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Legal Developments

IRS Reopens the Determination Letter Program for Certain Plans

As of September 1, 2019, plan sponsors of qualified plans with M&A activity and hybrid formulas will once again be eligible to file for updated determination letters. This is a first step to allowing plan sponsors with ongoing plans to have the IRS bless their plan document form, which was commonplace prior to the substantial restriction of the program in 2016.

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On May 1, 2019, pursuant to Revenue Procedure 2019-20, the Internal Revenue Service (IRS) opened up its long-standing determination letter program for individually designed plans (as opposed to pre-approved plans) set forth in Revenue Procedure 2019-4 for certain ongoing plans. Specifically, as of September 1, 2019, plan sponsors of qualified plans with merger and acquisition (M&A) activity and hybrid formulas are eligible to file for updated determination letters. This is an important first step to allowing plan sponsors with ongoing plans the ability to have the IRS bless their plan document as to the form (as opposed to plan operations), which was commonplace prior to the substantial restriction of the program in 2016. Set forth below, in question and answer format, is a summary of the expanded program.

Background

Prior to Revenue Procedure 2019-20, what plans were eligible to file for updated determination letters?

Only new plans, plans that had never obtained a determination letter, and terminated plans were eligible to receive a determination letter.

When did the IRS stop allowing ongoing qualified plans from obtaining an updated determination letter?

In 2016, the IRS announced, in Revenue Procedure 2016-37, the end of the long-standing five-year cycle determination letter program for individually designed plans (Cycle A-E, based generally on the plan sponsor's Employer Identification Number), and the end of plans being able to file for updated favorable determination letters. The Cycle A plans were the last group to make filings under the program on January 31, 2017. After that, it was only plans that never received a determination letter or terminated plans that could receive a determination letter.

Do the old determination letters expire?

No, although a prior determination letter may indicate an expiration date, the IRS announced in Revenue Procedure 2016-37 that the forms were evergreen, that is, they continue to apply with respect to the plan terms that have not been amended, and to the extent that the law has not changed.

Why the need for an updated determination letter?

Although the filing for determination letters is optional, having an updated determination letter provides a number of benefits: (1) the IRS's review and blessing as to the form of the plan document, which is invaluable for new design changes; (2) helpful to show to Form 5500 auditors, IRS auditors, and investment funds advisors to validate that the plan document is tax-qualified; (3) supports rollover contributions and US and foreign reporting and withholding treatment; (4) facilitates M&A and other corporate transactions where a review of qualified plans is key; (5) supports anti-alienation/assignment determinations; and (6) provides some protection against a retroactive plan disqualification under 7805(b) relief.

Revenue Procedure 2019-20 Expansion

When did the determination letter program changes take effect?

September 1, 2019.

What changes to the determination letter program were made?

Revenue Procedure 2019-20 expands the determination letter program in permitting hybrid plans and merged plans to obtain an updated determination letter.

What is a hybrid plan and when can it be submitted for a determination letter?

Revenue Procedure 2019–20, defines a hybrid plan by reference to the hybrid plan regulations under Treasury Regulation Section 1.411(a)(13)-1(d)(5). This includes cash balance plans, pension equity plans, and certain variable annuity plans. It expressly includes plans that contain other formulas, and would extend to frozen plans as well.

There is a one-time filing window of September 1, 2019–August 31, 2020 for hybrid plans. After the window closes, these plans will no longer be eligible to obtain a determination letter for an ongoing plan unless they qualify as a merged plan.

What is a merged plan and when can it be submitted for a determination letter?

A defined benefit or defined contribution plan is eligible to file for a determination letter under the special merged plan rules, if the following three requirements are satisfied:

1. *M&A Transaction*. There is a corporate merger, acquisition, or similar business transaction among unrelated entities (that is, not within the same controlled group or affiliated service group);
2. *Plan Merger*. There is a merger of two or more formerly separate plans into a merged plan no later than the last day of the first plan year that begins after the plan year that includes the Date of Corporate Merger (that is, effective date of the transaction); and
3. *Form 5300 Filing Deadline*. The determination letter is filed within the period beginning on the Date of the Plan Merger (that is, effective date of

the plan merger) and ending on the last day of the first plan year of the merged plan that begins after the Date of the Plan Merger.

For example, if a plan sponsor acquired an unrelated entity in a corporate transaction as of September 1, 2018, and then merged the acquired company's plan into its plan on January 1, 2019 (but, in any event, no later than December 31, 2019), then the deadline for submitting a determination letter application would be December 31, 2020 (assuming these are all plans with calendar year plan years).

What is the process for applying for a determination letter?

Form 5300 is filed with the IRS in accordance with the procedures set forth in Revenue Procedure 2019-4 (which is updated annually). Typically, a plan sponsor files a plan restatement with the IRS, along with the trust document, for a determination letter. The filing includes all plan amendments and restatements effective since the last determination letter. The filing fee is currently $2,500 (which can be paid from plan assets), and the process generally takes at least a year.

Is there a risk of sanctions when filing for a determination letter?

Yes, to the extent that the IRS discovers a plan document failure (called a nonamender failure), the IRS generally may assert between 150 percent–250 percent of the VCP filing fee (higher fees in rare instances for egregious failures). These fees are not payable from the plan, and are otherwise non-deductible.

To the extent that the plan sponsor is aware of the nonamender failure, they can simultaneously file with the determination letter a VCP filing to avoid the 50 percent–150 percent markup. (The current VCP filing fee ranges from $1,500–$3,500, depending on the size of the plan.) [Rev. Proc. 2019-19]

Importantly, Revenue Procedure 2019-20 provides for no sanctions with regard to the hybrid regulations or the merger provisions, and any other document failure that was adopted timely and in good faith (or in good faith the plan decided that an amendment was not needed) are only subject to 100 percent of the VCP fee. Notably, the determination letter changes do not extend the anti-cutback relief that was made available for changes in interest crediting rates before the 2017 plan year.

Conclusion

What are appropriate next steps?

Plan sponsors should review the date of the last favorable determination letter, and consider if an updated letter is available for the plan; that is, is the plan now eligible for a determination letter as either a hybrid or a merged plan. If so, review the existing plan amendments that are not protected by the determination letter, and consider other design changes that you may want to implement prior to the applicable filing deadline.

What if my plan is not eligible for a favorable determination letter?

To the extent that the plan is not eligible for an updated determination letter, review the latest Cumulative List (which is still provided, as needed, for pre-approved plans), all the Required Amendment Lists, and the Operational Compliance Lists to ensure that the plan is in both form and operation compliant with these provisions. The plan sponsor also might consider obtaining a legal opinion of counsel regarding the tax-qualified status of the plan. To the extent the company engages in M&A activities, consider if the new merged plan rules will trigger the ability to obtain a determination letter in connection with the transaction. Finally, if the plan sponsor was considering converting to a hybrid formula, now is the time. ■