according to the legislative history, of a plan passing muster in age discrimination terms.[21]

When accruals after age 65 under this flat benefit formula are measured in the fashion I think the statute requires – as actuarially equivalent annuities starting at age 65, – the result is declining benefit accruals after age 65.[22] This result,

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[19] Justice Scalia attributed this metaphor to Judge Harold Leventhal. *See* Conroy v. Aniskoff, 507 U.S. 511, 519 (1993) (Justice Scalia, concurring).

[20] Shea, Francese and Newman, *supra* note 3, at 768 ("Both the statute and the legislative history make clear that Congress enacted the current age discrimination rules for defined benefit plans to protect employees who continue to work after normal retirement age."); 770 ("the accruals Congress cared most about – those after normal retirement age.") This is a more careful formulation of this position than the conclusion of the *Onan* Court, i.e., that the statutes only apply after normal retirement. *See* note 40, *infra*.

[21] *Id.* at 769.

[22] *Id.* at 769-70. Lest the reader suspect that we are now engaging in actuarial alchemy, the intuitive explanation for what is occurring here is straightforward. Each year as the older participant ages, he is one year farther from age 65 and one

Messrs. Shea, Francese and Newman argue, is so at variance with congressional intent and legislative history as to negate my reading of the statute which tests for age discrimination by comparing projected annuities as of normal retirement age.

Having plucked this flat benefit example from the legislative history, Messrs. Shea, Francese and Newman treat this example as the authoritative statement of the law – rather than grappling with the statutory language itself. If the pension age discrimination statutes gave significant compass to the reader (my first and second categories), I would find persuasive the position advanced by Messrs. Shea, Francese and Newman since I agree, as a matter of policy, that a flat benefit plan of the sort described in the legislative history should not be deemed age discriminatory. However, given the constraining nature of the statutory language relative to age discrimination and pensions, the relevant inquiry is not my policy preferences or an example from the legislative history, but the rule embodied in the statutes.

To be sure, even in the face of apparently constraining language, it is appropriate to consider the implications of reading statutory language closely: "keep off the grass" is unlikely to mean that the groundskeeper cannot mow the lawn. However, the implications of my statutory analysis in the post-retirement context are not as outlandish as Messrs. Shea, Francese and Newman believe.

To avoid age discrimination after normal retirement age, a flat benefit plan would, under a respectful reading of the statutes, need to increase the flat benefit earned in each year worked after such age. Thus, for example, a sixty-six year old

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year closer to death. Because his life expectancy is declining, the lump sum value of his annuity is decreasing because the annuity is expected to last for a shorter remaining life expectancy. Moreover, when that lump sum is discounted to its present value as of age 65, that present value is smaller because 65 is receding farther back in time as the participant ages. When those smaller present values are then projected forward, they buy less annuity income on an annual basis.

continuing to work might need to accrue $11 of annuity income for each month of employment (as opposed to the $10 of pension income earned each month by his younger co-workers); a sixty-seven year old might need to earn a pension annuity of $12 for each additional month worked; and so on. Only by increasing annuities in this fashion for the post-retirement period are those annuities, projected back to age 65, stable in value.

While this result is not the one I prefer as a matter of policy, it is not so beyond the pale as to suggest the need to ignore the literal terms of the age discrimination statutes. In this setting, the increase in the incremental pension annuity earned each year after normal retirement offsets the participant's shorter life expectancy as he grows older – a plausible outcome, particularly given the paucity of individuals who work after normal retirement.[23]

Thus, in this context, as in others,[24] fidelity to statutory text is intimately tied to issues of institutional responsibility and of willingness to accept broad ranges of outcomes, even when these outcomes strike the reader as suboptimal from a policy perspective. Tax and pension policymaking is ultimately the responsibility of Congress and the President who speak through statutes; the disparagement of those statutes makes the tax and pension law less accountable and predictable. The values of accountability and predictability require the acceptance of policy outcomes emerging from the political process.

