Employee Benefits Corner

By Elizabeth Thomas Dold and David N. Levine

IRS Updates the Filing Process for Qualified Plans–Part II

In the January 2012 edition of our column, we provided an update on IRS procedures and guidance that must be followed in order for the IRS to make a determination that qualified plan documents comply, as to form, with the requirements of the Internal Revenue Code of 1986, as amended ("the Code"). Notably, we addressed the following pieces of additional guidance:

- Rev. Proc. 2011-49, which updates the rules for submitting pre-approved plans to the IRS
- The new Form 5300 determination letter application for individually designed plans[1]
- The new "LRMs" (Listing of Required Modifications) for defined contribution plans[2]
- EP Determinations Quality Assurance Bulletin 2012-1 addressing verification of prior plan documents[3]

Just as the January 2012 column headed to press, a new set of IRS guidance that further revises the determination letter process was issued, so this March 2012 edition of our column turns to the following additional guidance provided by the IRS in late 2011:

- Announcement 2011-82[4] and Rev. Proc. 2012-6,[5] which set forth new rules for obtaining determination letters. These restrictions to the process were intended to streamline the IRS' workload, and are generally effective May 1, 2012. This translates into a last call for plan sponsors filing for determination letters for defined benefit pre-approved plans by the April 30, 2012, deadline.
- Notice 2011-97[6] sets forth the 2011 Cumulative List that sets forth the plan amendment items under review for "Cycle B" filers, which can begin filing for Pension Protection Act of 2006 (PPA) determination letters as of February 1, 2012.

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We address these pieces of guidance in two parts—one section for individually designed plans, and one section for pre-approved plans.

Individually Designed Plans

Cycle B Determination Letter Filers–2011 Cumulative List

Beginning February 1, 2012, the IRS will open the determination letter process to "Cycle B" plans (*i.e.*, individually designed plans sponsored by an employer whose EIN ends in 2 or 7 and multiple employer plans). Cycle B plans that wish to maintain a favorable IRS determination letter should file their plans with the IRS for review between February 1, 2012, and January 31, 2013. The IRS will review these plans for legal changes included on the new 2011 Cumulative List.[7] And, the favorable letters issued by the IRS on these plans will cover only the items listed on this Cumulative List.

The 2011 Cumulative List deletes all items that were reviewed by the IRS during the prior determination letter cycle. However, if a Plan was not previously reviewed for items on prior Cumulative List (*e.g.*, a new Plan established after the end of the previous Cycle B period), these items must still be addressed in the plan document. Some of the more significant items on the latest Cumulative List include the following:

- **Two New Items.** There are only two new items on the Cumulative List (although the first item is listed under several different Code sections). First, Notice 2011-19 provides guidance on the meaning of the terms "readily tradable on an established securities market" and "readily tradable on an established market," as applicable to employee stock ownership plans. Second, Code Sec. 431(b)(8) adds two special funding rules for multiemployer plans. For many plans, these changes will be of minimal impact.
- **Post–October 1, 2011, Guidance Not Subject to Review in Cycle B.** Generally, the IRS will not consider (1) any guidance issued, or statutes enacted, after October 1, 2011, (2) qualification requirements first effective in 2013 or later, or (3) statutory provisions that are first effective in 2012 if no relevant guidance is identified on the Cumulative List. Accordingly, the IRS will not consider provisions related to the benefit restriction rules of Code Sec. 436, including the recent sample amendment provided by the IRS.[8] In addition, taking into account Notice 2011-85[9] (which announced that the IRS intends to amend the final hybrid plan regulations to delay the effective date of certain regulations until no earlier than January 1, 2013) the IRS says it "will not consider the 2010 final hybrid plan regulations (other than with respect to Code section 411(a)(13)(A)) unless the plan has been amended to satisfy those regulations. For this purpose, the IRS will only consider those provisions of the regulations that are effective for plan years beginning on or after January 1, 2011."
- **Treatment of Proposed Regulations.** The IRS's review of matters addressed by proposed regulations will be based on a "reasonable interpretation" of the underlying statute, final regulations or other IRS guidance. The IRS notes that compliance with proposed regulations meets this standard, but the favorable IRS letter "cannot be relied on with respect to whether the plan complies with the proposed regulations." The Cumulative List expressly refers to proposed regulations under the following Code sections (which were also included on the 2010 Cumulative List): 401(k), 401(m), 402(f), 411(a)(11), 411(a)(13), 411(b)(1), 411(b)(5), 417 and 432.

