ADVISORY COMMITTEE ON
TAX EXEMPT AND GOVERNMENT ENTITIES
(ACT)

Employee Plans:
Analysis and Recommendations Regarding the IRS's Determination Letter Program

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I. EXECUTIVE SUMMARY

The Employee Plans subcommittee of the Internal Revenue Service ("IRS" or "Service") Advisory Committee on Tax Exempt and Government Entities (the "ACT") has endeavored to conduct a comprehensive review of the staggered determination letter program that has been implemented by the Service. The ACT believes now, near the end of the first five-year Cycle period for individually-designed plans and the first two-year restatement period for preapproved defined contribution plans, is the opportune time to conduct such a review, as enough time has passed and experience been garnered that meaningful analysis and recommendations can be made, and changes in course can be made prior to the next full Cycle commencing in February 2011. In order to gather the necessary information for this review, the ACT has reached out to all types of stakeholders in the benefits community for input and suggestions, including but not limited to IRS Employee Plans specialists, plan sponsors, benefits attorneys, actuaries, accountants, third party administrators, consultants, plan document providers and organizations representing participants.

This Report provides an historical overview of the Service's determination letter program and includes insights and commentary on the current program received from practitioners. The Report also includes several recommendations that are based on the surveys conducted by the ACT with various stakeholders in the benefits community. These recommendations propose changes to the Service's current determination letter program which are intended to further the Service's goal of ensuring that the rights of plan participants and beneficiaries are adequately protected, and also foster a reasonable expectation among plan sponsors that they will be able to achieve, with reasonable time, expense and commitment, compliance under the applicable qualification rules.

A substantial portion of the ACT's findings relate to the current interim amendment requirement, which is placing a heavy burden on the entire private pension system. The fact that Congress explicitly superseded the existing interim amendment rules in each of the last three pieces of employee benefits legislation is also indicative of the need to reform these rules.[1] The ACT recommends that these interim amendment rules be modified and that future plan amendment adoption deadlines be clarified. With respect to governmental plans, the ACT recommends that better guidance and supporting

The Project Leader, Marcia S. Wagner, gratefully acknowledges her husband, Craig White, and their children, Jessica Hope, Olivia Faith, Cassandra Charity and Craig Isaac, for their love, support and understanding during the development of this Report.

[1] The three pieces of employee benefits legislation include the Pension Protection Act of 2006, Pub. L. No. 109-280 (2006), the Worker, Retiree, and Employer Recovery Act, Pub. L. No. 110-458 (2008) and the Heroes Earnings Assistance and Tax Relief Act, Pub. L. No. 110-245 (2008).

information that address the particular problems of governmental plans be provided to plan sponsors seeking favorable determinations. Similarly, the ACT recommends that the Service address several specific issues in connection with its development of an approval letter program for § 403(b) plans.

The Report also includes recommendations for changes to the determination letter program that the Service may wish to consider in order to: (i) improve customer service, (ii) streamline the determination letter process, (iii) improve its coordination with the Service's Employee Plans Compliance Resolution System, and (vi) prioritize certain off-cycle filings. The ACT recommends that the Service create a taxpayer advocate or designated EP determination letter specialist for resolution of unique issues that arise during the determination letter process and modify its prior plan documentation requirements for employers that do not have copies of their most recent determination letters. In addition, this Report includes other related recommendations with respect to the Service's determination letter program, including suggestions related to funding, training and staffing for the EP Determinations unit.

The ACT respectfully submits this Report with the hope that its findings and recommendations will be helpful in maintaining and strengthening the United States retirement system.

II. INTRODUCTION

In order to receive tax-preferred treatment under the Internal Revenue Code ("IRC" or the "Code"), a retirement plan and its related trust must satisfy the requirements of IRC §§ 401(a) and 501(a), respectively, for the tax year in which the employer is claiming the deduction and the tax year in which employees are deferring receipt of compensation. IRC § 401(b) sets forth the deadline by which the terms of the plan may be retroactively amended to satisfy these qualification requirements. These deadlines are extended by statute if the plan sponsor timely requests a favorable determination letter regarding the terms of the plan and related trust. Such deadlines may also be extended at the discretion of the Service. The division within the IRS that has the authority to issue favorable determination letters is the Tax Exempt/Government Entities ("TE/GE") Division. The effect of a favorable determination letter is similar to that of receiving a favorable private letter ruling from the Service.[2] While the plan sponsor is not required to request a favorable determination letter, the Code requires the IRS to opine if a favorable determination letter is requested.

From 1942 to 1974, the IRS experienced a relatively stable number of favorable determination letter requests regarding the qualified status of retirement plans. Due to the enactment of the Employee Retirement Income Security Act of 1974 ("ERISA") and other major pieces of subsequent legislation governing employee benefit plans,[3] the Service experienced major cyclical fluctuations in determination letter requests, requiring it to periodically divert resources away from plan examinations and towards plan document review and compliance.

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2 Rev. Proc. 2009-1, 2009-1 I.R.B. 1, § 13.01.

3 Employee Retirement Income Security Act (ERISA) of 1974, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 26 and 29 U.S.C.). The other major changes included: Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, Pub. L. No. 97-248, 96 Stat. 324 (codified as amended in scattered sections of 26 U.S.C.); Deficit Reduction Act (DEFRA) of 1984, Pub. L. No. 98-369, 98 Stat. 494 (codified as amended in scattered sections of 26, 29, and 42 U.S.C.); Retirement Equity Act (REA) of 1984, Pub. L. No. 98-397, 98 Stat. 1426 (codified as amended in scattered sections of 26 and 29 of U.S.C.); Tax Reform Act (TRA) of 1986, Pub. L. No. 99-514, 100 Stat. 2085 (codified in scattered sections of 26 U.S.C.); GUST (the acronym used to refer to multiple acts to which the Service applied a single plan amendment deadlines as a matter of administrative feasibility) which includes: Uruguay Round Agreements Act of 1994, Pub. L. No. 103-465, 108 Stat. 4809 (codified as amended in scattered sections of 17, 19, and 26 U.S.C.), Uniformed Services Employment and Reemployment Rights Act (USERRA) of 1994, Pub. L. No. 1032-353, 108 Stat. 4172 (codified as amended in scattered sections of 28 U.S.C.), Small Business Job Protection Act (SBJPA) of 1996, Pub. L. No. 104-188, 110 Stat. 1755 (codified as amended in scattered sections of 26 U.S.C.), Taxpayer Relief Act (TRA) of 1997, Pub. L. No. 105-34, 111 Stat. 788 (codified as amended in scattered sections of 26 U.S.C.), Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 26 U.S.C.), and Community Renewal Tax Relief Act of 2000, Pub. L. No. 106-554, 114 Stat. 2763 (codified as amended in scattered sections of 26 U.S.C.), Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001, Pub. L. No. 107-16, 115 Stat. 38 (codified as amended in scattered sections of 26 and 29 U.S.C.); Pension Protection Act (PPA) of 2006, Pub. L. No. 109-280, 120 Stat. 780 (codified as amended in scattered sections of 26 and 29 U.S.C.).

Thus, in 2001, the IRS began a comprehensive review of its policies and procedures for issuing determination letter requests. Through the release of two White Papers, discussions with practitioners, and the release of a draft revenue procedure, the IRS revised its determination letter program in Revenue Procedure 2005-66,[4] which formally adopted a new system of cyclical remedial amendment periods ("RAPs") governing applications for a determination letter. At that time, the Service agreed that it would continue to evaluate how the program was working, identify potential problems and make recommendations during the initial years of the program's implementation. To that end, the Service has conducted a review, which is discussed in Part IV. D. of this Report.

To assist the IRS in its review, the Employee Plans subcommittee of the TE/GE's Advisory Committee has undertaken an analysis to determine what may be learned from the new process, whether it has been successful in its goals, and what may be recommended as improvements. In this endeavor, the ACT has reached out to all stakeholders (e.g., IRS Employee Plans specialists, plan sponsors, benefits attorneys, actuaries, accountants, third party administrators, consultants, master and prototype ("M&P") sponsors and volume submitter ("VS") providers[5]) for input and suggestions. The ACT also worked collaboratively with the IRS to provide and produce a report of practical importance and significance.[6] The goal is to create a determination letter program that functions efficiently so as to promote the viability and vitality of the employer-provided retirement system for all employers – small, medium and large. To that end, the ACT Report is divided into various components – Part III provides historical information regarding the Service's determination letter program; Part IV analyzes the Service's internal review and recommendations regarding the new determination letter program and the input of Employee Plans Specialists; Part V summarizes the results of the ACT's survey conducted with various stakeholders; Part VI provides the ACT's recommendations involving policy issues; and Part VII summarizes the ACT's recommendations involving administrative issues.

The importance of a robust yet reasonable determination letter program should be emphasized. The private pension system, while voluntary, imposes significant responsibilities and liabilities on plan sponsors and fiduciaries, particularly plan

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[4] Rev. Proc. 2005-66, 2005-2 C.B. 509, modified and superseded by Rev. Proc. 2007-44, 2007-28 I.R.B. 54.

[5] In Rev. Proc. 62-23, 1962-2 C.B. 487, § 3.02, the Service defines M&P and VS as follows: a "master plan" as a "standardized form of plan, with a related form of trust (or custodial) agreement, where indicated, administered by a bank or insurance company each acting as the funding medium for the purpose of providing plan benefits on a standardized basis," whereas the term "prototype plan" referred "to a standardized form of plan, with or without a related form of trust (or custodial) agreement, which is made available by the sponsoring organization, for use without change by employers who wish to adopt such a plan, and which will not be administered by the sponsoring organization which makes such form available."

[6] See Section IX. A. for the extensive list of persons and entities who have provide input to the ACT.

sponsors. As a result, it is important for plan sponsors to ensure that their plan documents satisfy the requirements of the law, and can assure themselves of this by the issuance of a favorable determination letter from the Internal Revenue Service. Moreover, the accounting profession typically requires a copy of a recent determination letter in order to issue a clean auditor's report.

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III. BACKGROUND

A. Reasons for a Determination Letter Program

Retirement plans that satisfy the requirements of IRC § 401(a) are qualified and therefore extended favorable tax treatment. Treasury regulations require that a qualified retirement plan must be a definite written program established and maintained by an employer and that it satisfy the requirements of IRC § 401(a) in form (i.e., the terms of the plan document must comply with the law), in operation (i.e., the plan must be operated in compliance with its terms and in compliance with the qualification requirements of IRC § 401(a)), and demographically (i.e., the plan must satisfy the Code's various nondiscrimination tests, even as the plan sponsor's employee workforce changes).[7]

The IRS's determination letter program permits a plan sponsor to have the IRS review the form of the plan for compliance. The Service refers to this as "up-front compliance."[8] Such compliance does not protect the plan sponsor from plan operational or demographic failures. Thus, failure to comply with either the plan form, or the operational or demographic qualification requirements (referred to as a "disqualifying provision") of the Code subjects the plan to potential disqualification. The IRS has the power to disqualify a plan should it contain a "disqualifying provision," and the courts have affirmed this authority, irrespective of the significance of the defect, the innocence of the wrongdoer, or the unreasonableness of disqualification compared to the violation committed.[9] The Service also contends that once a disqualifying provision occurs, the plan remains disqualified until the defect is rectified, regardless of the statute of limitations.[10]

While the determination letter program has been designed to assure plan document compliance, the IRS also has a correction program to assure plan operational and demographic compliance and to permit certain retroactive plan amendments to assure

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[7] Treas. Reg. § 1.401-1(a)(2).

[8] *The Future of the Employee Plans Determination Letter Program: Some Possible Options, available at* www.irs.gov/irs-tege/paper1.pdf. The Service used the expression "up-front compliance" as the determination letter program, as it then existed, ensured that the form of the plan document or plan amendments is qualified from its inception. Such approach was traditionally viewed as the preferred method to ensure future compliance.

[9] See e.g., Buzetta Construction Corp., v. Comm'r., 92 T.C. 641 (1989); Martin Fireproofing Profit Sharing Plan and Trust v. Comm'r., 92 T.C. 1173 (1989); Basch Engineering Inc., v. Comm'r., 59 T.C.M. 482 (1990).

[10] Under the tainted asset theory, if a plan becomes disqualified for more than five years with money remaining in the plan, the IRS can disqualify the plan even for years barred by the statute of limitations. See Rev. Rul. 73-79, 1973-1 C.B. 194 and Martin Fireproofing Profit Sharing Plan and Trust v. Comm'r., *supra* note 9.

plan document compliance. This correction program is known as the Employee Plans Compliance Resolution System ("EPCRS").[11]

B. IRS's Determination Letter Program in Pre-ERISA Years

Early on, the Service established the authority and procedures by which the District Directors could determine the disposition of requests regarding the qualification of retirement plans.[12] By 1954, the Service referred to such disposition responses as "determination letters."[13] A determination letter was defined as "a written statement issued by a District Director of Internal Revenue in response to an inquiry by an individual or an organization, and solely by way of application to the facts involved in a particular inquiry or request of the principles and policies previously established by the National Office."[14] Such letters would be issued "only where a determination can be made on the basis of clearly established rules as set forth in the statute, Treasury Decisions or Regulations, or rulings, opinions or court decisions published in the Internal Revenue Bulletin."[15] The determination letter grew in importance as the plan sponsor could now rely on a favorable determination letter from the Service, absent a revocation of such determination. The authority of the District Offices to issue determination letters was, at this time, discretionary.[16]

Since then, the determination letter program has undergone several changes to accommodate changes in the law and clarifications in the procedure. The first notable change followed the Internal Revenue Act of 1954. Prior to the Act, employee plans qualified for favorable tax treatment under IRC §165, whereas after the Act, plans became qualified under IRC § 401. Thus, in 1956, the Service issued Revenue Procedure 56-8,[17] amending its determination letter procedures to reflect the legislative changes and listing the specific issues with respect to which the District Offices would issue determination letters:

- Initial qualification of stock bonus, pension, profit sharing and annuity plans under IRC § 401(a);

[11] See Rev. Proc. 2008-50, 2008-35 I.R.B. 464 for the rules governing the use of EPCRS. See also Wagner, Marcia and Cohen, Diane, EPCRS – Plan Correction and Disqualification, BNA Tax Management Portfolio (2010).

[12] Rev. Rul. 32, C.B. 1953-1, as referenced in Rev. Rul. 54-172, 1954-1 C.B. 394.

[13] Rev. Rul. 54-172, 1954 -1 C.B. 394 at § 4.01, *amplified by* Rev. Proc. 56-33, 1956-33, 1956-1 C.B. 1394, *modified by* Rev. Proc. 56-12, 1956-1 C.B. 1029, Rev. Proc. 60-6, 1960-1 C.B. 880 and *superseded b*y Rev. Proc. 62-28, 1962-2 C.B. 496.

[14] *Id*. at § 2.03.

[15] *Id.*

[16] *Id*. at § 5.01.

[17] Rev. Proc. 56-8, 1956-1 C.B. 1024.

- Initial exemption from federal income tax under IRC § 501(a) of trusts forming a part of such plans;

- Amendments, curtailments, or terminations of such plans and trusts; and

- Effect on the qualification of such plans and the exempt status of such trusts where plan assets were invested in the stocks or securities of the employer.

Later that year, the Service added to this list amendments that were made to existing qualified trusts participating in a common pension fund or group trust.[18]

The next significant change to the determination letter program came in 1963 as a result of the Self-Employed Individuals Tax Retirement Act of 1962. Revenue Procedure 62-23[19] authorized the issuance of determination letters to self-employed plans. It also authorized the Service's National Office to issue opinion letters as to the acceptability of M&P plans under IRC § 401(a) for use by self-employed individuals.[20] Such rulings did not constitute a determination, as an adoptee of a M&P plan still needed to request an individual determination letter.[21] Then in 1969, the Service approved procedures for issuing determination letters for M&P plans for use in the corporate arena, as well as the self-employed arena.[22]

C. IRS's Determination Letter Program: ERISA and Post-ERISA Years

The passage of ERISA in 1974 brought a wave of changes to the determination letter program. In September 1974, the Service temporarily suspended the issuance of determination letters for new individually designed plans[23] and of opinions on the acceptability of new M&P plans.[24] Determination letters issued to pre-existing plans before the passage of ERISA became ineffective for plan years beginning after December 31, 1975.

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[18] Rev. Proc. 56-42, 1956-1 C.B. 54, § 3.

[19] Rev. Proc. 62-23, 1962-2 C.B. 487.

[20] *Id*. at § 3.02.

[21] *Id*. at § 3.03.

[22] Rev. Proc. 68-45, 1968-2 C.B. 957.

[23] Rev. Proc. 74-38, 1974-2 C.B. 492, § 4.07.

[24] Rev. Proc. 74-39, 1974-2 C.B. 494, § 3.03, *superseded by* Rev. Proc. 75-51, 1975-2 C.B. 590, *modified by* Rev. Proc. 75-38, 1975-2 C.B. 567 and Rev. Proc. 74-40, 1974-2 C.B. 494; *superseded by* Rev. Proc. 75-52, 1975-2 C.B. 592, *modified by* Rev. Proc. 75-42, 1975-2 C.B. 575.

In 1975, the Service resumed issuing opinion letters and determination letters.[25] As part of its preliminary guidance, the Service established standardized forms for applying for determination letters:

- Form 5300 for defined benefit plans;
- Form 5301 for defined contribution plans; and
- Form 5303 for collectively bargained plans.[26]

Prior to 2002, subsequent changes to the Service's procedures included:

- In 1977, the creation of the "pattern plan" whereby a law firm could obtain approval from a District Director as to the form of a pattern plan which the firm intended to use in submitting determination letter applications on behalf of its clients, limited to certain types of defined contribution plans;[27]
- Appeals of an adverse determination letter from a District Office could be made to the appropriate Regional Office and then to the National Office, and finally to the Tax Court once all administrative remedies were exhausted;[28]
- Establishment of the "short form" (Form 5307) for those seeking favorable determinations on an already approved M&P plan;[29]
- Creation of the "field prototype plan" under which a firm (other than a trade or professional association, bank, insurance company or regulated investment company) with at least ten (10) clients could obtain approval from Key District Directors of the form of a plan which the sponsors contemplate using as a field prototype plan, for both defined benefit and defined contribution plans, but not for plans with self-employed participants;[30]
- As of 1980, adopters of standardized "self-employed" M&P plans could rely on a favorable opinion obtained by the plan's sponsor whereas adopters of a "corporate" M&P plan needed to obtain an individual determination letter for reliance;

[25] Rev. Proc. 75-47, 1975-2 C.B. 581; Rev. Proc. 75-48, 1975-2 C.B. 583.

[26] *Id.* at § 4.02.

[27] Rev. Proc. 76-15, 1976-1C.B. 553, at § 2.02.

[28] Rev. Proc. 77-25, 1977-2 C.B. 534, § 5.

[29] Rev. Proc. 77-22, 1977-2 C.B. 529.

[30] Rev. Proc. 77-23, 1977-2 C.B. 530, § 2.02.

- In 1984, unification of the distinct "corporate" and "self-employed" M&P plans and reliance by the corporate standardized M&P adopters on the favorable opinion obtained by the plan sponsor;[31]

- Creation of an experimental "mass submitter" program, providing preference to a sponsoring organization provided at least ten (10) such organizations adopt the plan "word for word." This was created in response to the volume of opinion letter submissions generated by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA");[32]

- In 1988, the establishment of a fee schedule for rulings, opinions and determinations, pursuant to the Revenue Act of 1987;[33]

- In 1989, the establishment of the "volume submitter" ("VS") program which required a submitter to have at least thirty (30) determination letter applications for plans that are substantially identical to a previously approved lead plan;[34] and

- In 2001, a simplification of the determination letter application process, which included the optional submission of demographic data to show compliance with the Code's and ERISA's coverage and nondiscrimination requirements.[35]

D. Role of IRC § 7476

While nothing in the Code compels a plan sponsor to seek a determination letter, IRC § 7476 provides the Tax Court with the power to issue a declaratory judgment with respect to the qualification of a retirement plan if the IRS fails to make a determination regarding the plan's qualification, provided the petitioner has exhausted administrative remedies within the IRS.[36] Such statutory requirement thus mandates the Service to issue determination letters upon request.

[31] Rev. Proc. 84-23, 1983-2 C.B. 457.

[32] *Id*. The mass submitter program was made permanent in 1989. Rev. Proc. 89-9, 1989-1 C.B. 780, § 4.04.

[33] Rev. Proc. 88-8, 1988-1 C.B. 628. The fee schedule, set forth in Rev. Proc. 89-4, 1989-1 C.B. 767, § 6.03, was structured to create economic incentives to use the mass submitter or volume submitter programs.

[34] Rev. Proc. 89-4, 1989-1 C.B. 767, § 2.03. The volume submitter plan does not require the plan adopters to be a "sponsoring organization" (bank, insurance company, etc.) as with the mass submitter plan.

[35] Announcement 2001-77, 2001-2 C.B. 83, § I.

