



AMERICAN BENEFITS  
COUNCIL

October 1, 2015

*Filed by email to notice.comments@irsounsel.treas.gov*

CC:PA:LPD:PR (Announcement 2015-19)  
Room 5203  
Internal Revenue Service  
P.O. Box 7604  
Ben Franklin Station  
Washington, DC 20004

**Re: Announcement 2015-19 - Revisions to the Employee Plans Determination Letter Program**

Dear Sir or Madam:

This letter is submitted on behalf of American Benefits Council (the "Council") in response to Internal Revenue Service ("IRS" or "the Service") Announcement 2015-19, discussing upcoming revisions to the Employee Plans determination letter program for individually designed qualified retirement plans.

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either directly sponsor or provide services to retirement and health plans that cover more than 100 million Americans. Our members maintain individually designed qualified retirement plans and will be significantly impacted by the changes the Service contemplates in Announcement 2015-19.

Announcement 2015-19 indicates that the IRS will eliminate the staggered 5-year determination letter remedial amendment cycles for individually designed plans and limit the scope of the determination letter program for individually designed plans to initial plan qualification and qualification upon plan termination, beginning in 2017. As a result of this change, Announcement 2015-19 also indicates that the extended remedial

amendment period described in Rev. Proc. 2007-44 will no longer be available after December 31, 2016.

## **THE SUCCESS OF DETERMINATION LETTER PROGRAM**

We appreciate that the Service's resources in recent years have been severely constrained and the Service has had to make difficult choices about the programs that it can continue. In our view, however, the determination letter program for individually designed plans, and the staggered remedial amendment period the Service has maintained for the past decade, is one of the Service's most successful programs. The ability to periodically submit a plan document for review, as Congress routinely amends the qualification rules and regulatory complexity increases, enhances compliance and protects plan participants. In fact, the vast majority of the trillions earmarked for retirement in the U.S. originate in a plan that has been reviewed by the Service.

If the changes covered in Announcement 2015-19 are fully implemented, some plan sponsors will be able to shift to a pre-approved plan, but many will not. While pre-approved plans have been very successful for many plan sponsors, they are not suited to large plans with many legacy features or custom provisions that suit a complex benefit program. The individually designed plan model promotes innovation in benefit design. We have a particular concern, in fact, that the loss of the determination letter program will harm the creation and maintenance of defined benefit plans, many of which have complex grandfathered features.

## **IMPACT ON PLANS AND PLAN PARTICIPANTS**

The elimination of the determination letter program except for initial plan qualification and termination means that, after the initial qualification letter, employers generally will assume the risk of *any errors* in subsequent amendments and continually face the threat of disqualification – the so-called “nuclear bomb.” The existence of a favorable determination letter has become almost an expected part of prudent plan administration and fiduciary oversight. In fact, one significant advantage of the determination letter program is that it focuses employers on periodically reviewing the plan's terms. The application requires a restatement which encourages employer to maintain a restated plan document reflecting all amendments. In business transactions, it is routinely expected that a well-operated business maintains current determination letters, and auditors typically expect to see that the plan is covered by a favorable ruling. The elimination of the staggered remedial amendment period and the determination letter program for ongoing plan amendments will have major impacts on plans and participants.

**Disincentive to offer new features:** Not all amendments to qualified plans are mandatory. Congress often amends the tax code to facilitate new plan designs and features that improve participant outcomes. For example, the Pension Protection Act of 2006 opened the door to a variety of automatic enrollment features, which have proven to be one of the most successful plan design innovations in recent memory. But a plan sponsor would be reluctant to adopt such a feature to an existing plan if it cannot receive assurance that the plan terms implementing the feature did not disqualify the plan.

**Increased cost:** Continual updates to the plan documents will require greater costs than the current five-year staggered remedial amendment period. Even worse, many plan sponsors will be forced to obtain costly legal review regarding the plan and any amendments adopted (or not adopted).