In contrast, Messrs. Shea, Francese and Newman reject the conclusions emerging from a serious engagement with the statutory text – flat benefit plans must increase pensions earned after normal retirement to avoid age discrimination –

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[23] Today, early retirement is prevalent and late retirement is rare. *See, e.g.*, John H. Langbein and Bruce A. Wolk, *Pension and Employee Benefit Law* (3rd ed. 2000) at 449-54.

[24] *See* note 15, *supra*.

and thus resort to extratextual authority to justify the result they prefer. As a matter of policy, I prefer their result also – but not at the price of degrading the statutory text.

In yet another formulation of their argument about congressional intent, Messrs. Shea, Francese and Newman contend that this debate about the rate of benefit accrual is all beside the point. Congress, they assert, merely intended to outlaw explicit plan provisions specifying a particular age at which benefit accruals cease or decline: "Congress probably intended what it said, namely, that defined benefit plans should no longer be able to specify an age after which an employee's benefit accruals will be reduced or eliminated."[25]

Actually, Congress said nothing of the sort. In three essentially identical statutes, Congress said that benefit accruals cannot stop or decline because of the attainment of "*any* age," not on account of an age specified in the plan text. Messrs. Shea, Francese and Newman buttress their disregard of the statutory text by pulling from the cocktail party of legislative history a passage stating that the pension age discrimination statutes outlaw plans which stop or reduce benefit accruals at a specified age.[26]

This reference is not as supportive of their position as Messrs. Shea, Francese and Newman suggest. The language they quote indicates that the discrimination statutes bar plans from containing specified ages at which benefits decline or stop. This is surely an accurate reading of the statutes which proscribe age discrimination on the basis of "any age," including presumably any age specified in the plan.

However, Messrs. Shea, Francese and Newman read this passage of the legislative history as indicating that the statutes bar *only* discrimination on the basis of ages specified in the plan. This is an aggressive interpretation of the

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[25] Shea, Francese and Newman, *supra* note 3, at 772.

[26] *See id.* at note 21.

passage they quote and, incidentally, an easy standard for a competent drafter to avoid.[27]

But let us assume *arguendo* that Messrs. Shea, Francese and Newman are correct in their understanding of the legislative history as indicating that the statutes only bar explicit use of age to stop or reduce benefit accruals. On this assumption, we again confront the reality that the statutes three times declare as unlawful discrimination declines or stoppages of benefit accruals based on "any age," not "any age specified in the plan." Messrs. Shea, Francese and Newman's case thus reduces to the proposition that, in the face of conflict between the statutes and the legislative history, the legislative history controls.

I respectfully disagree. The production of legislative history, once a cottage industry, is today a massive enterprise with congressional staff, surrounded by armies of lobbyists, manufacturing voluminous quantities of such history, quantities dwarfing the output of a simpler age. It is possible, perhaps inevitable, that this massive output will at times be self-contradictory and at other times will contradict the statute supposedly being explained. Whatever the value of this output when statutory language is open-ended or when such language demarcates boundaries within which courts must work, when the legislative history conflicts with constraining statutory language, the issue is which shall control.

When the issue is posed this directly, I suspect that few would argue for the primacy of legislative history over statutory language. It is therefore not surprising that Messrs. Shea, Francese and Newman seek to open the door to legislative history by suggesting that the statutory language

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[27] Age-based reductions in benefit accruals could be accomplished by proxy, thereby avoiding the specification in the plan of a particular age. For example, such reductions could commence when the participant is first eligible for social security benefits.

("the rate of benefit accrual") cannot be read in context but must instead be explicated by resort to legislative intent and history. This brings us back to where we started: if we engage the statutory text seriously, the term "the rate of benefit accrual" is undefined because it need not be.