[36] Section 7476 of the Code was added by ERISA § 1041(a), 88 Stat. 949. See Treas. Reg. § 601.201(o)(10), specifying when administrative remedies with the IRS have been exhausted. See also

When ERISA was passed in 1974, IRC § 7476 provided that interested employees and the Pension Benefit Guaranty Corporation, as well as employers and trustees, could petition the Tax Court regarding an employer's request for a determination letter.[37] This judicial remedy was available if the IRS had issued an unfavorable determination letter or had failed to issue a determination after exhaustion of administrative remedies. The issue then arose as to whether this judicial remedy was available if the IRS rendered a plan disqualified upon a subsequent audit (due to operational failures) even though the employer had a favorable determination letter regarding the initial qualification of the plan. After an adverse ruling in Tax Court,[38] the statute was amended to empower the IRS to retroactively disqualify a plan which previously had a favorable determination letter.[39] However, in the absence of a change in law or guidance, or operational or demographic defects, it is rare for the Service to revoke a previously issued favorable determination letter.[40]

E. Role of IRC § 401(b)

Closely tied to the issue of disqualification, especially retroactive disqualification, is the role of IRC § 401(b). This section sets forth the rules that determine the deadline by which a plan must be retroactively amended as a result of changes in the law or published guidance that is necessary to keep the plan qualified. This period of time—between the date the change in the law or guidance is effective and the deadline under IRC § 401(b) for adopting the retroactive plan amendment—is referred as the "remedial amendment period" ("RAP"). This period affords plan sponsors additional time for adopting necessary plan amendments.

Under IRC § 401(b), a plan's qualification status is in jeopardy if there exists a "disqualifying provision," which refers to a provision in the plan or absence of a provision in the plan which would cause the plan document to fail to meet the Code's qualification requirements.[41] As long as the plan is retroactively amended by the end of the RAP, it

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McManus v. Comm'r., 93 T.C. 79, 83-86 (1989), collecting cases regarding exhaustion of administrative remedies.

[37] Pub. L. No. 93-406, § 1041(a), effective as to pleadings filed after September 2, 1975.

[38] See Sheppard v. Meyers, Inc., 67 T.C. 26 (1976), where the court held that it lacked jurisdiction to issue a declaratory judgment regarding the plan's qualification status after the IRS issued a favorable determination letter but there was no subsequent plan amendment or plan termination.

[39] See IRC § 7476(a) which now provides for such remedy.

[40] Treas. Reg. § 601.201(l)(5), Statement of Procedural Rules. See also Rev. Proc. 2003-6, 21.04, 2003-1 I.R.B. 191.

[41] Treas. Reg. § 1.401(b)-1(b)(3) defines a disqualifying provision as one that either (1) results in the failure of the plan to satisfy the qualification requirements of the Code by reason of a change in those requirements that is effective after December 31, 2001, or (2) is integral to the qualification requirements of the Code that has been changed effective after December 31, 2001, but only if the provision is integral to the plan provision that is a disqualifying provision under the plan.

will be deemed to be in compliance with the qualification rules. There are certain exceptions to this general rule.[42]

Generally, the RAP ends on the due date of the employer's tax return for the tax year in which the disqualifying provision arose.[43] However, by applying for a determination letter for an individually designed plan on or before the end of the RAP, the deadline is extended until 91 days after the determination letter is issued.[44] For pre-approved plans, the deadline is extended to six (6) months after the opinion or advisory letter is issued.[45] The Service also has discretion under the remedial amendment rules to extend the time limit for retroactive amendment for plan sponsors who request a determination letter.[46] In recent years, the Service has repeatedly extended the amendment deadlines due to the sheer number of legislative changes and required regulatory guidance.[47]

In contrast, any other amendment made to a qualified plan not required for legal compliance is deemed to be discretionary. Such amendment, to the extent it does not result in a cutback of benefits, must be generally adopted by the end of the plan year in which the provision was first effective.[48] However, it is not always obvious whether part or all of a plan amendment is mandatory (in order to avoid a "disqualifying defect") or discretionary. For example, a regulation may be promulgated interpreting the qualification requirements of IRC § 401(k) and providing an optional safe harbor – use of the safe harbor is discretionary, whereas the other portions of the regulation are mandatory.

F. Overhaul of the IRS's Office of Employee Plans

Major IRS reform legislation occurred under the Internal Revenue Service Restructuring and Reform Act of 1998 ("RRA '98"), establishing an office of employee plans and exempt organizations. Thus, the division of Tax Exempt and Government Entities

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[42] Exceptions include: plan changes that reduce a protected benefit (as defined under IRC § 411(d)(6)) are required to be made before the change is effective; the law itself may grant an extension (e.g., the Pension Protection Act of 2006 delayed the plan amendment deadline until the 2009 plan year); IRC § 412(c)(8) provides a funding exception of 2½ months after the close of the plan year; and Treas. Reg. § 1.401(a)(4)-11(g) provides for corrective amendments relating to coverage and discrimination testing that may be made within 9½ months after the close of the plan year.

[43] IRC § 401(b) (2006).

[44] Treas. Reg. § 1.401(b)-1(e)(3) (as amended in 2009).

[45] Treas. Reg. §§ 1.401(b)-401-1(e)(1)-(2) (as amended in 2009).

[46] Treas. Reg. § 1.401(b)-1(f) (as amended in 2009).

[47] For example, Rev. Proc. 2005-66, 2005-2 C.B. 509, *modified and superseded by* Rev. Proc. 2007-44, 2007-28 I.R.B. 54, extended the EGTRRA remedial amendment period to the end of the initial five- and six-year remedial cycles for qualified plans.

[48] Rev. Proc. 2007-44, 20077-28 I.R.B. 54, § 5.05(2).

("TE/GE") was formed to serve employee benefit plans, tax exempt organizations, tax exempt bonds and government entities (federal, state and local, and tribal governments). The TE/GE Division replaced the unit of the former Assistant Commissioner (Employee Plans and Exempt Organizations), which was established by ERISA. Area Managers replaced Key District Directors. Employee Plans ("EP") Rulings and Agreements is a division of TE/GE and is responsible for the issuance of determination letters. Presently, Revenue Procedure 2010-6[49] sets forth the procedures for issuing determination letters on qualified retirement plans and related trusts. The issuance of determination letters is now centralized—all determination letter applications are submitted to the Cincinnati Campus in Covington, Kentucky, whereas pre-approved plan requests are submitted to the Pre-Approved Plan Coordinator EP Determinations in Cincinnati, Ohio.

G. Comprehensive Overhaul of the IRS's Determination Letter Program

Since most plan sponsors apply for a determination before the end of the RAP, affording them more time to make such amendments, the Service has experienced peaks and valleys in the submission of determination letter requests. Since ERISA's passage, the IRS has experienced the following number of determination letter submissions:

Year	Act	Approximate Number of Requests
1978	ERISA	In excess of 200,000
1986	TEFRA/DEFRA/REA	In excess of 450,000
1994	TRA '86	Almost 200,000
2002	GUST	Approximately 225,000

The net result was a financial and manpower toll on the IRS, forcing it to pull examination agents away from audit or other programs and re-train them so that they could review determination letter requests. The IRS announced changes to the determination letter program in Announcement 2001-77,[50] relieving plan sponsors from some of the prior program's burdens. The Service's introduction of a new processing system, known as the Tax Exempt Determination System ("TEDS"), was intended to speed up the internal process for issuing determination letters.[51] As of 2002, the decline in such requests reflected the fact that the majority of plan sponsors had moved to pre-

[49] 2010-I.R.B. 193. This revenue procedure is revised annually. See also Department of Treasury, Internal Revenue Service, No. 794, *Favorable Determination Letter* (2006), for additional information regarding the scope of the determination letter, including the requirement that all information submitted in the application be retained as a condition of reliance.

[50] Announcement 2001-77, 2001-2 C.B. 83.

[51] TEDS is currently being used by the IRS to electronically store all images and case data for initial determination applications, providing immediate access to such information without the movement of paper case files from one location to another. Currently, determination letter applications can be processed in TEDS up to the point of closure.

approved plans and away from individually designed plans. However, the continuance of peaks and valleys has taken its toll on the IRS.

In an attempt to consider alternatives to the then existing determination letter program, the IRS issued its first White Paper entitled The *Future of the Employee Plans Determination Letter Program: Some Possible Options*.[52] On August 8, 2001, it invited the public to participate in a dialogue on the future of the determination letter program, extending the comment period until July 1, 2002.[53] The first White Paper set forth the following alternatives:

- Eliminate the determination letter program
- Replace the current system with a third party certificate program
- Self certification or registration program by plan sponsors
- Stagger the application process and remedial amendment process over five (5) years; or
- Keep the status quo.

With some of these options, the IRS discussed the issue of whether immediate amendments should be required for law changes (e.g., under a staggered remedial amendment process, would immediate amendments nevertheless be required within the staggered period of time *or* would they be delayed to the end of the RAP)?

Based on the comments the IRS received, it issued a second White Paper entitled The Future of the Employee Plans Determination Letter Program: Evaluation of Public Comments and Additional Explanation of Staggered Remedial Amendment Period Option.[54] In the follow-up discussion, the IRS eliminated the first three original options and discussed the last two options. Later, the Service decided to implement the immediate amendment requirement, now commonly referred to as the "interim amendment" requirement.[55]

In Announcement 2004-32,[56] the Service announced that it would proceed with a five-year staggered determination letter program for individually designed plans and a six-year staggered program for pre-approved plans. It then asked for public comments

[52] Announcement 2001-83, 2001-2 C.B. 205.

[53] *Id.*; Announcement 2002-36, 2002-1 C.B. 703.

[54] Announcement 2003-32, 2003-1 C.B. 933.

[55] The interim amendment requirement was not in the draft of the proposed staggered RAP revenue procedure, but was added to the final version.

[56] Announcement 2004-32, 2004-1 C.B. 860.

regarding its draft revenue procedure.[57] The formal revenue procedure, Rev. Proc. 2005-66,[58] established the new determination letter program:

- A five-year staggered determination program for individual designed plans would be based on the employer identification number ("EIN") of the plan sponsor.[59] Each remedial amendment cycle would then end in a different year.[60] The end of a plan's remedial amendment cycle would be the last day by which the plan could be retroactively amended to correct a disqualifying provision, provided, however, that the plan sponsor adopts "good faith interim amendments."

  – Cycle A (for EINs ending in 1 or 6) initial RAP would end January 31, 2007;

  – Cycle B (for EINs ending in 2 or 7) initial RAP would end January 31, 2008;

  – Cycle C (for EINs ending in 3 or 8) initial RAP would end January 31, 2009;

  – Cycle D (for EINs ending in 4 or 9) initial RAP would end January 31, 2010;

  – Cycle E (for EINs ending in 5 or 0) initial RAP would end January 31, 2011.

  – Each cycle's subsequent RAP would end five (5) years later than its prior RAP.

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[57] Announcement 2004-71, 2004-2 C.B. 569.

[58] Rev. Proc. 2005-66, 2005-2 C.B. 509, *modified and superseded by* Rev. Proc. 2007-44, 2007-28 I.R.B. 54.

[59] *Id.* The cycles for three categories of plans would not be based on an EIN: multiple employer plans would be Cycle B, governmental plans would be Cycle C and multiemployer plans would be Cycle D. Note that governmental plans have the option to file in Cycle E instead of Cycle C. See IRS Employee Plans News (Nov. 5, 2008), *available at* http://www.irs.gov/pub/irs-tege/se1108.pdf.

[60] *Id.*

- A six-year staggered determination letter program would apply for pre-approved defined contribution and defined benefit plans.[61]
  - Defined contribution plan sponsors and practitioners would submit opinion or advisory letter requests in year one (which ended January 31, 2006, for defined contribution EGTRRA plans), to be reviewed by the IRS in years 2 and 3, and employers would adopt the updated plans in years 4 and 5 (April 30, 2010, for defined contribution EGTRRA plans).

  - Defined benefit plans would submit determination letter requests in year 3 (which ended January 31, 2008, for EGTRRA plans), to be reviewed by the IRS in years 4 and 5 and employers adopting the updated plans in years 5 and 6 for defined benefit EGTRRA plans.[62]

- The new staggered determination letter program would require timely adopted good faith interim amendments. A good faith interim amendment represents the sponsor's good faith effort to amend the plan to satisfy a particular qualification requirement and must be adopted by the end of the normal IRC § 401(b) RAP (i.e., the due date of the tax return for the year in which the disqualifying provision arose), unless otherwise extended by statute, not the end of the sponsor's staggered RAP. In contrast, a discretionary plan amendment (i.e., one adopted for reasons other than to correct a disqualifying provision) must be made by the end of the plan year for which the amendment is effective.

- The IRS's review of individually designed plans during each applicable Cycle would be based on the most recently issued Cumulative List of Changes in Plan Qualification Requirements, to be published before the commencement of the Cycle.[63] Since the earliest an on-Cycle employer could submit a determination letter request is February 1st, the Service wished to provide some lead time for the required amendments to be made. Hence, the Cumulative List setting forth the plan amendments required for qualification ends as of the October 1st of the prior year. This creates a gap between the

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[61] *Id.* Pre-approved defined contribution plans would have a different six-year cycle than pre-approved defined benefit plans. The first advisory or opinion letter cycle for pre-approved defined contribution plans opened February 17, 2005, whereas the first advisory or opinion letter cycle for pre-approved defined benefit plans opened February 1, 2007. See Rev. Proc. 2005-16, , 2005-1 C.B. 674, *modified and superseded by* Rev. Proc. 2005-66, 2005-2 C.B. 509, and Rev. Proc. 2007-44, 2007-28 I.R.B.

[62] Announcement 2010-20, April 30, 2012.

[63] For Cycle A plans, Notice 2004-84, 2004-52 I.R.B. 1030, *modified by* Notice 2005-95, 2005-2 C.B. 1172, applied to defined contribution pre-approved plans and Notice 2005-101, 2005-52 I.R.B. 1219, applied to individually designed plans. For Cycle B plans, Notice 2007-3 , 2007-2 I.R.B. 255, applied to individually designed plans, pre-approved defined benefit plans and multiple employer plans. For Cycle C plans, Notice 2007-94, 2007-51 I.R.B. 1179, for individually designed plans. For Cycle D plans, Notice 2008-108, 2008-50 I.R.B. 1275, for individually designed plans. For Cycle E plans, Notice 2009-98, 2009-52 I.R.B. 974, for individually designed plans.

amendments that the Service will review for purposes of the determination letter and the amendments that may have actually been made to the plan to maintain its legal compliance but are not listed on the Cumulative List.

- Similarly, the IRS publishes a List of Required Modifications ("LRMs"), which are information packages to assist sponsors of M&P plans to conform to applicable law and guidance.[64]

H. Governmental Plans Initiative

As part of its efforts to overhaul the determination process, in 2007, the IRS launched its Governmental Plans Initiative to expand its knowledge of public sector plans.[65] The IRS is concerned that many state and local entities seem unaware of the importance of compliance with the tax qualification requirements and the value of a favorable determination letter. The IRS wants to bring them into the fold.

The Initiative's first public effort was a Governmental Plans Roundtable held April 22, 2008, to establish a dialogue with the governmental plans community. It was attended by representatives from various state and local retirement systems, consultants, benefits attorneys and actuaries. Over 40 government agencies were represented. The IRS was interested in communicating several messages:

- why tax compliance is critical,
- the need for timely amendments, and
- how the IRS voluntary compliance program can help.

The IRS also wanted to better understand the issues and barriers that governmental plans face in attempting to satisfy tax qualification requirements.[66] To that end, the attendees described actual and potential conflicts between federal law requirements and state constitutional and statutory law protections applicable to public plan benefits; the difficulties of meeting adoption deadlines when the legislative body meets infrequently; the problem of compiling the plan "document" when terms may be incorporated in statutes, ordinances, and regulations and the adoption process does not necessarily produce signed documents; the need for clear guidance in order to identify problems, assess the remedies and convince the decision makers of the need to make

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[64] There is a LRM published for each major set of law changes, and for defined contribution and defined benefit plans separately.

[65] See *Pilot Questionnaire for Governmental Plans Initiative*, Form 14035, Feb. 2009, p. 2.

[66] *Id*., pp. 1-2.

corrections; and the need for IRS personnel trained in and dedicated to the special needs of governmental plans.[67]

The sheer size of the public sector establishes state and local governmental plans as a force to be reckoned with, both in terms of the number of people affected and the amount of assets involved.[68] A 2007 study by the Government Accounting Office estimated that 12 percent of the nation's workforce are employees of state and local governments. Their numbers include public school teachers, police, firefighters, and correctional officers to name just a few categories.[69] A 2008 survey by the Bureau of Labor Statistics found that 84 percent of state and local governmental workers have access to a defined benefit pension plan. Total assets of state and local governmental plans are estimated at $2 trillion.[70]

Historically, federal regulation of public sector plans has been minimal in comparison to the regulation of private sector plans. In large part, the limited oversight is due to Congress's decision to exempt governmental plans from most provisions of ERISA.[71] Governmental plans have been spared from some of the more challenging provisions of the Code as well, including the minimum funding requirements,[72] minimum participation and nondiscrimination requirements,[73] and minimum vesting requirements.[74]

The legislative record indicates that Congress believed that public plans already incorporated generous vesting provisions and that the power of state and local entities to raise funds through taxation ensured they could fulfill their funding obligations for the promised benefits. Some members of Congress worried that imposing ERISA requirements would have unacceptable cost implications for state and local entities. Above all, the principles of federalism made Congress hesitant to allow federal

[67] See *Employee Plans News*, Special Edition, May 9, 2008.

[68] During the Roundtable discussion Steven Miller, Commissioner, Tax Exempt and Government Entities pointed out that one out of five employees in the United States is a government employee and that governmental plans hold $3.5 trillion in assets.

[69] *Public Fund Survey, Summary of Findings for FY 2008*, prepared by Keith Brainard, National Association of State Retirement Administrators, October 2009.

[70] *The Structure of State and Local Government Retirement Benefits, 2008*, William J. Wiatrowski, Bureau of Labor Statistics, U.S. Department of Labor, *posted* February 25, 2009.

[71] 29 U.S.C. §§ 1004(b), 4021(b).

[72] IRC § 412(e)(C).

[73] IRC § 401(a)(5)(G).

[74] IRC § 411(e)(1)(A). However, in order to maintain qualification, governmental plans must satisfy the vesting requirements of pre-ERISA §§ 401(a)(4) and 401(a)(7).

regulation to interfere in the relationship between state and local governments and their employees.[75]

Because of the ERISA exemption, public plans are regulated to a large extent by a mixture of state and local constitutional and contractual law and certain Code requirements. Specific plan terms generally are set out in statutes, ordinances, promulgations and policies that are unique to each jurisdiction. The principal qualification requirements they share with private employer plans are limited to the written plan requirement of IRC § 401(a), the exclusive benefit rule of IRC § 401(a)(2), the compensation limit of IRC § 401(a)(17), the IRC § 415 limits on compensation and benefits, the minimum required distribution rules in IRC § 401(a)(9), the mandatory rollover rules in IRC § 401(a)(31) and the requirements applicable to retiree health benefit accounts within a pension plan in IRC § 401(h).

Since holding the Roundtable, the IRS has taken other significant steps to address barriers to compliance, particularly those related to the determination letter process. It established the Governmental Plans Web page[76] where members of the governmental plans community can submit questions, comments and suggestions and find the most recent information on relevant IRS guidance in one place. The IRS also has sent a pilot questionnaire to 25 randomly selected governmental plans to elicit demographic information and information on plan documentation, administration, communication, and the structure of public retirement systems. The IRS intends to use feedback from the pilot to refine the questions that will be sent to a larger group of state, county and local governmental plans.

The IRS also has given governmental plan sponsors, whose plans initially were scheduled for submission in Cycle C (deadline January 31, 2009), a one-time opportunity to delay submission to Cycle E (deadline January 31, 2011) based on feedback it received about obstacles to governmental plans' filing within the Cycle C timeframe.[77] Importantly, the IRS has used its dedicated governmental plans Web page to post responses to frequently asked questions ("FAQs") regarding the determination letter and voluntary processes specific to governmental plans.[78]

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[75] H.R. Rep. No. 533, 93d Cong., *reprinted in* 1974 U.S. Code Cong. & Ad. News 4667 (generous vesting provisions); S.Rep. No. 383, 93rd Cong., *reprinted in*, 1974 U.S. Code Cong. & Ad. News 4965 (tax power ensures adequate funding); H.R. Rep. No. 807, 93d Cong., *reprinted in* 1974 U.S. Code Cong. & Ad News 4829-4830 (cost implications); 1 *Legislative History of ERISA* 220 (1976) (federalism), *cited in* Feinstein v. Lewis, 477 F. Supp. 1256 (SDNY 1979).

[76] *Available at* http://www.irs.gov/retirement/article/0,,id=181779,00.html.

[77] Rev. Proc. 2009-36, 2009-35 IRB 304, § 4, Aug. 12, 2009; *Employee Plans News*, Special Edition, November 5, 2008.

[78] *Available at* http://www.irs.gov/retirement/article/0,,id=184690,00.html and http://www.irs.gov/retirement/article/0,,id=184417,00.html.