**Corporate transactions:** A current determination letter is routinely requested during a corporate transaction, so that an acquiring company can receive assurance that the plans of the acquired or merging company are qualified without having to take the time to review every provision of the plan. This will have a real impact on participants, because companies will be reluctant to merge their plans together. In fact, the Service's new policies actually *encourage* an acquiring company to terminate the plan of an acquired entity before the transaction closes, because the terminated plan can receive a favorable determination letter. The acquiring company may be willing to accept rollovers from a terminated plan with a favorable determination letter, but not the merger of an ongoing plan with an outdated determination letter. This is decidedly not in the interest of participants.

If a 401(k) plan is involved, because of the alternative plan rules in Treas. Reg. § 1.401(k)-1(d)(4)(i),<sup>1</sup> the participants of the acquired plan may be put in very difficult situation if the plan is terminated after the transaction closes. The acquiring entity may simply be unwilling to accept rollovers or transfers because of the risk to the acquiring entity's plan. That leaves employees unable to receive a distribution that can be rolled over into an IRA. In fact, the alternative plan rules for 401(k) plan terminations implicitly assume that a robust determination letter process is available to allow comfort to transfer assets from one 401(k) to another.

**Financing and other lending agreements:** Lenders typically require warranties and covenants covering the employee benefit plans of the borrower, including a warranty to have and maintain a favorable determination letter. Once the Service closes its determination letter program except in the case of initial qualification and plan

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<sup>1</sup> Under these rules, a distribution may not be made on account of plan termination if the employer maintains an alternative defined contribution plan at any time during the next 12 months. For this purpose the term "employer" is applied based on the date of termination. Thus, in a stock deal, there is an incentive to terminate the plan prior to closing.

termination, many financing agreements will trip inadvertently into default. Going forward, because lenders may be wary of the costs associated with a disqualified pension plan, it may be more costly to obtain credit for businesses.

**Collective trust and insurance company separate account investments:** Collective trusts, insurance company separate accounts and other non-registered investments typically require evidence that an investing plan is tax-qualified. In fact, securities law *requires* investment by only qualified retirement plans in some cases.<sup>2</sup> Similarly, only qualified plans can invest in a group trust under Revenue Rulings 81-100 and 2014-24. Accordingly, sponsors of collective trusts and insurance company separate accounts typically require a favorable determination letter, because accepting assets from a plan that turns out to be nonqualified creates significant risks for all of the investing plans. These non-registered investments can be less expensive than registered investments, or can offer features like stable value investments that are very valuable, and therefore if these vehicles are harder to access, participants are the ones who are harmed.

**Foreign securities and American depository receipt (ADR) holdings:** Income tax treaties between the United States and foreign countries often reduce the tax withholding rate assessed on income and/or capital gains earned on foreign securities or ADRs when it is paid to a resident of the United States, including qualified retirement plans. In order for plans to qualify for this relief, some custodians acting as foreign withholding agents require a copy of the plan's valid determination letter to withhold at treaty-reduced rates. Other custodians and many treaty partners require the IRS to certify that the person claiming such treaty benefits is a resident of the United States for federal tax purposes. The IRS provides certification on Form 6166 and a plan can request certification using Form 8802. The Instructions for Form 8802 indicate that an application made on behalf of a plan not subject to ERISA or not otherwise required to file Form 5500 must include a copy of the plan's determination letter as part the application. If the applicant cannot provide a Form 5500 or determination letter, the process is more involved: the applicant must provide evidence that it is entitled to certification and provide a statement under penalty of perjury explaining why it does not have a determination letter. This issue is particularly relevant for plans whose custodians withhold at treaty-reduced rates based on the plan's favorable determination letter and for plans that are not required to file Form 5500 but hold foreign investments. In addition, it is important to note that certain foreign countries have statutory exemptions for plan investors and require a valid determination letter to qualify. These exemptions are not treaty based and are intended to attract tax exempt investors by offering lower tax rates on their returns. Plans would not be able to take advantage of these incentives if they cannot provide a valid determination letter to evidence their exempt status.

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<sup>2</sup> See Investment Company Act of 1940, § 3(c)(11) ("Any employee's stock bonus, pension, or profit-sharing trust which meets the requirements for qualification under section 401 of the Internal Revenue Code of 1986").

