

CONFIDENTIAL

March 25, 2009

Approval: 4/1/09

PENSION COMMITTEE

Meeting 08/5

2:30 p.m., December 5, 2008

M. Portugal, Chairman

**Committee Members**

P. Alonso-Gamo (SPR)  
A. Ghosh (RES)

**Alternate Members**

I. Ábel (BE)  
J. He (CC)  
N. Imamura (JA)  
M. Majoro (AE)

P. Gotur, Committee Secretary  
W. Rahman-Garrett, Assistant

**Also Present**

A. Al Nassar (SA)  
J. Cova (CE)  
A. Ducrocq (FF)  
S. El-Khouri (MI)  
P. Gasiorowski (SZ)  
Y. Ha (AU)  
D. Heath (UA)  
T. Kudiwu (AF)  
A. Rieck (GR)  
A. Rojas (AG)  
Y. Yakusha (NE)

African Department: T. Richardson. External Relations Department: S. Culhane. Finance Department: M. Nilssen. Human Resources Department: D. Marzouk, M. Rodlauer, M. Vicini. Legal Department: J. Lester, B. Patterson. Office of Budget and Planning: G. Conway. Office of the Managing Director: K. Miranda. Research Department: A. Ghosh. Secretary's Department: P. Martin, W. Rahman-Garrett. Strategy, Policy, and Review Department : P. Alonso-Gamo. Senior Advisors to Executive Directors: G. Aboobaker (AE), S. Nget (ST). Advisors to Executive Directors: H. Li (CC), A. Maciá (BR), I. Mwanawina (AE).

**PENSION COMMITTEE—AMENDMENTS TO THE  
SUPPLEMENTAL RETIREMENT BENEFITS PLAN TO COMPLY  
WITH U.S. TAX REGULATIONS**

The Chairman (Mr. Portugal) made the following statement:

The purpose of this meeting is to discuss this paper which proposes amendments to the Supplemental Retirement Benefit Plan (SRBP), to make it compliant with U.S. tax law. The supplemental plan was established in 1985 to pay pensions that exceed certain limits under U.S. tax law, for benefits that are paid from qualified pension plans.

The changes that are being proposed here would bring the plan into compliance with the changes in the tax laws governing this nonqualified pension plan, and will become effective, if they are approved here, as of January 1 2009.

If we did not enact these changes, then the U.S. participants whose benefits would start from next year would be subject to a penalty tax of 20 percent on the entire value of the pension that comes from this supplemental plan. So up to now they have been able to make one set of elections, both for the normal staff retirement plan and the supplemental retirement plan but, after this year, they will have some restrictions on the elections that they can make regarding the payment of pensions.

There are two possible elections. One election that would be restricted is the election to commute up to one third of the pension into a lump sum payment. The second election is the option to defer the start of the pension until after they have become eligible to receive the pension.

The changes in U.S. law do not affect the normal staff retirement plan or the pensions paid from this supplemental retirement plan to non-U.S. citizens—for this there is no change whatsoever. For the U.S. staff, these changes that are proposed protect the treatment of benefits that they have been vested in before 2005. In order to limit the impact of this law as much as possible, we are proposing this amendment that would apply only to benefits that are payable to U.S. staff. Under this amendment, they would be given the opportunity to make an election up to the end of this year, and if they do so, their pension payments would be according to the current rules.

From next year onwards, for those who do not make that election, U.S. staff would still be able to make the election to commute or defer the start of their pension, but then they would have to comply with certain rules that are established in this tax law. One is that the election has to take place 12 months before the date that the pension starts, and the other is that any election would automatically defer the start of the pension that is paid from this supplemental plan. If they make an election that does not comply with these two rules, then they would be subject to a 20 percent penalty tax on the benefit that is paid out of this supplemental pension plan.

We received an opinion from the actuary which has determined that these changes do not increase the costs to the plan, and this opinion is attached. We also got outside legal opinion to introduce these changes.

These changes have to be approved by the end of this year, so the issue has gone simultaneously to the Pension Committee and to the Administration Committee, which has already reviewed and discussed the paper. After this discussion, if this is approved, we are going to submit to the Executive Board on a lapse-of-time basis. Before opening the floor for discussion, I would ask Mr. Rodlauer, who is the Chairman of the Administration Committee, which has already approved these changes, to give us an overview of the discussion.

