

# THE WALL STREET JOURNAL.

## Many Ties Link Pension Lobby To Regulators

By **Ellen E. Schultz** and Theo Francis

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THE RETIREMENTS OF millions of Americans could hang partly on the relationships between those who regulate pension plans -- and are drafting regulations -- and pension lobbyists and consultants hired by employers and financial firms.

The relationships are social as well as professional. Consider a recent party at the Washington home of William F. Sweetnam Jr., a lawyer at the Treasury Department who is playing an important role in drafting regulations for what are known as cash-balance pension plans. The party was thrown to welcome a new congressional staffer working on pension issues. It was co-hosted by Brian Graff, a lobbyist for the American Society of Pension Actuaries, a group representing those who make a living running employer-sponsored pension plans, which has lobbied in favor of cash-balance plans.

Not invited were any of the few lawmakers and congressional staffers who have staked out strong positions against cash-balance plans, which offer financial benefits to employers but can reduce payments to older workers.

Instead, among the invited guests -- aside from a smattering of congressional and Treasury staffers who work on pension issues -- was a long list of lobbyists representing employers on pension and retirement matters. They included individuals from the Erisa Industry Committee and the American Benefits Council, whose members include International Business Machines Corp., AT&T Corp. and hundreds of other large employers with a financial stake in the outcome of the pension regulations Mr. Sweetnam is drafting.

Also invited were lobbyists from the American Council of Life Insurers; Wall Street's Securities Industry Association; Davis & Harman and Groom Law Group, law firms that lobby on behalf of employers and benefits consultants; and Cigna Corp., which is defending an age-discrimination suit involving its cash-balance plan.

Mr. Sweetnam, the Treasury's benefits tax counsel, says the party to welcome Judy Miller, an actuary from Montana joining the Democratic staff of the Senate Finance Committee, was a social event, not work, and the staffers and lobbyists he invited were people with whom he works regularly and "who are also my friends."

Says Mr. Graff, executive director of the ASPA, who has also worked on the staff of the Joint Tax Committee of the House and Senate, and for Groom Law Group: "The pension community is certainly a relatively close-knit group . . . because there aren't that many people with a great deal of technical pension expertise."

There is nothing new about lobbyists, congressional staffers and regulators socializing. But this is a crucial time for the pension business: The Treasury is expected any day to issue regulations on cash-balance plans, determining whether the plans violate age-discrimination laws, and it is developing proposed regulations to determine whether employers can pay departing workers smaller lump sums from cash-balance plans under certain circumstances. Employers have been increasingly eager for favorable regulations since IBM lost an age-discrimination suit in a federal district court in July, and Xerox Corp. in August lost its appeal in a cash-balance case involving the underpayment of lump sums.

Cash-balance plans are controversial because when employers switch to them, older workers often lose the advantage of many years with their employer. The new-style plan changes the formula for figuring how large a pension an employee eventually would be owed. Unlike traditional pensions, which grow rapidly in later years, cash-balance plans base benefits on a percentage of pay each

year, plus interest. Older workers can see their final pensions cut between 20% and 50% when their plans are converted.

While the Treasury has been working on cash-balance regulations for more than 15 years, more than 300 employers converted their plans. The change typically reduces pension liabilities and, even in rare cases where benefits aren't cut, adopting a cash-balance plan brings an accounting windfall that indirectly boosts earnings.

Many employers hope they can count on the Treasury to issue regulations favorable to them. Many officials developing the pension regulations previously represented employers on pension issues, either on Capitol Hill or by helping employers establish cash-balance plans, before being appointed to their government jobs.

Treasury Secretary John Snow, who has final say on cash-balance regulations, once headed CSX Corp., which implemented a cash-balance plan for newly hired workers this year. Mr. Snow also was on the human-resources committee of Verizon Corp.'s board when it voted to adopt a plan for Verizon employees.

Mr. Sweetnam joined Sun Co., now Sunoco Inc., in 1989, as it was implementing one of the first cash-balance plans. In 1995, he joined Towers Perrin, a benefits-consulting firm that has been a prominent promoter of cash-balance plans. He became majority tax counsel to the Senate Finance Committee in 1998, serving primarily as an adviser to the then-chairman, Sen. William Roth Jr., where Mr. Sweetnam supported cash-balance plans. Mr. Sweetnam says his positions on the finance committee reflected Sen. Roth's stances.