**Audited financials:** Almost all plans with 100 participants or more must be audited annually. An audit will, of course, include a statement as to whether the plan is tax-qualified. In fact, the Department of Labor's recent report on plan audits noted that not requesting a determination letter as part of an audit is a "major" unacceptable finding.<sup>3</sup> If there is no current determination letter, an auditor will presumably need another way to test compliance of the plan document, which could require an expensive opinion from the company's counsel. This will significantly increase the cost and time associated with a plan audit.

**Rollovers:** Accepting a rollover without adequate procedures puts the accepting plan at significant risk of its own disqualification. Some plan administrators require a determination letter to accept a rollover from another plan. Even if a determination letter is not required, since most plans have them, the risk of accepting rollovers is relatively low. But when *no plan* can obtain an updated determination letter, the risk of accepting a rollover from another plan is increased significantly. Plan sponsors may decide to no longer accept rollovers from other plans.

**Bankruptcy protection:** The Bankruptcy Code provides special protection for assets held in a qualified plan that has obtained a favorable determination letter.<sup>4</sup> While a favorable determination letter is not required for the debtor/participant to obtain an exemption from the bankruptcy estate, the process is more complicated, requiring a *demonstration* by the debtor that plan benefits are held in a plan in substantial compliance with the Code. This means more cost imposed on precisely those participants least able to bear that cost.

**EPCRS:** The determination letter system is intertwined with the Employee Plans Compliance Resolution System ("EPCRS"). In a number of cases, EPCRS requires the submission of a determination letter application. Further, EPCRS itself recognizes that a current determination letter is evidence of an attention to compliance: generally only plans with a favorable determination letter may correct significant operational failures.<sup>5</sup>

**Lack of availability of legal opinion:** Some of the above issues may be partially addressed if a plan sponsor is able to obtain a legal opinion. But it is far from clear that law firms will be willing to issue a legal opinion regarding the qualification of a plan, given that Code subsection 401(a) itself *has 37 separate paragraphs*, many incorporating

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<sup>3</sup> Department of Labor, Assessing the Quality of Employee Benefit Plan Audits (May 2015), available at: <http://www.dol.gov/ebsa/pdf/2014AuditReport.pdf>

<sup>4</sup> 11 U.S.C. § 522 ("If the retirement funds are in a retirement fund that has received a favorable determination under section 7805 of the Internal Revenue Code of 1986, and that determination is in effect as of the date of the filing of the petition in a case under this title, those funds shall be presumed to be exempt from the estate.").

<sup>5</sup> Rev. Proc. 2013-12 § 4.03.

complex rules in other sections of the Code. Tax opinions are typically issued only on narrowly and specifically defined issues, and only at significant expense. It is not clear to the Council's members that legal opinions can fill in the gap that will be left by the elimination of the determination letter program.

## NEED FOR COORDINATED RESPONSE BY TREASURY AND THE SERVICE

If the Service, despite the clear downsides to regulatory oversight and plan administration, decides to move forward, the elimination of the determination letters for individually designed plans after initial qualification will require a coordinated response to the regulations and guidance that apply to qualified retirement plans.<sup>6</sup> The Service, in conjunction with the Department of the Treasury, will need to take on a project to determine the proposed changes' impact on all of the regulations, revenue procedures, and other rules upon which plans rely for ensuring tax qualification. We recommend the following steps and changes:

**Rethinking the Service's unbending view of plan document failures:** Based solely on a statement in Code section 401(a) that a qualified plan be in "writing," and must "provide" certain rules, the Service has taken the inflexible view that a trust associated with a qualified plan is completely disqualified if the plan's written terms fail at any time to exactly meet every single requirement in section 401(a) and all other accompanying requirements. This is true even if the plan is administered at all times in compliance with the Code's requirements. But this view is not compelled by the statute, and EPCRS represented a leap forward in providing broad and appropriate relief from disqualification. We believe there is room for a flexible approach to the formal plan document requirement.