The Acting Director of the Human Resources Department (Mr. Rodlauer) made the following statement:

The Administration Committee considered, as Mr. Portugal said, the plan changes and has endorsed them. They did note that these are very complex and difficult questions and issues, so they did grapple, for some time in the meeting, to understand them, as did we all. They recognize and appreciate that the plan changes go beyond what we were required to do. The World Bank is proposing, for its “gross” pension plan that is similar to the Fund SRP, to establish a default setting that everybody receives the pension as an annuity, which complies with the new U.S. law. We have been trying to give more flexibility to our staff, in order to be able to preserve as much as possible the elections that they currently can make under the SRBP, even though in some form those elections will be restricted.

In summary, as Mr. Portugal has indicated, this paper does three things. It establishes a default procedure for benefit payments under the SRBP. Each of the various groups of U.S. citizens affected, if they do nothing, will have a certain default way of receiving their benefits from the SRBP, they will comply with the U.S. law, and they will not draw a penalty tax.

Second, on the issue of elections, we provide this additional flexibility over and above what the IDB and the World Bank are doing. We are providing the same flexibility that currently exists under the pension plan for all those staff members that are affected who are ready to make such an election before the end of this year. So there is no change in the kind of elections that people can make, if someone is ready to make this election before the end of this year, because, legally, we can present that election as part of the changed plan, and therefore, it is not subject to any penalty.

And third, if somebody is not ready to make that election, then that is fine. He or she will still have a second opportunity of electing later on, after the U.S. tax changes become effective on January 1, 2009. Those later elections, however, come with some restrictions — for example, if one makes an election of a deferred payment, one has to defer for at least five years, so it is more complex, but there is still flexibility.

That is the gist of the paper. I do recognize that these are very complex and very difficult changes. We are somewhat late in bringing this to the Board and to our staff members. I will not hide the fact that our staff could have done this earlier, had we not been so overloaded with the downsizing and with all the pension changes that were made over the winter and earlier this year. We have had a sizeable team of experts working on this, and the interpretation of the implications of the law have also been in flux until very recently. This is where we are right now, and we hope that in doing this, we do provide maximum possible service to our staff who are potentially affected by this change in U.S. law.

Mr. Imamura expressed his general support for the proposed amendment, but asked the staff to clarify whether steps were also being taken to ensure SRBP compliance with the country tax laws of non-U.S. participants.

Mr. Ge expressed his support for the proposed amendment, and asked the staff to clarify whether the changes applied just to U.S. nationals or also to U.S. residents.

Mr. Ábel expressed his support for the proposed changes.

The staff representative on the Pension Committee (Ms. Alonso-Gamo) made the following statement:

Thank you for putting this proposal to the committee. I support the changes, and I would like to acknowledge the very hard work of the people who prepared this complex paper, which must have been a phenomenal amount of work. I have one question and one comment.

My question is, does this affect Fund staff who are not U.S. nationals, but who, after retirement, become permanent U.S. residents?

My comment is that I deplore the fact that this very complex financial decision has to be made by the staff in a period of less than three weeks. Even if it is true that it has been very difficult to prepare the papers, at a minimum it would have been helpful if the staff knew that this was coming. Even if the options were not clear, it would have been helpful to know that some decision was going to be made, because some people—who may be on mission, for example—may have to consult accountants or financial experts, and some advanced notice would have been useful.

I think that we can draw a lesson for proposed changes that may be brought to the Pension Committee in the future. First, however, it is useful to alert not only the staff but also members of the committee that proposals will be made. The end result would be much better, and the staff would be better informed.

Mr. Ge agreed that more advanced notice of such proposals would be helpful.

The staff representative on the Pension Committee (Mr. Ghosh) made the following statement:

Let me join others in thanking the staff for their hard work in preparing this paper. It is a very complex issue, and when we make fiscal policy recommendations, perhaps we do not fully realize that

somewhere down the road, somebody has to figure out what all this means.