Finally, Messrs. Shea, Francese and Newman point to alternative methods of measuring the rate of benefit accrual which have been developed under Section 401(a)(4), the Code provision barring economic discrimination in favor of highly compensated employees.[28] Among these methods is the calculation of annuities commencing immediately, in contrast to deferred annuities projected to start at normal retirement. When cash balance allocations are converted to immediate annuities, such allocations pass muster in age discrimination terms since there is no age-based decline in immediate (as opposed to deferred) annuities.[29]

In invoking the Section 401(a)(4) regulations and their immediate annuity methodology, Messrs. Shea, Francese and Newman's disregard of statutory text becomes total. Consider first the Code's version of the pension age discrimination rules. These rules are part of Code Section 411. Section 411(a)(7)(A)(i)'s definition of an accrued benefit as a projected annuity at normal retirement applies "(f)or purposes of this

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[28] *See* Shea, Francese and Newman, *supra* note 3, at 772-74.

[29] Messrs. Shea, Francese and Newman's argument for measuring benefit accrual via immediate annuities underpins the criticism of my analysis advanced by Hubert V. Forcier of Faegre & Benson, LLP. See 2000 TNT 140-48. *See, also,* Fred Williams, "Zelinsky's interpretation of discrimination laws attacked," *Pensions & Investments* (August 7, 2000) at 47. While the purpose of this article is to reply to Messrs. Shea, Francese and Newman, I would note that Mr. Forcier, with commendable candor, acknowledges that his analysis assumes that the Shea-Francese-Newman argument is correct, i.e., that the rate of benefit accrual for pension age discrimination purposes can be measured in terms of immediate annuities. As noted in the text of this article, I think that premise is wrong as it pushes aside the statutory definition of accrued benefits in terms of deferred annuities and as that premise incorporates the immediate annuity methodology developed under Code Section 401(a)(4), a provision of the tax law of dubious relevance in this context.

section," i.e., for Section 411. When interpreting Code Section 411(b)(1)(G) and its prohibition on age discrimination, it is a strange methodology to ignore Section 411's own definition of accrued benefit (a deferred annuity starting at normal retirement) in favor of a regulatory definition propounded for another, separate section of the Code, i.e. Section 401(a)(4).[30]

Mr. Shea, Francese and Newman's resort to the Section 401(a)(4) regulations becomes even stranger when we consider the parallel provisions of ERISA outlawing age discrimination in pensions. ERISA Section 204(b)(1)(H)(i) (tracking the equivalent Code terminology) is part of ERISA's Title I and prevents defined benefit plans from stopping or reducing "the rate of an employee's benefit accrual" because of age. ERISA Section 3(23) (again tracking the Code) defines "accrued benefit" "for purposes of" Title I as a deferred annuity starting at normal retirement. In invoking the regulations under Code Section 401(a)(4) to define the rate of benefit accrual in terms of immediate annuities, Messrs. Shea, Francese and Newman skip ERISA's own definition of accrued benefit in ERISA Section 3(23) (a projected annuity at normal retirement) and instead import into ERISA's jurisprudence the regulations from Code Section 401(a)(4), a Code provision with no ERISA counterpart. For those who take statutes seriously, it is a strange methodology when reading a statute to look to the regulations under another statute rather than to the provisions of the statute being read.

Instructive in this context are the recent decisions of the 11th and 2nd circuits in *Lyons v. Georgia-Pacific Corporation*

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[30] Because of the severe textual problems in importing the Section 401(a)(4) regulations into Section 411, I will not explore the different purposes of these two Code provisions, differences which might explain their divergent approaches to measuring benefit accruals, i.e., immediate annuities to assess economic discrimination under Section 401(a)(4) and deferred annuities to measure age discrimination under Section 411.

