



September 2017

# PENSION ANALYST

Important information—Plan administration and operation



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## IRS restructures pre-approved qualified plan program

### Who's affected

These changes affect qualified defined benefit and defined contribution plans and qualified defined benefit and defined contribution governmental and non-electing church plans.

### Background and summary

Last year, the IRS issued [Revenue Procedure 2016-37](#), making major changes to the determination letter program for individually designed defined benefit and defined contribution plans. As part of the continuous effort to streamline plan document programs, the IRS released [Revenue Procedure 2017-41](#) in June, restructuring its opinion letter program for pre-approved defined benefit and defined contribution plans.

Pre-approved plan documents operate under a system of six-year cycles. During the first year of the cycle, document providers update their plans to reflect both law changes and changes to the IRS' program and prepare opinion letter applications. During the second and third year of the cycle, the IRS reviews and approves the plan documents. During the fourth and fifth years, adopting employers sign the updated documents. In the sixth year, the IRS issues guidance for the next six-year cycle.

To encourage employers that maintain individually designed plans to convert to a pre-approved plan format, the IRS has revised the procedures for issuing opinion letters regarding qualification in form of pre-approved plans. An "opinion letter" is a written statement issued by the IRS to a document provider as to the qualification in form of the plan.

The revised program:

- Eliminates the distinction between prototype and volume submitter plans;
- Liberalizes the types of plans eligible for pre-approved status; and
- Affords greater flexibility in the design of pre-approved plans.

The changes to the pre-approved plan program are effective October 2, 2017. The changes apply to opinion letter applications for a pre-approved plan's third and subsequent six-year remedial amendment cycles. The submission period for the third six-year remedial amendment cycle for providers of pre-approved defined contribution plans has been modified to begin October 2, 2017, and end on October 1, 2018.

The IRS also issued [the 2017 Cumulative List of Changes in Plan Qualification Retirements for Pre-Approved Defined Contribution Plans](#). The IRS will use this list to review pre-approved defined contribution plans that fall under the third restatement cycle for plan document compliance. A separate list will apply to pre-approved defined benefit plans.

### Action and next steps

Plan sponsors of pre-approved plans should read the information discussed in this newsletter. If Prudential Retirement provides document services for your plan, we will contact you regarding any changes needed to your plan document and will work with you to ensure documents are updated in a timely manner.

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## Changes to the pre-approved plan program

One of the most significant changes of the recent guidance is the combination of the prototype and volume submitter programs into a single opinion letter program involving two types of plans: nonstandardized and standardized. Both plan types may use either a basic plan document with an adoption agreement or a single plan document. Like existing volume submitter documents, an adopting employer of any nonstandardized plan may adopt minor modifications, thus allowing more flexibility in plan design options. An employer that modifies a preapproved plan may file for a determination letter to obtain reliance.

The recent guidance also expands the types of plans that may be eligible for pre-approved plans. Money purchase pension plans and 401(k) or profit-sharing plans may now be combined in the same pre-approved plan document. In addition, a nonstandardized employee stock ownership plan (ESOP) may also include a 401(k) feature.

The guidance also makes the following changes:

- A cash balance formula under a nonstandardized plan may now permit the interest crediting rate to be based on the actual return on plan assets. The rate, however, cannot be based on a subset of plan assets.
- Opinion letters may now be requested for non-electing church plans. Document providers will need to submit for approval separate basic plan documents and adoption agreements for specific types of employers.
- A nonstandardized plan may allow for either safe harbor or non-safe harbor hardship distributions. If the plan provides for non-safe harbor hardship distributions, the distributions must be based on nondiscriminatory and objective criteria contained in the plan.
- The IRS will no longer rule on the exempt status of the plan's trust or custodial agreement. This change allows service providers to use trust or custodial agreements without having to determine if that agreement has been approved for use with a certain document.

