MELLON SURVEY OF CASH BALANCE PLANS
DISPELS COMMON MYTHS AND AFFIRMS POSITIVE FEATURES

Mellon's 2003 comprehensive survey on cash balance plans is nearing completion. Because some of the key findings in the survey are inconsistent with assertions commonly made by cash balance critics, we are issuing these preliminary results.

The 2003 survey has been combined with a similar survey conducted in 2000, resulting in a combined survey of 157 cash balance plans with assets of about $190 billion covering about 1.7 million workers.

The preliminary results include the following key findings:

- Employer Costs Usually Do Not Decrease
- Valuable Transition Benefits Are Normally Provided
- Lowering Opening Balances by Using High Interest Rates is Uncommon
- Benefit Distribution Favors Lower Paid Workers
- Not All Cash Balance Plans Arise From Conversions

Employer Costs Usually Do Not Decrease

Total employer costs were expected to remain about the same or increase in 70% of the conversions from traditional defined benefit plans to cash balance plans, taking into account shifting of costs to other retiree programs such as 401(k) plans. This result is contrary to the common assertions that cash balance plan conversions are motivated primarily by cost savings.

Valuable Transition Benefits Are Normally Provided

Over 80% of the conversions to cash balance plans included one or more of the most common transition approaches: supplemental transition pay credits; continuing the prior plan benefit formula, either automatically or upon election; and providing benefits based on the greater of the cash balance and prior benefit formulas. Many of the other conversions provided different transition enhancements. Invariably the oldest workers and many of the middle-aged workers are given protections that go well beyond those provided when a plan terminates or when benefit accruals are frozen. These results are contrary to claims that generous transition provisions are the exception rather than the rule.

Lowering Opening Balances by Using High Interest Rates is Uncommon

The vast majority of the cash balance conversions included “opening balances” based on the present value of employees’ accrued benefits under the prior benefit formula as of the date of conversion. The interest rates used in determining the opening balances are determined in a variety of ways, typically reflecting the level of market rates at or shortly before the conversion date. Almost 75% of these plans used an interest rate for this purpose that was no higher than the range of 30-year U.S. Treasury bond rates in the nine-month period before the conversion date. This result is contrary to the assertion that employers typically understate opening balances by using unduly high interest rates and that such practice leads to the so-called “wear-away effect.”

Benefit Distribution Favors Mobile and Lower Paid Workers

Cash balance plans deliver retirement benefits broadly across an employer’s workforce, providing more meaningful benefits to shorter-service, lower-paid employees. One indication of this from the survey is that, compared to the benefit formulas they replaced, the cash balance formulas tended to provide proportionately more benefits to lower paid workers through elimination of “Social Security integration.” While 73% of the plans before the conversion took into account Social Security benefits directly or indirectly, only 36% of the ongoing cash balance formulas are integrated with Social Security.

Not All Cash Balance Plans Arise From Conversions

Nine of the plans in the survey were not the result of conversions from traditional defined benefit plans. Many critics have asserted that the only time cash balance plans are adopted is for employees who were already covered in a traditional defined benefit plan.