Salaried Employees Retirement Plan[31] and *Esden v. Bank of Boston*[32]. In both cases, the courts of appeals held that, for years before 1994,[33] the lump sum distributions payable to cash balance participants prior to normal retirement are determined by projecting interest credits forward to normal retirement and then discounting the projected total back to present value using a statutorily-mandated interest rate. The appeals tribunals thus properly understood Mr. Lyons' and Ms. Esden's respective benefits on early distribution in terms which project forward to normal retirement. From this premise, it is textually anomalous to calculate participants' distributions by projecting to normal retirement per the literal terms of the statute, but to test for age discrimination on a different basis, e.g., by looking at immediate annuities. Nevertheless, that inconsistency emerges from the analysis of Messrs. Shea, Francese and Newman who would test for age discrimination via immediate annuities even though, as the courts have correctly observed, actual distributions in the cash balance context are determined by projecting account balances to normal retirement. It is difficult to square that inconsistency with the literal terms of the statutes which define participants' accrued benefits in terms of projected annuities starting at normal retirement.[34]

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[31] 221 F.3d 1235 (11th Cir. 2000).

[32] 229 F.3d 154 (2d Cir. 2000).

[33] Since the relevant statutes were amended in 1994, the result for years covered by the newer version of the statutes should be different. *See* Zelinsky, *supra* note 1, at 748-53. The Eleventh Circuit carefully noted that its decision was restricted to the pre-1994 variant of the statutes. The Second Circuit took less pain to distinguish between pre- and post-1994 law. However, it cited the Eleventh Circuit as correctly stating the legal merits of the situation – and, as noted, the Eleventh Circuit was careful to limit its holding to pre-1994 distributions.

[34] Under a respectful reading of the post-1994 version of the statutes, the interest rates used to project benefits forward and then to discount to present values will be those rates stated by the plan, not the statutory interest rate. *See* Zelinsky, *supra*, note 1, at 748-53. When plans specify the same interest rates for both projecting to early retirement and for reducing to present value, the lump sums payable to participants will equal their respective account balances since the two

As a matter of policy, there is much to commend Messrs. Shea, Francese and Newman's proposal that age discrimination in the cash balance context be measured by immediate annuities. The rub is the statute, indeed three essentially identical statutes which indicate that the relevant accrued benefit is a deferred annuity projected to start at normal retirement. Insofar as Messrs. Shea, Francese and Newman are frustrated that our overly-complex regulation of pension plans precludes their preferred outcome, I share that frustration. Insofar as Messrs. Shea, Francese and Newman believe that our frustration justifies disregard of statutory text to reach our preferred policy outcome, I respectfully disagree.

B. Because of The Attainment of Any Age

Messrs. Shea, Francese and Newman also argue that, even if I am right about the need to measure the rate of benefit accrual by converting cash balance allocations to projected annuities starting at normal retirement, I misread another portion of the statutes: "because of the attainment of any age." The annual decline in the annuity value of each year's cash balance contribution, they maintain, does not reflect the employee getting older, but rather manifests inflation-protection built into cash balance arrangements.[35]

In the typical cash balance plan, the employee is credited with a percentage of that year's compensation ("the pay credit") as well as theoretical interest until retirement ("the interest credits"). If an employee moves to a new employer and leaves his cash balance account behind,[36] he generally

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rates will cancel out. When, on the other hand, plans specify different interest rates for projecting account balances to normal retirement and then discounting to present value, lump sum values and account balances will differ.

[35] *See* Shea, Francese and Newman, *supra* note 3, at 774-75.

[36] Proponents of cash balance plans say this won't happen often since a major virtue of the cash balance format is portability, i.e., the ability of cash balance

continues to accrue this theoretical interest until he actually withdraws his lump sum entitlement from the cash balance plan, a lump sum which will thus embody the sum of his pay credits from the period he worked for the employer, interest credits for the period of such employment, and interest credits for the period after the employee severed his employment with the sponsor of the cash balance plan.

In theory,[37] Messrs. Shea, Francese and Newman note, one could envision a cash balance plan under which there is no post-employment accrual of interest.[38] Under such a plan, the employee who switches jobs but leaves his cash balance account with his former employer would receive, on his subsequent retirement, merely the amount to which he was entitled when he switched jobs. For the post-employment period, the former employee's cash balance account would lie fallow and his subsequent distribution from the plan would consist of the figure frozen at the time he left the employer.