## Plans and provisions not covered by opinion letters

The recent guidance contains a list of plans and provisions not permitted in pre-approved plans, including:

- Multiemployer plans;
- Single-employer collectively bargained plans. This rule does not preclude an employer from covering employees of the employer that are included in a unit covered by a collective bargaining agreement if it is adopting a pre-approved plan for its non-bargaining employees or from adopting a pre-approved plan pursuant to such agreement as a single-employer plan that covers only bargaining employees of the employer;
- Stock bonus plans other than ESOPs;
- ESOPs that are a combination of a stock bonus plan and a money purchase plan;
- ESOPs that provide for the holding of preferred employer stock;
- Certain pooled fund arrangements;

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- Certain statutory hybrid plans, such as those that have a benefit formula that is not a cash balance formula;
- Defined benefit plans that provide a benefit derived from employer contributions that is based partly on the balance of the separate account of a participant;
- Target benefit plans, other than plans that, by their terms, satisfy certain nondiscrimination safe harbor rules;
- Governmental defined benefits that include “deferred retirement option plan” (DROP) features, or similar provisions in which a participant earns additional benefits for continued employment post-normal retirement age in the form of credits to a separate account under the same plan;
- Plans under which the defined benefit and defined contribution limits (under Code section 415) are incorporated by reference;
- Defined contribution plans under which the ADP or ACP tests are incorporated by reference;
- Standardized 401(k) plans that provide for hardship distributions under circumstances other than those described in the safe harbor rules;
- Nonstandardized 401(k) plans that provide for hardship distributions under circumstances not described in the safe harbor rules, unless these distributions are subject to nondiscriminatory and objective criteria contained in the plan;
- Fully-insured section 412(e)(3) plans, other than certain non-statutory hybrid plans;
- Plans that include purported fail-safe provisions for section 401(a)(4) or the average benefit test;
- Plans that include blanks or fill-in provisions for the employer to complete, unless the provisions have parameters that preclude the employer from completing the provisions in a manner that could violate the qualification rules;
- Plans designed to satisfy provisions relating to accident or health benefits;
- Plans that include 401(h) retiree medical funding accounts;
- “Eligible combined plans” consisting of a defined benefit plan and defined contribution plan held in a single trust; and
- Variable annuity plans and plans that provide for accruals that are determined in whole or in part based on the value of, or rate of return on, identified assets, including plan assets.

Additionally, the IRS, at its discretion, may decline to issue opinion letters for other types of plans or provisions not described above.

## Employer reliance on opinion letter

### Standardized plans

An employer adopting a standardized plan may rely on the plan’s opinion letter if the below conditions are met:

- The plan currently has a valid opinion letter;
- The employer’s plan is identical to the standardized plan;
- The coverage and contributions or benefits under the plan are not more favorable for highly compensated employees than for non-highly compensated employees; and
- The employer had not amended the plan other than to choose options provided under the plan or to make [certain amendments](#).

In addition:

- An employer may not rely on an opinion letter for a standardized plan with respect to defined benefit and contribution limit and top heavy requirements without obtaining a determination letter if the employer maintains or has maintained, another qualified plan covering some of the same participants. An employer that adopts a standardized defined contribution plan will not be considered to have maintained another plan if such plan had been terminated before the effective date of the standardized defined contribution plan and there were no annual additions credited to the terminated plan within a limitation year of the standardized plan;
- An employer that has adopted a standardized defined benefit plan may rely on the opinion letter with respect to the minimum participation rules only if the plan satisfies the minimum participation rules with respect to its prior benefit structure; and
- An employer that adopts a standardized plan may not rely on the opinion letter with respect to:

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- Whether the timing of any amendment satisfies certain nondiscrimination rules; or
- Whether the plan satisfies the effective availability rules with respect to any benefit, right, or feature.

## Nonstandardized plans

An employer adopting a nonstandardized plan may rely on that plan's opinion letter if the below conditions are met:

- The plan currently has a valid opinion letter;
- The employer's plan is identical to the nonstandardized plan; and
- The employer has not amended the plan other than to choose options provided under the plan or make [certain amendments](#).

