

Additional Temporary Nondiscrimination Relief for Closed Defined Benefit Plans through 2020

Notice 2019-60

I. PURPOSE

This notice provides additional temporary nondiscrimination relief for closed defined benefit plans (that is, defined benefit plans that provide ongoing accruals but that have been amended to limit those accruals to some or all of the employees who participated in the plan on a specified date) that generally meet the eligibility conditions for the relief provided in Notice 2014-5, 2014-2 I.R.B. 276, as extended. Specifically, this notice provides that, if a plan satisfies the conditions specified in this notice, the plan is deemed to have satisfied certain of the nondiscrimination requirements relating to benefits, rights, and features.

II. BACKGROUND

A. Law and Regulations

Section 410(b) provides in general that a plan is a qualified plan only if the classification of employees who benefit under the plan does not discriminate in favor of highly compensated employees (HCEs). Section 410(b)(6)(B) provides that two or more plans may be aggregated for purposes of satisfying § 410(b), but only if those plans are also aggregated for purposes of § 401(a)(4).

Under § 1.410(b)-2(b), a plan generally satisfies § 410(b) with respect to employees only if the plan satisfies either the ratio percentage test of § 1.410(b)-2(b)(2) or the average benefit test of § 1.410(b)-2(b)(3) (which requires satisfaction of the nondiscriminatory classification test of § 1.410(b)-4 and the average benefit percentage test of § 1.410(b)-5). The ratio percentage test and the nondiscriminatory classification test are applied using a plan's ratio percentage, which is defined in § 1.410(b)-9 for a plan year as the percentage determined by dividing the percentage of the nonhighly compensated employees (NHCEs) who benefit under the plan by the percentage of HCEs who benefit under the plan.

Section 401(a)(4) provides in general that a plan is a qualified plan only if the contributions or the benefits provided under the plan do not discriminate in favor of HCEs. Compliance with § 401(a)(4) generally may be demonstrated on the basis of either contributions or benefits (including equivalent benefits). Section 1.401(a)(4)-9(b) contains special rules that apply for purposes of determining whether an aggregated plan that includes one or more defined benefit plans and one or more defined contribution plans (referred to as a DB/DC plan) satisfies the requirements of § 401(a)(4). A DB/DC plan may demonstrate compliance with § 401(a)(4) on the basis of equivalent benefits only if the DB/DC plan satisfies one of three alternative conditions set forth in § 1.401(a)(4)-9(b)(2)(v).

Section 1.401(a)(4)-4 provides rules regarding nondiscriminatory availability of benefits, rights, and features. Under § 1.401(a)(4)-4(a), benefits, rights, and features are provided to employees in a nondiscriminatory manner only if each benefit, right, or feature satisfies the current availability requirement of § 1.401(a)(4)-4(b) and the effective availability requirement of § 1.401(a)(4)-4(c). In general, a benefit, right, or feature satisfies the current availability requirement if the group of employees to whom the benefit, right, or feature is currently available during the plan year satisfies § 410(b) (without regard to the average benefit percentage test of § 1.410(b)-5). Under the effective availability requirement, based on all of the relevant facts and circumstances, the group of employees to whom a benefit, right, or feature is effectively available must not substantially favor HCEs.

The nondiscrimination regulations under § 401(a)(4) provide that the Commissioner may, in revenue rulings, notices, and other guidance published in the Internal Revenue Bulletin, provide any additional guidance that may be necessary or appropriate in applying the nondiscrimination requirements of § 401(a)(4), including additional safe harbors and alternative methods and procedures for satisfying those requirements. See § 1.401(a)(4)-1(d).

B. Notice 2014-5 Temporary Nondiscrimination Relief for Closed Defined Benefit Plans

Notice 2014-5 addresses the increasingly common situation of a defined benefit plan that has been closed to new entrants. The plan sponsor of a closed defined benefit plan typically provides a defined contribution plan for its new hires. Under these arrangements, in the early years after the defined benefit plan has been closed to new entrants, the plan may be able to satisfy the coverage requirement of § 410(b) without being aggregated with the defined contribution plan. However, the § 410(b) minimum coverage test typically becomes more difficult for the closed defined benefit plan to satisfy over time, as the proportion of plan participants who are HCEs increases. This might occur for several reasons, including the tendency of NHCEs to have higher rates of turnover than HCEs, as well as the potential for some of the NHCEs in the closed plan to become HCEs as they continue employment and their compensation increases.

