Employee Benefits Corner

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2010 Plan Amendments and EGTRRA Determination Letter Filing Deadline

Plan sponsors of tax-qualified plans, such as a 401(k) profit-sharing plan, have the option of adopting either a pre-approved plan document (where the plan terms have been approved by the IRS in advance) or adopting an individually designed plan document (where the plan sponsor has the freedom to design its own features). Regardless of the type of plan document adopted, most plan documents need to be updated annually for design and legal changes. A summary of the 2010 plan year changes is set forth below.

The type of plan does, however, impact how assurance can be obtained by a plan sponsor that a plan document complies with applicable Internal Revenue Code requirements. Plan sponsors and fiduciaries using a pre-approved plan document may generally rely on an IRS opinion or advisory letter obtained by the pre-approved plan sponsor, often a financial institution, third-party administrator or law firm. An IRS determination letter specific to the individual plan may also be requested by filing IRS Form 5307. For individually designed plans, a Form 5300 must be filed in order to receive a determination letter that states that the plan document terms satisfy applicable Internal Revenue Code requirements. The timeline for filing determination letter applications is detailed further below.

2010 Plan Amendments

Regardless of whether a plan uses a pre-approved plan document or an individually designed plan document, all qualified plans are entitled to a number of favorable tax advantages—tax-deferral for participants, immediate employer deductions for plan contributions, and no taxation on the trust that funds the plan. In order to retain these benefits, plans must be operated consistent
with the terms of their plan documents and plan documents must be timely amended for recent statutory and regulatory law changes. The timing of plan amendments is complex and depend on a number of factors—the general plan amendment timing rules (which vary depending on whether the amendment is an “interim” or optional amendment) set forth in Rev. Proc. 2007-44 and related IRS guidance; amendment timing rules (if any) contained in newly enacted laws; and the Code’s anti-cutback requirements that, in most cases, prohibit a retroactive reduction of accrued benefits. Taking these rules into account, a number of possible plan amendments are required for the 2010 plan year. Note, however, that collectively bargained plans and governmental plans may have extended deadlines. These amendments are summarized below.

- **2010 design changes.** Any plan design changes, including collective bargaining agreement changes, that were implemented in 2010 should be adopted as plan amendments by the end of the plan’s 2010 plan year. Possible advance participant notice requirements (called a “204(h) notice”) and anti-cutback protections should be considered for amendments that may reduce benefits. The 204(h) notice rules apply only to pension plans, such as cash balance, traditional formula, money purchase plans, and does not apply to profit-sharing plans. For example, to reduce the matching contribution or profit-sharing contribution, a plan amendment should be adopted prior to the effective date of the change (i.e., a prospective change), but no 204(h) notice is required.

- **2011 design changes.** Any design changes contemplated for the 2011 plan year that would result in a reduction of benefits, such as a reduction in matching or profit-sharing contributions, may also need to be adopted before the start of such year. Moreover, some plan design changes must often be made effective as of the first day of the plan year, such as certain safe-harbor 401(k) plan features. As noted above, any pension plan amendments reducing the “future rate of benefit accrual,” including accruals and subsidies, must generally also provide participants with a 204(h) notice that describes the changes at least 45 days before the effective date of the change.

- **PPA amendments.** Under the Pension Protection Act of 2006 (PPA), as amended by the Worker, Retiree, and Employer Recovery Act of 2008 (WRERA), a number of amendments were required to be adopted by December 31, 2009. However, this deadline has not yet expired for many plans with non-calendar-year plan years. If a calendar-year plan failed to timely adopt required PPA amendments, a streamlined VCP application with a reduced filing fee may be filed under Rev. Proc. 2008-50. Otherwise, a calendar year may face significant penalties if these late PPA amendments are raised during a subsequent determination letter review or on audit.

- **Hurricane/flood relief.** The Emergency Economic Stabilization Act of 2008 (EESA) provides for optional flood-related distributions, recontributions of withdrawals for home purchases and special loan rules. EESA-related amendments must generally be adopted by the end of the 2010 plan year.

