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The Current State of Retirement Document Drafting

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This article surveys the current state of document drafting, including an overview of IRS-recognized document types and recommendations for improvement to the IRS determination letter program. Suggestions include allowing new types of plans into the pre-approval program and modifying the required interim amendment procedures. The article also discusses when to request a determination letter and provides general drafting tips.

Major Classifications of IRS-Recognized Document Types

Most of the IRS procedures discussed in this article are found in Revenue Procedures ("Rev. Proc.") 2007-44 and 2005-16. Rev. Proc. 2007-44 provides detailed rules regarding the five-year restatement cycle for individually designed plans and the six-year cycle for pre-approved

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plans. Rev. Proc. 2005-16 provides rules and definitions relating to pre-approved plans.

These revenue procedures describe two principal types of plan documents as recognized by the IRS: pre-approved plans and individually designed plans. Pre-approved plans are further broken down into either the master and prototype ("prototype") or volume submitter classifications. Individually designed plans are generally used by larger adopting employers that require more control over document terms and may require sophisticated protections such as merger appendices. Conversely, pre-approved plans are largely used by smaller adopting employers because of their typically lower cost and less need for customization.

The pre-approved plan program has many benefits to the IRS, practitioners, and adopting employers. Pre-approved plans virtually eliminate the need for IRS review of individual plan documents. In addition, preparation time for practitioners is significantly reduced, particularly when the pre-approved plan is generated using document-generation software. Smaller employers and practitioners also greatly benefit from the ability of the pre-approved sponsor to adopt amendments on behalf of an employer, resulting in cost-savings by reducing or eliminating IRS filing fees and high practitioner costs. Recent data from Forms 5500 indicates that approximately 80 percent of all retirement plans use pre-approved plan documents.

One of the principal differences between pre-approved and individually designed plans is that pre-approved plans follow a six-year standard restatement cycle (all pre-approved plans restate during the same two-year window), and individually designed plans follow a five-year restatement cycle with deadlines that are generally dependent on the last digit of the sponsor's Employer Identification Number. From a practitioner perspective, it is certainly simpler to restate less often and can be administratively simpler to have all plans on the same six-year cycle whenever possible. To help ensure that a pre-approved document remains on the six-year cycle or to enable an individually designed plan to assume a six-year cycle, the IRS has published Form 8905, which allows an adopting employer to indicate its intent to adopt a pre-approved plan. A detailed description of the Form 8905 requirements is beyond the scope of this article and can be found in Rev. Proc. 2007-44.

The difference between the two pre-approved plan types (prototype and volume submitter) is further explained below. This is followed by a description of individually designed plans.

Pre-approved Plan Documents (Prototypes and Volume Submitters)

Which pre-approved document to use for a given plan is largely a matter of practitioner choice. Although the IRS has eliminated many of the artificial differences between the prototype and volume submitter documents in recent years, several important differences remain including the following:

- Prototype sponsors that apply for opinion letters in their own names are permitted to apply for prototype language that is a minor modification of the mass submitter plan [Rev. Proc. 2005-16, § 12.02].
- Employers may currently make minor, post-approval modifications to a volume submitter document and file for a determination letter using Form 5307.
- Any post-approval modification to a prototype results in the loss of pre-approved status (the plan becomes individually designed). However, a minor modification to a volume submitter document does not cause the document to lose pre-approved status.
- Both programs permit the pre-approved sponsor to adopt amendments on behalf of an employer. If any modifications are made to prototype language, however, the sponsor will lose the ability to amend on behalf of plan sponsors. Modifications to volume submitter language do not have this result; the pre-approved sponsor's ability to amend on behalf of adopting employers is conditioned on the document receiving an individual determination letter using Form 5307.
- Rev. Proc. 2011-6, Sections 9.02(2)(c) and (g) require that the volume submitter practitioner be named on the power of attorney (Form 2848) if a plan submits a request for determination letter. This is not a requirement of the prototype program.
- In non-standardized prototypes, the number of allocation groups for non-highly compensated employees ("NHCEs") is restricted based on the number of eligible highly compensated employees ("HCEs") [IRS List of Required Modifications ("LRM") 94]. There are no such limitations on the number of allocation rate groups in volume submitter plans. Because the ability to have each participant in his or her own allocation group is a recommended planning technique, many practitioners prefer volume submitter documents for cross-tested plans.