At the Internal Revenue Service, which is also responsible for formulating cash-balance and other pension regulations, some of the top positions traditionally filled by career experts have gone to lawyers and consultants with backgrounds representing employers, under a measure adopted in the late 1990s to bring in private-sector experts to help reshape the tax agency. Paul T. Shultz III, who worked on cash-balance pension issues for many years at Towers Perrin, was chosen in March 2000 as director of employee plans rulings and agreements. In March 2001, the position of senior technical adviser went to Thomas Terry, who was with Groom Law Group, lobbying for employers.

In statements sent through the IRS's media office, Mr. Shultz says his role with cash-balance plans is small. Mr. Terry says, "I have not been in a decision-making role at the IRS involving cash-balance plans."

Some career IRS staffers say the influence of employer groups has grown in recent years.

Until late last year, Mark A. Weinberger was assistant Treasury secretary for tax policy, overseeing the office that handled the cash-balance issue. Mr. Weinberger had been listed as a lobbyist for the Cash Balance Coalition, a group formed by a Washington lobbying firm called Washington Council Ernst & Young, a unit of accounting firm Ernst & Young LLP. Mr. Weinberger's successor, Pam Olson, was prior to her appointment in January the chairwoman of the American Bar Association's Section of Taxation, whose members include benefits-industry lawyers.

Tara Bradshaw, a Treasury spokeswoman, says Ms. Olson "complied with all the ethics rules," and was unavailable to comment. Mr. Weinberger, now a top tax official at Ernst & Young, couldn't be reached for comment yesterday.

Ms. Miller, for her part, says that with few acquaintances in Washington outside her immediate co-workers, the party was a "a very gracious thing for them to do." Although she has been a member of ASPA, which she views as a professional society, Ms. Miller says she will probably let her membership lapse now that she is no longer practicing.

Ms. Bradshaw, the Treasury spokeswoman, objected to questions about the party. The policy positions of those invited to the party "had no bearing on whether they were invited or not," Ms. Bradshaw said. "This was two buddies throwing a party for friends."

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John D. McKinnon contributed to this article.



## THE WALL STREET JOURNAL

### **Leading the News: House Acts to Derail Pension Rules --- Amendment May Prevent Cash-Balance Regulations Proposed by the Treasury**

By **Ellen E. Schultz** and Theo Francis

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In an unexpected move that involved possibly doctored Treasury documents, an expensive full-page advertisement in the New York Times and a lot of heat over cash-balance pension plans, the House passed an amendment that could prevent the Treasury from issuing controversial pension regulations.

Rep. Bernie Sanders, a Vermont independent, offered the amendment, which was tacked on to an appropriations bill, to stop the Treasury from issuing final regulations on cash-balance pension plans -- regulations that have been on the drawing board for more than 15 years. The vote passed 258 to 160, with 65 Republicans and 192 Democrats in favor.

Cash-balance plans are controversial because they usually cut pensions for older workers. In late July, a federal district court in Illinois concluded that International Business Machines Corp.'s cash-balance plans had discriminated against older workers.

Mr. Sanders and his co-sponsors, who include Reps. Gil Gutknecht (R., Minn), George Miller (D., Calif.) and Maurice Hinchey (D., N.Y.), say the Treasury regulations would have reversed the court's decision in the IBM case. "The court found that IBM knew that older workers would lose up to 47% of their pensions under the cash-balance conversion," Mr. Sanders said. "Now the Treasury is about to help employers make an end run around the courts and illegally cut pensions."

Although the final regulations haven't been issued, the Treasury is widely viewed as sympathetic to employers in pension matters, and in December issued proposed regulations that said cash-balance plans wouldn't be subject to age-discrimination rules.

Hundreds of large employers have adopted cash-balance plans, which usually save companies money by cutting pensions for older workers, and indirectly boost earnings by cutting pension liabilities.

The adverse decision in the IBM case alarmed employers, which are seeking favorable regulations from the Treasury, which they hope will aid them in their cases in the courts.

