Update on Future of the EP Determination Letter Program

Announcement 2004–32

This announcement provides an update on the status of the Service's continuing review of the Employee Plans determination letter program. The Service has considered the public comments on the second white paper on the future of the program that was published last year and has decided to implement a system of staggered remedial amendment periods under § 401(b) of the Internal Revenue Code for individually designed plans. This system will be implemented initially to stagger the expiration of individually designed plans' remedial amendment periods for the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107–16 (EGTRRA). The Service will closely monitor the implementation of this system so that any appropriate adjustments or changes to the system can be promptly made. The Service is also contemplating implementation of a system of six-year amendment/approval cycles for pre-approved plans (that is, master and prototype (M&P) and volume submitter plans), beginning with the submission of these plans for EGTRRA opinion and advisory letters.

Background

The Service has maintained an Employee Plans determination letter program for many years, essentially in its present form. Under this program, the Employee Plans (EP) component of Tax Exempt and Government Entities (TE/GE) issues letters of determination regarding the qualified status of retirement plans under § 401(a) and the status of related trusts under § 501(a). Determination letters provide assurance to plan sponsors, participants and other interested parties that the terms of employer-sponsored retirement plans satisfy the qualification requirements of the Code. Qualified plans offer significant tax advantages to employers and participants.

In recent years, the Service has undertaken a comprehensive review of its policies and procedures for issuing determination letters on the qualified status of retirement plans. The impetus for this review was a need for the Service to strike a more effective balance in the application of its limited resources among the EP determinations, examinations, voluntary compliance and customer education and outreach programs. The current determination letter program has been subject to periodic fluctuations (that is, peaks and valleys) in workload as a result of legislative changes. These fluctuations make resource planning and allocation difficult and may have an overall negative effect on the administration of the various EP programs. Thus, a goal of the program review has been to identify program improvements that will result in a more level determination letter workflow. While this review is still ongoing, the Service has already made a number of significant improvements to the determination letter program. See, for example, Announcement 2001–77, 2001–2 C.B. 83.

As part of the program review, the Service has published on its web site two white papers on the future of the EP determination letter program. The first white paper, published in August 2001, described a number of options for change as the Service looks to the future. The second white paper, published in May 2003, provided a more detailed explanation of a proposed system of staggered remedial amendment periods under § 401(b) that was one of the original options.

The staggered remedial amendment period system would establish regular five-year cycles for plan amendment and determination letter renewal. The cycles, which would be based on taxpayer identification numbers, would ensure that employers would not have to request determination letter applications more frequently than every five years.

The white paper proposed that the staggered remedial amendment period system could be implemented beginning with the remedial amendment period for EGTTRA. Notice 2001–42, 2001–2 C.B. 70, provides that the remedial amendment period for EGTRRA will not end before the end of the first plan year beginning on or after January 1, 2005.

Commentators on the second white paper were asked to express their preference between a staggered system and the status quo with respect to the remedial amendment period rules under § 401(b). The commentators were also asked to respond to specific questions about other options described in the second white paper. The commentators' responses to these questions, and the Service's conclusions, are summarized in general terms below.

Comments and Conclusions

1. Staggered versus status quo.

On the question that asked commentators to indicate a preference between a staggered remedial amendment period system and the status quo, comments were divided. More commentators recommended the status quo than the staggered system, but several made a strong argument that the staggered system would make the amendment and determination letter process considerably more manageable for employers and practitioners and would also improve compliance. Even among those who expressed reservations with the staggered system, several described changes to the system outlined in the white paper that would improve the system and perhaps tilt the balance in its favor.

The Service has continued to examine the effect of the fluctuations in determination letter workload on its resources and other programs. Despite significant changes that have already been made to

the determination letter program, and the resource savings that the changes have generated, the Service has concluded that the limitations on its resources and the interests of sound tax administration require consideration of a more fundamental change. Accordingly, the Service has decided to implement a staggered remedial amendment period system for individually designed plans. The system will be implemented initially to stagger the expiration of individually designed plans' remedial amendment periods for EGTRRA. The system will generally be designed along the lines of the white paper proposal, so that, for example, plans may use their EGTRRA remedial amendment periods to adopt retroactive remedial amendments for guidance changes. The Service recognizes that the system described in the white paper may have to be adjusted or changed based on actual experience. The Service will closely monitor the initial implementation of the system and, on the basis of its experience and the experience of parties affected by the system, will make appropriate changes as quickly as possible.

2. Annual Plan Updates

The second white paper discussed the possibility of requiring plans to be updated annually. An annual plan update requirement could be established either without making other changes to the current determination letter program or in combination with a system of staggered remedial amendment periods. In the latter case, plan sponsors would not need to request determination letters more frequently than every five years to have reliance even though plan amendments could be required every year.

Although a few commentators recommended a requirement for annual plan updates as the surest way to keep plans in compliance and safeguard participant rights, most commentators expressed the opinion that such a requirement would be so costly and burdensome as to be an impediment to plan formation and preservation. While annual plan updates are desirable, the Service will not consider this option further at this time. The Service may revisit this option in the future.