- **Special PPA deadlines for defined benefit plans.** Although PPA-related amendments to defined benefit plans were generally required to be adopted by the end of the 2009 plan year, the deadline to adopt a number of requirements were pushed back into 2010 pending the issuance of additional IRS guidance addressing the following PPA changes to the Internal Revenue Code: (1) funding-based limits on benefit accruals and distributions, and (2) for cash balance and other hybrid pension plans, provisions relating to three-year vesting, special rules for comparing accruals to similarly situated younger participants and the “market rate of return” rules for cash balance plan interest credits.

- **Right to diversify employer stock.** Although PPA-related amendments to defined contribution plans were generally required to be adopted by the end of the 2009 plan year, the deadline to adopt amendments addressing the employer stock diversification rules added by the PPA was pushed back into 2010 because proposed rules interpreting this requirement were not issued by the end of 2009.

- **Normal retirement age.** For pension plans with a normal retirement age between age 55 and 62 that are changing their normal retirement age to comply with Notice 2007-69, the amendment to NRA must be made by the end of the first plan year beginning after June 30, 2008, or, if later, the tax return deadline, plus extensions, for the plan sponsor’s return that includes the first day of the first plan year beginning after June 30, 2008. Many calendar-year plans were amended last year to reflect this change, but if not already amended, they then have until the 2009 tax return deadline, plus any extensions timely requested, to amend the plan.
HEART Act. Plan amendments related to the Heroes Earnings and Assistance Relief Tax Act of 2008 (HEART) were generally effective as early as January 1, 2007. However, HEART-related amendments must be adopted by the end of the 2010 plan year. In general, the optional provisions should be adopted by the tax filing deadline (plus extensions) for the plan year in which the provision becomes effective (or, if later, the end of the 2010 plan year). Relevant HEART provisions include the following:

- **Death benefits.** All tax-qualified plans (401(a) (including 401(k)), 403(b) annuities and governmental 457(b) plans) must provide a beneficiary of the participant who dies on or after January 1, 2007, while performing “qualified military service” to any additional benefits (other than benefit accruals related to the period of qualified military service) that would have been provided under the plan had the participant resumed employment and then terminated employment on account of death.

- **Differential pay for Code Sec. 415 purposes.** For purposes of applying the maximum contribution (in a defined contribution plan) or benefit (in a defined benefit plan) limits, any differential pay paid by an employer must be counted as compensation under the plan. “Differential pay” means any payment that (1) is made by an employer to an individual with respect to any period during which the individual is performing service in the uniformed services while on active duty for a period of more than 30 days; and (2) represents all or a portion of the wages the individual would have received from the employer if the individual were performing services for the employer. This provision applies to renumeration paid after December 31, 2008. Note that defined benefit plans maintained by a government or multiemployer are not subject to this provision because the Code Sec. 415(b) compensation limit does not apply to these plans.

- **Benefit accrual for death or disability.** A plan may provide that for benefit accrual purposes, a participant who dies or becomes disabled while performing qualified military service is treated as if he or she resumed employment in accordance with USERRA reemployment rights on the day preceding the death or disability and then terminated employment on the actual date of death or disability. This provision must be applied on reasonably equivalent terms for similarly situated participants. This provision can be elected at any time for death or disability occurring on or after January 1, 2007; however, the nondiscrimination provision regarding the timing of plan amendments applies if the nondiscrimination rules apply to the plan (i.e., nongovernmental plans).

- **Differential pay as benefitable compensation.** The plan may provide that differential pay, as defined above, is treated as compensation for purposes of determining contributions and benefits under the plan.

- **Distribution of elective deferrals.** The plan may provide that elective deferrals under 401(k), 403(b)(7), 403(b)(11) and 457(b) can be distributed as a deemed “severance from employment” while the participant is on active duty for a period of more than 30 days. However, this distribution triggers a six-month suspension provision on the participant's elective deferrals or employee after-tax contributions from the date of distribution. (HEART also extended the PPA's qualified reservist distribution rules indefinitely.)

- **Rollovers by nonspousal beneficiaries.** Plans must be amended to allow rollover of benefits by nonspousal beneficiaries by the end of the plan year beginning after December 31, 2009, or, if later, the tax return deadline (plus extensions) for the sponsor's return that includes the first day of the such plan year. Prior to 2010, this requirement, as originally added by the PPA, was optional. A number of calendar-year plans make this change to comply with this requirement when adopting their PPA amendments last year.