On Monday, an IBM lobbyist, Susan M. Siemietkowski, sent a document she called the "Treasury's statement of opposition" to various lawmakers' staffs, including Mr. Gutknecht. The Treasury document, on official Treasury letterhead, noted "Treasury Strongly Opposes the Sanders Amendment" and advised lawmakers to oppose the amendment, which it said "will weaken the defined benefit system."

Tara Bradshaw, a spokeswoman for the Treasury, said the agency didn't issue the document. "It is a Treasury generated fact sheet stating our position on a set of [past] amendments that were never offered. However, they were not sent in the format you provided and, therefore, appear to have been doctored."

She said the Treasury had prepared an earlier document pertaining to an amendment offered by Mr. Sanders last year, but that the original document was "designed for informational purposes and was not formally released," she said. "We were not aware the document had been circulated beyond a very limited number of select staff."

IBM spokesman Bill Hughes says, "We received the document from the Erisa Industry Committee, and we understand it was prepared by Treasury and distributed to members of the House last week. We believe that the document was not changed from what the Treasury distributed." He added, "We're doing everything we can to get to the bottom of this."

The IBM lobbyist also sent lawmakers a document titled "IBM-Wash Post.doc," which included text that appeared yesterday, in full-page ads in the New York Times and the Hill, a daily newspaper for members of Congress and their staffers.

The Microsoft Word document labeled its creator as Richard C. Shea, a lawyer at Covington and Burling, which is defending IBM's case.

When asked if he wrote the advertisement, Mr. Shea said no. When told that his name was attached to the document, he said he was aware of "various versions" of the ad "floating around," and said he didn't write it. He declined to say whether he was involved in the ad campaign, saying one of its sponsors was a client and hadn't authorized him to discuss it. "It's possible someone took a document I had originally drafted and prepared a new one on top of it," he said.

The ad carried the headline "Don't Destroy America's Pension System," and said the Sanders amendment would "outlaw vast numbers of pension plans." It was signed by a handful of lobbying groups, including the Erisa Industry Committee and the American Benefits Council, lobbying groups to which IBM belongs, and paid for by Erisa Industry Committee. Also listed was the Coalition to Preserve the Defined Benefit System, an employer lobbying group. The Web site for the coalition doesn't identify its members. However, the site's address is registered to Watson Wyatt, a consulting firm that is IBM's actuary, and which helped it implement its cash-balance plan.

When asked about Watson Wyatt's relationship to the coalition, Eric Lofgren, global director of the firm's benefits-consulting group, says Watson Wyatt was "in at the birth" of the coalition "with a bunch of employers," and functions as an adviser to the group.

Last year, Mr. Sanders offered a similar amendment, which passed the House 308-121, with most Democrats and 47% of Republicans voting in favor; it ultimately was stripped from the final bill.

Sen. Thomas Harkin (D., Iowa) also is expected to introduce a limitation amendment aimed at preventing the Treasury from issuing cash-balance regulations. If the reconciled amendments ultimately pass, the final regulations on cash-balance plans won't come out for another year.

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## **THE WALL STREET JOURNAL.**

### **Treasury Says Employees of IBM Doctored Item Sent to Lawmakers**

By **Ellen E. Schultz**

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(Copyright (c) 2004, Dow Jones & Company, Inc.)

The Treasury Department's inspector general said employees of International Business Machines Corp. had doctored a Treasury document that was circulated to lawmakers last fall, adding that he hasn't ruled out criminal prosecution.

Dennis Schindel, the Treasury's acting inspector general, made the comments in response to questions from Rep. Bernard Sanders, (I., Vt.), at a hearing in Washington held by the House Financial Services Subcommittee on Oversight. It was the first public acknowledgment of the status of the investigation being conducted by the inspector general.

The investigation was begun last fall after an IBM lobbyist sent a document, with an official Treasury letterhead, to various House staff members, encouraging them to oppose an amendment they were about to vote on. The document noted: "Treasury Strongly Opposes the Sanders Amendment."

The amendment, introduced by Mr. Sanders, was aimed at preventing the Treasury from issuing pension regulations pertaining to cash-balance pension plans, which are controversial because they reduce pensions for most older workers. The regulations, if implemented, could have been used to overturn a federal court's ruling that IBM's cash-balance plan violated age-discrimination laws. The amendment subsequently passed with wide bipartisan support; on Tuesday, the Treasury withdrew its proposed regulations.

