

Employee Benefits Corner

By Elizabeth Thomas Dold and David N. Levine

IRS 2009–2010 Guidance Plan—A Look at What’s Coming

Each year the IRS issues a list of its top-priority guidance initiatives for the year, called the guidance plan. The long-awaited list of items was issued in late 2009, and sets forth the plan for issuing much-needed guidance for the July 2009–June 2010 year. Of the 42 qualified plan items on the list, 18 of those items were already completed when the guidance plan was released (and a few more have been completed as of the drafting of this article). The task for the IRS through June is to complete as many of the remaining 20-some items as possible, while also being mindful that other priorities may arise to distract from this goal, such as the need to provide guidance for intervening legislation. It is not uncommon for some issues to remain on the guidance plan for several years. A look at a number of provisions from the guidance plan that remain to be addressed, based on the type of plan, will give us an idea of what is in store for the coming year.



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Defined Contribution Plans (401(k) Plans, Profit Sharing Plans, Money Purchase Pension Plans)

Lifetime Income from Defined Contribution Plans

401(k) and Profit Sharing Plans were initially designed to merely supplement a participant's retirement funds, with the participant's lifetime payments being made from their traditional defined benefit plan. As a supplemental plan, there was no requirement to offer lifetime benefits and many 401(k) plans today do not offer such payments, and even when offered, they are rarely elected. As 401(k) plans quickly become the sole retirement plan for many employees, there is a new need for



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lifetime payments. And, as market forces play such a heavy role in an individual's retirement future, the need to lock in a guaranteed income stream even prior to retirement is becoming more and more important to many plan participants.

To fill this need, a new line of annuity products are beginning to come onto the market that provide guaranteed lifetime benefits, while providing participant's with control and flexibility over their pension assets. This guidance plan provision may result in additional guidance as to these and other similar lifetime payment options. Legislative proposals encouraging annuity options and a joint study with the Department of Labor and Treasury Department will likely bring new ideas for promoting the use of lifetime payment streams (<http://edocket.access.gpo.gov/2010/pdf/2010-2028.pdf>).

Diversification Guidance

The Pension Protection Act of 2006¹ added new diversification rules for publicly traded employer securities held in defined contribution plans. Certain plans, such as one-participant retirement plans and certain ESOPs, are carved out from these rules. For the past several years, plan sponsors have been operating under IRS transition guidance (Notice 2006-107² and Notice 2008-7³). Final regulations will allow plan sponsors to amend their plans, as necessary, to bring them into compliance before the extended amendment deadline (*i.e.*, generally the end of 2010), for these rules.⁴

Safe Harbor Plans—Nonelective Contributions

In reaction to the economic hardship facing many safe harbor plan sponsors, in 2009, the IRS issued proposed regulations that provided limited relief for companies in financial hardship to suspend, reduce or stop employer nonelective contributions for safe harbor plans. Previously, there had only been guidance on the suspension of safe harbor matching contributions. The guidance plan includes finalization of these regulations. A number of practitioners have requested the plan sponsors be treated in the same manner regardless of the safe harbor design selected—either the safe harbor matching contributions or nonelective contributions—which would require advance participant notice and nondiscrimination testing in the event that such employer contributions were changed or suspended, but no requirement of employer financial hardship. Many

practitioners are also hoping that the final regulations (or other guidance) will include sample plan language that can be used that will not impact the continued reliance on the pre-approved plan's advisory or opinion letter, and that no additional language will be required to be included in the annual safe harbor notice to explain the employer's right to suspend or change the contributions (and the implications thereof).

Defined Benefit Plans

Outlined below are some of the items set forth on the guidance plan for defined benefit plans, including cash balance plans and traditional final average pay type benefit formulas. If defined benefit plan funding relief, which is being advocated by a number of groups, is enacted in early 2010, the need for quick guidance on this relief may result in additional work for the IRS and a possible further delay in one or more of the following items.

Hybrid Plan Guidance

Final regulations and additional proposed regulations addressing hybrid plans (including cash balance plans) that implement the Pension Protection Act provisions under Code Sec. 411(a)(13) and(b)(5) will provide further guidance on the rules for hybrid plans that went into effect over the past several years. Of specific note in this upcoming guidance is the requirement that a hybrid plan provide for a "market rate of return." Practitioners have raised a number of concerns about the IRS's proposed guidance and have requested a wider range of permissible interest rates.