As Messrs. Shea, Francese and Newman observe few, if any, cash balance plans are structured in this fashion.[39] However, the theoretical possibility that a cash balance plan could freeze employee accounts upon termination of employment, according to Messrs. Shea, Francese and Newman, highlights the inflation protection inherent in plan designs which continue to accrue hypothetical interest for the departed employee until he withdraws his cash balance account.

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participants to take their notional account balances with them when they go to a new employer.

[37] This is a highly theoretical (though heuristically useful) example since a cash balance plan which stopped interest credits in this fashion would likely flunk the accrued benefit requirements of Code Section 411(b). *See* Zelinsky, note 1 *supra* at 719-23. *See also* Notice 96-8, 1996-1 C.B. 359.

[38] *See* Shea, Francese and Newman, *supra* note 3, at 776-77.

[39] That few, if any, cash balance plans are actually designed in this fashion undoubtedly reflects the likelihood that such a design could flunk the accrued benefit rules of Section 411(b). *See* note 37, *supra*.

The decline in annuity values as cash balance participants age reflects the continually shorter periods for collecting interest until normal retirement. Thus, Messrs. Shea, Francese and Newman conclude, that decline is not because of age but because of inflation-protection, i.e., the accrual of interest until retirement.

Until the end of this argument, I largely agree with Messrs. Shea, Francese and Newman: it is heuristically useful to contrast a theoretical cash balance plan which stops interest accruals when the participant leaves employment with the near universal pattern under which hypothetical interest accrues on the employee's cash balance account even after he goes to work elsewhere. Such continuing accruals do provide a form of inflation protection. Arithmetically, the annual decline in the annuity value of equal pay contributions as the employee ages reflects the decline in the period during which interest accrues since the older employee is closer to normal retirement.

It is, however, unconvincing to say that such decline is not because of age. Consider two otherwise identical employees who are one year apart in age and who participate in a standard cash balance plan under which interest accrues until retirement. Each of these employees receives the same theoretical allocation to his hypothetical cash balance account. But for the one year difference in age, the annuity value of these allocations would be identical.

True, one could in theory postulate a plan which freezes hypothetical interest allocations when the employee terminates employment. Since the age discrimination inquiry is fact- and plan-specific, it could well be that such a plan can pass muster in age discrimination terms.

However, none of us believe that, in practice, there are many (perhaps any) cash balance plans of this sort. And as to cash balance plans which do exist and provide for continuing

interest accruals, the annuity value of equal cash balance allocations declines as employees age.[40]

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[40] In *Eaton v. Onan Corp.*, No. IP97-0814-C-H/G (S.D. Ind. September 29, 2000), the United States District Court for the Southern District of Indiana held that a cash balance plan did not violate the pension age discrimination statutes. In important respects, the District Court's analysis tracks the arguments of Messrs. Shea, Francese and Newman. The *Onan* Court, for example, relies on the same flat benefit illustration which Messrs. Shea, Francese and Newman cite from the legislative history. The *Onan* Court similarly defines the concept of the "rate of benefit accrual," not by a searching reading of the statutory text, but by resort to the court's policy predilections favorable to cash benefit arrangements ("cash balance plans offer obvious benefits to employees"). The *Onan* Court also accepts the argument embraced by Messrs. Shea, Francese and Newman that the age-based impact of cash balance plans can be dismissed as inflation-protection.

To the extent the *Onan* Court tracks the arguments of Messrs. Shea, Francese, and Newman, my rejoinder is the same: a serious confrontation with the statutory text leads to a different conclusion. However, in several respects, the *Onan* Court's opinion goes further than the Shea-Francese-Newman analysis and thus requires brief response.

The *Onan* Court (going beyond Messrs. Shea, Francese and Newman) concludes that the pension age discrimination statutes only apply to individuals who work after normal retirement. Instead of confronting the contrary language of the statute (which prevents pension discrimination at "any age"), the *Onan* Court buttresses its appeal to legislative history by citing the "revised and extended remarks" of four representatives which remarks were "not actually delivered on the floor of the House."