- Money purchase pension plans with target benefit allocation formulas are prohibited from using prototypes.
- A prototype document may not be used for a Multiple Employer Plan ("MEP"). This can create a major compliance trap, especially in the small plan arena, where changes in ownership may cause business entities to cease being part of the same controlled group and operationally convert the plan into an MEP. Consultants servicing qualified plans generally do not learn about ownership changes until after the end of the year when they send annual questionnaires to their plan sponsor clients. The change in ownership and conversion to an MEP may result in a prototype document inadvertently losing pre-approved status and, therefore, being treated as individually designed and placed on the five-year restatement cycle.
- Prototype documents may not offer non-safe-harbor hardship distributions and may not allow employees to irrevocably elect not to participate in the plan, whereas volume submitters can provide for these optional features.

In the past, the differences between prototypes and volume submitters were more pronounced. Volume submitters could not use an adoption agreement/basic plan document format ("prototype format") but were required to use a customized single plan document where practitioners and employers often had to read through lengthy sections to determine the features provided under the plan. Only prototype sponsors were permitted to adopt amendments on behalf of plan sponsors. Adopting employers were required to file Forms 5307 for all volume submitter plans, i.e., they could not rely on the pre-approved plan's advisory letter, even without modifications, whereas prototypes could rely upon the opinion letter if no modifications were made to the pre-approved language. Finally, the two document types were reviewed in different IRS offices. Now both are handled by one IRS office, leading to much greater consistency in how similar provisions are reviewed.

Individually Designed Documents

Plans sponsored by larger adopting employers may not be able to fit into pre-approved documents. Larger employers often require multiple benefit/allocation formulas and special provisions applying to groups of acquired employees. In addition, there are many instances in which IRS procedures do not permit a specified plan type to use a pre-approved document, including:

- Multiemployer plans,
- Union plans (this does not preclude an employer from using a volume submitter for employees who are included in a collective bargaining unit or adopting a volume submitter document as a single employer plan pursuant to such agreement as long as it covers only its employees),
- Stock bonus plans,
- Employee stock ownership plans ("ESOPs"),
- Annuity contracts under Section 403(b),
- Cash balance plans,
- Plans described in Internal Revenue Code ("IRC") Section 414(k), relating to defined benefit plans that provide benefits derived from employer contributions based partly on the balance of a separate account of the participant, and
- Church plans described in IRC Section 414(e) that have not made the election provided by IRC Section 410(b).

One of the benefits of an individually designed plan is that there are fewer limitations on incorporation by reference. Statutory provisions, such as the benefit limitations under IRC Section 415 and the ADP/ACP tests, may be incorporated by reference in an individually designed document, but they must be described in full detail in a pre-approved document. These limitations on incorporation by reference by pre-approved documents serve little purpose, because the statutory provisions that must be included in a pre-approved document are quite lengthy and complex. As a result, the plan document cannot capture all nuances of the statutory provisions, and the practitioner administering the plan must still consult regulatory and other guidance provided outside of the plan document. Permitting incorporation by reference also saves the practitioner and IRS resources since it is not necessary to amend the plan any time changes are made to the underlying statutory provisions, which are incorporated by reference.

Recommendations for Improvement to the IRS Determination Letter Program

Expansion of the pre-approved document program to new document types, eliminating differences between the prototype and volume submitter programs, revision of the interim amendment requirements, and limited modification to the determination

letter procedures would substantially reduce IRS, practitioner, and employer time, as well as resources spent on ensuring plans meet applicable requirements—without a reduction in actual plan compliance.

Expansion of the Pre-approved Program to Other Document Types

403(b) Plans. The IRS has indicated in Announcement 2009-34 that it will be opening a pre-approved program for IRC Section 403(b) plans similar to the prototype program for qualified plans. Prior to the issuance of the final 403(b) regulations, there was little need for a formal plan document for a plan not subject to ERISA due to the fact that no such document was required under the IRC; however, the final regulations now mandate a written plan document for all 403(b) plans, even those not subject to ERISA. Coincident with the publication of Announcement 2009-34, the IRS published draft 403(b) LRMs {http://www.irs.gov/pub/irs-tege/draft_lrm_403b_prototypes.pdf}.