**Modify Audit CAP penalty and make other EPCRS changes:** If a plan document error is discovered on audit, it can be corrected under EPCRS using the Audit CAP program. But the possible penalty is draconian. It begins with calculating the "Maximum Payment Amount," which is essentially the maximum tax that could be collected if the Service collected tax on the trust, on the employer for loss of deductions, and on every participant, including tax on any distribution rolled over to other plans or IRAs, plus all the interest and penalties that might apply. EPCRS provides that Audit CAP penalties will be a "negotiated percentage" of the amount and "will not be excessive and will bear a reasonable relationship to the nature, extent, and severity of the failures,"<sup>7</sup> but the massive amounts involved mean Audit CAP is a process that no plan sponsor ever wants to face. Audit CAP's penalties do their job – encourage use of

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<sup>6</sup> This need for major adjustments to the rules governing qualified plans will take an investment of resources that may significantly diminish any value the Service gains from curtailing the determination letter program.

<sup>7</sup> Rev. Proc. 2013-12 § 14.01.

the determination letter program. But without a determination letter program, the threat of an audit and Audit CAP penalty will loom over every plan.

We recommend that the Service revise the Audit CAP penalties so that, when an ordinary plan document failure is involved, a penalty structure similar to VCP applies. In other words, a plan document error could be corrected on audit with a maximum penalty based on the size of the plan. These rules could, of course, have an exception allowing the Service to disqualify a plan in cases of deliberate or egregious evasion of the qualification requirements.

Alternatively, if a routine plan document error is discovered on audit, the Service could direct the employer to submit the error for correction under VCP, possibly with an enhanced penalty to encourage the voluntary correction of errors (particularly failure to timely adopt required amendments).

Finally, a variety of other changes will be necessary for EPCRS. For example, we urge the Service to consider expanding the ability of plans to make retroactive amendments through self-correction.

**Offer determination letters for significant plan amendments:** Many amendments to plans are routine changes to reflect changes in the law or adjustments in administrative procedures. But some amendments are critical to the plan and its benefit. Announcement 2015-19 states that Treasury and the Service intend to issue determination letters in “certain other limited circumstances that will be determined by Treasury and the IRS.” We offer the following suggestions along these lines, but we caution that this list may need to be expanded as plan sponsors come to terms with the new paradigm:

- *A determination letter should be available when two plans merge.* This is critical in the contexts of corporate acquisitions. Without the possibility of a determination letter, a company that acquires another entity with a smaller plan will be under significant pressure to terminate the plan, which is not in participants’ best interest.
- *A determination letter should be available for conversions of plan type.* Many defined benefit plans have in recent years modified their benefit structure. A cash balance plan conversion is the most common example, but there are others. Congress created specific (and complex) rules for hybrid plan conversions in the Pension Protection Act. These conversions have been critical in allowing employers to continue to maintain their defined benefit plans. Faced with the choice of freezing a defined benefit plan or converting the formula without any protection for the plan, many employers will simply freeze the plan.

**Offer private letter rulings regarding qualification issues:** Currently, questions regarding a plan's qualification must be handled through the determination letter program. A private letter ruling (PLR) from the Employee Plans Rulings and Agreements office is not available for matters relating to plan qualification.<sup>8</sup> The PLR process is generally more expensive and involved, but some employers may have plan amendments that are so important that they are willing to pay the fee associated with the PLR program to obtain a ruling. The PLR need not consider all of the plan terms, but could focus on only those provisions cited by the employer.

**Remove the "expiration date" on determination letters:** Determination letters generally have an expiration date. We see no reason that this should be the case in the absence of a cyclical remedial amendment period. We recommend that the Service allow an employer to rely on a determination letter with respect to any law or regulation that has not changed since the determination letter was issued. This would allow for a more focused review by counsel or auditors reviewing a plan only on amendments or changes in the law since the last determination letter.

**Revise the remedial amendment period and eliminate "interim" amendments:** The current structure provides a staggered five-year remedial amendment period but requires annual "interim" good faith amendments. The interim amendment process has been somewhat of a burden on employers, but if it made sense at all, it only makes sense if the employer can correct any errors when the plan is later submitted for determination letter as part of the cycle. It no longer makes sense to require rapid amendments. Instead, the Service should adopt a reasonable period for adoption of amendments to reflect changes in the Code or regulations (or other guidance). As a starting point, we recommend that plans receive a minimum of three years to amend a plan, unless Congress specifically provides another deadline. Of course, this transition period would only be applicable to the plan document itself; not plan operation.