IV. THE IRS'S INITIAL EXPERIENCE WITH THE NEW DETERMINATION LETTER PROGRAM

The ACT directly solicited the opinions of many employees in Treasury and the Service (see Section IX. A. 1. for list of such persons). Furthermore, the ACT solicited the opinion of all EP Specialists working with determination letters – persons "in the trenches" – for their input and thoughts (see Section IX. B. for memorandum sent to such persons from Vickie A. Surguy, and Section IX. C. for a transcription of the EP Specialist survey results). What follows is a summary of our findings.

A. Expected versus Actual Determination Letter Submissions

The following table sets forth the Service's expected number of determination letter submissions for each Cycle versus the actual number of determination letter submissions for Cycles A, B, C and D and projected number of determination letter submissions for Cycle E:[79]

Form	Projected Cycle A	Actual Cycle A	Projected Cycle B	Actual Cycle B	Projected Cycle C	Actual Cycle C	Projected Cycle D	Actual Cycle D[80]	Projected Cycle E
5300	10,800	7,244	7,800	9,989	11,500	6,844	11,500	7,861	7,000
5307	16,000	6,774	16,000	4,907	11,000	3,281	121,000[81]	12,620	2,000
5310	8,000	3,663	8,000	3,275	4,000	3,307	4,000	2,902	4,000
Total	34,800	17,681	31,800	18,171	26,500	13,432	136,500	23,383	13,000
Closed %		97%		83%		43%		8%	

There were two unrealized assumptions under the original projections:

- It was anticipated that there would be an annual average rate of 16,000 Form 5307 applications, but the Service closed the Form 5307 program as it switched from GUST to EGTRRA. Hence, the actual number of Form 5307 submissions dropped significantly.

[79] Forms 5300 are based on 2/1 to 1/31 dates; Cycle A started 2/1/06; Forms 5310 and Form 5307 are based on FY of 10/1 to 9/30.

[80] The above numbers are as of April 7, 2010.

[81] This number is high because of the anticipated Form 5307 influx for pre-approved plans.

- It was anticipated that there would be an annual average rate of 8,000 Form 5310 applications, whereas the actual number dropped to approximately 4,000 per year.

For the Service, the new staggered determination letter procedure has leveled out the annual number of individually designed plan submissions for the first four Cycles; however, what the Service did experience was what it refers to as "mini-spikes," specifically, approximately 75 percent of the submissions came to the Service in the final weeks of the Cycle, which created instant backlogs in inventory. The Service would clearly prefer that submissions come in ratably during the Cycle year. In addition, case age (i.e., the time to process a submission) may be reduced if the applications were received ratably throughout the year. The average case age is 189 days, as compared to the case age of 467 days prior to the implementation of the staggered determination letter approach. Hence, the turnaround time on determination letter submissions has greatly improved, but further improvements can and should be made.

B. Successes of the New Determination Letter Program

The Service is generally pleased with the new determination letter program as it has eliminated major inventory spikes that have burdened it since the passage of ERISA. The Service has been able to process defined contribution pre-approved lead plans and individually designed cases with all EP determination specialists, no longer having to rely on the use of exam agents; it successfully completed the review of all the defined contribution pre-approved plans by the end of March 2008, within two (2) months of its target date.

C. Challenges for the Service (initial and ongoing)

Initially, the Service experienced a number of challenges: the five-month period between the issuance of Revenue Procedure 2005-66[82] and the beginning of Cycle A submissions made it difficult for EP to prepare for a major business change; the assignment of Cycle A plans to staff was delayed until September 2006; new internal controls and pre-screening procedures had to be implemented; and problems with the publication system delayed the issuance of Alert Guidelines until September and October of 2006.

Ongoing challenges for the Service include: issuance of annual Cumulative Lists, annual lists of Interim Amendments and annual Alert Guidelines; and internal quality control documents (e.g., recurring issue reports and worksheets, termination issue focus, and pre-screening criteria and tools).

[82] Rev. Proc. 2005-66, 2005-37 I.R.B.509.

D. Problem Areas for the Service

1. Interim Amendments

The IRS has experienced some unforeseen consequences of the interim amendment rule. There has been a dramatic increase in the number of plans requiring interim amendment corrections through the voluntary correction program ("VCP") under EPCRS or through closing agreements ("CA"). Either rectification method results in a monetary sanction for the plan sponsor, which was not the case under the prior determination letter rules. Since the commencement of Cycle A, the Service has entered into approximately 160 CAs, including an umbrella CA affecting over 600 plans, to resolve interim amendment nonamender issues in determination letter application cases. The revenue procedure governing EPCRS was altered in 2006 to address this problem by adding a special procedure (Appendix F) for such plans, effective September 1, 2006.[83] During the first six months of Appendix F's availability, 463 interim nonamender VCP cases were closed; during the fiscal year 2008, 703 interim nonamender VCP cases were closed. While the average hours per Appendix F case was about two hours, there was still a significant impact on the workload of the VCP staff due to the volume of cases.

The interim amendment requirement has increased the amount of the EP determination specialist's review time, generally between one to two hours per case. However, as time progresses, by the time the specialists reach Cycle E and each Cycle year thereafter, there could be up to five or more sets of separate interim amendments required to be submitted with every plan, and each will have different adoption deadlines. This will permanently add more hours to each case and likely will increase the case age of each submission for the EP determination specialist.

2. Off-Cycle Plans

The flexibility that existed under the prior determination letter program that permitted an application for a determination letter to be submitted at any time is no longer possible under the new procedure. A plan desiring a favorable determination letter is supposed to submit its application during its appropriate cycle; an application submitted in an alternate cycle is characterized as off-cycle and "will not be reviewed until all on-cycle plans have been reviewed and processed."[84] Revenue Procedure 2007-44 identified several categories of off-cycle applications that would be given priority treatment (e.g., new plans or sponsors that had urgent business needs). However, this change has had a minimal effect. As of August 25, 2007, the Service had received 925 off-cycle applications, a number that was not anticipated by the Service, and the Service has been unable to process the vast majority of these submissions.

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[83] See Rev. Proc. 2008-50, 2008-35 I.R.B. 464, *superseding* Rev. Proc. 2006-27, 2006-1 C.B. 945, as *modified by* Rev. Proc. 2007-49, 2007-30 I.R.B. 141.

[84] Rev. Proc. 2007-44, 2007-28 I.R.B. 54.

3. Returned Applications

During Cycle A, the Service experienced a 10% return rate in determination letter submissions as compared to its previous 1% return rate. Applications were returned for a number of reasons, many relating to the new requirements of the determination letter program (e.g., failure to restate the plan; failure to include EGTRRA good faith amendments, non- or wrong submission of user fees, etc.).

4. Internal Training

The Service's internal training should continue to be strengthened, especially as to the annual Cumulative Lists and the specialty training for certain types of plans (e.g., governmental, multiemployer and multiple employer plans).

5. Staffing and Inventory

In its original estimates, the Service predicted that it would need approximately 152 EP determination letter specialists to process determination letter applications; currently, the Service has 125 such specialists. The Service's goal was to process each Cycle's cases within one year after the end of the submission period. Thus, a valid assessment of staffing needs is an ongoing initiative. Under the IRS's current system, determination letter submissions are first graded and then assigned to an EP determination specialist at that grade level. Many determination letter specialists are at grade 13 (a grade suitable to handle complex cases) and the bulk of the determination letter applications, approximately 31%, are at grade 13. However, the open inventory at grade 13 is approximately 40%, because of the complexity of such matters. Since it takes more time to process the open grade 13 inventory than other grade inventory, the Service has found that the available grade 13 staff hours are seriously short of the hours needed to process all grade 13 cases within the one-year goal. Thus, at the current grade 13 staffing levels, the Service does not expect to meet its objective of closing determination cases within one year of the end of the Cycle, thereby leading to an ever increasing backlog of older Cycle cases and increasing Cycle times. Coupled with the fact that the vast majority of the applications are filed at the end of the Cycle, this problem will become exacerbated over time.

Furthermore, union work rules agreements present difficulties due to limitations on the assignment of higher-graded work to lower-graded employees.

E. Insights from EP Determination Specialists

With the cooperation of the EP determinations leadership, the ACT conducted an online employee survey. Desiring the feedback from EP determination specialists who are primarily responsible for reviewing and approving determination letter applications (i.e., persons "in the trenches"), the anonymous survey requested input regarding three areas:

1. Remedial and interim amendment requirements;

2. Staggered timing of the current Cycle filing process; and

3. The determination letter process, including the time it takes to process an approval letter.

Between 15 and 19 responses, or approximately 15% of the persons surveyed, were received in each area for which feedback was solicited. Below is a summary of the responses. The verbatim responses from EP determination specialists are included as an Appendix to this Report, at Section IX. C.

1. Remedial and Interim Amendment Requirements

With respect to the remedial and interim amendment question, we received 17 responses. Although a few respondents felt strongly about preserving the current system, the most common theme was that the current system is confusing, complex, and difficult for plan sponsors, practitioners and the IRS itself.[85] In particular, there were comments indicating that the required interim amendments deadlines are not articulated clearly and that it would be helpful if there were an up-to-date listing of each amendment requirement for a given Cycle, consisting of amendment deadlines and effective dates. There was also a suggestion that model language be published for each interim amendment. This listing could be maintained on irs.gov.

2. Staggered Timing of the Current Cycle Filing Process

This topic received 15 responses. Again, the overarching theme of the responses received is that the staggered system is complex and confusing. In particular, it has been suggested that the five-year Cycle system contains too many exceptions, thereby adding to the confusion. Additionally, by having a mixed inventory, one EP determination specialist noted that they have to constantly "switch gears" as they work different cases from different Cycles. As a result, specialists continuously have to refer to their training manuals and the related revenue procedures in order to ensure that they are applying the correct requirements for a given Cycle. Finally, a few responses noted the difficulties created by the lack of staffing necessary to properly handle the workload.

[85] The BNA has reported that not only do practitioners find it difficult to comply with Internal Revenue Service rules for interim amendments, but the IRS finds it challenging to enforce the interim amendment rules, a senior tax law specialist told practitioners at a February 5 joint meeting of Baltimore area TE/GE councils and pension liaison groups. "As difficult as it is for the practitioner community to work with interim amendments, it's also difficult for us to enforce them," said Donald Kieffer, IRS senior tax law specialist. BNA Pension & Benefits Daily, February 10, 2010.

3. The Determination Letter Process, Including The Time it Takes to Process an Approval Letter

The third area received 19 responses. Several of the responses focused on the technology (including TEDS) being used to process cases. These responses indicate that certain specialists feel the current processing systems increase the amount of time it takes to process cases, in certain instances. Additionally, the responses noted that the practitioner community has a stake in the timeliness. In particular, the completeness of an application when submitted has an impact on the amount of time an application takes to process. Also, the tendency to file applications within a few weeks of the end of a given Cycle creates mini-spikes that are difficult for the Service to process.

V. Practitioner Experiences and Goals

A. Responses to Practitioner Survey and Outreach

The ACT published through various online venues a list of five questions, reproduced in Section IX. D., which asked practitioners to provide their experiences with certain aspects of the current determination letter program as well as their suggestions as to how the current program can be improved. Summaries of the responses to each question are provided below. A transcription of those responses is contained at Section IX. E. Also contained in Section IX. E. is the formal response of ASPPA. Furthermore, the ACT reached out to industry and practitioner groups listed in Section IX. A. 3 and held a public conference call.

1. Remedial and Interim Amendment Requirements

The overwhelming majority of survey respondents spoke extremely negatively about interim amendment requirements. Many thought that the new process is more difficult to manage, results in unnecessary additional costs to plan sponsors, and increases the likelihood of missing an amendment or filing deadline. One respondent's comment was representative of the whole: "The logic and reasoning behind the structured cycle filing method was easy to understand and seemed like a very good idea. In practice, however, it has thus far proven to be as cumbersome as the old process in many ways. The current process of requiring interim amendments to be made, even when there are no discretionary elections for the Plan Sponsor, needs to be reviewed."

At the TE/GE Annual Joint Conference that was held Friday, February 5 at the University of Baltimore School of Law, the members of the three TE/GE Advisory Councils presented the IRS with a paper entitled "Practitioner Viewpoint Turning The Tables: What's In Our Inbox? A 'Top 10' List of Practitioner Issues for IRS Consideration." Item #4 was the Good Faith Interim Amendment topic, which stated: "Practitioners and plan sponsors are groaning under the increased burdens imposed by this requirement. The Service also is bogged down by the EPCRS load generated by this requirement and the determination issues it raises. The verdict seems unanimous – this requirement should be eliminated or modified."

2. Staggered Timing of the Current Cycle Filing Process

Concerning the staggered timing of the current cycle filing process (for new plans and for restated plans), the survey revealed quite a mix of responses—roughly half liked the staggered cycle as opposed to the prior regime. Some thought that five years was too short of a time frame to have to restate individually designed plans. Numerous concerns were raised about the length of time it takes to process determination letter filings for off-cycle plans, particularly for new plans or plans that redesigned their benefit formulae mid-cycle.

A great deal of confusion still remains in the practitioner community with respect to the cycles of controlled groups, merger and acquisition situations, changes in plan sponsors, adoption of new plans and for employers who maintain both individually designed plans and prototypes or volume submitter plans. These situations multiply the complexity of an already complex process, creating uncertainty in the practitioner community because of the many exceptions to the typical filing cycle period that these situations create.

Other practical issues raised with respect to the staggered cycle filing process and interim amendment requirements relate to the perplexing effect that it has on certain types of plans. For instance, EGTRRA restatements for defined benefit plans will occur almost more than 10 years after the legislation was enacted, yet many plan sponsors will have already executed amendments for the Pension Protection Act of 2006, which was enacted five years later.

3. The Determination Letter Application Process

Concerning the determination letter application process, including the time it takes to process an approval letter, most respondents believe that the process takes far too long. Many practitioners offered various examples of long delays in the application process, several of which were due to interim amendment issues, as well as the restarting of the process due to a change in assigned personnel. Expectations appear to have been created in the practitioner community that the transition to a staggered restatement cycle system would expedite the review and processing of applications for determination letters, but virtually all survey respondents indicate that the assignment, response and processing times from the Service remains too long.

Suggestions for improvement of the filing process include the creation and use of an automated/online filing system, more routine and consistent training for IRS personnel processing and reviewing the applications, and streamlined forms and procedures.

4. Experience with IRS Personnel Who Review the Plan Filings

Survey respondents offered a wide variety of opinions and experiences, but a majority expressed satisfaction with determination letter specialists reviewing and processing the filings. Practitioners feel that determination letter specialists are professional, knowledgeable, and helpful, but are constrained from working efficiently by the complexity of the process and their perceived lack of experience with the determination letter review process. Some practitioners expressed frustration with the apparent strict adherence by reviewers to "checklists and processes" without respect to the actual details of a plan filing. Furthermore, there is a general perception that IRS has no common method of how and when to respond to determination letter applications.

Suggestions for improvements included improved communications protocols by determination letter specialists, resulting in more specificity and uniformity. Due to concerns about the variability in the knowledge level of determination letter specialists, survey respondents suggested that the Service provide more comprehensive and standardized training for personnel reviewing the filings.

5. Other Input Related to the Filing and Restatement Process

Other issues raised by practitioners include the erosion in confidence in the value of a determination letter as several reported that prior determination letters received were not granted deference because of plan defects that were missed by the prior determination letter specialist, or changes in the IRS's positions with respect to certain regulations (e.g., IRC § 401(a)(4)).

Additionally, the new determination letter program has created the need to spend much more time tracking deadlines (e.g., interim amendments which have no or little impact on the plan's operation) that add no or little value to the plan sponsor's benefit program, thus increasing the expense to and frustration of the plan sponsor.

B. EPCRS Issues

The Employee Plans Compliance Resolution System ("EPCRS") is highly regarded by the plan sponsor and practitioner community because it permits a plan sponsor who meets certain conditions to make "common sense" corrections to errors made in the form or operation of its plan. If such corrections meet the criteria of the Service, a plan sponsor is assured that the error and its correction will not jeopardize the qualified status of the plan. Operational errors that are not permitted to be remedied through self-correction may be corrected through the Voluntary Correction Program ("VCP"). VCP requires plan sponsors to make an application to the Service in which they identify the plan errors, and illustrate the correction method in detail. The Service then reviews the VCP application and the correction method and, if both are approved, issues a "compliance statement" to the plan sponsor.

Due to varying required deadlines for both nondiscretionary and discretionary amendments, and the need to continuously amend the plan document to meet interim amendment requirements, an increasing number of plan sponsors are failing to amend their plans properly or on a timely basis. However, plan document failures are not permitted to be corrected through the self-correction method under EPCRS, no matter how inconsequential the effect of the amendment may be. Thus, to preserve the qualified status of the plan, the employer's only recourse is to correct the failure by amending the plan and filing a VCP application with the Service.

Based upon conversations between the ACT and Joyce Kahn, Manager of Voluntary Compliance (the "VC Unit") for the Service, it is our understanding that the VC Unit has seen a significant increase in its workload due to VCP submissions relating to plan document failures, which by far are the most common type of failure processed by the VC Unit.[86] During fiscal year 2008, the VC Unit received a total of 2,950 VCP submissions. Over half of them related to nonamender failures. From fiscal year 2007

[86] See also discussion in Section IV. D. 1.

to fiscal year 2009, there has been a 35% increase in the number of VCP filings related to interim/good faith nonamender failures.

The VC Unit handles a wide diversity of applications related to compliance failures. However, due to the complexity of the interim amendment requirements, the VC Unit has difficulty discerning if a plan document failure relates to an interim or discretionary amendment. In many instances, a VCP applicant will submit a determination letter filing in tandem with the VCP filing, in accordance with the EPCRS guidance for correcting plan document failures under VCP. Thus, the VC Unit is encumbered with the process of reviewing determination letter applications, even though it is not as proficient at reviewing plan language requirements as the Service's Determinations unit.

With respect to the relevant EPCRS guidance, many practitioners have had significant interpretive difficulty with the VCP rules concerning whether and when a determination letter filing must be submitted in connection with a VCP application to correct a plan document failure. The confusion in this area appears to arise from the broad manner in which the terms "interim amendment" and "nonamender failure" are defined under such guidance.[87] Although a literal interpretation would suggest that a Nonamender Failure would include the failure to timely adopt an interim amendment (an "Interim Failure"), our best reading of the relevant EPCRS guidance is that an Interim Failure is intended to mean a separate type of plan document failure, which is distinct from a Nonamender Failure. This distinction is significant, because the EPCRS guidance expressly provides for different procedural requirements with respect to determination letter submissions, depending on whether a plan document failure is a Nonamender Failure or an Interim Failure.

1. Nonamender Failure Issues

A "Nonamender Failure" is a failure to timely amend a disqualifying provision before the end of the applicable remedial amendment period. For example, if an employer fails to timely restate and submit its plan document within the applicable remedial amendment cycle, any disqualifying provision in the document will result in a Nonamender Failure. When a plan is submitted under VCP in order to correct a Nonamender Failure, an application for a determination letter with respect to the corrective plan amendment must be submitted in tandem with the VCP application.[88] The determination letter application is required regardless of whether the plan sponsor submits the plan for its

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[87] See Rev. Proc. 2008-50, 2008-35 I.R.B. 464, *superseding* Rev. Proc. 2006-27, 2006-1 C.B. 945, as *modified by* Rev. Proc. 2007-49, 2007-30 I.R.B. 141, defining an "interim amendment" as an amendment with respect to a disqualifying provision and a "nonamender failure" as a failure to amend the plan to correct a disqualifying provision within the applicable remedial amendment period.

[88] Rev. Proc. 2008-50, 2008-35 I.R.B. 464, *superseding* Rev. Proc. 2006-27, 2006-1 C.B. 945, *as modified by* Rev. Proc. 2007-49, 2007-30 I.R.B. 141.

Nonamender Failure under VCP during an on-Cycle or an off-Cycle year.[89] Except as otherwise specified in Revenue Procedure 2008-50, the general procedural guidance provided under Revenue Procedure 2007-44 governs the determination letter application. Thus, unless an off-Cycle submission relates to an urgent business need or falls under another specific exception, the off-Cycle submission will not be given the same priority as an on-Cycle filing.

It does not appear that a Nonamender Failure includes filing past the Cycle due date; this leaves the plan sponsor in the difficult position of not having § 401(b) reliance, and no way of obtaining such reliance. Specifically, practitioners have had difficulty determining the extent to which VCP may be used to address situations where the plan sponsor has timely amended and restated the plan document in good faith but has failed to file a determination letter application during its on-Cycle year. In the absence of a VCP filing, such plan sponsor would have little choice but to file a determination letter application after the end of the plan's applicable remedial amendment period in an off-Cycle year. It is our understanding that any favorable determination letter issued as a result of the off-Cycle filing would result in a gap in the reliance period (from the end of the expired remedial amendment Cycle through the date of the late filing). Furthermore, as a result of the delayed filing after the end of the plan's remedial amendment cycle, any plan document failure identified by the Service in connection with its review of the off-Cycle filing would presumably be viewed as a disqualifying provision that must be corrected under the Service's closing agreement program, potentially resulting in substantial penalties for the plan sponsor.