During Wednesday's hearing, Mr. Sanders asked if anyone at the Treasury had helped alter the document. Mr. Schindel said his staff was still looking into that. "There are several aspects of this investigation involving IBM employees, lobbyist employees and Treasury employees," he said. Mr. Schindel said he hoped to issue a report within two months.

An IBM spokeswoman said, "We believed we were redistributing a public document that we have understood to have been widely distributed already by the Treasury." She said the company "has cooperated fully with the Treasury Department."

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## THE WALL STREET JOURNAL

Leading the News

### **IBM Sets Accord On Pension Plan For \$300 Million**

By **Ellen E. Schultz**, Theo Francis and William M. Bulkeley

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International Business Machines Corp. agreed to pay \$300 million to thousands of older current and former employees to partially settle litigation over its pension plan.

The company and plaintiffs in the case also agreed to cap further damages to an additional \$1.4 billion, both sides said yesterday afternoon.

The agreement, announced in separate late-afternoon statements, still requires approval from the federal court in Illinois that ruled against IBM last year, finding that the company had discriminated against older current and former employees when it changed to a cash-balance pension plan in 1999.

A traditional pension multiplies years of service by average salary, producing a benefit that escalates rapidly in value in later years. When companies change to cash-balance plans, they freeze the pension, which subsequently grows only by small annual increments, based on a worker's pay. As a result, older employees may see their retirement income decline by 20% to 50%.

IBM said it will take a \$320 million charge in its third quarter, equal to about 13 cents a share after taxes. It said the one-time charge won't affect its operating results, and won't involve any cash outlay because the payment will be made by its overfunded pension fund. Earlier this month, IBM settled another element of the suit; of IBM's charge, \$20 million reflects that smaller partial settlement.

This settlement caps what IBM and its pension plan ultimately will have to pay. IBM said it still expects to appeal two aspects of the ruling pertaining to age-discrimination claims. If IBM wins on the remaining claims, it will pay only the \$300 million portion agreed to yesterday. Otherwise, it would pay at most the additional \$1.4 billion.

The company previously estimated that losing the case would force it to pay out an additional \$6.5 billion in benefits for more than 130,000 current and former workers. However, in its ruling last year, the court didn't issue a specific dollar figure.

IBM Treasurer Jesse Greene said that "this settlement protects the company and our shareholders." He said that even if it loses the sections it is appealing, "the remedies are within IBM's ability to handle." IBM said it expects to prevail on appeal.

Douglas R. Sprong, one of the plaintiffs' attorneys, said, "We are confident the class will win any appeal, because under both the conversion formula and the cash-balance formula, older workers received less than their younger counterparts for no reason other than age."

The case has been watched closely both for the impact on IBM and the implications for other companies with cash-balance plans. Employer groups have warned that a judgment against IBM will spell the death of cash-balance plans and trigger a flood of lawsuits.

But the court's decision about IBM likely will have little immediate effect on the roughly 300 to 400 other companies with cash-balance plans, because Congress is expected eventually to pass legislation saying that cash-balance plans aren't inherently age-discriminatory, a move that would insulate other companies from similar lawsuits.

Toni Sacconaghi, an analyst with Sanford C. Bernstein, said the settlement is "modestly positive because IBM closed the door on some uncertainty."

Even if IBM ultimately loses its planned appeals, the company itself won't have to pay a dime, because the money would be paid from the well-funded pension plan over many years. Under pension law, there are no punitive or compensatory damages, so essentially, IBM merely would be paying out benefits it already has funded over the years.

The roots of IBM's dispute lie in the 1990s, when hundreds of large employers converted their traditional pensions to cash-balance plans, a move that slashed the pensions of millions of workers in their 40s to 60s by changing the way their pensions are calculated.

When companies change to a cash-balance formula, they essentially freeze the pension, so additional years on the job don't make it grow. This frozen pension is converted to a dollar value (the lump sum the person would receive if the value of all his monthly retirement checks were converted to an immediate payout). The frozen pension value, called the "account balance," grows slowly each year, typically with a flat "credit" based on pay, say, 4%.

