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Determination Letter Limbo

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IRS makes Changes to Determination Letter Program

Sponsors of individually designed qualified retirement plans will need to adjust to the idea of operating without the IRS's official blessings when changing the plan document to comply with new laws and regulations. The changes won't affect plan sponsors who have adopted standardized preapproved plans, as many small plan sponsors do. Earlier this year, the IRS laid out its plans to scale back its plan determination letter program. Here's what you need to know.

"Off-Cycle" Submissions

The IRS established a system of rolling five-year reporting periods. Each sponsor of a non-preapproved standard plan was assigned to one of the periods based on the plan sponsor's employer identification number. Sponsors could seek a determination letter for remedial plan amendments (such as an amendment remedying a plan provision that might have been noncompliant) only once during its assigned five-year period.

Now, as of July 21, 2015, the IRS will no longer accept determination letter applications that are submitted "off-cycle." An off-cycle application is one that is filed "other than during the last 12-month period of a plan's remedial amendment cycle, that is, the 12-month period ending on January 31 of the last year of the cycle."

The timing question will become moot beginning in 2017, however, when the five-year remedial amendment cycle program will disappear entirely. At that time, the IRS will no longer issue determination letters for remedial amendments to sponsors of nonstandard plans. Plans covered by the "A" five-year cycle, however, get a small break: These plans will be able to submit determination letters between February 1, 2016, and January 31, 2017.

Surviving Determination Letter Categories

Determination letters will still be issued to all nonstandard plans, however, when a new plan is formed (the "initial determination letter") or is terminated. The IRS times these determination letter requests to the underlying events, not to a five-year cycle.

The IRS gave itself the freedom to make exceptions under "certain other limited circumstances that will be determined by the Treasury and the IRS." The agencies also can seek public suggestions on appropriate circumstances to grant an exception.

Avoiding Penalties

Why the changes to the determination letter program? The IRS is trying to more efficiently direct its limited resources because of budget cuts while at the same time Congress has enacted new laws that have stretched the agency's legal staff thin.

Although the IRS is scaling back its determination letter program, it's not cutting back on its regulatory compliance enforcement efforts, including plan audits. In the absence of remedial determination letters, audited plans determined to have compliance deficiencies could be subject to greater penalties than might otherwise have been the case. As a result, third parties that audit qualified plans might begin seeking formal assurances from the plan sponsor that its plan is compliant.

Keeping up to Date

Plan sponsors should keep a close watch for additional IRS guidance on the issues left unresolved by the IRS determination letter announcement. Moving ahead without formal approval from the IRS for remedial amendments may be tricky.

Master and Prototype, Volume Submitter Plan Document Guidance Updated

The IRS has updated some guidance on requesting preapprovals for master and prototype and volume submitter plan documents. The new guidance modifies and updates previous positions.

Most notably, under the new guidance, the IRS will now issue preapproval letters for many kinds of Employee Stock Ownership Plans (ESOPs) and defined benefit plans containing cash balance features.

Among other requirements for preapproval letters, cash balance plans must provide that, at all times, prior accrued benefits (and other enumerated benefits) are protected. If the cash balance plan was the subject of a conversion amendment, the plan must comply with the IRS minimum vesting standards and regulations for plan conversion amendments. And if it contains any structure of principal credits that increase with age, service or other measure during a participant's employment, those plan provisions must

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be definitely determinable, operationally nondiscriminatory, and at all times in compliance with the “133 1/3 percent rule” and enabling regulations.

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