



July 24, 2018

Internal Revenue Service
CC:PA:LPD:PR (Notice 2018-24)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Notice 2018-24 – Request for Comments on Scope of Determination Letter Program for Individually Designed Plans During Calendar Year 2019

Dear Sir or Madam:

The American Institute of CPAs (AICPA) submits the following comments in response to Notice 2018-24 – Request for Comments on Scope of Determination Letter Program for Individually Designed Plans during Calendar Year 2019 (“the Notice”). The Notice requests feedback related to the types of individually designed plans (IDPs) that the Internal Revenue Service (IRS) and the Department of the Treasury (“Treasury”) should consider when accepting determination letter applications if the scope of the determination letter program is expanded during 2019.

This letter was developed by members of the AICPA Employee Benefits Tax Technical Resource Panel and approved by the Tax Executive Committee.

Summary of Recommendations

1. The AICPA encourages the IRS and Treasury to expand the scope of the determination letter program to accept applications for determination letters for certain IDPs during 2019 and after.
2. The AICPA recommends accepting applications for determination letters for IDPs in the following circumstances:
 - a. Certain Employee Plan Compliance Resolution System matters and plans with adoption agreements that include significant pre-approved plan document changes;
 - b. Qualified plans with multiple benefit structures; and
 - c. Employee Stock Ownership Plans.

Background

The purpose of the determination letter program is to provide assurance to plan stakeholders (e.g., plan sponsors, participants, beneficiaries, auditors, counsel, etc.), through the issuance of a favorable determination letter by the IRS that the written terms of a qualified retirement plan are in compliance with the tax qualification requirements of section 401(a)¹ of the Internal Revenue Code (IRC).

If a plan is deemed qualified, plan sponsors and participants are assured of the following tax benefits:

- Employer receives a current tax deduction in the amount of the contribution made to the plan (subject to limitations);
- Participants can defer tax on the amount contributed to the plan; and
- Participants receive tax-free growth on the contributions until distributed from the plan.

Prior to January 2, 2017, determination letters were issued by the IRS upon the request of qualified retirement plan sponsors, generally upon establishment and termination of a qualified retirement plan. Additionally, plan sponsors could request determination letters when changes in the law could affect the plan. To inform plan sponsors of law changes, the IRS publishes, on an annual basis, a Cumulative List of Changes in Plan Qualification Requirements (“Cumulative List”). Determination letter requests based on law changes in the Cumulative List are known as interim determination letter requests. Plan sponsors were permitted to file interim determination letter requests based on the listed changes during the determination letter review process for applications filed during a 12-month submission period.

In an effort to coordinate the receipt of the high volume of interim determination letter requests, the IRS established a 5-year remedial amendment filing system. The system provided that an IDP’s determination letter filing due date was based on the employer identification number (EIN) of the plan’s sponsor. An IDP is a retirement plan that meets the specific needs of a single employer or multi-employer group which has not been approved by the IRS. Under this system, sponsors of IDPs were generally permitted to apply for a determination letter once every 5 years. If a determination letter application was filed with the IRS anytime other than during the last 12-month period of a plan’s remedial amendment cycle, the application was considered filed off-cycle.²

Due to its limited resources, the IRS issued Announcement 2015-19 – Revisions to the Employee Plans Determination Letter Program, which eliminated the staggered 5-year remedial amendment cycle for IDPs beginning on January 2, 2017. Since January 2, 2017, IDPs are entitled to submit applications for determination letters solely under the following circumstances:

¹ All section references in this letter are to the Internal Revenue Code of 1986, as amended, or the Treasury regulations promulgated thereunder.

² Revenue Procedure 2007-44, section 14.01.

- As sponsors of Cycle A plans described in section 9.03 of Revenue Procedure 2007-44;
- During initial plan qualification on Form 5300, *Application for Determination for Employee Benefit Plan*; and
- Upon plan termination.

Due to the decision by the IRS and Treasury to reduce the frequency with which IDPs can apply for a determination letter, plan stakeholders lack certainty regarding whether the written terms of an IDP remain qualified when certain changes to the plan documents are made.

We applaud the IRS and Treasury for recognizing, through the issuance of Notice 2018-24, the need for stakeholders of IDPs to receive assurance that the written terms of the plan remain qualified by possibly accepting their application for a determination letter in 2019. Notice 2018-24 requests comments on the potential expansion of the determination letter program to allow, during 2019, sponsors of IDPs to request a determination letter beyond the limitations proposed in Announcement 2015-19. Specifically, the IRS and Treasury have inquired about the types of plans they should consider in the determination letter application process, as a result of significant law changes (as defined in Rev. Proc. 2016-37), new approaches to plan design, and the inability of certain types of plans to convert to pre-approved³ plan documents.