If the closed defined benefit plan cannot satisfy the coverage requirement of § 410(b) on its own, it must be aggregated with another plan in order to satisfy that coverage requirement. If the defined benefit plan is aggregated with a defined contribution plan that covers the employer's new hires to satisfy the coverage requirement, then it is also required to be aggregated with the defined contribution plan for purposes of satisfying the nondiscrimination requirements of § 401(a)(4). In the typical case, the aggregated plans will fail the requirements of § 401(a)(4) unless they are permitted to demonstrate compliance with the nondiscrimination requirements on the basis of equivalent benefits. The aggregated plans usually may demonstrate nondiscrimination on the basis of equivalent benefits in the initial years of aggregation without the need for benefit changes. However, the same demographic forces that drive the increase in the proportion of HCEs in the closed plan over time might lead to the aggregated plans being permitted to demonstrate nondiscrimination on the basis of equivalent benefits

only if the plans satisfy the minimum aggregate allocation gateway (which requires a minimum level of benefits to be provided to NHCEs).

Notice 2014-5 provides temporary nondiscrimination relief for certain closed defined benefit pension plans. Specifically, for plan years beginning before 2016, Section III.B of Notice 2014-5 permits a DB/DC plan that includes a closed defined benefit plan (that was closed before December 13, 2013) and that satisfies certain conditions set forth in the notice to demonstrate satisfaction of the nondiscrimination in amount requirement of § 1.401(a)(4)-1(b)(2) on the basis of equivalent benefits even if the DB/DC plan does not meet any of the existing eligibility conditions for testing on that basis under § 1.401(a)(4)-9(b)(2)(v). That is, such a DB/DC plan may satisfy the nondiscrimination requirements on the basis of equivalent benefits without being required to satisfy the minimum aggregate allocation gateway.

A series of notices extend the temporary nondiscrimination relief provided in Notice 2014-5 by applying that relief to plan years beginning before 2021 if the conditions of Notice 2014-5 are satisfied. See Notice 2015-28, 2015-14 I.R.B. 848, Notice 2016-57, 2016-40 I.R.B. 432, Notice 2017-45, 2017-38 I.R.B. 232, Notice 2018-69, 2018-37 I.R.B. 426, and Notice 2019-49, 2019-37 I.R.B. 699.

C. Proposed regulations to provide nondiscrimination relief for closed defined benefit pension plans

Proposed regulations relating to nondiscrimination requirements for closed plans were published in the Federal Register on January 29, 2016 (81 FR 4976). The proposed regulations set forth relief for closed plans under §§ 1.401(a)(4)-4, 1.401(a)(4)-8, and 1.401(a)(4)-9 (subject to satisfaction of certain conditions set forth in the regulations) and contain other proposed nondiscrimination rules. The regulations generally are proposed to apply to plan years beginning on or after the date of publication of the final regulations in the Federal Register. The proposed regulations provide that taxpayers are permitted to apply certain provisions of the proposed regulations (including all of the provisions that apply specifically to closed plans) for certain plan years beginning before the proposed applicability date. Notice 2019-49 states that it is expected that the final regulations will provide that the reliance granted in the preamble to the proposed regulations may be applied for plan years beginning before 2021. Thus, for plan years beginning before January 1, 2021, taxpayers may apply the relief in Notice 2014-5 (as extended), as well as the rules relating to closed plans in the proposed regulations.

The provisions under the proposed amendments to § 1.401(a)(4)-4 with respect to defined benefit plans provide relief from nondiscrimination testing with respect to a benefit, right, or feature that is made available only to a grandfathered group of employees with respect to a closed plan. Specifically, if the eligibility conditions in the proposed regulations are satisfied, the special testing rule treats a benefit, right, or feature that is provided only to a grandfathered group of employees as satisfying the current and effective availability tests of § 1.401(a)(4)-4(b) and (c). Because the special testing rule does not apply until plan years that begin on or after the fifth anniversary of the closure date (as defined in the proposed regulations), the benefit, right or feature

must be currently available to a group of employees that satisfies the minimum coverage requirements of § 410(b) (without regard to the average benefit percentage test of § 1.410(b)-5) for plan years that begin within the 5 years immediately following the closure date.