In addition, adopting employers of nonstandardized plans:

- May not rely on the opinion letter with respect to:
  - Certain nondiscrimination, minimum participation, minimum coverage, or compensation testing rules; or
  - If the employer maintains or has maintained another plan covering some of the same participants. An employer that adopts a nonstandardized defined contribution plan will not be considered to have maintained another plan if such plan had been terminated before the effective date of the nonstandardized defined contribution plan and there were no annual additions credited to the terminated plan within a limitation year of the standardized plan;
- May rely on the opinion letter with respect to minimum coverage and minimum participation if all nonexcludable employees benefit under the plan;
- May rely on an opinion letter with respect to nondiscriminatory amounts if the plan allocates contributions or provides benefits using one of the design-based safe harbors and the plan has a satisfactory definition of compensation; and
- May rely on the opinion letter with respect to whether the form of the plan satisfies the actual deferral percentage test (ADP test) or actual contribution percentage test (ACP test) if the employer elects to use a safe harbor definition of compensation in the test.

## Other limitations and conditions on reliance

In addition, the following limitations and conditions on reliance apply regardless of the pre-approved plan type:

- An adopting employer may rely on an opinion letter for a plan that amends or restates a plan of the employer only if the plan that is being amended or restated was qualified;
- An adopting employer will not have reliance if the employer's adoption of the plan precedes the issuance of an opinion letter for the plan;
- An adopting employer will not have reliance if the adoption agreement or other elective provisions are not completed correctly when adopted by the employer;
- An adopting employer may rely on the opinion letter only if the plan is identical to a pre-approved plan with a currently valid opinion letter. Thus, the employer may not have added any terms to the pre-approved plan and must not have modified or deleted any terms of the plan other than by choosing options permitted under the plan or amending the document in a [permissible manner](#);
- An adopting employer of any pension plan in which the normal retirement age selected by the employer is less than 62 will not have reliance on the opinion letter that such age is reasonably representative of the typical retirement age for the employer's industry; and
- The trust or custodial agreement may not contain a provision that states that the provisions of the trust override the provisions of the plan. An adopting employer may not rely on an opinion letter to the extent that provisions of the trust or custodial account that are a separate portion of the plan override or conflict with the provisions of the plan document.

## Permissible plan amendments

The following types of plan amendments will not cause an employer with a pre-approved plan to lose reliance on the opinion letter:

- Amendments to add or change a provision (including choosing among options in the plan) and/or to specify or change the effective date of a provision, as long as the provision is allowed under the terms of the plan and the qualification requirements, and, except for the effective date, the provision is identical to a provision in the pre-approved plan;
- Sample or model amendments published by the IRS that specifically provide that their adoption will not cause a plan to fail to be identical to the pre-approved plan;
- Amendments that adjust the defined contribution and defined benefit limits, elective deferral limits, compensation limits, and threshold amounts for determination of highly compensated employees to reflect annual cost-of-living increases, other than amendments that add automatic cost-of-living adjustment provisions to the plan;
- Plan language completed by the employer if the overriding language is necessary to satisfy the limitations on benefits and contributions or top heavy rules because of the required aggregation of multiple plans;
- Interim amendments or discretionary amendments that are related to a change in qualification requirements;
- Amendments that reflect a change of a plan provider's name; and
- Amendments to the administrative provisions in the plan (such as provisions relating to investments, plan claims procedures, and employer contact information).

## Third restatement cycle

The third six-year remedial amendment for pre-approved defined contribution plans began on February 1, 2017, and ends on January 31, 2023. The 12-month applicable on-cycle submission period for pre-approved plans was to begin on August 1, 2017, and end on July 31, 2018. The new guidance changes the beginning date and ending dates for the third six-year remedial amendment cycle for pre-approved defined contribution plans to October 2, 2017 and October 1, 2018.

The next filing cycle for pre-approved defined benefit plans is not changed by the new guidance, and is scheduled to begin on February 1, 2019.

## Next steps

The IRS has significantly changed the pre-approved plan program. Plan sponsors should become familiar with the guidance in this newsletter. While the revised program provides greater flexibility for pre-approved plans than in the past, certain restrictions continue to apply.

For plans that use Prudential Retirement's document services, we will keep you informed of any changes that could impact your plan as we continue to analyze this guidance and work with document vendors.

### Pension Analyst by Prudential Retirement

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