Alternatively, the plan sponsor could file a VCP submission for any potential Nonamender Failures contemporaneously with its off-Cycle determination letter filing, with the expectation that any plan document failures identified by the Service in the course of processing the determination letter submission would be addressed under the VCP filing. However, the VCP rules contemplate the correction of specific plan document failures identified by the plan sponsor as of the time of the VCP application, and these rules do not clarify the extent to which a plan sponsor may use VCP (i) to correct unspecified Nonamender Failures that may be identified by the Service in the course of processing the related determination letter filing, and (ii) to secure a favorable determination letter without any gap in its period of reliance.

[89] Rev. Proc. 2008-50, 2008-35 I.R.B. 464 , § 6.05(2), *superseding* Rev. Proc. 2006-27, 2006-1 C.B. 945, as *modified by* Rev. Proc. 2007-49, 2007-30 I.R.B. 141. It provides that an application is required for a determination of whether the plan document, including the corrective amendment, complies with the qualification requirements of § 401(a) if the plan sponsor submits the failure under VCP during an on-cycle year. An "on-cycle year" means the last 12 months of the plan's remedial amendment cycle set forth in Rev. Proc. 2007-44. It further provides that a determination letter application is required to correct a nonamender failure under VCP, whether or not the plan is submitted under VCP during an on-cycle year.

2. Interim Failure Issues

In contrast to the procedural rules for Nonamender Failures, in the case of an Interim Failure, a determination letter application is only required if the plan is submitted under VCP during an on-Cycle year.[90] In other words, a determination letter application should not be submitted with a VCP submission during an off-Cycle year to the extent it only involves an Interim Failure in the plan document. Our best reading of the EPCRS guidance is that an Interim Failure includes the failure to satisfy the ongoing requirement to adopt "good faith" amendments, but does not include the failure to amend a plan within the applicable remedial amendment cycle. For example, the failure to adopt a good faith EGTRRA amendment would result in an immediate Interim Failure, but the failure to submit a restated plan document which included deficient EGTRRA provisions within the applicable remedial amendment cycle would be viewed as a Nonamender Failure (and not an Interim Failure).

3. Compliance Fee Matters

The compliance fee under VCP to correct a Nonamender Failure is determined in accordance with the fee schedule in Revenue Procedure 2008-50 based on the number of participants in the plan. It ranges from a minimum fee of $750 for a plan with 20 or fewer participants, to a maximum fee of $25,000 for a plan with over 10,000 participants. However, this fee is reduced by 50% if the submission is made within a one-year period following the expiration of the plan's remedial amendment period. The compliance fee to correct an Interim Failure is significantly less than the VCP fee for a Nonamender Failure. A VCP submission to correct Interim Failures only is a flat $375. In all cases, the VCP compliance fee is in addition to the user fee for any related application on Form 5300 for a determination letter with respect to the corrective plan amendment.

[90] Rev. Proc. 2008-50, 2008-35 I.R.B. 464, §§ 60.5(2)(a)(i) and 6.05(3), *superseding* Rev. Proc. 2006-27, 2006-1 C.B. 945, *as modified by* Rev. Proc. 2007-49, 2007-30 I.R.B. 141.

VI. RECOMMENDATIONS – POLICY

Our private pension system is based on voluntary participation, and it will ultimately fail unless the rules governing such participation give plan sponsors a reasonable expectation of achieving compliance, within a reasonable timeframe, and with expertise and commitment. While many aspects of the new staggered determination letter program have improved the voluntary process for gaining assurance that a plan is qualified as to its form, other aspects of the program have created new challenges for both plan sponsors and practitioners. The interim amendment requirements, in particular, are adding stress to the private pension system. The content, timing and frequency of the amendments are taking their toll. These requirements and certain other elements of the determination letter program should be examined and reformed.

The ACT's recommendations to improve the determination letter process are as follows:

A. Modification of Interim Amendment Requirements

1. Service's Authority

The Service has the authority and the flexibility to modify the Interim Amendment requirements, through its power to designate a plan provision (or absence of such provision) as a "disqualifying provision" under Code § 401(b). The regulations under Code § 401(b) provide that a plan that does not satisfy a qualification requirement solely as a result of a disqualifying provision will be deemed to have satisfied such requirement if the provision is amended on or before the last day of the remedial amendment period ("RAP") and it is made retroactively effective to the beginning of the RAP. In other words, the relief under § 401(b), which enables plan sponsors to fix potential plan document failures, is available with respect to the "disqualifying provisions" in their plan documents.

The regulations grant the Commissioner the discretion to designate certain plan provisions as disqualifying provisions and to extend their applicable RAPs. They also give the Commissioner the power to impose limits and additional rules regarding the amendments that may be made with respect to disqualifying provisions during the RAP.

The Service used this discretion to impose a "good faith" amendment requirement with respect to disqualifying provisions subject to the EGTRRA RAP. The related relief was expressly contingent on the timely adoption of good faith EGTRRA amendments. Notice 2001-42[91] specifically provides that an EGTRRA-related plan provision will be treated as a disqualifying provision, and therefore subject to rectification during the RAP, only if it was timely adopted on an interim basis.

[91] 2001-2 C.B. 70.

The good faith amendment concept was expanded further by Revenue Procedure 2005-66[92]. In addition to establishing the new staggered determination letter program, it established deadlines for the timely adoption of both interim and discretionary amendments. If an interim or discretionary amendment has not been timely adopted, or if the interim amendment is not reasonable or in good faith, the remedial amendment cycle is no longer available to the plan.

A historical summary of the guidance from the Service regarding plan amendments and remedial amendment periods, which proves by its very length and breadth the Service's broad discretion in this area, is included as an Appendix under Section IX. F.

Based on the authority granted pursuant to the Code § 401(b) regulations, the Service can and has frequently in the past exercised the same discretion it used to establish the interim amendment rules and to revise and refine them. Given its broad authority, the Service should consider exercising such discretion and using its authority to make the changes recommended in the sections below.

2. Comments Received

The comments received from the various stakeholders in the benefits community were highly critical of the interim amendment requirement in its current form, and none of the comments received expressed satisfaction with the current rules. Based on their experience with the interim amendment requirement, the stakeholders noted the surprising complexity of the rules and the administrative burden and increased expenses that they imposed on plan sponsors and benefits practitioners. A number of comments expressed the view that the rules and uncoordinated deadlines were confusing and traps for the unwary and wary alike, and that they posed a compliance challenge for even the most sophisticated plan sponsors and experienced practitioners. Employers, third-party administrators, consultants and attorneys found it difficult and challenging to track the separate sets of interim amendments required for different types of tax-qualified plans, each with different adoption deadlines. In many instances, there is a lack of guidance or clarity regarding when amendments are needed and what the amendments must contain. The comments received reflected an overall view that the interim amendment requirement raised policy concerns, and that compliance with these rules necessitated a disproportionate amount of attention, adversely affecting and overloading the stake-holders' limited time and resources within the current pension system.

Likewise, the interim amendment rules have also imposed a significant additional burden on the Service. The dramatic increase in the number of plans that have been corrected through the VCP under EPCRS and through closing agreements to resolve interim amendment and non-amender issues confirms and substantiates this view. From the Service's perspective, the cumbersome nature of the interim amendment

[92] 2005-2 C.B. 509.

requirement has diverted, and will continue to divert, significant resources from other priorities. The complexity of the requirements has made it difficult for the Service's auditors in the field to know when a plan has been timely amended. In the absence of any reform to these rules, this drain on resources will increase substantially in the future if sponsors of individually designed plans were to file off-Cycle applications for determination letters, as a defensive strategy to gain assurance their plan documents were being maintained in compliance with the interim amendment rules.

It should also be noted that each of the last three pieces of employee benefits legislation passed by Congress included its own specific deadlines for plan amendments.[93] Presumably, Congress incorporated these adoption deadlines into its statutes in order to provide relief to plan sponsors from the existing interim amendment requirements, which would have otherwise imposed earlier adoption deadlines. The fact that Congress explicitly superseded the existing interim amendment rules on three separate occasions suggests that the applicable rules are in need of reform and introduces inconsistency into the process as plans sponsors must amend for some changes as they become effective while they can wait for as long as three years to amend for others.

3. Alternatives

Based on the comments received from stakeholders, the ACT believes there are six basic alternatives for dealing with the interim amendment rules, with the understanding that there must be a reasonable balance between the need to hold down unnecessary costs and complexity and the need to keep plan documents current:

i. Keep the interim amendment requirement in its current form.

ii. Require the timely adoption of all applicable interim amendments by a clear deadline set each year.

iii. Require the biennial adoption of all applicable interim amendments by the end of established two-year periods, or require the adoption of all interim amendments by the midpoint of the plan's Cycle.

iv. Permit delayed adoption of plan amendments by the end of the remedial amendment period, subject to adoption of a cumulative summary of plan changes on an interim basis.

v. Require the annual or otherwise timely adoption of certain core amendments ("Core Amendments"), and permit the delayed adoption of non-core amendments ("Non-Core Amendments") to

[93] The three pieces of employee benefits legislation include the Pension Protection Act of 2006, Pub. L. No. 109-280 (2006), the Worker, Retiree, and Employer Recovery Act, Pub. L. No. 110-458 (2008) and the Heroes Earnings Assistance and Relief Tax Act, Pub. L. No. 110-245 (2008).

the end of the applicable Cycle. The distinction between Core and Non-Core Amendments is set forth below.

vi. Require the adoption of all interim amendments by the end of the remedial amendment period, provided any amendments impacting "section 411(d)(6) protected benefits" within the meaning of Treasury Regulation § 1.411(d)-4 are adopted in accordance with the current rules.[94]

The ACT evaluated each of these six basic alternatives in light of two competing policy considerations. On the one hand, in light of the general principle that plans must be operated in compliance with their terms in order to remain qualified, plan documents should include provisions that timely reflect the terms of such plans, and participants should be made aware of new and changing provisions. The Service's review procedures for plan documentation are based on the premise that the rights of participants should be adequately protected, and that such rights are derived entirely from the terms of a legally-binding plan document that has been formally adopted by the employer.[95] On the other hand, the need for a timely amended plan document should not unreasonably burden plan sponsors and benefits practitioners, nor should participants be deluged with plan notices. Additionally, the determination review process for plans to confirm that their documentation timely and properly reflects changes in the applicable law should not disproportionately consume the limited resources of the Service.

The first alternative, keeping the interim amendment requirement in its current form, is not a viable option. As discussed previously, in the absence of any reform, the requirement will continue to impose an undue burden on the Service, plan sponsors and other stakeholders. The second and third alternatives have also been rejected on similar grounds, since neither option, when coupled with the requirement to timely amend for changes affecting § 411(d)(6) benefits, would significantly reduce the administrative burden that is currently imposed on the Service, employers and practitioners.

The fourth alternative would eliminate the burden and cost of adopting fully realized, detailed plan amendments on an interim basis. Under this proposed approach, plan sponsors would need to adopt an amended and restated plan document prior to the end of the applicable remedial amendment cycle reflecting all necessary changes in plan operation and applicable law. In addition, to ensure the rights of participants are adequately protected under this alternative, plan sponsors would be required to

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[94] "Section 411(d)(6) protected benefits" as defined under Treas. Reg. Section 1.411(d)-4, Q/A1, generally include a participant's accrued benefit, early retirement benefits and retirement-type subsidies, and optional forms of benefits.

[95] EP Determinations Quality Assurance Bulletin, *Verification of Prior Plan Documents in the Absence of a Determination Letter,* dated September 8, 2006.

maintain a cumulative summary of the changes being made to the plan, which must be adopted by the employer pursuant to a corporate action (which could be delegated to an appropriate party such as the Plan Administration Committee, the Director of Human Resources, etc.) where the change does not involve § 411(d)(6) protected benefits. With respect to any plan change that prospectively decreases or eliminates any § 411(d)(6) protected benefits, such change would need to be included in the employer's written cumulative summary and adopted by the employer under formal corporate procedures. Although this and similar approaches have been proposed by various members of the benefits community, the ACT does not endorse them, as the ACT believes the formal written maintenance of the cumulative changes would likely be as burdensome as the current interim amendment requirements.

The fifth alternative would mandate the interim adoption of any "Core Amendments." Like the sixth alternative, this approach would generally require the adoption of amendments impacting § 411(d)(6) protected benefits on an interim basis, while adoption of Non-Core Amendments could be delayed to the end of the remedial amendment period. However, the fifth alternative would additionally require the interim adoption of any amendment materially or significantly affecting benefits and rights of importance to participants, as well as any other amendment deemed to be a Core Amendment by the Service in its discretion. The advantage of this approach would be that: (i) plan sponsors would be required to adopt significantly fewer plan amendments on an interim basis, reducing the annual burden and cost of maintaining their plan documentation, and (ii) the rights of participants would be adequately protected by virtue of the fact that all Core Amendments would have to be timely adopted. Although Non-Core Amendments would not be required on an interim basis, we note that the Service (in conjunction with the DOL) could impose a participant notification requirement. To implement this alternative, guidance would need to be provided to plan sponsors and practitioners clarifying which types of changes in the law constitute Core Amendments.

Under the sixth alternative, a plan sponsor would be able to delay the adoption of a plan amendment to the end of the remedial amendment period, if it does not involve a prospective decrease or elimination of a § 411(d)(6) protected benefit. Although amendments that do not involve a cut-back in § 411(d)(6) protected benefits would not be required on an interim basis, we note that the Service (in conjunction with the DOL) could impose a participant notification requirement.

4. Recommendations – In the Alternative

The ACT is making two recommendations, the fifth and sixth, in the alternative to reform the interim amendment rules. We note that either of the recommendations, if adopted, would constitute a substantial improvement over the current scheme and would benefit plan sponsors significantly. The ACT urges the Service and Treasury to consider adopting one of the following recommendations.

a. Core amendments as interim amendments.

(i) The Recommendation. The ACT recommends the Service and Treasury give serious consideration to the fifth alternative listed above. Under the ACT's proposed approach, the interim amendment rules would be modified to require the adoption of any Core Amendment by the later of: (i) the last day of the plan year during which a Core Amendment becomes effective, (ii) the due date for filing the employer's tax return (plus extension) for the taxable year during which the provision becomes effective, and (iii) any applicable amendment deadline established under the relevant statute; except, and the ACT specifically acknowledges, that any amendment prospectively decreasing or eliminating an IRC § 411(d)(6) protected benefit might have to be made at an earlier point, given that no amendment can retroactively reduce a benefit once accrued and certain amendments must be in place prior to the benefit structure's operation (e.g., cash or deferred provisions). The proposed rule would permit the retroactive adoption of any Non-Core Amendments by the end of the IRC § 401(b) remedial amendment period.

(ii) Core Amendment – Defined. Core Amendments would include mandatory and discretionary plan amendments that: (i) materially or significantly affect any benefit, right or feature ("BRF") of importance to the general population of plan participants, (ii) permit or require an action to be taken by participants with respect to benefits under the plan, (iii) prospectively decrease or eliminate any § 411(d)(6) protected benefits, except to the extent such plan amendment merely reduces or eliminates a § 411(d)(6) protected benefit that has already accrued in a manner that is permitted to be reduced under the applicable regulations and guidance from the Service,[96] or (iv) are deemed to be Core Amendments as determined by the Service in its discretion and announced in published guidance. As a general matter, any modification that affects eligibility, or vesting, or materially changes benefits, should be considered a Core Amendment.

Since Core Amendments would include amendments involving any BRF of importance or broad applicability, this approach would provide protection for more than § 411(d)(6) protected benefits. Although § 411(d)(6) protected benefits generally include important benefits and rights under a plan (e.g., early retirement subsidy, installment payment option), many important benefits and rights are not necessarily § 411(d)(6) protected benefits. Examples of benefits and rights that are of significant importance to participants, but that are not § 411(d)(6) protected benefits, include the right to make elective deferrals under the plan and the right to direct investments. A Core Amendment would include a plan amendment that: (i) provides participants with the

[96] Treas. Reg. Sections 1.411(d)-3, 4 provide for the permissible elimination of certain types of § 411(d)(6)(B) protected benefits, including but not limited to: (i) optional forms of benefit that are redundant, (ii) noncore optional forms of benefit where core options are offered, (iii) protected benefits that create significant burdens and complexities, and (iv) protected benefits to the extent their elimination or reduction does not result in the loss of either a valuable right or a subsidized optional form of benefit but only as permitted by the Commissioner.

freedom to diversify their investments in publicly traded employer securities in accordance with Code § 401(a)(35), or (ii) accelerates the vesting of employer nonelective contributions in accordance with Section 904 of the Pension Protection Act of 2006.

(iii) Non-Core Amendments – Defined. Non-Core Amendments would include all amendments that are not Core Amendments. It is intended that Non-Core Amendments be limited to plan amendments that: (i) reflect plan changes that are purely operational, ministerial or technical in nature[97], (ii) are immaterial for, or would have a *de minimis* impact on, the general population of plan participants and with respect to which the provision of a notice summarizing the impact of the applicable amendment would be a sufficient safeguard for the small number of affected participants[98], or (iii) involve an area in which incorporation by reference is permitted. Examples of Non-Core Amendments might include a plan amendment that: (i) eliminates the need to calculate gap-period earnings when distributing excess deferrals as provided under the Worker, Retiree, and Employer Recovery Act of 2008 ("WRERA"), (ii) implements changes in accordance with the final regulations under § 415[99], or (iii) adds required provisions relating to employees who are in the military in accordance with the Heroes Earnings Assistance and Relief Tax Act of 2008 ("HEART").

Non-Core Amendments would also include an amendment that merely reduces or eliminates a § 411(d)(6) protected benefit that has already accrued in a manner that is permitted to be reduced under the applicable regulations and guidance from the Service. For example, a technical amendment that is required due to a change in the law or published guidance impacting § 411(d)(6) protected benefits, but which is allowed to be eliminated because of its *de minimis* impact in accordance with applicable regulations or guidance from the Service, should be viewed as a Non-Core Amendment. Such view is consistent with the statutory language in IRC § 411(d)(6)(B), which expressly provides anti-cutback relief to a plan amendment that creates significant burdens or complexities for plans and participants, unless such amendment adversely affects the rights of any participant in more than a *de minimis* manner.

(iv) Service – Issue Guidance as to what is Core v. Non-Core. In connection with its proposal, the ACT recommends that the Service issue guidance under which it will determine which types of plan amendments constitute Core Amendments, and, whenever possible, when the law changes, issue timely guidance

[97] For example, inclusion of § 132(f) fringe benefit in definition of compensation.

[98] For example, 2009 waiver of minimum required distributions.

[99] The ACT notes that one of the strengths of the Core v. Non-Core proposed approach is its flexibility; some practitioners, for certain of their plan sponsor clients, will determine that § 415 changes are, indeed, Core Amendments. For example, those plan sponsors providing robust stock options might consider the gain on such options as material to the § 415 definition of compensation, whereas for the vast majority of plan sponsors this would not be material.

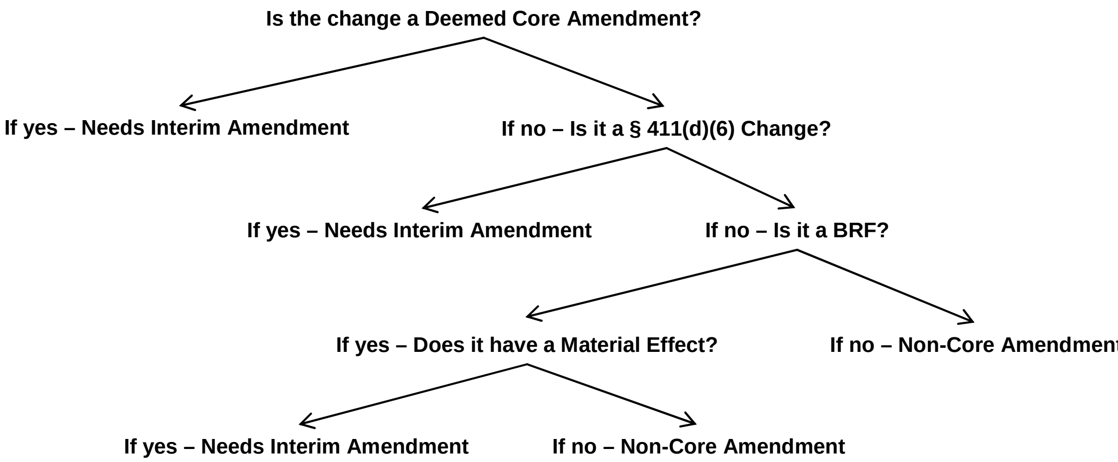
regarding whether resulting amendments are Core or Non-Core. To the extent there is ambiguity as to whether a type of plan amendment should be viewed as a Core Amendment, under the ACT's proposal, the Service would retain the power to designate it as a Core or Non-Core Amendment in its discretion.

