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IRS Cracks Open Determination Letter Program for Merged Plans and Hybrid (Cash Balance) Plans

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Effective September 1, 2019, plan sponsors can ask IRS to review the plan qualification of hybrid plans and certain merged plans through the IRS determination letter program. This opportunity will last 12 months for hybrid plans and is ongoing for merged plans.

Background

When IRS curtailed its program for issuing determination letters for individually designed plans (other than for initial plan qualification and for qualification on plan termination) effective January 1, 2017, it promised to consider special circumstances that would merit their attention. Last year, IRS asked for input on what special situations would warrant review. Constituents identified mergers and acquisitions and hybrid plans such as cash balance plans among other scenarios (see our July 10, 2018 *For Your Information*).

And the winners are…

In Revenue Procedure 2019-20, IRS announced both limited and ongoing changes to the determination letter program that will allow more plans to be reviewed. While the review is underway, the plan's remedial amendment period is extended under the normal rules for plan submissions. This allows for any necessary amendments until the expiration of 91 days after the date the letter is issued. IRS notes that this will not provide anticutback relief such as that provided for a limited period in the hybrid plan regulation.

Hybrid plans — a 12-month window of opportunity

Starting September 1, 2019, sponsors of individually designed hybrid plans (such as cash balance and pension equity plans) may ask for a review of their documents. This opportunity closes August 31, 2020.

The review will be based on the 2017 Required Amendments List (Notice 2017-72), which included the final hybrid plan regulations and the final regulations for partial annuity distribution options (see our December 12, 2017 *For Your Information*). It will also consider all Required Amendments Lists, and Cumulative Lists issued prior to 2016.

Because the IRS may impose sanctions if document failures as defined in EPCRS are discovered during its review, this opportunity cannot be used to avoid VCP user fees (for example, for failures involving interim amendments). However, under this program, sanctions will not be imposed for failures identified by IRS that are related to the final hybrid plan regulations.

Mergers & acquisitions — ongoing availability, but within a limited time period after the transaction

Starting September 1, 2019, IRS will accept determination letter applications for merged plans if:

- the plan merger occurs no later than the last day of the first plan year that begins after the plan year when the corporate merger, acquisition, or similar transaction between the plan sponsor and a previously unrelated entity occurs, and
- the application is submitted after the plan merger and before the end of the first plan year that begins after the plan merger effective date.

The review will be based on the Required Amendments List issued during the second full calendar year preceding the submission of the determination letter application, as well as on all previously issued Required Amendments lists and Cumulative Lists.

Comment. The transition period for coverage testing ends on the same date by which the plan merger must take place to file for a determination letter under this program. Under the coverage rules, the transition period would be cut short by a significant coverage change under the plan — so a merger date that would allow the plan sponsor to request a determination letter under this program may cut the transition period short if benefit formula changes for either of the pre-merger groups are made effective on that date. Although a plan merger (without any change to the plan benefit formulas or other rights) would not be considered a significant change in coverage to cut the transition period short, it is not clear how nondiscrimination testing on a combined 401(k) plan would be performed under certain circumstances.

Possible sanctions

Reduced sanctions (equal to the VCP user fee that would have applied) will apply to plan document defects discovered under this program if the amendment that caused the failure was either adopted timely in good faith with the intent of maintaining the plan's qualified status, or if a required amendment was not timely adopted based on the plan sponsor's reasonable and good faith belief that an amendment was not required. If the requirements for reduced sanctions are not met, the usual rules for determining Audit CAP sanctions would apply.

As with hybrid plan submissions, IRS may impose sanctions if document failures as defined in EPCRS are discovered during its review. Sanctions will not be imposed for failures related to the amendment to effectuate the merger.

In closing

Employers with hybrid plans and those merging plans previously maintained by separate entities should consider the option of requesting an IRS determination letter after first sorting out any plan language defects.

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