



# CLIENT ACTION Bulletin

Employee Benefits

## Single-Employer Pension Funding Relief Elections May Require Immediate Action

### SUMMARY

Single-employer pension plan sponsors taking advantage of the funding relief provisions contained in a 2010 law may have only a brief window to formally make an election for either the 2009 or 2010 plan year (or both plan years) and to notify the PBGC, under the IRS's recently issued *Notice 2011-3*. For calendar-year plans electing one of the two alternative amortization schedules permitted, the IRS's guidance will require a signed election by Jan. 31, 2011, and PBGC notification shortly thereafter.

This *Client Action Bulletin* focuses on the IRS's guidance on electing the relief, the calculation of the reduced contribution, and the notifications. The IRS's guidance on the accelerated installment amounts triggered by excess compensation and shareholder payments if plan sponsors opt for the funding relief is complex and beyond the scope of this CAB.

### DISCUSSION

#### Background

The "Preservation of Access to Care for Medicare Beneficiaries and Pension Relief Act of 2010" (PRA 2010), enacted in June 2010, permits single-employer (and multiple employer) defined benefit plan sponsors to elect to extend the plan's amortization period of the funding shortfall over either a nine-year period or a 15-year period, rather than the seven-year period required under the 2006 Pension Protection Act (PPA) (see **CAB 10-11R**). The law also imposed certain restrictions on plan sponsors electing the available relief, including a requirement that they increase their plan contributions to match "excessive employee or shareholder payments." This particular condition may moderate the number of large, publicly traded employers opting for the funding relief, but nonpublic companies and not-for-profit organizations that sponsor a pension plan may be less troubled by this limitation in seeking relief.

Notice 2011-3 contains 56 questions and answers about specific provisions of PRA 2010. The Notice includes guidance on the alternative amortization schedules that a plan sponsor may elect for up to two of the plan years beginning in 2008, 2009, 2010, and 2011, provided that the final due date for contributions for the plan year falls on or after June 25, 2010 (i.e., the relief generally is available for plan years beginning on or after Oct. 10, 2008, and before Jan. 1, 2012).

#### Calculation of Shortfall Amortization Installments

The Notice explains how the alternative amortization schedule is applied to a plan's shortfall amortization base for a plan election year. It also describes how the plan's actuary must calculate the annual installments under the alternative amortization schedules.

- *For the "2 plus 7-year amortization schedule,"* the Notice instructs plan sponsors to make a contribution for the first two years (of the nine years) of the "interest" only on the shortfall amortization base, using the "effective interest rate" for the plan year. Starting in the third year, the remaining seven annual payments revert to payments consisting of both interest and principal. The determination of the remaining payments uses the PPA valuation rates that were effective for the plan in the election year. The outstanding amount of the remaining payments is equal to the original shortfall minus the discounted value of the first two installments. This remaining shortfall is amortized over the payment years three through nine.
- *For the 15-year amortization schedule,* the amortization factor is calculated in the same manner as it would be under the PPA, changing the period of amortization to 15 years instead of seven years.

Plan sponsors should note that if the accelerated installment amounts for excessive employee or shareholder payments are triggered, these restrictions must continue to be analyzed for future plan years after the year for which the relief election is first made. If "2+7" is elected, the accelerated installment amounts must be analyzed for three plan years; if the 15-year schedule is elected, the analysis must continue for five plan years. In some cases, the election of funding relief may result in neutralizing the desired reduction in the cash contribution. And the ability to revoke the election requires formal approval by both the IRS and the PBGC.

### Other Key Areas Addressed

The Notice also provides guidance on:

- *Electing an alternative amortization schedule* – Plan sponsors must make an election by the latest of: the last day of the plan election year; 30 days after the valuation date for the plan election year; or Jan. 31, 2011. They must provide a written, signed notice of an election to the plan's actuary and to the plan administrator. The notice must include information about the plan (e.g., plan name, number, plan sponsor, employer identification number, mailing address), the alternative amortization schedule elected and the plan election year, and a statement that notification to the PBGC and plan participants/beneficiaries will be made.
- *Notice to plan participants/beneficiaries and to the PBGC* – Plan sponsors must notify participants in writing (and may be furnished in paper or, under reasonable conditions, in electronic form) by the later of 120 days after the end of the plan election year or May 2, 2011. The notices must include information about the plan, the election, and the plan administrator, as well as a general description of the effect of the election, including the fact that the election will delay pension funding. The IRS's Notice provides sample language for two notices, one for electing one-year relief and the other for electing relief for two years. *Notification to the PBGC is required in e-mail format by the later of 30 days after the date an election is made or Jan. 31, 2011.*
- *Reporting requirements* – Because the IRS did not release the Notice before most plan sponsors filed the annual reports (*Form 5500*, including Schedule SB) for the (2008 and) 2009 plan years, the agency is permitting – but not requiring – plan sponsors to file an amended *Form 5500* to reflect the funding relief election or to comply with the calculation methods described in the Notice. Alternatively, plan sponsors may reflect the election or explain the corrected calculation as an attachment to Schedule SB for a subsequent plan year (but no later than the 2010 plan year filing).
- *Transition rules* – An election for funding relief made by a plan sponsor before Jan. 1, 2011, remains valid, even if the election did not include all of the information required by the IRS's Notice. Thus, a plan sponsor may not revoke such an election without IRS approval and must provide the required notices to the PBGC and to participants/beneficiaries in a timely fashion. The IRS Notice provides transition rules that allow plan sponsors to make certain retroactive adjustments to the funding standard carryover balance and the prefunding balance, even if the normal deadline for doing so otherwise has passed. For these special elections, a plan sponsor must do so by the normal due date for such elections or, if later, March 31, 2011.

### ACTION

Single-employer defined benefit plan sponsors should immediately discuss with their actuaries whether electing funding relief is feasible and appropriate. Many considerations will go into the determination, including complex calculations under different scenarios. If a decision to do so is made, plan sponsors must act quickly to make the election and notify the PBGC and participants/beneficiaries. Plan sponsors that already elected funding relief should review the IRS's Notice and work with their actuaries and other advisers to determine whether to amend the *Form 5500* or to address any changes necessary when filing a subsequent annual report. They must, however, comply with the notification requirements stipulated in the IRS Notice in a timely fashion. In addition, even if funding relief is not elected for plan years through 2010, plan sponsors that might consider doing so for the 2011 plan year should consider the options and the requirements that are spelled out in the IRS's guidance. Sponsors electing relief for the 2011 plan year have until Dec. 31, 2011, to make the election.

For additional information about the IRS's Notice 2011-3 or for assistance with funding relief elections, please contact your Milliman consultant.

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