For older workers, freezing their pension just when it is beginning to rise rapidly in value, and instead giving them the equivalent of a 401(k) with only a few years of growth, is devastating: Their retirement income can fall by 20% or more. In IBM's case, the court noted last year that the cash-balance plan reduced pensions for some people by more than 40%.

What's more, many companies also lowballed the opening account balances. For instance, if someone's frozen pension was valued at \$100,000, the employer would give him an opening account balance of, say, \$80,000. As a result, the employee has to wait until the annual pay "credits" bring his account back up to \$100,000 before his pension can grow again. In contrast, a new or young worker would begin to build up new benefits right away.

Companies that converted to cash-balance plans enjoyed significant financial rewards. Under accounting rules, when a company reduces a liability (which is what happens when it cuts benefits), the move produces accounting gains, which boost income, and hence earnings. In its ruling last year, the federal court noted that in 2001 alone, IBM's pension plan contributed more than \$1 billion to income, accounting for 13% of its net income. Last year, IBM's pension plans contributed \$560 million, or 7% of the total, to net income.

An IBM spokeswoman said recently that the pension's past contributions to IBM's income were "not at all unusual" for a fully funded pension plan.

Companies generally told workers that they were converting "old fashioned" pensions because cash-balance plans were easier to understand, and better for a mobile work force, because job hoppers can take their money in a lump sum. While workers did, in fact, like the idea of a portable pension

(not knowing that traditional pensions also can be paid out that way), few understood that their pensions had been frozen or that in many cases their opening balances were lowballed.

That changed dramatically in 1999 when some IBM workers reverse-engineered the numbers, and concluded their pensions were being cut by 20% to 40% or more.

Within months, the backlash from enraged employees triggered Senate hearings, an investigation by the Equal Employment Opportunity Commission and a moratorium by the Internal Revenue Service, which to this day hasn't approved a cash-balance conversion.

IBM employees then filed suit, saying the cash-balance plan violates age-discrimination rules. Under pension law, the rate at which a pension builds (its "accrual rate") can't decline with age.

The suit also complained that for thousands of employees IBM established opening balances that were lower than the frozen pension values, a phenomenon called "wearaway."

In July 2003, Judge G. Patrick Murphy at the District Court in Illinois concluded that the cash-balance plan discriminated against older workers. Attached as exhibits in the case were memos and e-mails between IBM executives and consultants, who discussed how the changes would benefit younger workers, how older workers' pensions would fall and how some would experience "wearaway."

IBM has said the memos just were part of the planning process. It settled the "wearaway" claim in the suit.

As for the age-discrimination issue, IBM hasn't disputed that pension-accrual rates decline with age in its pension program, but says the age-discrimination rules for pensions shouldn't apply to cash-balance plans, because they are intended to resemble 401(k)s. The age-discrimination issue is one of the two remaining claims in the suit, which IBM is appealing to the Seventh U.S. Circuit Court of Appeals in Chicago.

Congress is likely to begin discussions on how it would change pension law so that cash-balance plans are exempt from the age-discrimination rule (which forbids a declining accrual rate for older workers; it isn't illegal to freeze pensions, or to cause "wearaway" periods during which pensions don't grow).

Still, even if legislation is passed next year or afterward, and were retroactive, it wouldn't necessarily help IBM, because Congress can't enact legislation reversing a federal-court judgment that was based on the law in effect when the suit was brought.

Meanwhile, IBM's chance for help from regulators or lawmakers has eroded. Earlier this year, the Treasury Department abandoned plans to issue regulations that would have concluded that cash-balance plans aren't age discriminatory, after a spirited backlash from employee groups, AARP, and others.

IBM also lacks universal support from lawmakers, who may be reluctant to enrage older voters in an election year. Last week, the House of Representatives passed an amendment introduced by Rep. Bernie Sanders (I., Vt.) that would prevent the government from helping overturn last year's federal-court ruling in the IBM case, by a vote of 237-162, with 52 Republicans and 184 Democrats in favor.

The Office of the Inspector General of the Treasury confirms that it recently broadened its continuing investigation of the use of a document bearing the Treasury's official seal, which an IBM lobbyist gave lawmakers last year when they were about to vote on a pension matter that might affect IBM.

IBM has said it did nothing improper.

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