To determine the ease by which a Core v. Non-Core determination could be made and what portion of recent amendments would be Core v. Non-Core, the ACT reviewed the required and optional amendments under PPA, HEART and WRERA for Cycle D filers and designated each applicable plan amendment as either a Core Amendment or a Non-Core Amendment in accordance with the principles outlined above. The ACT's findings are included as an Appendix to this Report, at Section IX. G, which should be read in conjunction with and is an important part of this section of this Report. This deliberative process was effectively and quickly accomplished, and the designation of each provision as either a Core or Non-Core Amendment was a clear-cut and unambiguous finding, although in certain instances it was somewhat challenging to articulate the precise rationale for designating an amendment as either Core or Non-Core. In this regard, the proposed test is remarkably similar to the famous "I know it when I see it" test articulated by the late United States Supreme Court Justice Potter Stewart.[100] It is our belief that the Service would be able to conduct its own reviews of plan amendments in a similarly straightforward and definitive fashion. We note that if the Service determines all or a majority of law changes constitute Core Amendments, this recommendation is meaningless. However, we favorably note that Service personnel reviewed the ACT's Core v. Non-Core determinations listed in Section IX. G hereof and considered the methodology and factors utilized in making such determinations reasonable; of course, this was an informal review and does not mean that the position of the IRS officially expressed following a formal review would necessarily be the same. Furthermore, we favorably note that this Section IX. G demonstrates that, absent plan design changes, the majority of interim amendments are Non-Core.

Based on the guidance to be published by the Service under this proposal, plan sponsors and practitioners would determine which individual plan amendments are Core Amendments subject to interim adoption requirements and which plan document changes are Non-Core Amendments. Below is a prototype "decision tree" for determining if an amendment is Core or Non-Core.

[100] Jacobellis v. Ohio, 378 U.S. 184 (1964).

Decision Tree[101]



(v) Best Efforts Compliance. The ACT recommends that plan sponsors be held to, and be able to rely on, a "best efforts" compliance standard for operational compliance with Non-Core Amendments which must, under the ACT's recommendation, be adopted no later than the end of the applicable remedial amendment period. Even though plan sponsors would be permitted to delay adopting Non-Core Amendments to their plan documents until the end of such period under this proposal, plans would need to operate on a best efforts basis as though such Non-Core Amendments had been adopted during the relevant interim period.

Additionally, the Service could require "best efforts" compliance to include the distribution to employees of a notice summarizing any changes in plan operation in a manner calculated to be understood by the average plan participant.[102] Although such notice would not include detailed provisions, it would constitute a written record that operational changes were being made under the applicable plan. The intention would be to incorporate the same standard for disclosure that applies under Title I of ERISA and is typically met by distributing a Summary of Material Modification ("SMM"), but would in no way have Title II (i.e., Code Section 401(a), et. seq.) implications.

[101] Assumptions and definitions:
"Deemed Core Amendment" means an amendment characterized as a "Core amendment" by the Service in regulations or other guidance.
"§ 411(d)(6) Change" means a change that prospectively decreases or eliminates a § 411(d)(6) protected benefit, except as permitted by applicable regulations or IRS guidance.
"BRF" means a benefit, right or feature within the meaning of § 401(a)(4) regulations.
"Material Effect" means a change that is likely to cause significant loss in the value of a BRF for most participants in a plan (for example, at least 60%) or offers a choice that requires participant action.

[102] A summary of any material modification in the terms of the plan must be written in a manner calculated to be understood by the average plan participant in accordance with ERISA § 102(a) and furnished to plan participants in accordance with ERISA § 104(b)(1).

Furthermore, in order to avoid many of the same issues plan sponsors are facing with respect to interim amendments, guidance would be needed to clarify the timing and content of the notices. The deadline to distribute the notices should be uniform and long enough to ensure that adequate time is available to prepare and distribute such notices. So that plan sponsors do not have to incur the additional cost of delivery for such notices, plan sponsors should be permitted to deliver them simultaneously with, or efficiently incorporated into, other participant communication materials. For example, the notice could be combined, or distributed, with a defined contribution plan's Summary Annual Report ("SAR") or a defined benefit plan's Annual Funding Notice.[103]

This best efforts standard for Non-Core Amendments would be a higher standard than the "reasonable, good faith" standard applicable under the current rules for interim amendments, since it would entail the concrete step of providing a SMM-like notice.[104]

It should be noted that like any other situation where the deadline for adopting amendments is delayed, the proposed rule may have implications under Title I of ERISA. ERISA § 404(a)(1)(D) requires plan fiduciaries to discharge their duties in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of ERISA. Accordingly, if the adoption of a Non-Core Amendment were delayed until the end of the RAP, it could be asserted that the plan's fiduciaries should follow the plan document's provisions without regard to the Non-Core Amendment during such interim period. By their nature, the adoption of Non-Core Amendments would not materially affect the benefits and rights of participants, but, in theory, a participant may nevertheless assert a claim under ERISA that turns on whether the plan document is deemed to include a Non-Core Amendment during the interim period. Requiring employers to provide SMM-like notices for Non-Core Amendments may mitigate any related concerns arising under Title I of ERISA. The ACT recommends the Service and the Department of Labor create a working group to review and resolve any potential issues arising ERISA § 404(a)(1)(D) with respect to this proposal, and to develop guidance with respect to the manner in which SMM-like notices for Non-Core Amendments should be delivered to participants. The ACT recommends such working group pay particular attention to how

[103] ERISA §101(f) generally requires the administrator of a defined benefit plan to provide a plan funding notice for each plan year to each plan participant. Large plans must provide this notice within 120 days after the end of the plan year, and small plans must provide it on or before the filing of the Form 5500. ERISA § 104(b)(3) generally requires the administrator of any plan that is not subject to ERISA §101(f) to furnish a copy of the plan's Summary Annual Report ("SAR") to each plan participant. Such notice must be provided within 9 months after the close of the plan year (or 2 months after the extended deadline for Form 5500 in the case of an approved extension).

[104] The ACT met with a staff attorney of the Pension Rights Center, which provides assistance to and is a powerful advocate for plan participants. The staff attorney stated that plan participant rights, including being able to rely on up-to-date, accurate plan documentation, would not be adversely impacted by the ACT's recommendations regarding modifying the interim amendment requirements, especially if there were a "best efforts" standard along with an annual SMM-like notice regarding amendments.

an SMM-like notice would be carried out in the context of prototypes, where one provider is providing services to thousands of clients.

b. Interim amendments for § 411(d)(6) benefits only

The ACT recommends consideration of the sixth alternative listed above. Under this proposed approach, only those plan amendments required to avoid a cutback in a participant's plan benefits under Code § 411(d)(6) must be made prior to the end of a plan's RAP, unless such § 411(d)(6) amendment is required or permitted to be made in a particular year due to a specific statutory or regulatory directive or transition rule. All other plan amendments may be delayed until the end of the plan's applicable remedial amendment cycle. This alternative has the distinct advantages of simplicity and ease of administration, and is more in line with what the practitioner community originally envisioned for the Cycle RAP system. Moreover, this approach may be administratively more efficient and simpler for sponsors of prototype and volume submitter plans.

The IRS unquestionably has the authority to adopt this proposal as demonstrated by the numerous occasions on which it extended the remedial amendment period. We note that this approach is similar to the plan amendment rules that were in place before the Service began to require good faith amendments with respect to EGTRRA plan documentation and the interim amendments that are currently required under the new staggered determination letter program. For example, with respect to TRA '86 plan documentation, the Service generally did not require a plan sponsor seeking a determination with respect to its plan to have adopted mandatory and optional plan amendments timely.[105]

In order to assist plan sponsors with making the necessary plan amendments, the ACT recommends that the IRS indicate in each year's Cumulative List, or, preferably, in a new comprehensive notice discussed in Section B immediately below, which amendments it believes involve a potential impermissible § 411(a)(6) cut-back if not made currently.

Similar to the "Core" and "Non-Core" proposal above, the ACT would recommend that plan sponsors be held to, and be able to rely on, a "best efforts" compliance standard with respect to all non-§ 411(d)(6) amendments, which, under the ACT's recommendation, must be adopted no later than the end of the applicable remedial amendment period. As discussed above, plans would need to operate on a "best efforts" basis as if such non-§ 411(d)(6) amendment had been adopted during the relevant interim period, including, as also discussed above, a written notification to plan participants. See discussion in Section VI. A. 4. a. (v) above.

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[105] With respect to determination submissions prior to Revenue Procedure 93-39, the Service may have reviewed plan documents to verify the timely adoption of certain provisions relating to Code §§ 401(a)(17) and 401(a)(31). EP Determinations Quality Assurance Bulletin, *Verification of Prior Plan Documents in the Absence of a Determination Letter,* dated September 8, 2006.

* * * * * * *

The bottom line is that the ACT firmly believes that adopting recommendations five or six will go a long way to unraveling the Gordian Knot that is the current interim amendment requirement.

B. Clarify Deadlines

The comments received from stakeholders concerning their experience ascertaining and identifying the adoption deadlines for interim amendments were highly critical of the existing guidance. A number of comments expressed the view that the information for such due dates is not readily accessible and that certain guidance is confusing. One explanation provided for such confusion is that the Service had made multiple changes to due dates in certain instances. Another explanation is that the due date information for interim amendments is scattered across Treasury decisions, Revenue Procedures and Notices, and that other related information concerning the timing of interim amendments is contained in Revenue Rulings, Announcements and the applicable statutes.

1. New Comprehensive Notice

Regardless of how the IRS decides to deal with the interim amendment requirements, the ACT recommends the Service clarify when interim amendments are due by publishing a single Notice with an interim amendment chart stating the effective dates and deadlines for adoption. Proposed plan amendment language would be extremely useful to plan sponsors and benefits practitioners, and model provisions could also be included in this Notice. The Service's *2007 Interim and Discretionary Amendments*, an informational release that appears to be available only through its Web site, is a helpful resource, but it is not a complete and comprehensive guide to the separate deadlines for all applicable sets of interim amendments.[106] As discussed below, such proposed Notice would be most helpful if issued in early September of each year. This Notice should also be updated and re-published each time a change in the law or published guidance requires a plan amendment.

With respect to the proposed Notice, the ACT further recommends this guidance be presented in a chart format, with: (i) a reference to the applicable Code section and/or new law that pertains to each change, (ii) a brief description of the required change, (iii) effective dates, (iv) the due date for adoption of the interim amendment, (v) a description of whether the change is discretionary or mandatory, and (vi) commentary concerning the nature of the amendment. The chart should be printed twice in the proposed Notice, once organized by Code section and a second time organized by due date. An updated Notice (which would include an updated chart) should be published for any new change in the law or published guidance requiring a plan amendment, and

[106] *Available at* http://www.irs.gov/retirement/article/0,,id=173372,00.html

annually. A sample of what the Notice might look like is included as an Appendix under Section IX. H. The format and content for the Cumulative List should also be conformed to the format and content of the proposed Notice. Thus, intra-year updates to the Cumulative List and the proposed Notice would involve substantially similar changes for both documents.

2. Cumulative List Changes

The Notice containing the Cumulative List of Changes in Plan Qualification Requirements (the "Cumulative List") is published annually. Under the Service's current procedure, the target date for publishing the Cumulative List is mid-November of each year. The ACT notes that the Cumulative List comes out too late, particularly for prototype providers. The ACT recommends that consideration be given to an earlier release of the Cumulative List, for example, early September of each year.

The ACT recommends that the IRS post on its Web site a notice published as frequently as necessary after the publication of the Cumulative List that provides new changes which will be on the next Cumulative List. This Web-based notice should also be updated and re-published each time a change in the law or published guidance requires a plan amendment.

3. Gap Period/Interim Amendment Issues

Under the Service's current procedure, the target date for publishing the Cumulative List is mid-November of each year. The Cumulative List identifies changes in the qualification requirements that will be considered by the Service in its review of plans for determination letters, whose submission period begins on the February 1st following the issuance of the Cumulative List. Accordingly, as currently provided under Revenue Procedure 2007-44[107], any changes in the law or published guidance during the period (the "Gap Period") which begins with the issuance of the Cumulative List (mid-November) and ends with the start of the applicable submission period (February 1st) will not be considered by the Service in its review. The Service should modify its submission procedures so that any changes in applicable law or published guidance arising during the Gap Period and adopted by the plan sponsor as interim amendments are considered in its review of plans for determination letters; the adoption of the ACT's recommendation in Section VII. A. 2 regarding the plan sponsor's submission of a "self-identification sheet" of all interim amendments and the order of their acceptance could be helpful and practical to the Service in this regard.

[107] 2007-28 I.R.B. 54.

C. Approval Letter Program for Individually-Designed IRC § 403(b) Plans[108]

On April 15, 2009, the IRS issued Announcement 2009-34[109] in which it published a draft Revenue Procedure that (when finalized) will permit an employer sponsoring certain eligible § 403(b) retirement arrangements to apply for an opinion letter or advisory letter issued by the IRS with respect to the qualified status of such sponsored arrangements under § 403(b). Announcement 2009-34 indicates that the IRS also intends to establish a document approval program for individually designed IRC § 403(b) plans at a later date. IRS representatives have informally indicated that the IRC § 403(b) pre-approved plan program will be finalized by mid-2010. The IRC § 403(b) individually designed document approval program will in all likelihood not be available until 2011.[110]

Practitioners anticipate that most small IRC § 501(c)(3) organizations that maintain such § 403(b) arrangements will utilize pre-approved prototype or volume submitter plan documents prepared by the IRC § 403(b) vendors handling the investment and/or compliance and administration of such plans. However, it is anticipated that a significant number of large § 501(c)(3) organizations (e.g., health care systems, colleges and universities) will choose to maintain individually-designed IRC § 403(b) plans.

The IRS has already received numerous comments from IRC § 403(b) practitioners and vendors on the proposed prototype plan program and draft revenue procedure, so this Report will not address issues related to such program, other than to note that the interim amendment issues discussed elsewhere in this Report will present the same significant challenges and problems in the IRC § 403(b) world as they already have in the IRC § 401(a) tax-qualified plan world. However, we would like to offer the following recommendations regarding the IRC § 403(b) Approval Program:

1. Release 403(b) Approval Program Rev. Proc. in Draft Form

The ACT recommends that the Revenue Procedure that will be utilized to implement the IRC § 403(b) Approval Program be released in draft form for comment prior to its finalization, as was done for the IRC § 403(b) prototype plan program.

[108] The ACT notes that many 403(b) plans are sponsored by governmental entities. Our recommendations relevant to governmental § 403(b) plans contained in Section VI. D. hereof should be considered incorporated by this reference.

[109] 2009-18 I.R.B. 916.

[110] The IRC § 403(b) individually designed document approval program is hereinafter referred to as the "403(b) Approval Program."

2. Determine Estimated Number of 403(b) Document Approval Submissions

The current IRC § 401(a) qualified plan determination letter program utilizes five cycles for employer submissions. The same five cycles and related employer identification numbers can, of course, be used for the IRC § 403(b) Approval Program. However, it is not clear at this time what the actual number of submissions will be under such program. If they are few enough in number, perhaps a five-year cycle system will not be needed. We recommend that the IRS work with the IRC § 403(b) practitioner and vendor community prior to releasing a draft revenue procedure for the IRC § 403(b) Approval Program to attempt to determine the level of submissions that will be made under it. Such an estimate will also be important for staffing the program.

3. Include Special Remedial Amendment Determination Rules in 403(b) Approval Program Rev. Proc.

Sections 10.02, 10.03 and 10.04 of Revenue Procedure 2007-44 provide special remedial amendment rules for determining the appropriate filing cycles for multi-employer plans, multiple employer plans and governmental plans. The ACT recommends that these special rules be included under the IRC § 403(b) Approval Program, if there is a staggered or cycle feature to the program. Section 10.07 of Revenue Procedure 2007-44 provides a special rule for a group of tax-exempt employers that do not constitute a controlled or affiliated service group under Code §§ 414(b), (c) or (m) but that are participating in the same (or virtually the same) § 401(a) tax-qualified plan maintained by a "centralized organization" (such as a national headquarters or a common administrative committee). The controlled group rules for tax-exempt organizations permit certain tax-exempt employer groups that coordinate their day-to-day activities to elect to be treated as a controlled group under Treas. Reg. § 1.414(c)-(5), and such groups will, presumably, be able to utilize the Cycle filing rules that will be applicable to controlled groups. However, there will no doubt be instances in which the special rule contained in Section 10.07 of Revenue Procedure 2007-44 will be useful, so the ACT also recommends its inclusion in the 403(b) Approval Program.

4. Identify 403(b) Changes As Such in Cumulative List

In preparing the annual Cumulative List of Changes in Plan Qualification Requirements called for under § 4.01 of Revenue Procedure 2007-44, the ACT recommends that provisions applicable only to IRC § 403(b) plans should be identified as such in the list. Consideration should also be given to whether a separate Cumulative List should be issued for IRC § 403(b) plans.

5. Include Underlying Annuity Contracts and Custodial Agreements in Scope of DL

Section 5.04 of Revenue Procedure 2007-44 reflects the requirement that a § 401(a) tax-qualified plan be maintained pursuant to the terms of a written plan document. The final Section 403(b) regulations contain a similar written plan document requirement, but

IRS personnel have indicated informally at public conferences that the IRC § 403(b) written plan document requirement can be satisfied by "paper clipping" more than one document together to constitute the required written plan. For example, an employer may draft a IRC § 403(b) plan document that serves as an "umbrella" plan document covering different underlying annuity contracts issued by insurance companies or custodial agreements entered into with mutual fund providers. The "umbrella" plan document will typically incorporate the terms and provisions of the underlying annuity contracts and custodial agreements. Under this scenario, when an employer applies for an individually designed IRC § 403(b) plan approval letter, the issuance of the letter only with respect to the "umbrella" plan document would not seem to provide the employer with the desired IRC § 7805(b) protection. The ACT therefore recommends that the IRC § 403(b) Approval Program be structured so that a favorable approval letter will also cover any underlying annuity contracts and custodial agreements utilized in connection with a IRC § 403(b) plan.

If annuity contract certificates and custodial accounts will be covered under the IRS 403(b) prototype program, the ACT also recommends that the IRS develop a procedure so that IRC § 403(b) vendors can have their respective annuity contract certificates and custodial agreements pre-approved so that IRS reviewers will not need to review such certificates and agreements in connection with each individually-designed plan utilizing them. Changes to annuity contracts must be approved by state insurance regulators, and the same standard annuity contracts and custodial accounts are often used for many different plans, meaning that it would be virtually impossible to make changes in the context of one single plan. A procedure whereby annuity contract certificates and custodial agreements can be pre-approved would be preferred by all 403(b) providers. This will avoid providers' annuity contract certificates and custodial agreements being subject to review (and proposed changes) as part of each determination letter request. This could perhaps be accomplished under the IRC § 403(b) prototype program because vendor annuity contract certificates and custodial account agreements will presumably be submitted for approval under that program. Alternatively, the IRS could create a "snap-on" amendment or rider that will satisfy the IRS's review requirements, similar to the prototype IRA documentation that is currently available and updated from time to time by the IRS.

We also recommend that the IRS provide a schedule on which the employer can list all the IRS-approved vendor 403(b) contracts and agreements by providing the name of the vendor and an IRS reference number assigned to the pre-approved document. This approach will avoid the necessity of attaching the approved vendor documents to an individually-designed 403(b) plan approval filing.

6. Make 403(b) Approval Letter Available in the Event of a Plan Termination

Section 8 of Revenue Procedure 2007-44 sets forth the determination letter rules related to § 401(a) tax-qualified plan terminations. The ACT recommends that the IRC § 403(b) Approval Program contain a similar provision, and that the current IRS Form

5310 be revised to accommodate § 403(b) plan terminations, or another form be created to do so.

There continues to be some doubt within the IRC § 403(b) practitioner community over the issue of exactly when a IRC § 403(b) plan is, in fact, terminated. This is particularly true because, in the multiple vendor world of IRC § 403(b) plans, it may be disadvantageous to plan participants to terminate and distribute such plan assets due to surrender charges and early withdrawal penalties that may be imposed by vendors in connection with the termination. We recommend that this issue be addressed through the issuance of additional guidance.[111]

7. Permit Employers to Request Coverage and Nondiscrimination Rule Determinations as Part of the 403(b) Approval Process

Some IRC § 403(b) plans are subject to coverage and nondiscrimination testing under IRC §§ 410(b) and 401(a)(4) with respect to employer contributions when a safe harbor contribution or QACA is not utilized. Employee elective deferrals to IRC § 403(b) plans are subject to a universal availability requirement, under which the opportunity to make voluntary, elective deferrals must be made available to all nonexcludable employees. The current determination letter program for § 401(a) tax-qualified plans permits employers to elect (on the Schedule Q associated with IRS Form 5300) to have the IRS determine, among other things, that an employer's plan coverage rules satisfy the requirements of IRC § 410(b), that specified benefits, rights and features of the plan meet the § 401(a)(4) rules, that the plan satisfies the § 401(a)(4) nondiscrimination general test and that a plan's definition of compensation is nondiscriminatory. The ACT recommends that similar elections be made available under the IRC § 403(b) Approval Program. With respect to testing available benefits, rights and features, the ACT recommends that the IRS's determination also cover any underlying annuity contracts and custodial account agreements used as funding vehicles under the plan.