The Service will, when appropriate, require plan sponsors to adopt good faith plan amendments sooner than the end of the plans' remedial amendment periods. In this case, plan sponsors will have the full remedial amendment period in which to perfect any good faith amendments adopted earlier within the period. The Service will endeavor to publish model or sample amendments to assist plan sponsors in the adoption of required amendments and will design the amendments to permit their adoption by sponsors of M&P and volume submitter plans on behalf of adopting employers whenever practicable.

3. Pre-approved Plans

The second white paper proposed alternative special remedial amendment period rules for pre-approved plans (M&P and volume submitter (VS) plans). One alternative would require pre-approved plans to be amended every year so that the plans would always be up-to-date for employers whose five-year cycle ended in any given year. The other alternative would establish five-year cycles for updating the pre-approved document. This alternative would ensure that the pre-approved document would not have to be re-approved more than once every five years, based on the TIN of the document sponsor. Under this alternative, adopting employers' cycles would be the same as the cycle of their pre-approved document (rather than being based on the employers' TINs).

Persons who commented on these alternative rules generally expressed the opinion that the annual amendment alternative would be too burdensome. Many also noted that the other alternative would result in some pre-approved plans being significantly more up-to-date than others at any given time, a result also considered undesirable. As a result of these comments, the Service is considering a new approach with respect to pre-approved plans.

The new approach now being proposed would establish regular six-year amendment/approval cycles for all pre-approved plans, beginning with the submission of these plans for EGTRRA opinion and advisory letters. This system would generally work as follows: In year one, all pre-approved defined contribution plans would be required to be updated and submitted for approval based on the law in effect at that time. The Service would process these applications in years two and three. Adopting employers would then have a fixed date by which to adopt the approved plans (for example, by the end of year five). Meanwhile, in year three, all pre-approved defined benefit plans would be required to be updated and submitted for approval based on the law in effect at that time. The Service would process these applications in years four and five and adopting employers would have to adopt the approved plans by the end of year seven. The cycle would begin again in year seven; that is, in year seven, all pre-approved defined contribution plans would again be required to be updated and submitted for approval based on the law in effect at that time. As noted above, good faith plan amendments will be required to be adopted sooner than the end of plans' cycles, when appropriate.

While the general approach describes a fixed cycle repeating itself every six years that would not be interrupted or changed due to changes in law, the Service recognizes that the system would need to be flexible to allow the cycle to be modified when appropriate, particularly in response to the changing needs of plan sponsors. (For example, if it became clear that needed plan changes were more complex and time-consuming than anticipated, an appropriate delay could be provided.) Nevertheless, it is hoped that this system would introduce more predictability into the current process and allow for better planning.

This system would also eliminate the so-called 12-month rule on which the determination of adopting employers' remedial amendment period was formerly based. It would substitute a fixed, easily communicated and understood date that would apply to all adopting employers. It is also anticipated that this system would allow sponsors and VS practitioners to amend their plans and apply for new letters in years when they would not otherwise be required to file, provided that the plans are again amended, as necessary, and resubmitted in the next cycle year. Of course, applications filed in cycle years (that is, required applications) would be accorded higher priority and would therefore be reviewed before applications filed in "off-cycle" years.

Under this system, employers who are not adopters of a pre-approved plan, but who certify, before the end of their plan's

remedial amendment period, their intent to adopt a pre-approved plan, will be granted the appropriate extension of the remedial amendment period. For example, assume the remedial amendment period for an employer's individually designed plan ends on December 31, 2010, and on that date the employer certifies its intent to adopt M&P plan *A* which was updated and submitted for a new opinion letter in 2010. In this case, the plan's remedial amendment period will be extended to the end of the fixed period for "timely" adopting plan *A* after the new opinion letter is issued.

The Service is also considering whether there may be appropriate, limited circumstances in which the remedial amendment period for a plan that is not a pre-approved plan, but is substantially similar to a pre-approved plan and submitted by the pre-approved plan's sponsor, should be extended to the end of the period for "timely" adopting the pre-approved plan. The Service believes that providing such an extension generally to all "substantially similar" plans could undermine the pre-approved plan programs and invite abuse. However, the Service welcomes comments identifying limited circumstances where such an extension would be appropriate and would not pose such risks, and also welcomes suggestions for criteria to be used in determining that a plan is substantially similar to a pre-approved plan.

Next Steps

The Service intends to proceed with the development of guidance necessary to implement a staggered remedial amendment period system, essentially along the lines of the white paper. In developing this guidance, the Service will carefully consider those suggestions that have been made to improve the system outlined in the white paper. In addition, interested persons will be given opportunity for further input as the appropriate guidance is developed. The Service will initially implement the staggered remedial amendment period system in conjunction with the opening of the determination letter program for EGTRRA.

In Announcement 2004–33, page 862, this bulletin, the Service has asked for public comments on a draft revenue procedure for pre-approved plans. Persons submitting comments in response to Announcement 2004–33 are also invited to comment on the six-year amendment cycle for pre-approved plans described in this announcement.

Drafting Information

The principal author of this announcement is James Flannery of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this announcement, please contact the Employee Plans' taxpayer assistance telephone service at 1–877–829–5500 between the hours of 8:00 a.m. and 6:30 p.m. Eastern time, Monday through Friday (a toll-free number). Mr. Flannery may be reached at 1–202–283–9888 (not a toll-free number).