

Client Action Bulletin

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IRS Notice 2020-61: IRS Guidance on Special Funding and Benefit Limitation Rules for Single-Employer Defined Benefit Plans under the CARES Act

SUMMARY

The Internal Revenue Service (IRS) published Notice 2020-61, providing technical guidance on the special rules relating to funding of single-employer defined benefit (DB) pension plans and related benefit restrictions under the Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136). The Notice includes 18 detailed questions and answers (Q&A's) anticipating technical issues for permissible delayed (aka "extended due date") DB plan contributions and other changes for these pension plans under the CARES Act.

Notice 2020-61 does not delay any mandatory filing dates for Form 5500. Plan sponsors anticipating that the IRS would permit a filing date beyond October 15, 2020, for calendar year plan years should schedule accordingly. The IRS could advise differently between now and October 15, but that is unlikely. Plan sponsors should include preparation for an amended Form 5500 filing if extended due date contributions are part of DB plan contribution policy.

The CARES Act permits DB plan contributions that are otherwise due during calendar year 2020 to be made no later than January 1, 2021. These delayed contributions can be designated as satisfying the minimum required contribution rules under IRC Section 430 for prior plan years. Notice 2020-61 includes critical guidance regarding where, absent the CARES Act, these contributions would be deemed not made or made late, and could result in penalties to the plan sponsor, including excise taxes (IRC Section 4971), funding deficiencies, and notices to plan participants and federal agencies. Examples of complex interest adjustments to the contributions recognizing their delayed deposit dates are included in the Q&As.

Notice 2020-61 also provides technical guidance regarding CARES Act law about voluntary employer use of the prior plan year's Adjusted Funding Target Attainment Percentage (AFTAP) in order to avoid being deemed an "at-risk" plan under IRC Section 436. An at-risk plan, i.e., a plan with an AFTAP less than 80%, may be restricted from paying certain optional forms of pension benefits to participants.

BACKGROUND

The CARES Act became law with the purpose of providing emergency assistance and healthcare response for individuals, families, and businesses affected by the 2020 coronavirus pandemic.

Section 3608 of the CARES Act includes two provisions for single-employer DB plans.

Section 3608(a) provides relief from the minimum funding requirements for contribution dates originally due during the 2020 calendar year by delaying these contributions to no later than January 1, 2021. (Note that January 1, 2021, is a federal bank holiday.)

Section 3608(b) permits the plan sponsor to elect to treat the plan's AFTAP for the last plan year ending before January 1, 2020, as the AFTAP for plan years that include calendar year 2020, and with respect to IRC Section 436 only. The AFTAP is the ratio of the plan's assets over the actuarial liabilities calculated under IRC Section 436 rules.

Delayed contributions require interest adjustments using the "effective interest rate"

All contributions to a single-employer defined benefit pension plan that were due in calendar year 2020, irrespective of the starting date of the plan year, can be delayed to no later than January 1, 2021. To determine the amounts of these 2020 periodic installments, the contribution amount is adjusted from the actual payment date back to the original due date at the "effective interest rate" for the plan year.

The effective interest rate (IRC Section 430) is the single interest rate that would produce the same actuarial liability (the “funding target”) as the funding target produced using the IRS corporate bond yield curve segment rates. This rate is used for the interest adjustment on contributions to both the due date and to the plan’s valuation date. As an example, a contribution made on December 31, 2020, must be interest-adjusted first to the original due date, and then to the valuation date. For a plan year starting on January 1, 2019, the interest adjustment for this December 31, 2020, delayed contribution is for 24 months and would use the effective interest rate for the plan year that includes the actual payment date to discount from the payment date to the original due date for the delayed contribution.

Formal election of Section 3608(b) “look-back” AFTAP

The CARES Act permits a one-time written election by the plan sponsor to use the AFTAP from the last plan year ending before January 1, 2020, as the AFTAP for plan years that include calendar year 2020 in order to avoid applying benefit restrictions, as an “at-risk” plan, required by IRC Section 436. Those that elect to do so will need to include an additional attachment to the Form 5500 Schedule SB for any impacted plan year.

A DB plan is classified as an at-risk plan if the AFTAP is less than 80%. Applying benefit restrictions means that the choice to pay certain optional forms of pension benefits to participants can be prohibited or greatly changed. An optional form of payment that would be restricted for an at-risk DB plan is a single sum distribution, or lump sum. This could result in the participant receiving 50% of the lump sum value, while the remainder of the pension is paid as an annuity.

AFTAP certification on Schedule SB cannot anticipate future contributions

Notice 2020-61 includes guidance for the associated certification of the plan’s AFTAP by the plan’s enrolled actuary on Schedule SB. Notice 2020-61 emphasizes that an enrolled actuary is prohibited from certifying the AFTAP on Schedule SB without evidence of a contribution to the pension trust. This has not changed from certification requirements under the law prior to the CARES Act.

Anticipated amended Form 5500 filings

With proper filing extensions granted by the IRS, these DB plans can file Form 5500 no later than 9½ months after the end of the plan year. Form 5500, Schedule SB, generally must be signed by the plan’s enrolled actuary based on evidence of contributions made no later than 8½ months after the end of the plan year. Form 5500 filings are associated with meeting accounting promulgations under Accounting Standards Codification (ASC) Section 960, IRS tax deductibility laws, and AFTAP certification rules.

Plan sponsors with a plan year that starts on January 1, 2019, will need to decide whether or not to file the plan year 2019 Form 5500 with the enrolled actuary’s certification of the plan year 2019 AFTAP with contributions to date only, and then later amend the Schedule SB when the permissible delayed contributions are made. Note that other Form 5500 schedules will also need to be amended, such as Schedule H. It is anticipated that the plan sponsor will file an amended Form 5500 as soon as practicable after the final extended date contribution is made.

Other: Fiscal year-end disclosures under ASC 715-30, IRC Section 404 tax deduction, and PBGC Variable Rate premium final filing

The CARES Act does not affect any of the requirements and associated rules for compliance with ASC 715-30, disclosure of the pension plan financial statements (“footnotes”) that are part of the report to shareholders and the U.S. Securities and Exchange Commission (SEC).

The CARES Act does not affect the tax deduction to which a taxpayer may be entitled for contributions under IRC Section 404. If the CARES Act extended date contribution is made subsequent to the end of the taxpayer’s tax year, it appears that the tax deduction qualifies for the tax year in which it is made. Because Milliman does not practice tax law, taxpayers should seek guidance from their tax counsel.

The Pension Benefit Guaranty Corporation (PBGC) issued a memo on its website on July 20, 2020 to employers covered by the PBGC single-employer plan insurance program, emphasizing that the final date on which contributions can be made and be recognized for the calculation for the final premium payment year 2020 PBGC unfunded vested benefit will not be extended to the same date that the CARES Act permits a delay. Further, the PBGC does not permit the final premium payment filing to be amended.

ACTION

Plan sponsors should review with their enrolled actuaries the options available to comply with CARES Act extended due date contributions. As well, options should be discussed with third-party business partners assisting with Form 5500 filings about the likelihood of amended filings producing error messages because the software may not accept the extended CARES Act contribution due dates. In particular, expectations for amended Form 5500 filings or filings on the Schedule SB, the actions required, and their implications, absent the CARES Act relief, should be discussed, including whether contributions were late or missed and whether the plan has a funding deficiency.

Please contact your Milliman consultant to discuss critical steps to take now.



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