D. Special Issues of Governmental Plans

The IRS has publicly stated its intention to increase compliance among governmental plans. Encouraging participation in the determination letter program could be a key element in making this happen or it could simply create more frustration for both the applicants and the IRS if certain realities are not addressed beforehand. Reviewers are likely to encounter noncompliance on a scale and of a type not often seen with ERISA-covered plans. If reviews are conducted based on standard checklists, the IRS will lose an excellent opportunity to work toward its ultimate goal, which is tax-compliant plans. This section briefly explains some historical reasons for the current state of public

[111] The 403(b) regulations indicate that the delivery of a fully-paid individual insurance annuity contract is treated as a distribution for purposes of the plan termination rules. However, it is not clear that this provision covers all types of funding vehicles used in connection with 403(b) plans.

employer plans and makes several recommendations to create a workable determination letter program that will help the IRS achieve its goal.

While it is tempting to take the position that the same rules should apply to private employer plans and governmental plans (to the extent applicable), the reality is they are different creatures in several significant respects. The importance of governmental plans' exemption from ERISA cannot be overstated. It means that governmental plans do not file Form 5500 or generally submit any other type of annual report or return so federal regulators do not have an easy way to identify them or confirm their numbers. It also complicates the IRS's efforts to communicate and educate to promote compliance.

The motivation of private versus public plan sponsors is different, which bears on the kinds of protections that participants' interests need. The significant tax advantages afforded private for-profit employers for contributions to qualified plans is an important incentive for them to establish retirement plans and maintain their qualified status. In contrast, tax-exempt governmental plan sponsors establish pension plans primarily to attract and retain the best qualified employees. In many cases, public entities use a generous benefit package to offset lower salaries.[112] Governmental plan sponsors are motivated to avoid wrongdoing in order to preserve employees' tax advantages so they can continue to attract and retain the employees they want.

Making changes to governmental plans is often a complicated process fraught with potential legal challenges because of a patchwork of state and local constitutional and statutory protections applicable to plan benefits that has evolved over the years. In addition, governmental plan amendments typically are subject to some aspect of the varying state legislative processes. Obtaining approval for any type of change, including conforming legislation, is often subject to political considerations that create uncertainties in the outcome as well as the timing. Furthermore, the legislative bodies of the state and local entities with authority to amend state or local statutes that govern retirement plans may meet infrequently, which complicates meeting adoption deadlines.[113]

Historically, participants in public sector plans have relied on their pension plan benefits to serve as the foundation of their retirement income because a significant portion of the participants will never be eligible for full, or even partial, Social Security benefits. Thus, some of the ancillary benefits routinely offered under governmental plans are not entirely consistent with IRS requirements. According to Social Security Administration

[112] See *Public Fund Survey, Summary of Findings for FY 2008*, prepared by Keith Brainard, National Association of State Retirement Administrators, October 2009.

[113] In recent guidance, the IRS provided much-appreciated relief by extending the RAP for governmental plans to the 91-day period beginning after the last day of the first regular legislative session beginning more than 120 days after the determination letter has been issued or the declaratory judgment petition has been disposed of. Rev. Proc. 2009-36, 2009-35 I.R.B. 3004.

estimates, about 30 percent of state and local government employees are currently not covered by Social Security[114] so this is a significant issue.

Given the patterns and practices that have developed without much interference or input from the IRS over time, the more relevant question at this juncture should not be whether a plan was always technically compliant, but whether the plan's actions were consistent with the intent of the tax legislation. Several factors work together to limit the possibilities for doing harm to participants' interests: the employees' self-interest in protecting their primary source of retirement income; the relatively high percentage of represented employees in the public sector workforce;[115] and the scrutiny that the state and local legislatures as well as the voting public regularly apply to public pensions.[116] Thus, the ACT makes the following recommendations for the determination letter program that would apply specifically to governmental plans. The key components are limited amnesty determined under uniform principles for noncompliant past practices where participants' interests were not harmed and a user-friendly process for fostering compliance going forward.

[114] *Reported in* State and Local Government Retiree Benefits, Report 07-1156, U.S. Government Accountability Office, September 2007. Previously, many state and local governments chose not to participate in Social Security in order to avoid the employer contribution (currently 6.2 percent of covered pay). The tradeoff has been to offer employees a more generous pension plan that provides benefits roughly equivalent to the amount an employee in the private workforce would receive from a combination of Social Security and the employer-provided retirement plan.

[115] Over 40 percent of employees in federal, state and local government are covered by union agreements compared with about 10 percent of private sector workers. *State and Local Government Retiree Benefits, Current Status of Benefit Structures, Protections, and Fiscal Outlook for Funding Future Costs*, U.S. Government Accountability Office, Report no. GAO-07-1156, September 2007.

[116] The current economic downturn has heightened the scrutiny as legislatures and the tax paying public seek ways to decrease the enormous accrued liabilities associated with public plans.   See, e.g., *The Washington Post,* Jan. 2, 2010.

1. Combine the Determination Letter Program with a Voluntary Compliance Process for Governmental Plans During This First Cycle

Because of problems associated with the vested rights doctrine[117] and other historical developments, many if not most of the governmental plans submitted are likely to present the reviewer with some compliance issues. Unless changes are made to the current determination letter program, these instances of noncompliance will potentially require the involvement of the Voluntary Compliance Unit, which is already becoming overwhelmed with problem plans as described in Section V.B. It will also mean that governmental plans will no longer be handled by the reviewers specially trained in their idiosyncrasies, which will cause further delays and frustration. About 1,500 governmental plans submitted in Cycle C are already in the review queue. Thousands more are expected to be submitted in Cycle E, which ends on January 31, 2011. These numbers could overload the system; it is for this reason the ACT recommends that the IRS rely heavily on its trained governmental plans cadre to resolve issues consistent with clearly articulated principles by effectively combining the determination letter program with a voluntary compliance process, manned by those IRS specialists with preexisting governmental plan knowledge.

2. Leverage the Experience Acquired in Cycles C and E to Develop Fix-It Guides Geared to State and Local Governmental Plans

The IRS has developed Fix-It Guides for 401(k) plans, SEPs and IRAs that support up-front compliance by providing a wealth of practical information to plan sponsors and practitioners.[118] Charts identify common problems that can arise with all facets of plan administration (e.g., eligibility, contributions, distributions, vesting) and direct the reader to a summary of the appropriate corrective action and, if applicable, the correction program. This type of information could go a long ways toward allaying one of the big fears that governmental plan sponsors have identified as a hurdle to applying for a determination letter, namely, what happens if the IRS finds something wrong with our

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[117] Although there are variations on the definition of vested rights, the protections generally posit that an employee has a vested right to the terms of the plan in place on the employee's date of hire. See *State Constitutional Protection for Public Sector Retirement Plans*, prepared by the National Conference of Public Employee Retirement Systems, March 15, 207, *available at* http://www.ncpers.org/Files/News/03152007Retirement Benefit Protections.pdf. Any material changes can be made to apply only to new employees. The vested rights protections are not the same as those afforded a private sector participant's accrued benefit under § 411(d)(6). The latter allows changes to plan terms provided they do not reduce benefits accrued to date. The former prohibits changes to the terms that define an existing employee's benefit subject to a few narrowly drawn exceptions. See, e.g., Betts v. Board of Administration, 21 Cal. 3d 859 (1978). For example, if a public plan states that a plan member's benefits will be calculated with an age factor of two percent at age 60, with few exceptions, that factor cannot be changed for that employee during the employee's working life.

[118] *Available at* http://www.irs.gov/retirement/sponsor/article/0,,id=181908,00.html.

plan?[119] The type of clear explanations offered in the current Fix-it Guides can also help the plan administrative staff explain what needs to be corrected and the process to the boards that oversee them or the legislative body that must decide whether to make a legislative change.

The ACT recommends publication of a State and Local Government Fix-It Guide, once sufficient experience, gained in reviewing governmental plans in Cycles C and E, can be leveraged. Too early publication could be counterproductive to achieving the ultimate goal of widespread compliance among governmental plans if the remedies are unrealistic or too rigid. In the interim, much of the material already developed for 401(k) plans will also be useful for governmental entities that sponsor 403(b) and 457(b) plans.

3. Promote Coordinated Reviews for Large State Governmental Plans

Many states, including California,[120] have plans that cover state employees that also can be adopted by any state contracting agency for its employees. Typically, some optional provisions are permitted, but the core provisions embodied in state statutes are standard for all plans. Many county and regional entities offer a similar arrangement. The IRS could achieve significant efficiencies in the determination letter program if these plans were treated similar to volume submitters so that once the core provisions were reviewed, and compliance problems addressed, only optional provisions would need to be reviewed for a large number of plans. One promising example of the coordinated approach is presented by a group of county retirement systems in California. All are subject to the same statutory provisions although they are operated independently, and different practices have developed over the years. They are working with the Service to develop a process for having the common statutory provisions reviewed and uniform solutions worked out to address any compliance issues that are identified. Each system would also need to have its non-core provisions reviewed to obtain a determination letter, but the limited individual review could save the IRS, and the plan administrators, considerable time and frustration. The coordinated approach may also facilitate getting any legislative changes that may be needed through a fractious legislature. The IRS has encouraged this type of innovative response by demonstrating its flexibility in guidance, especially the FAQs.[121]

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[119] See *Employee Plans News*, Special Edition, May 9, 2008.

[120] The California legislature has established the California Public Employees' Retirement System. Cal. Gov't Code § 20000 *et seq*.

[121] For instance, the IRS responded as follows to the following question that almost all governmental plans face: if a plan has a failure that may be corrected under EPCRS and the provisions of the state law relating to the failure provide a higher benefit than the applicable provision of the Internal Revenue Code, will a state protected benefit be affected by the EPCRS principle of full correction?

> "State constitutions, statutes, and state court cases often provide participants with some protection or guarantee of their state provided retirement benefits. These governmental plans must satisfy a

4. Generally, Continue the Current Efforts at Education and Outreach

The governmental plans community has been out of the primary determination letter loop for many years. Rumors about Draconian consequences are widespread, fanning fears about letting the federal government in and fostering a defeatist attitude among plan sponsors. The experience of government plan filers in the current five-year Cycle could provide reassurance for those who held off because of all the unknowns. Already, there are indications that the IRS's helpful attitude is encouraging plans to come in.

To build on that momentum, the IRS should keep track of filers whose problems were dealt with quickly and fairly, and encourage them to appear at conferences attended by people who work in the public plan sector to discuss the determination letter process. If the IRS can reach consensus on the big issues, most notably how to address the state constitutional, statutory and common law protections, more governmental plans will seek the comfort regarding plan compliance that favorable determination letters offer.

E. EPCRS Improvements and Coordination

The EPCRS guidance for correcting plan document failures under VCP draws an important distinction between a "Nonamender Failure" to timely amend a disqualifying provision before the end of the applicable remedial amendment period, and an "Interim Failure" to timely adopt an interim amendment.[122] In the case of a Nonamender Failure,

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number of tax-qualification requirements under the Internal Revenue Code, including the benefit and contribution limits of section 415 and the compensation limits under section 401(a)(17). These plans must also follow their plan terms to retain their tax-qualified status so that the participants receive favorable tax treatment on their benefits and contributions. Under some circumstances the state provided benefits under the plan can conflict with the Internal Revenue Code requirements. Rev. Proc. 2006-27, containing the provisions of the Employee Plans Compliance Resolution System (EPCRS), provides that generally, 'a failure is not corrected unless full correction is made with respect to all participants and beneficiaries, and for all taxable years (whether or not the taxable year is closed).'

Under the EPCRS process, the correction should be reasonable and appropriate for the failure. What is reasonable and appropriate is based on the facts and circumstances of each case. Whether or not full correction is made is one of the facts and circumstances to be considered. While the IRS's expectation is that full correction will be made, the existence of a state law protecting pension benefits is one factor, among many, that may be taken into account in determining an appropriate correction method. A correction involving a state protected benefit should be submitted under the Voluntary Correction Program of EPCRS".

Retirement Plans FAQs regarding Governmental Plans and EPCRS, Q&A 3, *available at* *http://www.irs.gov/retirement/article/0,,id=181908.00.html.*

[122] Our best reading of the relevant provisions under Rev. Proc. 2008-50 is that separate procedural rules apply to (i) an Interim Failure, the failure to timely adopt an amendment during the interim period, and

the VCP rules require a determination letter submission, regardless of whether the VCP filing is submitted during an on-Cycle or an off-Cycle year.[123] On the other hand, in the case of an Interim Failure, a determination letter application should only be filed if the plan is submitted under VCP during an on-Cycle year.[124] Because of the confusion over the distinction between Nonamender Failures and Interim Failures, the ACT recommends that the Service clarify the difference between these two types of plan document failures and provide examples illustrating the separate procedural rules that apply to each.

The ACT also recommends that the Service provide clear guidance with respect to the manner in which VCP may be used to address situations in which the plan sponsor has timely amended and restated the plan document in good faith, but has failed to file a determination letter application before the end of its remedial amendment cycle. Specifically, the Service should clarify how such plan sponsors may make an off-Cycle filing and a simultaneous VCP submission (i) to correct any Nonamender Failures identified by the Service in the course of processing such off-Cycle filing, and (ii) to secure a favorable determination letter without any gap in its period of reliance. If this type of relief is deemed to be inappropriate or otherwise unavailable under VCP, a method of voluntary correction providing the relief described above should be developed for late filers and incorporated into the Service's determination letter program.

Due to the sizable difference between the VCP fee for Interim Failures and the significantly larger compliance fee for Nonamender Failures, the ACT also recommends that the Service review the fee structure under VCP for this type of plan document failure. The fees for each type of plan document failure should be rationalized so that they are proportionate to one another and to the nature of the document deficiencies corrected. The Service could undertake a study to determine the suitability and sufficiency of the compliance fees for correcting Nonamender Failures and Interim Failures in plan documents submitted under VCP. Based on the study's findings, the respective compliance fees should be modified to ensure that any difference in VCP fees for correcting plan document failures is appropriate and warranted.

When submitting off-Cycle determination letter applications in accordance with VCP requirements to correct Nonamender Failures, practitioners have found that such applications are not timely processed. To address this problem, the ACT recommends that the Service give off-Cycle submissions that are submitted in tandem with VCP applications, the same priority as on-Cycle submissions.

(ii) a Nonamender Failure, the failure to amend the plan to correct a disqualifying provision within the applicable remedial amendment period. See discussion in Section V.B. of this Report.

[123] Rev. Proc. 2008-50, 2008-35 I.R.B. 464.

[124] *Id.*

Given the significant increase in the workload of the Service's VC Unit due to submissions relating to plan document failures, the ACT also recommends that the Service further streamline the application and review process of the on-Cycle and off-Cycle submissions relating to Nonamender Failures and the on-Cycle submissions relating to Interim Failures. The Service could develop a new Appendix under its EPCRS guidance, providing model language designed to assist practitioners in drafting corrective amendments for specific types of Nonamender Failures and Interim Failures and to simplify the Service's review of such corrective amendments.

If the Service retains the interim amendment requirement in any form, the ACT further recommends that the Service permit Interim Failures to be remedied through the self-correction method under EPCRS. The Service could permit the adoption of an interim amendment by the end of the plan year following the plan year in which the good-faith amendment deadline occurred, provided that the plan amendment does not result in a violation of the anti-cutback rules under IRC § 411(d)(6).

In light of the complexity of the interim amendment rules and the confusion among practitioners with respect to the application of such rules, the ACT also recommends that the Service clearly identify for plan sponsors, the practitioner community and the VC Unit what interim amendments need to be made and when they need to be made (for an example of such a chart, see Section IX. H., and discussion regarding same in Section VI. B.).

F. Use of the Determination Letter Program for Policy Decisions

We note that there have been situations where the determination letter program has been used to effectuate policy changes. One example is the cash balance plan freeze on issuing determination letters.

1. Case in Point: The Cash Balance Plan Freeze 1999-2007

During the 1990s, a number of plan sponsors determined that a traditional defined benefit pension plan was no longer the appropriate retirement vehicle for their employees and instead decided to provide retirement benefits through cash balance plans. Some plan sponsors made this decision for economic reasons, others to better reflect that their workforces did not remain long enough to accrue a significant retirement benefit from a final average pay plan. Typically, the new program was implemented by a conversion of a traditional defined benefit plan to a cash balance plan.

Because a number of qualification issues arose due to conversions to cash balance plans, beginning September 15, 1999, a Field Directive was issued by the Service's Director, Employee Plans, requiring applications for a determination letter or a plan under examination that involved an amendment to change a traditional defined benefit plan into a cash balance plan ("cash balance conversions") to be submitted to the Washington, D.C. office of the Internal Revenue Service (the "National Office") for technical advice on the plan's qualified status.[125] In 2002, proposed regulations under Code § 411(b)(1(H) were issued that specifically addressed cash balance plans as part of a package of regulations that also addressed Code § 401(a)(4) nondiscrimination cross-testing rules applicable to cash balance plans.[126] In Announcement 2003-1[127], the Service announced that the cases subject to the 1999 Field Directive would not be processed pending issuance of regulations addressing age discrimination.

Congress also became interested in the cash balance plan and cash balance plan conversion issues after thousands of comment letters were submitted on the 2002 proposed regulations and the courts[128] began to address some of the age-discrimination issues in cash balance plan conversions. As a response to employer concerns over the 2002 proposed regulations, Consolidated Appropriations Act §5, (the "CAA")[129] provided that none of the funds made available under the Act could be used to issue any rule or regulation reaching similar results. Further, CAA required the Secretary of the Treasury to propose legislation providing transition relief for older and longer-service participants affected by cash balance conversions. As a result, in 2004, Treasury and the IRS withdrew the 2002 proposed regulations. In Announcement 2004-57, the Treasury and the IRS stated that they did not intend to process cash balance plan determination letter submissions which had been sent for technical advice to the National Office pursuant to the 1999 Field Directive while these issues are under consideration by Congress.[130]

As part of the Pension Protection Act of 2006, the Code, ERISA and ADEA were amended to remove the statutory and regulatory uncertainties involving cash balance and other hybrid plans by providing special rules relating to age discrimination in "applicable defined benefit plans." A special grandfathering rule applies to plans that were converted prior to June 30, 2005.[131] As a result, the IRS announced in Notice 2007-6 that it was beginning to process determination letter and examination cases that involved a conversion from a traditional defined benefit plan to a cash balance plan.

Although we understand that most of the cases which had been left in limbo have now been processed, such process was severely flawed. During the process, the IRS not only tried to implement and enforce new rules, it tried to do so retroactively.

[125] September 15, 1999 Field Directive (the "1999 Field Directive").

[126] 67 F.R. 76123. These proposed regulations replaced a 1988 proposal under §411(b)(1)(H).

[127] 2003-1 C.B. 281.

[128] See Cooper v. IBM, 274 F. Supp 2d 1010, (S.D. Ill 2003).

[129] Pub. L. 108-199.

[130] Announcement 2003-1, 2003-1 C.B. 281.

[131] Sec. 701(e)(5) of the Pension Protection Act of 2006 (the "PPA").

Prior to the 1999 Field Directive imposing the cash balance freeze, the IRS issued Notice 96-8.[132] This Notice provided certain guidance with respect to cash balance plans. This Notice provides: "The anticipated regulations will be effective prospectively. In addition, for plan years beginning before the regulations are effective, a frontloaded interest credit plan would not be disqualified for failing to satisfy section 411(a) or 417(e) if the amount of the distribution satisfied those sections based on a reasonable, good-faith interpretation of the applicable provisions of the Code, taking into account pre-existing guidance. For this purpose, plans that comply with the guidance in this notice are deemed to be applying a reasonable, good faith interpretation."

Notwithstanding the Notice's good faith interpretation standard, when processing cash balance plan determination letter submissions, the IRS, for the first time, disclosed its own interpretation of this Notice and notified plan sponsors this was the only valid good faith interpretation of the Notice. It then routinely told sponsors of plans that had otherwise complied with the Notice on a reasonable, good faith basis that their plans had to be retroactively amended to comply with the IRS's now disclosed interpretation of the Notice. Not only was the IRS's demand for retroactive correction contrary to the Notice's good faith interpretation standard, the IRS's interpretation of the Notice was contrary to the provisions of the Notice.

Cash balance plans were administered for 11-12 years (1996-2008) in compliance with Notice 96-8 based on its stated good faith interpretation standard. If the IRS wanted to change the guidance set forth in the Notice, it should have done so publicly and earlier through appropriate means. To attempt to retroactively change the rules via the determination letter process is unreasonable. The determination letter program should be a process solely to determine whether a plan complies with existing published rules. It should not be used as a mechanism to surprise plan sponsors by informing them of new, previously unpublished rules, especially where these rules are retroactive. To expect plans to alter prior plan administration (in this case 11-12 years' worth) to comply with new, unpublished rules wreaks havoc on the private pension system and provides employers even more reason to terminate existing plans or not adopt new ones.

2. Recommendation

The determination letter cycle program should be an efficient and straightforward process for plan sponsors to obtain a determination letter and should be based on current law and regulations. The use of the program by Treasury and the IRS to implement policy changes complicates and corrupts the process.

The ACT understands that Treasury and the IRS need to address policy issues as part of their responsibilities in administrating the tax laws. However, we do not think that those policy decisions should be made and implemented through the determination letter process. In this light, the ACT recommends that, in order to maintain the integrity

[132] 1996-1 C.B. 359.

of the determination letter process and at the same time avoid issuing favorable letters for unresolved issues, the Service could issue determination letters caveating that the letter does not address the particular issue (which the Service has done in other circumstances).