**Revisit the 401(b) regulations:** The regulations under Code section 401(b) are designed for a system in which plans can request determination letters.<sup>9</sup> In connection with the prior recommendation, we recommend that Treasury and IRS place on its business plan a project to amend the regulation to provide for an extended remedial amendment period both for disqualifying provisions and for required amendments because of changes in law or regulation. In connection with reviewing the Code section 401(b) regulations, we urge Treasury and the Service to reconsider the definition of "disqualifying provision," as noted above.

**Expand pre-approved plan program to offer more flexibility:** The master & prototype and volume submitter programs fill a critical role for many employers and service providers. In recent years, the pre-approved plan program has been expanded

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<sup>8</sup> See Rev. Proc. 2015-04 § 6.03.

<sup>9</sup> See, e.g., Treas. Reg. § 1.401(b)-1(e)(3).



to cover more plan types, including cash balance plans and ESOPs.<sup>10</sup> Historically, however, the Service has been reluctant to allow many kinds of plan designs in the pre-approved program, under the theory that a plan design could always be submitted for an individual determination letter. This has been particularly true with respect to the nondiscrimination rules and plan designs regarding eligibility and benefit criteria. The Service will need to be more flexible in the plan designs that it permits in the pre-approved program.

The Service should also consider expanding the conditions under which a pre-approved plan can be modified between review cycles without jeopardizing the favorable opinion or advisory letter. For example, the pre-approved plan sponsor could change investment or fiduciary provisions and have more flexibility for permissible design-related changes.

**Reopen applications on Form 5307 and allow review of modified pre-approved plans:** The Service has, in recent years, reduced the ability of a plan sponsor to receive a determination letter based on a prototype plan. Form 5307 is still available for adopters of modified volume submitter plans, for limited modifications that do not create an individually designed plan. It is not clear whether Form 5307 will continue to be available.

Many volume submitter plan documents include a superseding addendum where the plan sponsor can list legacy benefits, rights or features that must be preserved. It is critical that the Form 5307 continue to be available, and we encourage the Service to expand the kinds of benefits and features that can be included in a superseding addendum and still submitted under a Form 5307. The review by the Service, after all, needs to focus only on those legacy or other features in the addendum. In fact, retaining and expanding the Form 5307 program will help facilitate those employers that wish to move to a volume submitter plan but must preserve some plan benefits or features.

In any event, we recommend the Service consider allowing employers that adopt pre-approved plans, but make targeted changes to the plan document to suit their needs or reflect a legacy feature that must be preserved, and submit a Form 5307 or similar application for a targeted review. This would allow the Service to review just the modifications, as the other plan terms would have been closely reviewed by the Service.

**Provide for model amendments and allow incorporation by reference:** The Service will often publish model language for changes in the law. We urge the Service to make this a standard procedure, and to allow a plan to be amended to simply incorporate that language if the employer chooses to do so. The Service should take other opportunities to allow incorporation by reference. A plan document that restates word-for-word a regulation or IRS notice does not particularly aid in plan administration when the

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<sup>10</sup> See Rev. Proc. 2015-36.

language can simply be incorporated. This may not work in all instances, but should be available to simplify the amendment process and limit foot faults.

The Service will also need to continue offering a version of the “cumulative list” so that employers and their counsel can focus on the changes that the Service has concluded may require a plan amendment. The Service should consider other tools, like checklists, that might assist employers in keeping their plans compliant. Use of such checklists could serve as evidence of plan document compliance on audit and as the basis of reduced penalties under EPCRS.

**Provide transition relief for Cycle B, C, and D plans:** Announcement 2015-19 states that the Service will be allowing Cycle A and E plans to submit for a final determination letter under the remedial amendment cycle. This leaves Cycle B, C, and D plans in a transition period. The Service states that it will extend the remedial amendment period, but currently this could be as early as December 31, 2017. We think more time is needed, and we urge the Service to begin thinking as early as possible about an extended remedial period beyond that contemplated by Treas. Reg. § 1.401(b)-1.

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We look forward to discussing these issues as you move forward. Thank you for the opportunity to provide our views and suggestions.

Sincerely,

A handwritten signature in black ink, appearing to read "Jan Jacobson". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Jan Jacobson  
Senior Counsel, Retirement Policy