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Notice 2014-5

February 28, 2014

Submitted electronically via email to notice.comments@irs.counsel.treas.gov

CC:PA:LPD:PR (Notice 2014-05)
Room 5203
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Dear Sir or Madam,

Subject: Notice 2014-05

Black Hills Corporation appreciates the Internal Revenue Service's (IRS) recognition that employers are inadvertently being penalized in the nondiscrimination testing rules for trying to keep pension benefits available rather than freezing their defined benefit plans in order to preserve benefits for a group of participants currently in the defined benefit plan. Black Hills Corporation welcomes the opportunity to submit for your consideration our comments relating to the IRS's request for Comments on the Ability of a DB/DC Plan to Satisfy Nondiscrimination Testing Requirements on a Benefits Basis and Other Possible Related Modifications to Other Nondiscrimination Testing Requirements.

About Black Hills Corporation

We are a diversified energy company with a tradition of exemplary service and a vision to be the energy partner of choice. Our company is based in Rapid City, South Dakota, and we have corporate offices in Denver, Colorado and Papillion, Nebraska. We serve 765,000 natural gas and electric utility customers in Colorado, Iowa, Kansas, Montana, Nebraska, South Dakota and Wyoming. We also have a several non-regulated business segments that generate wholesale electricity, produce natural gas and crude oil, and mine coal. Our nearly 2,000 employees partner to produce results that improve life with energy.

Our Defined Benefit Plans and Nondiscrimination Testing Situation

We sponsor two defined benefit pension plans with nonunion participants within our controlled group—the Pension Plan of Black Hills Corporation ("BHC Plan") and the Black Hills Utility Holdings, Inc. Pension Plan ("BHUH Plan"). Both plans were closed to new entrants effective December 31, 2009 for nonunion employees. (Nonunion employees make up approximately 70% of our total employee population.) Subsequently, these plans were also closed to all union new employees effective

December 31, 2011. We wish to be able to continue to pass nondiscrimination requirements for those employees who continue to earn pension benefits in these defined benefit plans.

Recent pension cost increases and volatility, due to the current funding regulations, negatively impacted our ability to provide consistent and predictable electric and gas rates to our customers. We determined that consistent and predictable retirement costs were needed to help us better manage our business on behalf of our employees and customers.

After significant review and analysis, we determined that our best approach for achieving consistent and predictable retirement benefit costs was to replace future defined benefits with nonelective contributions in a defined contribution plan. We determined that nonelective contributions, combined with matching contributions, would provide our employees with retirement benefits that are competitive within our industry and provide significant retirement income in combination with employee savings, Social Security, and other retirement income sources.

During our analysis, we realized that if we immediately froze the plan, employees currently accruing defined benefit plan benefits would retire with much smaller ultimate retirement benefits (adding together their frozen accrued defined benefit plan benefit and future defined contribution allocations) than they would have if they had spent their entire careers in either the defined benefit plan or defined contribution plan. The ultimate retirement benefit would consist of the lowest defined benefit accruals (which generally happen early in one's career) and the lowest defined contribution equivalent accruals (which generally come later in one's career). Black Hills Corporation determined that the most effective and efficient way to mitigate these discrepancies was to allow those employees most at risk in the defined benefit plans the ability to continue accruing benefits in the defined benefit plans until they terminate or retire from Black Hills Corporation, and to provide the new benefit structure for employees less at risk who were hired after closing the defined benefit plans to new entrants.

Black Hills Corporation Testing Concerns

1. We are experiencing deteriorating coverage testing results for the defined benefit plans due to the decreasing size of the plan without new entrants. Assuming a steady state, we have determined that the defined benefit plans will continue to pass 410(b) coverage testing only for the next few years. Once the plans are no longer able to pass aggregating only with the other defined benefit plan (we will hereafter refer to the aggregated defined benefit plans as "the defined benefit plan"), we are concerned since the current regulations provide no other remediation steps for the following reasons.
 - (a) Black Hills Corporation has no other defined benefit plans with which to aggregate to pass a 410(b) coverage test;
 - (b) The Black Hills Corporation defined benefit plan will be unable to pass coverage by aggregating with the defined contribution nonelective allocations being

provided to those employees who are not currently accruing pension benefits. This is because the aggregated general test, on a contributions basis, fails due to the inherent disparities when converting defined benefit plan accruals into equivalent allocations to a defined contribution plan; and

- (c) A benefits basis general test is unavailable if the defined benefit and defined contribution plans are aggregated. The aggregated plan will not be able to pass any of the DB/DC cross-testing gateways by that time.

Consequently, we are concerned as to how our defined benefit plan can pass coverage testing in the future.

2. The only corrections available to a plan that fails a nondiscriminatory classification test is to add NHCEs (which is inconsistent with our desire to shift to the predictability of providing defined contribution benefits) or remove HCEs. However, ceasing benefit accruals to some HCEs requires notice before the beginning of a plan year. We will not know how many HCEs we need to remove, or which ones will cause the testing problems, until months after the plan year has ended (up to a year and a half after sending notices). Thus, we could still fail if we underestimate the number of HCEs to remove from the plan. Also, a large proportion of the HCEs who could cause the failure are not allowed to receive lost benefits in a nonqualified supplemental arrangement. Separate treatment of groups, such as HCEs eligible for nonqualified benefits, HCEs not eligible for nonqualified benefits, and all others, would result in a more complex and inequitable benefit program. We believe this is not an acceptable approach. Given the lack of reasonable options for correcting the issue, we fear our only option to remain compliant will be to completely freeze all defined benefit plan accruals, leaving many employees with lower retirement benefits as they are caught in the DB to DC transition.
3. Due to the 401(a)(26) rules for defined benefit plans, Black Hills Corporation will ultimately have to freeze the defined benefit plan before all employees in the plan terminate or retire. This will occur even if we can pass DB/DC gateways in order for the DB and DC benefits to be aggregated for testing and the aggregated DB/DC plans to pass both coverage and benefits testing. The rules seem to anticipate that employers have the ability to merge the small number of remaining participants into a replacement or other ongoing defined benefit plan. However, due to our transition to a DC plan for new entrants, the current regulations ultimately will not work for Black Hills Corporation.