G. Clarify Which IRC § 415 Limitations Can Be Incorporated by Reference

Practitioners would find it useful to have more clarity regarding which qualification requirements may or may not be incorporated by reference in the plan document. For example, the regulations permit a plan to incorporate by reference the limitations of IRC § 415.[133] If the IRC § 415 limits can be applied in more than one manner, but there is a statutory or regulatory default rule, the default rule applies if the plan incorporates the limitation of IRC § 415 by reference.[134] If the IRC § 415 limits can be applied in more than one manner, but there is no statutory or regulatory default, then the plan must specify the manner in which the limitation is to be applied in addition to incorporating the IRC § 415 limits by reference.[135]

In the context of the "definition of compensation" for purposes of the IRC § 415 limits, the regulations state that if the plan uses one of the safe harbor definitions of compensation set forth in Treas. Reg. §§ 1.415(c)-2(d)(2)-(4), the plan automatically is considered to satisfy IRC § 415(c)(3). Thus, a plan that incorporates the limits of IRC § 415 by reference does not need to explicitly define what constitutes IRC § 415 compensation. However, the Service has taken a contrary position. In the Internal Revenue Manual, it states "[a] plan that otherwise incorporates IRC § 415 by reference must specify which definition of compensation is incorporated."[136] In addition, the IRS's Alert Guidelines for Limitations on Contributions and Benefits state "[a] plan that incorporates § 415 by reference must specify which definition of compensation is incorporated," referring to the various safe harbor definitions of compensation set forth in the regulations.[137] We note that the EP Determinations has addressed this issue in a Quality Assurance Bulletin dated December 7, 2009.

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[133] Treas. Reg. § 1.415(a)-1(d)(3)(i).

[134] Treas. Reg. § 1.415(a)-1(d)(3)(ii).

[135] Treas. Reg. § 1.415(a)-1(d)(3)(iii). For example, where an employer maintains two or more qualified profit sharing plan and a participant participates in two such plans, then both documents must specify which of the plan's annual addition must be reduced if the aggregate annual additions would otherwise exceed IRC § 415 limits.

[136] Internal Revenue Manual, Part 4 Examining Process, Chapter 72 Employee Plans Technical Guidelines, Section 6 Section 415(b). See also EP Determinations Quality Assurance Bulletin, FY-2004 No. 5 (July 6, 2004), stating that the plan must specify exactly which definition of compensation is being used under the terms of the plan, even if it is citing one of the definitions in Treas. Reg. § 1.415-2(d).

[137] See Employee Benefit Plans, Pub. 7001 (Rev. 3-2008).

Such positions and varying guidance leave practitioners and the IRS EP DL specialists confused, making plan drafting and the determination letter process more time consuming and tedious; while the Quality Assurance Bulletin is helpful, such guidance is not formally binding, and there is a need for formally binding guidance. It would be helpful to have one clear rule; to that end, the ACT recommends, for the sake of clarity and ease of plan administration, that the IRS issue a revenue procedure or a notice clarifying that the definition of compensation for IRC § 415 purposes be required to be contained in the plan document.

VII. Recommendations - Administrative

A. Expedite and Streamline Determination Letter Process

The ACT has sought out the opinions of stakeholders regarding what practical measures should be considered to expedite and streamline the manner in which the Service handles the determination letter process; moreover, the ACT visited Covington, Kentucky and Cincinnati, Ohio to get a view of the process "from the trenches." The following recommendations result from this effort:

1. Practitioners Making Multiple Filings

The ACT understands that IRS personnel working in EP Determinations currently have an informal practice of "batching" individually-designed plan determination letter requests of practitioners that file 30 or more of such requests at the same time. The ACT also understands that EP Determinations personnel also "batch" individually designed plan determination letter applications filed by the same practitioners within a 45-day period. Revenue Procedure 2005-16 contains special determination letter procedures for volume submitter practitioners and master and prototype plan mass submitters. Generally, such special procedures are tied to the volume submitters or "M&P" prototype submitters submitting opinion letter applications on behalf of at least 30 unaffiliated sponsors adopting the same basic plan document or specimen plan. Expedited and less complicated determination letter processing is available if a determination letter application involves a prototype or volume submitter plan. The ACT recommends that the current informal practice described above be continued, and perhaps be made into a more formal process and expanded. For example, the practice could also be used for practitioners filing a smaller number of plans (e.g., 10), or plans filed by the same practitioner could be routed to the same reviewer or group of reviewers, whenever filed. This reviewer or group of reviewers could be changed intermittently to avoid any potential impropriety or appearance of favoritism that might ensue over time. The ACT believes that any practice that encourages more efficient and timely processing of determination letter applications should be encouraged.

2. List Interim Amendments

Under current determination letter procedures, practitioners requesting a determination letter during the appropriate cycle are required to submit all interim amendments made to the plan being submitted since the issuance of the last determination letter received by the plan. However, under current procedures, when the IRS issues a favorable determination letter on the plan, the letter does not expressly cover the interim amendments submitted for review. The ACT recommends that favorable determination letters issued in the future expressly cover submitted interim amendments. In order to most efficiently adopt this recommendation, the IRS could require practitioners to submit a list of all interim amendments and the date of their adoption,[138] which could be referred to as a "self-identification sheet." The self-identification sheet could then be attached as an appendix to and referenced in the favorable determination letter.

3. Plan Qualification Checklist

Under current IRS determination letter procedures, practitioners are required to provide information on certain key qualification requirements through a "check the box" approach. The information provided on Form 5300 through this method addresses, for example, general eligibility provisions of the plan and the type of vesting schedule used. However, the specific plan sections that contain the particular required provisions are not required to be identified, and only a few qualification issues are addressed in the current form. The ACT recommends that a checklist be created, to be attached to Form 5300, that identifies the plan sections in which the various Code qualification requirements are satisfied, with the goal of expediting a reviewer's handling of a plan submission.

4. Eliminate Mini-Spikes

One of the main purposes of adopting the five-year staggered determination letter program for individually designed plans and the six-year staggered program for pre-approved plans was to alleviate the major cyclical fluctuations in determination letter requests following changes in law and regulations which caused the Service to divert resources away from plan examinations and towards compliance. The ACT understands that although the adoption of these programs has spread the workload for plan review over the relevant periods, the vast majority of the filings in each Cycle are submitted in the last month of the Cycle period. Thus, each filing Cycle is experiencing "mini-spikes" during the final month ending with the last day for filing for the plan sponsor's assigned Cycle.

The ACT recommends that the Service provide certain incentives to plan sponsors to file early in their assigned Cycle. One incentive that could be used to expedite the process would be to provide reduced user fees for filings made before July 1st. The ACT understands that user fees are determined by the type of case and average time spent on the case. While these characteristics would not change if a filing were made early, it appears to the ACT that the result of spreading out a Cycle's filings so that IRS

[138] This does not necessarily work for prototypes unless the IRS issues guidance specifically applicable to prototype providers. Current IRS guidance does not require the prototype provider to evidence a date of adoption on the face of an amendment. Thus, there may be many amendments to prototypes where all the Service could practically receive would be the prototype provider's assurance that the amendments were timely adopted, but no specific "date of adoption." If the process discussed herein is established, where all interim amendments are referenced in the favorable determination letter, the fact that there was no process for prototypes beforehand needs to be taken into account in a way that does not limit the scope of reliance on a determination letter.

staff workload would not see a "spike" during the last month of the Cycle may be worth the change in process that this proposal would require.[139]

In lieu of incentives, the Service could consider assigning different filing due dates within an assigned cycle year of the plan sponsor. Generally, Cycles A-E are assigned by the last digit of the plan sponsor's EIN. For example, if the last digit is 1 or 6, then the assigned cycle is Cycle A; if the last digit is 2 or 7, then the assigned cycle is Cycle B, etc. The IRS could require those plan sponsors whose EIN ends in 1, 2, 3, 4 or 5 to file during the first six months of the assigned cycle year, i.e., February 1 through July 31 and if the EIN ends in 6, 7, 8, 9, or 0, the plan sponsor would be required to file in the second six months of the cycle year, i.e., August 1 through January 31. Assuming that EINs are assigned randomly, the determination letter work load should be split between the first half of the cycle year and the second half of the cycle year, smoothing out the submissions and reducing the strain on the Service's resources.

The ACT acknowledges that different user fees and/or different filing due dates may lead to increased complexity and mistakes, but believes that, after a transition period, the benefits could well outweigh the costs.

5. Auto Closure Procedures for Certain Applications

The ACT recommends that the Service's EP Division develop "auto closure" procedures similar to what has been developed within the EO Division for Form 1024, *Application for Recognition of Exemption Under Section 501(a)*. Such "auto closure" procedures could be administered so that they only apply to determination submissions for plans which, by reason of their simplified design or lack of "risk factors", do not warrant a special review.

a. Auto closure for certain Form 5307 Filings

Based on information provided to the ACT by several managers and directors from the Service involved in the determination letter review process, it is our understanding that the Service receives a large volume of Form 5307 applications involving pre-approved plan documents with especially "straightforward" plan designs. An example of such a plan might include a pre-approved, volume submitter document for a money purchase pension plan with simplified design features (e.g., eligibility after one year of service for all employees meeting statutory eligibility requirements, 6-year graded vesting, salary ratio allocation).

We understand that the Service has developed auto closure procedures for reviewing certain Form 5307 submissions on behalf of pre-approved defined contribution plans with straightforward plan designs. We applaud these efforts and urge that "auto

[139] The ACT understands that this type of incentive – reduced user fees – was used to incentivize the use of electronic submissions by exempt organizations.

closures" be expanded as much as possible to include submissions that are relatively straightforward, such as, by way of example, those submissions that do not include elective determination requests with respect to testing demonstrations, and that do not have more than a minimal amount of amendments since the prior restatement.[140]

The expansion of an "auto close" Form 5307 review process would represent a common-sense modification to the Service's review procedures. The ACT believes that the adoption of this proposal to further streamline the review process for Form 5307 would be appreciated and embraced by the practitioner community, and would lessen the burden on the Service.

b. Auto closure for certain Form 5300 and 5310 filings

Based on information provided by representatives of EP Determinations, it is our understanding that the Service receives a significant volume of Form 5300 and 5310 submissions for individually designed defined contribution plans with a single participant or a small group of participants consisting of highly compensated employees only. Such participants, who have a substantial amount of control and influence over both the plan and the plan sponsor, do not need the same level of protection from a policy perspective that other participants generally require. Thus, the Service does not necessarily need to give the documentation for plans that benefit sole proprietors, partners or highly compensated employees exclusively the same level of scrutiny that is applied to other types of plans. Moreover, the plan designs and plan document requirements for defined contribution plans are generally less complex than those for defined benefit plans.

Accordingly, the ACT recommends that the Service implement auto closure procedures with respect to individually designed defined contribution plans that benefit a single participant or a group of participants comprised exclusively of highly compensated employees with straightforward plan designs. Just as an auto closure procedure for straight forward Form 5307 applications would lessen the burden on the Service as described in the preceding section, an auto closure procedure for Forms 5300 and 5310 would be similarly beneficial.

6. Electronic Filing Process

The IRS and other government agencies such as the PBGC (online premium filings and payments) and the DOL (EFAST Form 5500 filings) have made significant progress in the utilization of the Internet to publish forms and guidance, and to give taxpayers and plan sponsors the ability to submit filings and information electronically. Additionally, the IRS has reformed its internal processes for cataloguing and tracking determination

[140] In developing such procedures for expansion of Form 5307 auto closures, the Service should ensure that "auto closure" occurs after the expiration of the 60-day comment period prescribed under the notice to interested parties in connection with any Form 5307 submission.

letter applications through the use of the TE/GE Determination System ("TEDS") software platform.

Based upon survey responses from both practitioners and EP specialists, the ACT believes that there is significant opportunity for the IRS to further improve the determination letter application process by increasing the use of the electronic "channel." Greater utilization of electronic means for filing plan documents will facilitate and expedite Form 5300 processing by providing greater uniformity of document submissions and related demonstrations.

The IRS should establish a goal of creating an online filing system that would allow applications for determination letters by plan sponsors to be submitted through the Internet. The ACT understands that various security concerns exist, as well as budgetary constraints. Since the submission process does not necessarily include any confidential information, security concerns should be able to be addressed. Any budgetary constraints that exist should be tempered by the increased efficiency of an online process that will automatically reject incomplete filings and greatly reduce the amount of paper expended.

In advance of the development of an online filing and processing system, the EP Determinations division could create Web-based "demo" forms similar to what has been done for VCP filings and the related schedules. Due to the fact that such forms require an OMB number, their usage would be voluntary (as it was done for IRS Form 8821, Tax Information Authorization) and could be provided in the popular Adobe format on the IRS's Web site.

B. Customer Service Issues

1. TEDS Improvements

a. Background information gathered

Based on observations made during an on-site demonstration of TEDS, the ACT believes that TEDS is a powerful technology-driven tool for EP specialists, allowing them to manage cases more effectively and to store and retrieve plan document information more efficiently. Although the ACT received negative feedback with respect to the usefulness of TEDS from certain EP specialists, such criticism of TEDS may have been based on a negative view of digital technology generally. EP specialists with high levels of computer literacy lauded the usefulness of TEDS. This dichotomy in the feedback provided to the ACT suggests that there may be a "generational" divide between EP specialists who are comfortable using computer-driven platforms and those who have had little exposure to such technology during their careers.

TEDS was created to implement the "paperless" system for determination letter filings and to provide for efficient storage and ease of transferring cases. However, customers have received inquiries on various occasions from DL specialists indicating that they were missing pieces of a filing that were included in the submission previously sent to the IRS, especially filings involving large, complex plan documentation. From the ACT's due diligence, it appears that in many situations, whole files were sent back erroneously and prior plan documents may have been lost.

It is our understanding that the submissions are currently being optically scanned into TEDS. Unfortunately, in certain instances, the persons scanning such documents into TEDS seem to lack training and are, at times, inputting one side only of two-sided documents and placing materials into "[o]ther documents, amendments and other categories" without noting where such items belong and whether the items are related to one another.

The ACT also learned that if plan amendments are not relabeled and broken out for TEDS, the closing letter takes longer to create, as each date must be identified properly. Previously, with paper files, an EP specialist would staple such amendments individually and pencil the date on the first page so it could be easily identified and checked by anyone reviewing the file.

Further, on TEDS, it takes numerous steps to record a simple action. For example, the ACT has learned that once an EP determination specialist receives a phone call from the holder of a power of attorney, instead of simply opening a physical folder and jotting down a comment to record the conversation, it takes six steps or more using TEDS to reflect the call.[141]

For a Form 5307 review with an adoption agreement and only a few amendments, it appears from the comments received, that the TEDS system is adequate for review, especially if the individuals inputting the documents for scanning have received proper training.

For transfer and storage, the TEDS system is extremely useful. One of the advantages of TEDS, by reason of its elimination of the Service's reliance on hard copies, is that Service personnel do not have to package and ship/mail heavy boxes or requisition large numbers of file cabinets to hold them. In addition, flexi-place employees only have to tote their computers home.

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[141] The EP determination specialist needs to log on to TEDS and then go through 3 or 4 screens in addition to creating the actual substantive entry and the time entry. By way of example, the steps are as follows:

1. Log on
2. Go to "In-box"
3. Go "My Cases" and select case
4. At the Basic Case screen, select "Case Chronology"
5. Go to "File" and click on "Create Case Chronology Entry"
6. Select a "Current role" (usually "Specialist") and "Activity" (usually "Review Case" or "Request Information").

Based on the information provided from on-site interviews, the ACT learned that TEDS cannot be used to issue favorable determination letters, although the system can be used for virtually all other stages of the determination letter process. Our understanding is that the funding for TEDS was exhausted before this functionality could be created on this new system. Thus, EP specialists are forced to create the final determination letter on the predecessor system and then import such letter into TEDS, adding an inordinately time-consuming step to the determination letter process.

In summary, although much of the feedback received by the ACT included praise for the enhanced data storage and retrieval features of TEDS, some end-users would like and have suggested certain improvements.

b. Recommendations

(i) We recommend that the IRS develop guidelines as to when EP specialists may be given the discretion to use hard copies of the plan, rather than TEDS, for example, in large complex case filings, including, but not necessarily limited to, submissions for governmental plans and multiple employer plans.[142]

(ii) From comments we have received, it is clear that in various instances the process by which documents are scanned is not working properly. Priority needs to be given to properly training "intake specialists" in the TEDS system so that errors, such as scanning only the first side of double-sided documents, do not occur. Such training should also ensure that the appropriate personnel learn how to organize, file and correctly identify different types of documents so that they can be filed and retrieved properly.

(iii) We recommend additional funding for TEDS, so that EP specialists can use this paperless system throughout all stages of the determination letter process, including the issuance of a determination letter. The current arrangement under which specialists must access the predecessor system is inefficient, and this change should be made as soon as practicable.

(iv) The Service needs to improve its scanning capabilities and, before sending a file back to the holder of the power of attorney or plan sponsor, request any missing (or lost or misplaced) documents. In addition, the Service could require a complete list of documents submitted with an application for a determination letter, and if the agent does not have a document on that list, it would be far more cost- and time-effective to have the agent provide a clear list of missing items and give the holder of the power of attorney or plan sponsor an opportunity to complete

[142] For example, a Form 5300 or 5310 submission with multiple sets of plan documents, each with more than 100 pages and with as many as a dozen or more amendments, should be reviewed in hard copy. Quickly flipping the pages of paper documents, which can be spread out and compared against one another, would be far more efficient with respect to both the quality and speed of the review, in comparison to the more trying task of skimming through digital images on multiple computer screens.

the application before returning it. If those items are not provided by a certain date, then the application should be returned as incomplete with the opportunity to refile.

(v) From the comments we have received, it is clear that certain EP personnel have an aversion to certain technological aspects of TEDS. TEDS software engineers should routinely reach out to EP determination letter specialists, i.e., those who actively utilize the system, for their suggestions, comments and suggested improvements. The system should be enhanced and modified to accommodate the functional needs of the end-users.

(vi) A system that allows plan sponsors to file Form 5300 or 5310 submissions electronically would eliminate the above-mentioned scanning issues altogether and would make it less likely that submission documents will be lost or misplaced. As discussed in Section VII. A. 6, above, we recommend that the Service consider establishing a system that will accommodate electronic submissions for Forms 5300 and 5310.

2. Determination Letter Database

The IRS should create an online searchable database that will allow practitioners to: (i) find information regarding the status of a determination letter application, and (ii) retrieve old and prior determination letters issued. TEDS seems to have this capability already, and all that would be required is the necessary modification for public access. Code Section 6103(e) provides that taxpayers and other persons having a material interest in a return have a right, upon written request, to inspect or have disclosure of the applicable return. Such persons would include a practitioner holding a power of attorney with respect to the determination letter submission. There are, of course, legitimate privacy concerns in the dissemination of this information (see Federal Information Security Management Act of 2002 (requiring federal agencies to implement and document security programs for their Internet-based systems and databases)). However, the Service could develop codes and passwords (e.g., IRS's acknowledgement letter could include a special code assigned to each plan for accessing the database and require the plan sponsor or authorized practitioner to obtain a special PIN number in order to access the filing) to alleviate such concerns if the Service is willing to devote the resources to this matter, which we advise it should consider given the goal of efficient administration and customer service.

3. Better Training for Reviewers

Agents reviewing submissions should be better educated on the relevant laws and, at a minimum, be able to tell the difference between mandatory and discretionary changes. This will curb agents insisting on amendments that have no possible effect on a plan. Updated and periodic training would lead agents to ask better questions and limit the agent's need to request more information from the plan sponsor.

The Service could also implement a policy under which agents may request more information or ask questions of filers twice or thrice, and then all further questions must be approved by a manager.

The goal should be that the reviewers act and behave in a consistent manner. Quality assurance across the determination letter process should be an ongoing area whereby improvement is constantly sought. Ultimately, this will create a review process that is relevant and much more efficient, resulting in a decrease in the number of submissions being open for review at any one time.

4. Cross-Functional Staffing

The survey of plan sponsors and practitioners revealed a concern with the ability of EP determination specialists to review the applications and filings of more complex and unusual plans. Clearly, within the EP Determinations unit there are highly qualified specialists who are more than capable of reviewing these types of plans, but there is not an unlimited supply.

The determination letter specialists capable of reviewing ESOPs, cash balance plans and other complex plan designs are generally at grade 13 (a grade suitable to handle complex cases). Under current union work rules agreements, pay-related limitations apply where EP Determinations personnel at grade 11 (a level that is lower than grade 13) are assigned to cases that should otherwise be assigned to grade 13 determination letter specialists.

Often, however, grade 13 specialists are required to spend at least some of their time working less complex cases, or their time is taken up in performing the more perfunctory and clerical aspects of a determination letter filing. Furthermore, grade 11 specialists are capable of working on the easier elements of the complex cases assigned to grade 13 specialists.