The relief under the proposed amendments to § 1.401(a)(4)-4 is available only if the amendment restricting the availability of the benefit, right, or feature also resulted in a significant change in the type of the defined benefit plan's formula. For example, a plan amendment that changes the plan formula from an annual percentage of final average annual compensation to a cash balance formula would be a significant change in the type of benefit formula, so that the special testing rule would apply to facilitate preservation of any subsidized early retirement factors for the employees who continue to benefit under the prior benefit formula. In addition, this proposed relief is available only if no plan amendment that affects the availability of the benefit, right, or feature (other than the closure amendment, as defined in the proposed regulations) is adopted or made effective during the period that began 5 years before the closure date (with exceptions for certain types of amendments, such as an amendment that expands or restricts the eligibility for the benefit, right, or feature, if, as of the applicable amendment date, the post-amendment ratio percentage of the group of employees eligible for the benefit, right, or feature is not less than the pre-amendment ratio percentage of the group of employees eligible for the benefit, right, or feature).

Many comments have been submitted on the proposed regulations, including oral comments at a public hearing held on May 19, 2016. The Department of the Treasury and the Internal Revenue Service (IRS) expect that the final regulations will include a number of significant changes in response to those comments.

III. ADDITIONAL RELIEF FOR CLOSED DEFINED BENEFIT PLANS WITH RESPECT TO BENEFITS, RIGHTS, OR FEATURES

A. Need for relief relating to benefits, rights, or features

At the time a defined benefit plan is closed to new entrants, the plan may provide for benefits, rights, or features that are not available to participants in other plans of the employer. For such a plan, the proposed regulations provide relief from the requirements of § 1.401(a)(4)-4 relating to benefits, rights, or features only if the amendment restricting the availability of the benefit, right, or feature also resulted in a significant change in the type of the defined benefit plan's formula. Thus, neither Notice 2014-5 nor the proposed regulations provide relief under § 1.401(a)(4)-4 for a defined benefit plan that is closed to new entrants but has not undergone a change in benefit formula with respect to existing participants. In addition, the relief in the proposed regulations relating to benefits, rights, or features is conditioned on compliance with requirements relating to plan amendments that may have occurred long before the proposed regulations were issued.

Commenters on the proposed regulations observed the need for relief relating to benefits, rights, and features for a plan if the plan is closed to new entrants (but has not undergone a significant change in the type of the plan's benefit formula). Commenters

also observed the need for relief relating to plan amendments that occurred before the proposed regulations were issued.

B. Temporary relief for certain closed defined benefit plans with respect to benefits, rights, or features

Pursuant to the authority under § 1.401(a)(4)-1(d) to provide alternative methods for satisfying the nondiscrimination requirements, this section III.B provides a closed defined benefit plan that generally meets the eligibility conditions for the temporary relief under Notice 2014-5 (as extended) with additional temporary relief from the requirements of § 1.401(a)(4)-4 relating to benefits, rights, or features.

1. Plans to which temporary relief applies

The temporary relief under this section III.B applies to a plan if it is a defined benefit plan providing ongoing accruals that was amended, by an amendment adopted before December 13, 2013, to provide that only employees who participated in the defined benefit plan on a specified date continue to accrue benefits under the plan. Thus, this relief applies to defined benefit plans for which the relief under Notice 2014-5 (as extended) is available (except that eligibility for this relief does not depend on the method used to satisfy the nondiscrimination requirements for the plan year beginning in 2013).

2. Period of temporary relief

The temporary relief under this section III.B applies for plan years ending after November 13, 2019, and beginning before January 1, 2021. Accordingly, the last plan year for which this relief applies is the same as the last plan year for which the relief under Notice 2014-5, as extended most recently by Notice 2019-49, applies.

3. Effect of temporary relief

The following treatment may be applied to a defined benefit plan described in section III.B.1 of this notice for a plan year described in section III.B.2 of this notice:

The plan is treated as satisfying § 1.401(a)(4)-4(b) and (c) for the plan year with respect to a benefit, right, or feature that was provided under the plan at the time the amendment described in section III.B.1 of this notice was adopted. This relief applies only if either:

- (i) No amendment adopted after January 29, 2016 expands or restricts the eligibility for the benefit, right, or feature; or
- (ii) If any such amendment has been adopted, then, as of the applicable amendment date for that amendment (determined under § 1.411(d)-3(g)(4)),¹ the post-amendment ratio percentage of the group of employees eligible for the benefit, right, or feature was

¹ Under § 1.411(d)-3(g)(4), the term “applicable amendment date,” with respect to a plan amendment, means the later of the effective date of the amendment or the date the amendment is adopted.

not less than the pre-amendment ratio percentage of the group of employees eligible for the benefit, right, or feature.

DRAFTING INFORMATION

The principal author of this notice is Diane S. Bloom of the Office of the Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes). However, other personnel from the IRS participated in development of this guidance. For further information regarding this notice, please contact Ms. Bloom or Linda Marshall at (202) 317-6700 (not a toll-free number).