Announcement on Pre-Approved Defined Benefit Plans

Announcement 2009-85 explained that on February 22, 2010, the IRS will temporarily stopped accepting applications for determination letters for defined benefit plans that are filed using Form 5307 for the GUST program. This action was taken because all pre-approved (*i.e.*, master and prototype and volume submitter) defined benefit plans will soon be required to be restated to comply with items identified for review in the 2006 Cumulative List (as published in Notice 2007-3⁵), including the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA)⁶ (with technical corrections made by the Job Creation and Worker Assistance

Act of 2002⁷), the Pension Funding Equity Act of 2004,⁸ the American Jobs Creation Act of 2004,⁹ the Gulf Opportunity Zone Act of 2005¹⁰ and certain law changes under the Pension Protection Act of 2006. These restated pre-approved plans will be submitted to the IRS for a determination letter (if needed) using Form 5307 during a period of approximately two years, which the IRS is likely to announce early in 2010. The temporary hiatus in accepting Form 5307 applications will allow the IRS to prepare to receive the applications submitted by adopters of these restated EGTRRA pre-approved plans.

Participant Notice

In fall 2009, the IRS issued final regulations addressing the Code Sec. 436 funding-based benefit restriction rules. As a follow-up, the guidance plan includes information on the participant notice requirement under ERISA §101(j) regarding notice requirements applicable to single-employer plans that become subject to these funding-based benefit limitations. This guidance is anticipated to include that ERISA §101(j) does not require notice of a benefit restriction affecting the availability of lump sums to participants and beneficiaries in pay status who—without regard to any Code Sec. 436 limitation—can no longer elect a lump-sum payment. This result of not having to provide notice to participants and beneficiaries to whom the limitation could have no application would reduce costs, administrative burdens and participant confusion.

Additional Guidance on Funding Rules

Although the IRS has already issued a number of pieces of guidance addressing the various changes to the defined benefit plan funding rules enacted in the Pension Protection Act of 2006, a number of additional pieces of guidance addressing (1) the Code Sec. 430 minimum required contribution rules, (2) the rules governing multiemployer plan amortization extension requests, and (3) additional guidance on the multiemployer pension plan funding rules are on the 2009–2010 guidance plan. In addition, if any additional funding relief is enacted by Congress in 2010, additional guidance on this legislation is likely to be issued as well.

403(b) Plans

In 2007, the IRS finalized its first major update of the Code Sec. 403(b) regulations in over 40 years. Un-

der these final regulations (as modified by the relief provided in Notice 2009-3), 403(b) plan sponsors were generally required to adopt updated, written plan documents by December 31, 2009. However, a number of additional 403(b) plan-related items that remain to be addressed are included in the 2009–2010 guidance plan.

Group Trust Guidance

Pursuant to Rev. Rul. 81-100¹¹ (and as modified in Rev. Rul. 2004-67¹²), the IRS permits the assets of plans described in Code Sec. 401(a), IRAs and governmental 457(b) plans to be commingled for investment in group trusts. However, a notable absence from this guidance has been the exclusion of 403(b) plans from inclusion in group trusts. Many practitioners expect that this group trust guidance will permit the inclusion of 403(b) plans in group trusts. Alternatively, this guidance may relate to the Form 5317 application for group trust determinations that is referenced in recently issued Rev. Proc. 2010-6.

403(b) Plan Terminations

For the first time, the final 403(b) regulations provide specific guidance on the termination of 403(b) plans. However, a number of questions have been raised about this termination process—ranging from how termination can be implemented in the case of individually held annuity contracts to how custodial accounts might be distributed on the termination of a 403(b) plan. Practitioners are hoping that the guidance referenced on the guidance plan will address these issues.

Prototype Program

In 2009, the IRS issued proposed listings of required modifications (which are basically model plan language) for 403(b) plans in connection with its development of a proposed 403(b) plan prototype program similar to that available to tax-qualified plans, where an plan sponsor can generally rely on a pre-approved plan document that is offered by a 403(b) provider. Consistent with the IRS's previously stated position that it intends to first open a prototype program for 403(b) plans and then provide for a determination letter program for individually designed plans, the guidance plan refers to a revenue procedure for this new prototype 403(b) plan program. It is likely that the listing of required modifications (LRMs) issued in 2009 will also be

updated to reflect comments and concerns (most notably adding provisions to permit prototype plans to include vesting schedules) in connection with the prototype plan program.