Changes to the Determination Letter Program May 1, 2012

The changes described below as set forth in Rev. Proc. 2012-6[10] were intended to eliminate features of the program that are of limited utility to plan sponsors in comparison with the burdens they imposed on the IRS, and are extended to reduce the time it takes the IRS to process determination letter applications, which, depending on the type and complexity of the plan, can easily be a multi-year process.[11] For example, the IRS is still processing EGTRRA determination letter applications filed in 2009.

For many years, the IRS has given plan sponsors the option to apply for IRS approval of its coverage (Code Sec. 410(b)) or nondiscrimination methodology (Code Sec. 401(a)(4))—for an additional fee—on Schedule Q (*Elective Determination Requests*) of Form 5300. This option included IRS determinations for the following issues, which were optional for 5300 filings (but some demonstrations were required for Form 5310 filing on Plan termination):

- **Demo 1: QSLOB Testing.** A determination on whether a plan that uses the qualified separate lines of business rules of Code Sec. 414(r) satisfies the

gateway test of Code Sec. 410(b)(5)(B) or satisfies the special requirements for employer-wide plans.

- **Demo 3: BRF Testing.** A determination that specified benefits, rights or features (commonly referred to as "BRF testing") meet the nondiscriminatory current availability requirement.
- **Demo 4: Plan Aggregation, Disaggregation and Restructuring for Coverage Testing.** A determination regarding the plan being restructured, mandatorily disaggregated, or permissively aggregated in order to pass Code Sec. 410(b) coverage testing.
- **Demo 5: Average Benefit Test for Coverage Test.** A determination regarding whether the plan passes the average benefit test under Reg. §1.410(b)-2(b)(3).
- **Demo 6: Certain Code Sec. 401(a)(4) Testing.** A determination regarding a non–design-based safe harbor or a general test under Code Sec. 401(a)(4).
- **Demo 7: Pre-Participation and Imputed Service.** A determination regarding a plan provision that provides for pre-participation or imputed service, or for a determination regarding a plan amendment providing a period of past service in excess of the safe harbor.
- **Demo 8: Floor Offset Arrangements.** A determination regarding a floor offset arrangement intended to satisfy the safe harbor in Reg. §1.401(a)(4)-8(d).
- **Demo 9: Definition of Compensation.** A determination that a definition of compensation is non discriminatory.
- **Demo 10: Defined Benefit Plan—Employee Contributions Not Allocated to Separate Accounts—Composition-of-Workforce Method.** A determination for a defined benefit plan with employee contributions not allocated to separate accounts that use the composition-of-workforce method to determine the employer-provided benefit.
- **Demo 11: Defined Benefit—Test to Show Employer-Provided Benefit Is Nondiscriminatory in Amount.** A determination for a defined benefit plan with employee contributions not allocated to separate accounts that use the grandfather rule to show that employer-provided benefit is non discriminatory in amount.

The IRS will no longer allow such "demos" in Cycle B and later cycles (*i.e.*, effective February 1, 2012, unless the Plan is terminating, then the effective date is May 1, 2012), except for requests for "design-based safe harbor" formulas. Moreover, the Plan will no longer be permitted to request that the plan be reviewed to determine that the ratio percentage test of Code Sec. 410(b)(1) is satisfied. Plans will, however, continue to be reviewed and may be relied upon, for whether a plan's terms satisfy the applicable requirements of Code Sec. 401(k) and 401(m) (nondiscrimination testing for 401(k) plans).

Moreover, the new procedures expressly states that a favorable determination letter does not constitute a ruling or determination as to whether the plan is (1) a governmental plan under Code Sec. 414(d) or if the contributions to the plan satisfy Code Sec. 414(h) (pick-up contributions), or (2) a church plan under Code Sec. 414(e). And although an affiliated service group and leased employee status may be reviewed as part of the determination letter application, the IRS no longer rules on the effect of these items on the plan's qualified status. However, an employer can still request a determination of whether a partial termination has occurred, and if so, its impact on plan qualification.

As noted in our January 2012 article, the Form 5300 was updated in 2011 and is required to be used for Cycle B filings. Notably, the applications must include (1) any EPCRS documentation, (2) documentation regarding the merger of plans, and (3) all interim and other plan amendments adopted since the submission of the most recent determination letter application. Although the Form 5300 was recently updated, along with the Form 8717 (*User Fee*) and Form 2848 (*Power of Attorney*), it is possible that there will be additional changes to Forms 5300, 5310 (Determination Letter on Plan Termination) and 8717 to reflect the new process.