Recommendations

A. Expand Scope of Determination Letter Program For 2019 and After

Recommendation

The AICPA encourages the IRS and Treasury to expand the scope of the determination letter program for IDPs during 2019 and after.

Analysis

The expansion of the determination letter program during 2019 and after would enable more plans to receive a favorable determination letter providing assurance to plan stakeholders that the written terms of a qualified retirement plan are compliant with current law.

B. Accept Applications for Determination Letters for Certain Employee Plans Compliance Resolution System Matters and Pre-Approved Plans with Adoption Agreements that Include Significant Pre-Approved Plan Document Changes

³ Pre-approved plans are standardized plans that have been “approved” by the IRS, based on the IRS’s review of the plan document and an agreement by the IRS that the plan document meets the requirements of sections 401, 403(a), or 403(b).

Recommendation

We recommend that the IRS and Treasury permit plan sponsors to apply for determination letter regarding certain Employee Plans Compliance Resolution System (EPCRS) matters and significant pre-approved plan document changes.

Analysis

Under EPCRS,⁴ a plan sponsor may cure certain qualification failures that arise within their plan document or with plan operations through a corrective plan amendment.

Plan document failures include the following:

- A plan provision, or the absence of a plan provision, violates the requirements of section 401(a) or section 403(a);
- A nonamender failure, including the failure to timely adopt a written section 403(b) plan;
- The failure to adopt good faith amendment(s); and
- A failure to adopt interim amendment(s).

Plan sponsors often cure operational failures by plan amendment to align plan provisions with plan operations. For example, a plan sponsor may request a retroactive plan amendment from the IRS under the Voluntary Compliance Program (VCP) or under the Audit Closing Agreement Program (“Audit CAP”) to align plan provisions with plan operations.

We suggest allowing a plan sponsor to include in their submission under VCP or a correction under Audit CAP, a request for an IRS determination letter on a proposed retroactive plan amendment. The receipt of a favorable determination letter under these circumstances will provide stakeholders with assurance that the form of the plan remains qualified under section 401(a) or section 403(a) after adopting a plan amendment in connection with the corrective action.

Additionally, plan sponsors may make a significant operational change (e.g., excluding a division of employees when the document does not allow the limitation while still passing section 410(b) coverage testing, utilizing an outside trust agreement that is not part of the pre-approved plan, etc.) to an IRS pre-approved plan document, adding features that cause the plan to vary from the pre-approved “check-the-box” format. In these instances, the plan may operate similarly to an IDP and would benefit from receiving a favorable determination letter indicating that the written plan documents remain qualified after making a significant operational change.

⁴ Rev. Proc. 2016-51.

C. Accept Applications for Determination Letters for Qualified Plans with Multiple Benefit Structures

Recommendation

We recommend that the IRS and Treasury permit plan sponsors of qualified retirement plans with multiple benefit structures, including collectively bargained plans and merged plans with multiple benefit formulas that were amended since the last determination letter, to submit a determination letter request during 2019 and after.

Analysis

Many qualified defined benefit plans with a traditional (i.e., final average pay) formula or a statutory hybrid formula are complex since they contain multiple benefit formulas within the plan document. The presence of multiple benefit formulas within a qualified plan reflects the choice of the plan sponsor to design the plan to meet organizational goals and protect legacy benefits. For example, the contracts for plans subject to collectively bargained agreements are often renegotiated resulting in intricate formula or benefit amendments. Also, merged plans often contain various benefit formulas in both the defined contribution and defined benefit context. The complexity caused by the presence of multiple benefit formulas within the plan makes it difficult for the plan to utilize a pre-approved plan. Generally, those plan sponsors use IDPs which are currently limited in terms of the circumstances under which they can apply for a determination letter.

Additionally, multiple benefit formulas are often required because the plans are subject to the “anti-cutback” rules of section 411(d)(6) which prohibit a plan sponsor from adopting a plan amendment that decreases a participant’s accrued benefit. The requirement to comply with section 411(d)(6) is a source of complexity within qualified benefit plan documents and often IDPs are needed to accommodate these requirements. For example, if the plan sponsor amends its plan to change the benefit accrual formula, the change only applies prospectively to current participants. Whether the plan sponsor makes the change prospective for plan participants or avoids a violation of section 411(d)(6) by applying the new formula only to new participants, the result is the same – a plan document that must contain provisions that describe more than one benefit formula.

An additional source of complexity regarding the requirements to comply with section 411(d)(6) relates to plan mergers. In many cases, the target company sponsors a qualified plan which the acquirer may retain and possibly merge into its own plan. It is likely that the benefit formula in the target plan differs from the benefit formula in the plan sponsored by the acquiring company. If the plans are combined, the plan sponsor could incur issues similar to those faced by a plan sponsor that amends its plan.