This approach puts us deep into cocktail party country. *See* note 19, *supra*, and accompanying text. After exhausting the reasonable text-based possibilities, it may be sensible to turn to the views of a bill's supporters to resolve ambiguity. However, it turns the process on its head to by-pass the statute and instead rely on remarks which no one actually spoke on the floor of Congress.

The *Onan* Court further concludes that "the rate of benefit accrual should be defined as the change in the employee's cash balance account from one year to the next." Indeed, the court states, "(t)here is no statutory or public policy reason" why cash balance plans should not be treated for these purposes the same as defined contribution arrangements.

This is wrong; there are severe statutory problems, in the age discrimination context, with treating cash balance plans as defined contribution pensions. Cash balance plans are defined benefit arrangements. For better or worse, the statute explicitly propounds one approach to age discrimination for defined contribution plans (to measure inputs) and another approach for defined benefit pensions (to measure outputs). "There is a no statutory" basis for ignoring this distinction and measuring cash balance arrangements (defined benefit plans) for age discrimination as if such arrangements were defined contribution plans; they are not.

IV. CONCLUSION

No issue is more hotly debated today[41] in the legal community than the appropriate approach to statutory texts. In the context of tax and pension disputes like the cash balance controversy, the issue is ultimately one of legitimacy and predictability: When politically accountable decisionmakers – the Congress and the President– formulate tax and pension policy, they do so through statutes; taking those statutes less than seriously makes the tax and pension

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Is this the right choice as a matter of policy? Along with the *Onan* Court, I think not. Is it appropriate to push the statute aside to reach the policy I prefer? Unlike the *Onan* Court, I think not.

The *Onan* Court correctly notes that the heading of the Code version of the pension age discrimination law refers to the period after normal retirement. After conceding that such "(s)tatutory headings are not necessarily overwhelming or controlling indications of the meanings of statutes," the Court proceeds on the opposite tack and treats this heading as definitive for the ERISA and ADEA versions of law, versions in which the heading does not appear.

The *Onan* Court suggests that the pension age discrimination rules need not apply prior to normal retirement since "(t)he more general terms of the ADEA continue to bar intentional age discrimination." However, as a textual matter, it is far from clear that the general provisions of the ADEA should apply to pensions when specific provisions of that same statute address the issue of pension age discrimination. Moreover, even if the general provisions of the ADEA apply in the face of the specific rules pertaining to pensions, it is far from clear how the general provisions should be understood. A searching reading of the pension age discrimination statutes ("any age") suggests a congressional purpose to protect all persons from age-based reductions in pension accrual rates.

In short, the *Onan* Court gives short shrift to what the statutes actually say to reach a result the court finds desirable as a matter of policy.

Eaton v. Onan Corp. is reported at 86 AFTR2d para. 2000-5350 and can be accessed electronically at http://pub.bna.com/pbd/ip970814.htm.

[41] It is, however, a mistake to assume that the issue is unique to our times. For example, the writings of Franz Lieber, a confidant of Abraham Lincoln, foreshadowed many of the issues with which contemporary legal commentators are today grappling under the heading of textualism. *See, e.g.*, "A Symposium on Legal and Political Hermeneutics, 16 *Cardozo L. Rev.* 1879 (1995).

Similarly, the classic debate in Jewish law between the school of Hillel and the competing school of Shammai was, in important respects, a debate about the appropriate approach to legal texts. *See* "Bet Hillel and Bet Shammai," 4 *Encyclopaedia Judaica* 736 (1973).

laws less accountable and predictable than they should be. Given the morass of data surrounding the tax and pension laws – committee reports, floor statements, proposed versions of legislation – something must be designated as the primary authority. If not the statutes, what?

As a matter of policy, I largely agree with Messrs. Shea, Francese and Newman and their preferences. However, before reaching questions of policy, the threshold inquiry arises: Does a discernible policy emerge from the relevant statutes?