- **2009 required minimum distribution relief.** WRERA suspended the required minimum distribution rules for the 2009 calendar year for defined contribution plans. Plan amendments addressing this requirement must be adopted by the end of the 2011 plan year to reflect this relief. IRS guidance provides model language for this amendment.

- **Required minimum distributions—Cycle E filers.** Defined benefit plans that are filing for a Cycle E
(as explained below) determination letter must be amended by January 31, 2011, to reflect the final MRD regulations, effective no earlier than January 1, 2003, and no later than January 1, 2006.

It is important to meet these timing rules as IRS determination letter reviewers thoroughly review plan amendments to ensure they have been adopted timely, including for acquired company plans. Failure to timely adopt can result in potential plan disqualification or monetary sanctions. Also, it is important to note that terminating plans must reflect all currently applicable rules prior to or at their termination date.

**EGTRRA Determination Letter Applications**

While filing a determination letter application is not required, determination letter applications are submitted for the majority of individually designed plan documents. Doing so provides protection against potentially expensive and complex retroactive correction issues that can be raised in the event of audit. In addition, some pre-approved plan adopters elect to submit their plans for determination letters as well.

**Cycle E EGTRRA Determination Letters—Individually Designed Plans**

Individually designed plans may generally submit their plans for IRS review during one year out of the IRS’s individually designed filing cycle. The first cycle, commonly referred to as the EGTRRA cycle, began in 2006 and ends in 2011. The first year of the cycle (generally for taxpayers with employer identification numbers ending in a “1” or “6”) is designated as Cycle A and the last year of the cycle (generally for taxpayers with employer identification numbers ending a “0” or “5”) is designated as Cycle E. In addition to the “regular” members of Cycle E, the following plans may also submit “on-cycle” in Cycle E:

- “Cycle D” filers whose plan year beginning in 2009 began after January 1, 2009, and ends on or after February 1, 2010, that made an election to defer submission until this cycle
- Governmental plans that did not file in Cycle C

Cycle E EGTRRA determination letter applications should be filed using IRS Form 5300 no later than January 31, 2011. Importantly, plan sponsors that made one-time elections to file in this Cycle E will revert back to their normal determination cycle (e.g., Cycle D for a filer with “4” or “9” as the last digit of their EIN, and Cycle C for governmental plans).

Sponsors who are filing in Cycle E should take caution to ensure that their plans are updated for the “Cycle E” Cumulative List, have corrected any delinquent amendments, and have provided all required documents, such as a restatement or working copy of the plan. Failure to take these steps can expose a plan to disqualification and significant IRS penalties.

A Cycle E favorable determination letter will generally cover all changes to the Internal Revenue Code and related regulations made since 2001. However, it will not consider HEART, the funding-related benefit restrictions added by the PPA, and the 2009 suspension of defined contribution plan required minimum distributions.

**EGTRRA Determination Letters—Pre-Approved Defined Contribution Plans**

For pre-approved plans, plans may rely on the IRS opinion or advisory letter regarding the tax-qualified status of the plan without seeking its own determination letter. In order to rely on the pre-approved defined contribution plan letter, the plan sponsor must have adopted the updated plan document, called the EGTRRA restatement, by April 30, 2010, which was also the deadline for filing for a determination letter using IRS Form 5307. For plans that failed to timely adopt the EGTRRA restatement, they may file for relief under the Employee Plans Compliance Resolution System in order to maintain the tax-qualified status of the plan. Specifically, Appendix F (Schedule 2) of Rev. Proc. 2008-50 (or its successor) is filed to reflect the late adopter, checking in Part I the box for the applicable 2004 Cumulative List and paying one-half of the standard VCP fee if filed by April 30, 2011.

For plans that were timely restated for EGTRRA but did not file by the April 30, 2010, deadline to seek a determination letter, no relief is currently available, although some requests for relief have been submitted to the IRS.

**EGTRRA Determination Letters—Pre-Approved Defined Benefit Plans**

For pre-approved defined benefit plans, the IRS recently announced that the EGTRRA advisory and opinion let-
ters will be issued soon, which will start the two-year period for plan sponsors to adopt the EGTRRA restatements and file for IRS Form 5307 determination letters. Pre-approved plan adopters will have until the end of the adoption window to file individual determination letter applications (on IRS Form 5300 or IRS Form 5307, as applicable), if desired.

Endnotes