Plans with multiple benefit structures often do not fit into the pre-approved plan “bucket” and IDPs are necessary to accommodate them. However, due to their complexity, it is imperative that plans with multiple benefit structures can obtain an interim determination letter from the IRS in order to assure stakeholders that the written plan documents remain qualified.

D. Accept Applications for Determination Letters for Employee Stock Ownership Plans

Recommendation

We recommend that the IRS and Treasury permit applications for determination letters for Employee Stock Ownership Plans (ESOPs) that have adopted certain amendments since their last determination letter, that affect the following plan provisions:

- Distribution provisions/policies;
- Contribution formulas; or
- Compliance with section 409(p) (applicable to S-corporation ESOPs).

Analysis

ESOPs often have complex plan designs that are not conducive to the utilization of pre-approved plan documents and, as a result, they use IDPs. While an ESOP can receive a determination letter upon its inception, if they are an IDP, plan sponsors will not receive determination letters related to the amendment of various significant plan provisions over the lifetime of the plan.

The following discussion represents examples of situations where an ESOP plan sponsor determines that it is necessary to amend specific provisions of the plan and utilize IDPs versus pre-approved plans:⁵

- Distribution policies and repurchase obligations;
- Contribution formulas; and
- Compliance with section 409(p).

Distribution Policies and Repurchase Obligations

A plan's distribution policy is a complex plan provision that may require amendment over the life of the plan. A plan's repurchase obligation is directly connected to the plan's distribution policy and is a primary consideration for all ESOP sponsors. Since repurchase obligations continuously change, it is likely that a distribution policy will not remain static over the lifetime of a plan, particularly for smaller employers. Managing the repurchase obligation is crucial to the continued success and financial strength of an ESOP and the plan sponsor. ESOP sponsors often develop complex distribution strategies to meet the repurchase obligations in order that the repurchase obligation does not adversely impact the plan sponsor's economic health. Generally, a pre-approved plan cannot accommodate these features and an IDP is required. Plan stakeholders would benefit from receiving a favorable determination letter indicating that the written plan documents remain qualified after plan amendments are made.

⁵ The list of situations where a plan sponsor must amend specific provisions of the plan is meant as a sample and is not meant as a comprehensive list.

Contribution Formulas

Another ESOP plan feature that may require the use of an IDP is the allocation formula for contributions that may change over time. For example, the sponsor of a 401(k) plan may also maintain an ESOP. Once the ESOP is implemented, the plan sponsor may begin making a matching contribution in the form of stock to the ESOP. The plan sponsor may require different matching formulas for different divisions, subsidiaries or companies in the controlled or affiliated service group. The receipt of a favorable determination letter would provide assurance to plan stakeholders that the written terms of the plan remain qualified after the appropriate amendments are made to the plan.

Diversification Out of Company Stock

Occasionally, after a leveraged ESOP loan is repaid and there are no new shares allocated to plan participants each year, it is difficult for new plan participants to become stockholders. This issue is commonly referred to as a “have and have nots” situation. Plan sponsors may need to amend the ESOP plan to expand statutory diversification which would allow higher rates and/or an extended period of time to choose to diversify. Shares that are diversified are often retained within the plan using cash from a current contribution.

Another strategy to provide shares available for allocation is to force terminated participants to discontinue investment in the employer’s stock. This strategy is sometimes called “mandatory diversification.” Requiring terminated participants to diversify out of employer stock can provide a steady stream of shares within the plan using current contributions for needed liquidity. IDPs are typically needed to provide these ESOPs with the type of plan design flexibility which allows for various share allocation strategies. Allowing these plans to apply for a determination letter would provide plan stakeholders with assurance that the written terms of the plan remain qualified once any necessary amendments are made to the plan.

Compliance with Section 409(p)

S corporations are required to comply with the anti-abuse rules of section 409(p). To meet the section 409(p) requirements, plan sponsors may need to make design changes to the plan via plan amendment after initial implementation of the ESOP as a result of sponsorship ownership and/or participant relationship changes. These design changes may include the implementation of a more liberal diversification policy or the addition of an in-service distribution policy to the plan. Generally, a pre-approved plan will not accommodate these changes and an IDP is used. Allowing ESOPs that make these types of changes to apply for a determination letter would provide assurance to plan stakeholders that the plan remains qualified once the amendments are made to the plan.

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We appreciate your consideration of these comments and welcome the opportunity to discuss these issues further. Please feel free to contact Jeff Martin, Chair, AICPA Employee Benefits Taxation Technical Resource Panel, at (703) 946-4467, or Jeffrey.martin@us.gt.com; Kristin Esposito, Senior Manager – AICPA Tax Policy & Advocacy, at (202) 434-9241 or Kristin.esposito@aicpa-cima.com; or me at (408) 924-3508 or Annette.Nellen@sjsu.edu.

Respectfully submitted,



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