Other Guidance Projects

In addition to the guidance specific to defined contribution, defined benefit, and 403(b) plans, a number of additional guidance projects are included in the guidance plan.

Governmental Plan Definition

The guidance plan includes a number of items related to governmental plans, most of which has been issued (e.g., the delayed effective date of the final normal retirement age regulations, the minimum required distribution rules for governmental plans, and extension of remedial amendment period amendment deadline for governmental plan amendments). However, a long-awaited significant piece of guidance listed on the guidance plan—the definition of a “governmental plan” under Code Sec. 414(d) has yet to be issued. The IRS, working with the Department of Labor and Pension Benefit Guaranty Corporation, has been working for several years to provide this guidance that is eagerly anticipated by governmental plan sponsors who have faced a number of questions relating to quasi-governmental and privatized governmental employees.

Church Plans

The guidance plan includes guidance on procedures for ruling requests under Code Sec. 414(e), which have been the subject of a moratorium for some time. These procedures may include a notice requirement to participants, and provide additional guidance on the definition of a church plan.

457(b) Plans

457(b) plans may provide for a distribution in the event of an “unforeseeable emergency.” The current definition of “unforeseeable emergency” under Code Sec. 457(b) varies slightly from the Code Sec. 401(k) definition of “hardship.” The guidance plan indicates that additional guidance on “unforeseeable emergency” distributions are likely to be forthcoming.

DB(k) Plans

The Pension Protection Act of 2006 added a new type of hybrid defined benefit-defined contribution plan that combines a defined benefit plan with a 401(k)

feature effective January 1, 2010. After requesting comments last year, the guidance plan indicates that additional guidance is forthcoming. Practitioners and sponsors of pre-approved plans are hoping for detailed additional guidance that enable the implementation of these plans in 2010.

Miscellaneous Issues

HEART Act

The Heroes Earnings Assistance and Relief Tax Act of 2008 (HEART Act)¹³ was enacted in 2008. The guidance referenced on the guidance plan was issued in late January (Notice 2010-15) to clarify the optional and required plan provisions for employees on active duty, such as that differential pay is not required to be counted for all plan purposes. With the general HEART Act December 31, 2010, statutory amendment deadline approaching (and the provisions already effective in operations), many plan sponsors were eager for this guidance. Comments on this guidance are due April 19, 2010, which may include requesting sample plan amendment language.

Cycle A Cumulative List

As with recent years, the guidance plan includes the issuance of the cumulative list for the next determination letter cycle beginning after the conclusion of the current guidance plan period. After five years of the current determination letter program, Cycle A individually designed plans (e.g., plans whose sponsors have an employer identification number ending in “1” or “6”) will need to again be updated and submitted into the determination letter process. The Cycle A filing period will run from February 1, 2011, to January 31, 2012.

International Tax Issues Related to Tax-Favored Retirement Plans

The 2009 report from the Advisory Committee and Government Entities had a specific focus on international employee benefits issues and recommended additional guidance on the tax treatment of retirement payments to nonresident aliens and citizens of Puerto Rico and other U.S. territories. As part of a renewed focus to closing the tax gap and proper 1042-S reporting, anticipate additional guidance (and educational materials) that may address the proper tax and reporting treatment for payments to nonresident aliens, certain expatriates, and residents of U.S. territories.

ENDNOTES

- ¹ Pension Protection Act of 2006 (P.L. 109-280).
² Notice 2006-107, 2006-2 CB 1114.
³ Notice 2008-7, IRB 2008-3, 276.
⁴ See Notice 2009-97.
⁵ Notice 2007-3, 2007-1 CB 255.
⁶ Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16).
⁷ Job Creation and Worker Assistance Act of 2002 (P.L. 107-147).
⁸ Pension Funding Equity Act of 2004 (P.L. 108-218).
⁹ American Jobs Creation Act of 2004 (P.L. 108-357).
¹⁰ Gulf Opportunity Zone Act of 2005 (P.L. 109-135).
¹¹ Rev. Rul. 81-100, 1981-1 CB 326.
¹² Rev. Rul. 2004-67, 2004-2 CB 28.
¹³ Heroes Earnings Assistance and Relief Act of 2008 (P.L. 110-245).

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