Pre-Approved Plans

Unlike individually designed plans, pre-approved plans can generally rely on the IRS opinion letter or advisory letter that was issued by the IRS on the form of the master and prototype (commonly referred to as "M&P") or volume submitter plan.

April 30, 2012, Deadline for Pre-Approved Defined Benefit Plans

For plan sponsors that provide a defined benefit plan through a pre-approved plan, the new EGTRRA approved document must be adopted by April 30, 2012. If these plan sponsors wish to also obtain a determination letter on their plan, they should file a Form 5307 determination letter application with the IRS by that same date. Plans that have converted from M&P or volume submitter status to an individually designed plan should also consider whether there is a need to

file a Form 5300 determination letter application by that date. Failure to timely adopt an EGTRRA approved document may result in the need to file a correction filing under Rev. Proc. 2008-50, the Employee Plans Compliance Resolution System,[12] in order to maintain the tax-qualified status of the Plan.

Importantly, from the changes in the program noted below, this is, in many cases, the last chance for plan sponsors to file for determination letters on pre-approved plans, which is common practice to obtain the additional level of protection of the determination letter, which is used largely to limit the amount of document production to be provided in the event of an IRS examination, and to address any coverage or nondiscrimination concerns raised in the mergers and acquisitions context. The impact of saving resources as part of the determination letter process hopefully will not result in additional complexities and burdens to plan sponsors in the IRS examination process.

Changes to the Determination Letter Program Effective May 1, 2012

As with individually designed plans, for many years, the IRS has given plan sponsors of pre-approved plans the option to apply for a determination letter for their Plan. A six-year determination letter cycle applies, and plan sponsors are required to file Form 5307. This determination letter request could also seek IRS approval of its coverage or nondiscrimination methodology—for an additional fee. Therefore, even though an employer adopts a pre-approved plan without any change (*i.e.*, it just selects among the available options), the employer may apply for an IRS determination letter, for example, to obtain reliance on coverage and nondiscrimination requirements (Schedule Q).

This option is being dropped effective May 1, 2012, except for volume submitters, where the employer made limited modifications to the language of the approved specimen plan. Therefore, as of May 1, 2012, the Form 5307 will be largely eliminated, except for plan sponsors that made minor modifications to the volume submitter document.

Importantly, there are a few situations were a pre-approved plan can file a Form 5300 determination letter application (and still be considered a pre-approved plan with reliance on the opinion letter/advisory letter), beginning as of May 1, 2012. Specifically, a Form 5300 can be filed for a pre-approved plan if (1) the application requests a determination regarding affiliated service group, leased employee status or partial plan termination; (2) the plan is a multiple employer plan; (3) a determination letter is required by the IRS (for example, in connection with a request for a funding waiver); (4) the employer has added language to an M&P plan to satisfy the requirements of Code Secs. 415 and 416 because of the required aggregation of plans; or (5) the plan is a pension plan with a normal retirement age earlier than age 62. Of course, as under current rules, if an employer makes too many changes in a pre-approved plan, it may be deemed to have an individually designed plan in any event, and losses reliance on the opinion/advisory letter and can request a Form 5300 determination letter.

In addition to having to complete the longer form, the "user fee" for Form 5300 filings is $2,500—compared with only $300 for Form 5307—making the process considerably more costly. We anticipate additional changes to Forms 5300, 5307, 5310 and 8717 to reflect the new process.

Endnotes

1 *www.irs.gov/pub/irs-pdf/f5300.pdf.*
2 *www.irs.gov/retirement/article/0,,id=97182,00.html.*
3 *www.irs.gov/pub/irs-tege/qab_102411.pdf.*
4 Ann. 2011-82, IRB 2011-52, Dec. 16, 2011.
5 Rev. Proc. 2012-6, IRB 2012-1, 197.
6 Notice 2011-97, IRB 2011-52, Dec. 12, 2011.
7 *Id.*
8 Notice 2011-96, IRB 2011-52, Nov. 29, 2011.
9 Notice 2011-85, IRB 2011-44, 605.
10 Rev. Proc. 2012-6, *supra* note 5.
11 *www.irs.gov/retirement/article/0,,id=218533,00.html.*
12 Rev. Proc. 2008-50, IRB 2008-35, 464.