Applying 2014–5 Proposed Remedies to Black Hills Corporation

Fortunately, Black Hills Corporation is currently not in need of the temporary relief offered for the next two years. However, because our defined benefit plan would qualify for this temporary relief, we do appreciate the relief that would be offered if our controlled group were to change unexpectedly in the next two years. We wish to point out that the proposed longer-term relief, if helpful, will only address our 410(b) coverage testing issue. The relief does not address our ultimate concerns regarding 401(a)(26).

We have reviewed our retirement plans as they relate to the longer-term relief proposals. For Black Hills Corporation, aggregating our DB and DC plans would solve our coverage

testing issue, so we encourage relief that makes such an aggregation possible. Applying the proposed relief in order to aggregate our closed defined benefit plan and the nonelective employer contributions in the defined contribution plan (and adding the match, where proposed), we have determined the following:

- **Current Application of Minimum Aggregate Allocation Gateway**—The highest HCE equivalent allocation rate comes from the DB plan and currently results in a required minimum allocation of 6% for NHCEs, but is close enough that it easily could have been 7%. The high HCE rate is a function of that DB participant's age, service, and pay increases, rather than any discrimination in the benefit formula provided. In general, each HCE or NHCE will age through increasing DB equivalent allocation rates and has the potential of such a rate at some point during a career. In fact, some NHCEs do have higher equivalent allocation rates than the highest HCE. Since we selected continued pension for an older group which has been aging since the defined plan closed to new entrants, the average DB NHCE equivalent allocations are not an issue for our plans. However, the DC NHCEs fall significantly short of the 6% or 7% needed.
 - Meeting the 6% or 7% requirement would require providing DC contributions that are double the average in our industry, and would provide no consistent guarantee that even a 7% allocation would meet testing requirements in future years. Future larger increases would be unaffordable and untenable within our industry and also would result in inconsistent and unpredictable benefit costs from year to year.
 - These failing gateway results for Black Hills Corporation reflect a plan that is still passing coverage testing and providing comparable and nondiscriminatory benefits to all participants in the plan. They essentially represent the nature of a DB plan rather than any discriminatory benefits.
- **Allowing Averaging of DC for Minimum Aggregation Allocation Gateway**—Our average DC allocation of 3% fails, and even if the maximum defined contribution allocation that Black Hills Corporation generally provides to those not in the defined benefit plan could be used, the plan would still fail this gateway.
- **Allowing an Average Match added to DC for Minimum Aggregation Allocation Gateway**—The highest HCE equivalent allocation rate comes from a DB plan participant with a match in the DC plan and increases the required minimum allocation to 7.5% for NHCEs. While the DB NHCEs continue to pass, including the match for the DC NHCEs remains short of the 7.5% needed.
- **Allowing a Safety Valve for Determining the Highest HCE for the Minimum Aggregate Allocation Gateway**—Although it may prove unlikely that allowing this safety valve would drop our threshold below 6%, we chose to assume a best case scenario that a 5% threshold would be available to use consistently in analyzing this alternative. Again, the DB group portion continues to pass. However, the lowest and even average DC rates still fail at both 5% and 6% thresholds. Further, we do not believe this approach is practical due to (1) the requirement for annual IRS approval for a safety valve, (2) the uncertainty and risk of not being approved in any given year, and (3) not knowing the result before the corrections deadline.
- **Allowing no Gateway if cross-testing performed at lower interest rate than 7.5%**—Since Black Hills Corporation's defined benefit plan has been passing on its

own, we are unable to assess at this time the impact of aggregating and cross-testing using a lower interest rate.

As a result of the factors outlined above, the proposed relief will not (1) provide relief for our plans or (2) allow us to aggregate our DB and DC plans in order to demonstrate that we do provide nondiscriminatory benefits to our nearly 2,000 employees.

Relief Needed for Black Hills Corporation

For coverage: We would hope that a fact set would be sufficient to allow DB/DC aggregation where:

1. The DB plan is closed to a nondiscriminatory group with nondiscriminatory benefits;
2. The DB plan provides no additional benefits only available to HCEs or to small groups including, without limitation, the highest paid HCEs;
3. Transition to the new program was simply intended to protect the group of employees most likely to be negatively impacted by the change in retirement income resulting from converting from DB to DC accruals during their careers;
4. The group receiving DC benefits will continue to pass all coverage and benefits requirements as a standalone plan; and
5. The controlled group passes an average benefit percentage test.

For 401(a)(26): Currently there is an exception for plans covering only NHCEs. Perhaps that could be expanded to be an exception for those plans (1) covering only employees who would not be legally entitled to participate in a nonqualified and (2) which cannot reasonably be merged with another DB plan in order to pass 401(a)(26).

Closing

If you have any questions or comments, please contact the undersigned at the telephone number or email address provided below.

Sincerely,



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