I would like to ask one question, which is similar to the question posed by Ms. Alonso-Gamo. If I understand correctly, this only applies to the portion of the pension that is coming from the supplemental plan. If a staff member acquires U.S. citizenship, let us say the day before retirement, does this then apply to everything that has accrued in what would have been the supplemental plan, or only the accrual since the staff member became a U.S. citizen?

Let me also support Ms. Alonso-Gamo's request, seconded by Mr. Ge, for the committee and the staff to be kept informed as soon as practicable in these situations.

I wonder whether HRD can set up a system whereby U.S. staff are alerted five years before their expected, or normal, retirement age that if they want to make this kind of election, it will lock things up for five years. It would also be helpful if we could have a systemic process at the one year mark.

The Acting Director of the Human Resources Department (Mr. Rodlauer) made the following statement:

To clarify, only the benefits that U.S. citizens accrued as U.S. citizens are affected. If a staff member participant retires and then becomes a U.S. citizen, there is no effect. If a staff member participant becomes a U.S. citizen two days before retiring, only the accrual for those two days is affected.

A question was raised why we need to act in a special manner for U.S. citizens, and whether we should also act in a similar fashion for nationals of other countries who might be affected by similar changes. However, I think that the U.S. is different, in the sense that the U.S. is the only country that taxes Fund compensation.

This is really a matter of taxation of compensation, meaning the accrual of benefits under the SRBP. No other country taxes the amounts accrued under our pension plans, or compensation more generally. Since that is the case here, we felt we had an obligation to act, similar to the tax allowance that we give to U.S. citizens.

The Chairman (Mr. Portugal) agreed that it was important to give participants advance notice of changes to the SRBP, and noted that the process of contacting affected participants had already begun.

Mr. Gasiorowski sought confirmation that robust legal opinion had been obtained on the implications of the tax law changes and the adequacy of the proposed changes to the SRBP.

Mr. El-Khoury asked for confirmation that the proposed amendment to the SRBP applied to participants who would start receiving their pensions after January 1, 2009.

The Acting Director of the Human Resources Department (Mr. Rodlauer) confirmed that the proposed amendment to the SRBP applied to participants who would start receiving their pensions after January 1, 2009.

Mr. Majoro requested confirmation that the small IT costs associated with software updating could be met from the existing budget.

Mr. Yakusha asked the staff to comment on the costs to the Fund associated with the proposed changes to the SRBP.

The Acting Director of the Human Resources Department (Mr. Rodlauer) confirmed that the IT costs would be small and absorbed within the regular budget, and clarified that legal opinion had established that the proposed changes to the SRBP would guard against U.S. citizen participants being obliged to pay additional tax.

The staff representative from the Legal Department (Mr. Patterson) remarked that the proposed changes to the SRBP had been developed in consultation with an expert outside tax counsel who had consulted with the U.S. Treasury. He also expressed confidence that, should a subsequent administration have a different interpretation of the tax laws, the U.S. Treasury would work closely with the tax counsel in order to ensure any necessary adjustments in the SRBP.

Mr. Heath referred to paragraph 11 on page 9 of the staff papers, and wondered whether, if the proposal was to give participants the option of receiving a lump sum that would not embody the future cost of living increases that were included in non-lump sum payouts, the proposed changes to the SRBP would save the plan money.

The Chairman (Mr. Portugal) noted that the option of receiving a lump sum already existed, but asked the staff representative from the Human Resources Department to provide a more detailed answer.

Mr. Heath wondered whether the changes in U.S. tax law would increase the number of participants electing for a lump sum payout, and thereby affect the financial position of the SRBP.

The Chairman (Mr. Portugal) replied that it was difficult to say whether participants would prefer the lump sum in light of changes to U.S. tax law.

The staff representative from the Human Resources Department (Ms. Marzouk) confirmed that the cost to the plan of a participant electing the lump sum payout was lower than the cost associated with a participant deferring annuity because of cost of living increases.

The Chairman (Mr. Portugal) announced that the Pension Committee had agreed to the changes to the SRBP that were proposed for adoption by the Executive Board, and noted that the decision would be approved by the Executive Board on a lapse of time basis.

APPROVAL: April 1, 2009