I suspect that most tax and pension lawyers, in the abstract, agree upon the primacy of statutory text. Indeed, I suspect that the power of that premise underpins Messrs. Shea, Francese and Newman's key move, i.e., to declare that the absence of a statutory definition for the "rate of benefit accrual" opens the door to consideration of legislative intent and history. It is necessary for Messrs. Shea, Francese and Newman to nudge[42] the statute aside in this fashion to justify the introduction of their intent- and history-based arguments.

In contrast, I suggest that fidelity towards statutory texts requires us to exhaust all the reasonable text-based solutions before turning to such extratextual considerations. Such exhaustion requires me to work with the statutory text when Messrs. Shea, Francese and Newman have moved on to extratextual sources of legislative intent.

In short, the intellectual integrity and institutional legitimacy of the tax and pension laws requires adherence to constraining statutory terminology. And the true test of such adherence occurs, not when the texts point in the direction with which one agrees, but when they do not.

In the case of the pension age discrimination statutes, those statutes specify that, in the defined benefit context, accrued benefits are measured by projecting anticipated

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[42] Not noodge. *See* William Safire, "On Language," *New York Times Magazine*, October 8, 2000, at 42.

annuities at normal retirement. Those statutes also provide that plans may not decrease the "rate of benefit accrual" on account of "any age." Given a commitment to the primacy of statutory law, the most natural reading of these concepts is that they are related – even though the result is an outcome in the cash balance context with which, as a matter of policy, I disagree.

The interaction of the cash balance format and the pension age discrimination statutes is yet another example of the overregulation of qualified plans and of the dynamic underlying that overregulation. When enacted, these statutes undoubtedly appeared straightforward and compelling to their supporters: Who, after all, favors age discrimination? What could be more obvious than testing defined contribution plans for discrimination on the basis of their contributions and testing defined benefit plans on the basis of projected benefits?

The problem, as with so much pension regulation, is that the apparent short-run advantages of these rules gave rise to long-run costs no one foresaw. In this case, the emergence of cash balance arrangements and the conflict between those arrangements and the pension age discrimination statutes preclude most cash balance plans, a result with which Messrs. Shea, Francese, Newman and myself all disagree. Our difference lies in our response to the "parchment barriers" of the statutes.[43]

I am no longer sanguine that the process of pension overregulation can be restrained, let alone reversed: The ideological underpinning of such regulation – current law constitutes a tax expenditure to be channeled statutorily - has never held stronger sway, despite the analytical weakness of that ideology.[44] The benefits of regulation are, in the short

[43] No. 48, *The Federalist Papers* (Madison).

[44] *See* Edward A. Zelinsky, "Tax Policy v. Revenue Policy: Qualified Plans, Tax Expenditures, and the Flat, Plan Level Tax," 13 *Va. Tax Rev.* 591 (1994); Edward

term, politically compelling; the costs of such regulation tend to be delayed and unanticipated, a classic imbalance biasing the legislative process towards action, rather than restraint.

In such a world, the unanticipated becomes the inevitable; more situations arise like the cash balance controversy where unforeseen developments run afoul of statutory constraints fashioned for other settings. The understandable temptation in such a world is the approach of Messrs. Shea, Francese and Newman, to derogate statutory text. For the long run, however, such an approach makes the pension and tax laws less accountable and predictable than they should be.

At its most basic, our system of tax and pension laws cannot function without fidelity towards statutory texts. Such fidelity often entails the acceptance of outcomes with which the reader disagrees as a matter of policy. Ultimately, however, a system of statutory law requires us to take statutes seriously. And taking the pension age discrimination statutes seriously leads to the conclusion that many, likely most, cash balance plans violate such statutes.

A. Zelinsky, "Qualified Plans and Identifying Tax Expenditures: A Rejoinder to Professor Stein," 9 *American J. of Tax Policy* 257 (1991); Edward A. Zelinsky, "The Tax Treatment of Qualified Plans: A Classic Defense of the Status Quo," 66 *North Car. Law Rev.* 315 (1988).