



Flashpoint: New IRS Procedure for Plan Documents

The IRS issued Revenue Procedure 2016-37 (the "Procedure") at the end of June, which significantly affects individually designed plans ("IDPs") and has some ramifications for pre approved documents, such as prototypes and volume submitter documents. The Procedure is puts into effect the changes that we foreshadowed last year in our FlashPoints ("Well, They've Done It: The IRS Jettisons the FDL Program" (7/24/15) and "Is This the End of Rico ... er, FDLs?" (4/1/15). The Procedure is the embodiment of the IRS's new approach to its requirement that all qualified retirement plans must meet form requirements—that is, they must be in writing and the writing must include certain specific language, and cannot include other proscribed provisions. Failure to meet these rules can cause a plan to lose its tax benefits (called "disqualification"), even if the plan actually operates in compliance with the tax rules. The stated purpose behind these changes is, in short, budgetary concerns: the IRS, with significantly reduced financial support from Congress and the Administration, claims it simply lacks the resources to keep up the current practice of reviewing IDPs to ensure that they meet the form requirements. The Procedure, coupled with other steps the IRS has taken in this regard, encourages the use of pre approved documents where possible.

What Changed for Preapproved Plans?

The main change for sponsors of pre approved plans is that the IRS will issue a new annual list, called the Operational Compliance List ("OCL") that will advise practitioners and sponsors of changes in operational qualification requirements that will be effective during the year. It is possible that an amendment will need to be adopted before the next required restatement (called an "interim amendment" in retirement plan parlance). If no interim amendment is needed, the plan still will need to be operated in compliance with the OCL changes, with a retroactively effective plan modification embodied in the next restatement. Notwithstanding its intentions for the OCL, however, the IRS still hedges its bets, noting that it does not guarantee that the OCL will be fully comprehensive. In other words, a sponsor will not be able to rely absolutely on compliance with the OCL to ensure that its operations meet all qualification requirements.

What Changed for IDPs?

Historically, IDPs have been restated (that is, amended in their entirety onto a new document) and submitted to the IRS once every five years—the exact year for any given plan depended for

the most part on the last digit of the plan's employer identification number. The IRS would then review the new document and ultimately issue a favorable determination letter ("FDL"), confirming that the plan met all qualification form requirements. The FDL would have an expiration date, denoting when the plan sponsor could no longer rely on the IRS's approval of the plan and would need to update and resubmit the plan for new approval. The IRS is now declining to provide FDLs to IDPs except on initial adoption and on plan termination. As changes are mandated in the interim, it will be incumbent on the plan sponsor and its document provider to update the plan to conform to the change. Language that is not modified and is not required to be modified will still be considered compliant based on the FDL issued for the plan. To assist IDP drafters in knowing the provisions that require modification to keep the plan qualified, the IRS will publish a new list each year called the Required Amendments List ("RAL") that will detail new requirements and their effective dates. Plan sponsors then will have until the end of the second calendar year following the calendar year in which the required modification first appeared on the RAL to actually adopt the required amendment. The plan must be operated in compliance with this amendment as of its required effective date, and the subsequent amendment must conform the plan to these operations. Needing to review—and potentially amend—an IDP each year should increase the work of the document provider and, likely, the fees that will be charged in this endeavor. The effective date on any FDL issued to an IDP is now void. (This was outlined in a procedure issued earlier this year, Rev. Proc. 2016-6.) The ability to rely on the IRS approval remains, subject to the required modifications on the RAL and any voluntary modifications that a plan sponsor decides to make (generally called "discretionary amendments," as differentiated from the required amendments discussed above). An interesting—and likely unintended—side effect of these rules is that restating an IDP onto another individually designed document, such as when a plan sponsor changes benefits counsel, will come with considerable risk. While the existing plan document will be able to rely in large part on its existing FDL, whenever it was issued, the new document will not be able to do so and a new FDL will be unavailable.

Feet, Don't Fail Me Now!

If you are a sponsor of an IDP and you're thinking, "Where do I get one of these pre approved plan thingies?" you are not alone. In fact, the IRS likely hopes you will do exactly that—amend your IDP to a pre approved document. The flexibility of pre approved documents has increased significantly since the IRS began considering its internal costs in issuing FDLs to IDPs. Therefore, it is likely that you should investigate whether a pre approved document may be used in the future. In addition, the IRS indicates in the procedure that a defined contribution IDP can be converted onto a pre approved document by April 30, 2017, and it will be able to rely on the pre approved document for form compliance until the end of the next pre approved plan cycle, expected to be in 2022 or 2023. Defined benefit pre approved plans are in the process of being reviewed for approval by the IRS; an existing IDP can adopt the pre approved document when it is made available. If an IDP is not converted onto a pre approved document or if the conversion occurs after April 30, 2017, the plan sponsor will need to adopt amendments required by the RAL as long as the plan remains an IDP.

Is There Any Reason to Keep an IDP?

Yes. First and foremost, there are types of plans that still cannot use a pre approved document. Historically, all cash balance defined benefit plans and employee stock ownership plans (ESOPs) needed to be individually designed, and will continue to remain so with some potential modifications. The next documents pre approved by the IRS will allow adoption by these types of plans, but only within certain limited parameters. Therefore, it is possible that your plan must retain its IDP. Second, your plan might, of necessity, contain provisions that are hard to fit onto the pre approved documents. For example, if your plan covers many company divisions or

subsidiaries with significantly different benefit features, or if your company commonly acquires other companies, it may be that you need more flexibility than a pre approved plan can offer. Nonetheless, it makes sense to discuss this issue with your document provider to determine if the cost and the risk attendant to maintaining an IDP are warranted.


Last Thoughts ...

The new Procedure has a few additional fine points too detailed to be recounted here. If you have an IDP and want to chat about these, please call one of our attorneys. The Procedure is definitely a reduction in the services that the IRS provides to encourage the adoption and maintenance of employer-sponsored retirement plans. That is disappointing, and we and other practitioners lobbied hard to prevent this course of action. (In fact, our firm's Alison Cohen chaired the 2016 IRS Advisory Committee on Tax-Exempt and Governmental Entities ("ACT"), a group of benefits lawyers and other service providers charged with the task of telling the IRS what it should do differently. That committee strongly recommended that the IRS revisit its thinking on this subject.)

Having said that, however, most plans will be able to fit onto a pre approved document. If not, the plan sponsor may consider changing the plan to make it fit. And, if changing the plan isn't possible, the sponsor will simply need to understand that there is some risk that is being assumed in the plan documentation.

Pensions on Peachtree 2017 is coming!
April 24 – 25, 2017
Marriott Century Center, Atlanta, Georgia

The 2017 Pensions on Peachtree Conference, co-sponsored by FIS and Ferenczy Benefits Law Center, is being planned as we speak. If you would like to make suggestions for topics to include in our event, just give us a call or send us an email. We look forward to seeing you there!



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