Thus, the ACT recommends that grade 11 specialists be assigned to work on the less difficult aspects of complex cases, leaving the more challenging aspects of the submission to grade 13 specialists. Such cross-functional staffing would provide valuable training for the less-experienced grade 11 specialists, giving them experience with plan designs to which they would otherwise have no exposure. Additionally, this type of vertical integration in case management could significantly improve the efficiency and organizational speed at which determination letter submissions are processed by EP Determinations, which should help to alleviate the backlog that is so commonly associated with more complex plan designs (e.g., ESOPs). We note that a precedent exists for this type of vertical integration in EP Determinations, as demonstrated in the handling of cash balance conversions following the relevant field directive in 1999.[143]

To test the efficacy of this proposed organizational change, EP Determinations could staff a representative sample of ESOP cases under the auspices of a "pilot" program. Under the terms of such pilot program, a pair of grade 13 and 11 specialists would be assigned to each of the covered ESOP cases. Since an ESOP is essentially a profit-sharing plan with benefits that are distributable in stock of the employer, subject to an overlay of special requirements under Code Sections 409 and 4975, the grade 11 specialist could be asked to review the profit-sharing plan elements of the plan document as well as the simpler ESOP elements, leaving the remaining components of the submission to the grade 13 specialist's review.

C. Problem Resolution – Taxpayer Advocate/Designated EP Determination Letter Specialist

The Code's qualification requirements set forth a complex and confusing set of rules for compliance. Such complexity has the potential to affect the relationship between the EP determination specialist and the practitioner representing the plan sponsor from that of a cooperative relationship to that of an adversarial relationship. Certainly, such result is not in the best interests of the plan participants, plan sponsors, practitioners or the Service. The Service has had a history of assisting taxpayers. For example, the Office of the Taxpayer Ombudsman was created in 1979 to serve as a primary advocate within the IRS for taxpayers.[144] The Ombudsman had the statutory authority to issue a Taxpayer Assistance Order ("TAO") "if, in the determination of the Ombudsman, the taxpayer is suffering or about to suffer a significant hardship as a result of the manner in which the internal revenue laws are being administered by the Secretary."[145] By 1996, the Ombudsman was replaced with a Taxpayer Advocate.[146]

In an effort to resolve issues efficiently and expeditiously, the ACT recommends that the EP determination letter program make more and better use of the Taxpayer Advocate,

[143] On September 15, 1999, the Service's Director, Employee Plans, issued a field directive requiring that open determination letter applications that involved the conversion of traditional pension plans to cash balance plans be submitted for technical advice with respect to the conversion's effect on the qualified status of the plan. Thus, certain aspects of these determination letter submissions were reviewed and handled by the National Office. See also Notice 2007-6.

[144] For the history of the Ombudsman program, see http://www.taspresskit.irs.gov/TAS-History. This position was codified in the Taxpayer Bill of Rights (TBOR 1), which was included in the Technical and Miscellaneous Revenue Act of 1988.

[145] See TAMRA, Pub. L. No. 100-647, Title IV, Sec. 6230, 102 Stat. 3342, 3733 (Nov. 10, 1988).

[146] See Pub. L. No. 104-168, Sec. 101, 110 Stat. 1452, 1453 (July 30, 1996), creating the Office of the Taxpayer Advocate with rights to (1) assist taxpayers in resolving problems with the IRS; (2) identify areas in which taxpayers have had problems in dealing with the IRS; (3) to the extent possible, propose changes in the IRS' administrative practices to mitigate identifiable problems; and (4) identify potential legislation changes that would be appropriate to mitigate such problems.

when disputes arise between the assigned EP determination specialist and the practitioner representing the plan sponsor. In order to do so, the Taxpayer Advocate would need to be specifically trained in EP matters, particularly the determination letter process.

In addition, or in the alternative, the ACT recommends that a specific EP determination letter specialist or specialists in Cincinnati serve as a "facilitator" when disputes arise between the assigned EP determination specialist and the practitioner representing the plan sponsor. The position could be filled by a dedicated determination letter specialist who oversees the other specialists or one of numerous specialists who rotate in and out of such position. Hence, an informal program should be established that would involve a single dedicated EP determination specialist as the designated point person or the rotation of various EP determination specialists in such a role.

D. Off-Cycle Exceptions for Individually-Designed Plans

Generally, off-Cycle applications for determination letters on behalf of individually designed plans will not be reviewed until all on-Cycle plans have been reviewed and processed. However, in accordance with Revenue Procedure 2007-44, the following types of applications are given the same priority as on-Cycle applications: (i) terminating plans, (ii) any new plan whose next regular on-cycle submission period ends at least two years after the open submission period, and (iii) applications submitted in accordance with any published guidance requiring an off-Cycle submission in connection with a particular event. Under the current procedure, the Service will also consider priority requests for off-Cycle applications due to urgent business needs, but such applications will only be prioritized in limited cases where exceptional circumstances exist.

In light of the good faith need for determination letters before an applicable plan sponsor's next on-Cycle submission period, the Service should consider expanding the types of off-Cycle applications that should be given priority treatment. Specifically, off-Cycle filings for plans with substantial benefit changes should be given the same priority as on-Cycle applications. Furthermore, off-Cycle filings for plans directly impacted, or that will be directly impacted, by transactions in which the sponsoring or participating employer is involved, such as a merger, acquisition or other corporate reorganization, should also be prioritized. If requested, the ACT would be available to consult with the Service in determining effective standards as to which off-Cycle submissions would be granted priority.

The Service could also consider permitting off-Cycle filings during the first half of a Cycle period (to avoid mini-spikes). See discussion in Section VII. A. 4.

Various benefits practitioners have noted that off-Cycle submissions are not being processed on a timely basis. The ACT recommends the Service allocate dedicated personnel for off-Cycle applications, including but not limited to off-Cycle submissions made for terminating plans on IRS Form 5310. This proposed staffing change would be intended to reduce any backlogs in inventory and decrease the processing time for off-Cycle submissions, by increasing efficiency.

To ensure that plan sponsors do not abuse the privilege of making off-Cycle requests, the ACT recommends the Service increase the user fee for such filings. The ACT believes that a higher user fee would dissuade non-substantive filings.

E. Cycle-Changing Events for Individually-Designed Plans

Revenue Procedure 2007-44 states that an individually-designed plan's remedial amendment cycle may be changed as follows:

- If plans with different Cycles are merged, the merged plan's Cycle will be based on the EIN of the employer maintaining the merged plan.
- If an employer acquires an existing employer and its plan, the acquired plan's Cycle will be based on the EIN of the acquiring employer maintaining the plan.
- If there is a change in the EIN, controlled group status, or affiliated service group of the employer maintaining the plan, the plan's Cycle will be based on the changed EIN, controlled group status or affiliated service group.
- If a portion of a plan is spun off, the spun-off plan's Cycle will be based on the EIN of the employer maintaining the spun-off plan.
- If a plan changes its status by becoming or ceasing to be a multiemployer plan or a multiple employer plan, the plan's Cycle will be based on the plan's new status.

Depending on the EIN of the new plan sponsor or the plan's changed status, as applicable, these Cycle-changing events may force an employer sponsoring an individually- designed plan to file an application for a determination letter more than once in a five-year period, or extend the plan's open remedial amendment Cycle beyond five years.

Since the purpose of the Service's established system of cyclical remedial amendment periods for individually designed plans was to put such plans into five (5) pre-determined tranches, the ACT recommends employers, at their election, be permitted to retain the plan's existing Cycle or move to a new Cycle based on the EIN of the new plan sponsor or the plan's changed status, as applicable.

F. Plan Documentation

Good faith EGTRRA amendments and interim amendments are routinely submitted to the Service in connection with determination letter submissions, so that EP specialists can confirm their timely adoption. However, in accordance with the Instructions for

Forms 5300 and 5307, additional prior plan documentation is required whenever plan sponsors do not have a copy of the latest determination letter, or if no determination letter has previously been requested by the employer.[147] Thus, many plan sponsors who file determination letter applications have also been required to provide copies of prior plan restatements and other historical amendments, since the original establishment of the plan in certain instances.

As an internal resource for its EP specialists, the Service maintains guidelines with respect to any plan sponsor seeking a determination without the benefit of a GUST determination letter, as provided under the EP Determinations Quality Assurance Bulletin, *Verification of Prior Plan Documents in the Absence of a Determination Letter*, dated September 8, 2006.[148] Under these guidelines, if a GUST determination letter (or a GUST advisory or opinion letter in the case of a pre-approved plan) has not been issued for the plan, the specialist must request and verify all of the employer's GUST documents. If the plan was not timely amended for GUST, verification of full compliance with the Tax Reform Act of 1986, the Unemployment Compensation Amendments Act of 1992, and the Omnibus Budget Reconciliation Act of 1993 (collectively, "TRA '86") is required. If a TRA '86 determination letter has not been issued, all TRA '86 plan documents adopted by the employer must be requested and reviewed in their entirety. If no GUST or TRA '86 amendments have been made, verification of plan documentation for the Tax Equity and Fiscal Responsibility Act of 1982, the Deficit Reduction Act of 1984, and the Retirement Equity Act of 1984 (collectively, "TDR") is required only if operational violations of significant TDR-related provisions are revealed during the determination case review.

The application of this prior plan document rule is problematic, especially in situations in which the plan sponsor received a prior determination letter but is merely unable to locate a copy of it. It is not uncommon for an employer to change its plan document vendor from time to time, and it may make such change on an ongoing basis every five to ten years, or on an even more frequent basis. Due to the employer's reliance on its document provider, turnover in its human resources personnel or any number of

[147] The instructions for Line 3b of Form 5300 state, "If you do not have a copy of the latest determination letter, or if no determination letter has ever been received by the employer, submit copies of the initial plan, or the latest plan for which you do have a determination letter, and any subsequent amendments and/or restatements including all adoption agreements." The instructions for Line 3f of Form 5307 similarly state, "If you do not have a copy of the latest determination letter, or if no determination letter has ever been received by the employer, submit copies of the initial plan (or adoption agreement along with the appropriate opinion or advisory letter), or the latest plan (or adoption agreement along with the appropriate opinion or advisory letter), and any subsequent amendments and/or restatements." Additionally, the instructions for both Forms 5300 and 5307 state, "The IRS may, at its discretion, require a plan restatement or additional information any time it is deemed necessary."

[148] The EP Quality Assurance Bulletins are an internal resource tool for the Service's agents, and which may not be relied upon by taxpayers. The Bulletins are issued by the Employee Plans Quality Assurance Staff, and they cover topics of interest to ensure the consistent processing of case files by EP specialists.

additional reasons, the sponsor may not have been able to maintain a comprehensive record of its plan documents for the relevant period. Requiring copies of all applicable prior plan documents and amendments often necessitates contact with a prior document provider, which may have warehoused such documents or even disposed of them.

It is also not uncommon for one or more "predecessor plans" to be merged into a "surviving plan." Thus, when the surviving plan files for a determination, it may be required to provide copies of historical plan documents with respect to the plans that have been merged into it. Since the sponsor of the surviving plan may have little or no ongoing contact with the sponsors of the predecessor plans, this requirement may be virtually impossible to satisfy.

The prior plan document requirement is often extremely burdensome to employers, document providers and other practitioners. Additionally, this requirement can add long delays and unnecessary expense for the plan sponsor, who often has to solicit the information from a former vendor. It also delays the Service's processing time and ties up valuable resources each time a filing is delayed indefinitely as the plan sponsor attempts to track down all of the prior documents and amendments requested.

In cases where the sponsor of an individually designed plan is unable to locate a copy of its most recent determination letter, the ACT recommends that the Service limit its request for prior plan documents to the specific restatement covered by such prior determination letter and any subsequent amendments. Thus, the Service should make the presumption that any historical amendments preceding the restatement covered by the most recent determination letter are qualified as to their form and in compliance with applicable prior law. Accordingly, even though an employer in this situation would need to submit a prior restatement of the plan, it would not need to locate any historical documents and amendments that preceded such prior restatement.

With respect to an employer filing a Form 5307 for a pre-approved plan document that is unable to locate a copy of its most recent determination letter for the prior pre-approved plan document, the ACT recommends that the Service make the presumption that the prior plan document covered by such determination letter is qualified as to its form, but only if (1) the sponsor of such prior plan document received a valid opinion or advisory letter with respect to such pre-approved plan, and (2) the employer furnishes evidence that it timely adopted the interim amendments required with respect to the most recent determination letter. With respect to the latter proposed requirement, in many cases, employers that are on a prototype do not adopt interim amendments, as such amendments are adopted by the prototype sponsor. To provide proof of such timely adoption, the Service could permit the employer to submit an affidavit signed by both the employer and the employer's plan document provider, third party administrator or recordkeeper, confirming that the interim amendments were actually adopted on a timely basis. Such affidavit could be based on a model form developed by the Service, with the requirement that it be signed by both the employer and the applicable provider under penalties of perjury.

As previously recommended in Section VII. B. 2., the ACT also recommends that the Service create a database that allows practitioners and employers to retrieve copies of prior determination letters in the event that the employer is unable to locate a copy.

The IRS might consider implementing an official registration mechanism for each plan sponsor adopting a prototype plan, which would be administered by the prototype sponsor. This would make the tracking of prototype plans and their compliance in form with new laws easier for the plan sponsors, the Service and the prototype sponsors.

G. Strong Interaction with Education and Outreach Determinations

1. Education for IRS Personnel

As noted above in our discussion relating to customer service issues, it appears that the IRS staff members responsible for scanning determination letter submissions into TEDS need additional training to assure that the complete document is scanned successfully and also filed under its proper category on TEDS.

Issues have also arisen with respect to the consistency of review by various IRS staff, many of whom are outside of the Cincinnati office. For example, certain agents were unaware of Announcement 2008-23, *Issuance of Opinion and Advisory Letters and Opening of the EGTRRA Determination Letter Program for Pre-Approved Defined Contribution Plans*, and its impact on submissions. In another situation, an agent requested that an EGTRRA pre-approved document be amended to incorporate the final 415 regulations, presumably unaware that such amendment was not required under the Service's most recent guidance for pre-approved plan documents. In both cases, the practitioner needed to send copies of these IRS pronouncements to the agent.

A lack of consistency also exists with respect to the scope and nature of informational requests made by IRS personnel in connection with the review of submissions, and the manner in which such requests are communicated. Certain agents consistently ask for proof of compliance with the GUST RAP, while others request only copies of interim amendments. In situations where a submission fails to include the user fee, certain IRS staff will simply fax a request for the fee, while others will return the entire filing and require a full resubmission with the proper user fee. Furthermore, certain IRS staff make requests for information or plan document changes over the telephone, rather than making such requests in writing. Such verbal communication can be imprecise, and may be challenging in situations where it is difficult to understand the reviewer due to language barriers. The ACT also notes that faxing or emailing a request for additional information provides the applicant with additional time to respond, since the postal mailing of such request effectively takes up to seven to ten days of the allotted response time.

The ACT recommends that additional training be given to input takers in the TEDS system. Additional training is also recommended for the DL specialists submissions, to assure that they are aware of all current pronouncements from the Service regarding submission requirements. Guidelines should also be provided to DL specialists, to assure consistency with respect to the type of follow-up information or action required of applicants, and to assure consistency with respect to the manner in which such requests are communicated to applicants. Specifically, DL specialists should be instructed to make requests for additional information or plan changes in writing, and to use fax or email in lieu of telephone requests whenever possible.

2. Education and Outreach for Plan Sponsors and Practitioners

a. Current interim amendment rules

There is confusion on the part of plan sponsors and practitioners with respect to the rules for determining applicable remedial amendment periods and the related interim amendments. For example, at least one prominent government official has stated that a sponsor of an individually designed plan who timely files a Form 8905, *Certification of Intent to Adopt Pre-Approved Plan*, and then timely adopts a pre-approved plan document, may still have a qualification issue to the extent it did not timely adopt the interim amendments required for the pre-approved specimen document. This statement was made without support from any published guidance for this position, causing confusion over the application of the RAP rules with respect to plan sponsors converting from individually designed plans to pre-approved plans.

The classification of amendments as either a "discretionary amendment" or a non-discretionary "interim amendment" is another area of confusion for plan sponsors and practitioners. For example, there is no clear guidance on whether the optional provisions in a compliance amendment relating to the final IRC § 415 regulations were, in fact, subject to the same adoption deadline for non-discretionary provisions (which were required to have been adopted by the due date of the employer's 2008 tax return in the case of plans with calendar plan and limitation years). Informal guidance from the Service suggests that such optional provisions did not have to be amended by this deadline, but practitioners remain uncertain in the absence of any formal pronouncement from the Service on this matter.

It is our understanding that the Service encounters numerous issues and makes administrative decisions relating to interim amendments, remedial amendment periods and other similar issues. The ACT believes such information would be especially useful to plan sponsors and practitioners. Thus, the ACT recommends that the Service publish more specific guidance on the substantive and procedural issues addressed in this Report. This guidance should be in writing so that all applicants have access to the same information. This recommendation should not be construed in a manner that discourages the ongoing communication between the Treasury and the Service and the rest of the benefits community, such as the informational exchanges that occur through bar association, accounting and actuarial meetings. However, if administrative decisions have been made on specific issues, it would be helpful to publish them in the Service's newsletter or other publications, with the appropriate caveats. As discussed elsewhere in this Report (Section VI. B.), so long as the interim amendments continue to be required, the Service should develop for each Cycle the necessary amendments, an example of which is contained in Section IX. H. hereof for Cycle D.

b. Communicating best practices for DL filings

The ACT further recommends that the Service issue a list of the "top 10" or "top 20" mistakes made when applicants file for determination letters, and describe the "best practices" for how such mistakes can be avoided, or if need be, corrected.

Based on conversations with representatives of EP Determinations, it is our understanding that, whenever the Service makes a written request for additional information to the applicable employer or its representative, an Applicant Identification Sheet ("AIS") is generated with a unique bar code. The AIS accompanies each written request made by the Service, and the information requested by the Service is supposed to be returned together with the AIS. Employers and practitioners are asked to return the AIS along with the requested information, so that this new documentation can be scanned electronically on TEDS and filed under the correct case file. However, employers and practitioners are unaware of the significance of the AIS, and the ACT recommends that the Service increase awareness of it within the benefits community by publicizing the importance of returning the AIS (along with any requested information).

In the course of discussing the capabilities of TEDS with EP Specialists, it was communicated to the ACT that supplemental information provided in the form of a "footnote" on the pages of a Form 5300 or Form 5307 is not easily scanned and filed onto TEDS. It would be much more helpful, from a processing standpoint, if applicants included any supplemental information for their determination letter submissions as separate attachments, rather than including such information as footnotes on the actual pages of the Form. The ACT recommends that the Service make this clarification in the instructions to the relevant Forms.

H. Increased Staffing for EP Determinations

As noted above, EP Determinations has a backlog of cases and it does not expect to meet its objective of closing determination cases within one year of the end of the each applicable Cycle based on its current staffing levels. In addition, although the new staggered determination letter procedure has leveled out the number of individually-designed plan submissions across multiple Cycles, EP Determinations continues to experience "mini-spikes" in the volume of submissions at the end of any individual Cycle.

The ACT does not believe that EP Determinations will be able to eliminate the backlog of cases without additional funding and staffing. We recommend that the funding for EP Determinations be increased, enabling it to hire and train additional determination letter specialists with the requisite expertise to review additional cases.

To address the problem of mini-spikes in the volume of submissions at the end of each applicable Cycle, the ACT recommends that the Service consider creating a "variable workforce" within EP Determinations which could increase in size to accommodate any such mini-spikes in the future. Variable staffing for determination cases could be achieved by having EP Examinations personnel rotate through EP Determinations on a pre-determined basis at the end of each Cycle whenever mini-spikes are expected to occur. Such experience and cross-functional training could be valuable for EP Examinations personnel, and the additional staffing would help EP Determinations eliminate its growing backlog of cases.

VIII. CONCLUSION

This Report, which was developed collaboratively with the IRS, was prepared with the goal of improving the Service's new staggered determination letter program and ensuring that it will function as efficiently as possible and that it will promote the viability and vitality of the employer-provided private retirement system. The recommendations made by the ACT in this Report were formulated after careful consideration of the comments and supporting information submitted from various stakeholders in the benefits community. Such commentary was submitted in response to the ACT's surveys and interviews, enabling the ACT to collect invaluable insights from all types of plan sponsors, benefit practitioners and plan service providers, as well as from members of the Service and Treasury.

As discussed at length in this Report, the overwhelming majority of survey respondents spoke extremely negatively about the interim amendment requirement. Many thought that the applicable rules are difficult to manage, resulting in unnecessary additional costs to plan sponsors and increasing the likelihood of missing an amendment or filing deadline. It is our view that these requirements and certain other aspects of the existing determination letter program are placing the current pension system at risk, and the program can and should be reformed as soon as practicable.

The recommendations in this Report include proposals for changing the interim amendment requirement as well as specific proposals for improving and further streamlining the determination letter program. Given the considerable deliberation, effort and care with which the Report was prepared and the overwhelming amount of commentary provided by survey respondents requesting that changes be made to the current program, we respectfully request that the Service consider modifying the program in accordance with the ACT's findings and the recommendations presented in this Report.