Cash Balance Plans. Based on Form 5500 data, more than 2,000 new defined benefit plans were adopted in 2009, and 825 of these were cash balance plans. Form 5500 also suggests that cash balance plans are being adopted primarily by smaller employers—5,315 of the 6,564 current cash balance plans have 100 or fewer participants. It is likely that documents for many cash balance plans are being provided by pre-approved document vendors, using predefined document templates. As a result, these plans are ideal candidates for the pre-approved program. Allowing pre-approved cash balance plans would streamline and/or eliminate IRS review. As discussed below, a pre-approved program should also resolve current issues in the cash balance area dealing with acceptable plan language, especially the definition of accrued benefit.

Employee Stock Ownership Plans. The IRS has informally indicated that ESOPs have been the primary source of delay for Cycle-A filings and are the only type of plan with a significant backlog of pending determination letter requests. Allowing ESOP provisions in the pre-approved program would drastically reduce IRS review time, especially for non-leveraged ESOPs. The IRS could establish criteria as to which type of ESOPs could be placed on a pre-approved document; larger, more complex ESOPs would still be appropriate candidates for individually designed plans. Form 5500 data suggests that many non-leveraged ESOPs are adopted by smaller employers with 2,100 out of 3,675 having 100 or fewer participants.

Eliminate Differences Between Prototype and Volume Submitter Documents

As described above, many of the key differences between prototype and volume submitter documents have already been eliminated over time. Combining these two programs into one by using the best features of both programs would substantially streamline the pre-approval process, reduce practitioner and employer confusion, and save substantial resources on all sides. The combination could create a "best of both worlds" situation where the new, single document type would permit minor modifications to be filed on Form 5307 and multiple employer sponsorship among the other flexible features permitted in either plan type.

Modification of the Interim Amendment Requirement

The bane of all document practitioners is the current requirement that all plans be amended annually for changes in law or regulation. Since the IRS formalized the interim amendment requirement in 2006, plan sponsors have had to execute amendments nearly every year. Prior to the issuance of the new procedures, a document only had to be amended at specified periods as a result of major changes to tax law. Many intervening legal and regulatory changes were folded into the major, periodic restatements. It is believed that the source of the current requirement to amend for every change in law is an opinion by individuals within the U.S. Treasury Department (under both Democratic and Republican administrations) that participants may not be sufficiently aware of their plan rights if the plan documents do not reflect current law. The authors have inquired of IRS personnel and other practitioners if they recall any situations in which participants were harmed under the prior procedures because documents did not reflect current law. No one questioned has been able to cite a specific instance. Thus, it appears that the current requirement that documents be amended contemporaneously with law changes is a solution in search of a problem.

The Advisory Committee on Tax Exempt and Government Entities ("ACT") made recommendations for changes to the interim amendment procedure in its June 2010 meeting. While many of these recommendations are praiseworthy, many did not address the central issue of determining when, in fact, an interim amendment is required. For example, one of the recommendations involved a four-node decision tree {http://www.irs.gov/pub/irs-tege/tege_act_rpt9.

pdf}. There are a large number of employees in the IRS rulings and examination divisions and even with crystal-clear guidance, differences in interpretation arise at different IRS offices. Without concrete guidance as to when an amendment is necessary, all parties spend undue time and effort negotiating various interpretations for particular plans. The IRS intended to alleviate some of these issues when it started publishing a Cumulative List of statutory and other law changes. However, in an abundance of caution, the IRS has placed many items on the Cumulative List that do not require amendments. Thus, the Cumulative List is of limited usefulness for providing definitive guidance.

In some years, the IRS Web site has offered "soft" guidance about which regulatory provisions would require amendments. While this guidance has been extremely helpful, it often occurred very late in the year and did not allow time for the document vendors who actually draft most interim amendments to provide the necessary language and for other service providers to distribute (and in some instances, have the employer sign) the amendments.

According to informal discussions with IRS personnel, it appears the requirement for interim amendments is not popular with IRS personnel either and oftentimes serves as a drain on IRS resources that could be better used elsewhere. For example, one IRS manager indicated that each determination letter application requires the reviewer to spend, on average, one hour confirming that prior interim amendments have been adopted. IRS examination staff has also indicated that they spend a significant amount of time on plan audits documenting the existence of prior interim amendments. Changing procedures to permit interim amendments on a fixed two- or three-year cycle would lessen practitioner and IRS burden. A timely published list of required amendments for each cycle should be a central ingredient to any new procedure.

Revisions to the Favorable Determination Letter Rules

It is apparent from IRS data that most determination letter filings are made by larger plans. The average plan size for 401(k) plans seeking favorable determination letters is more than three times the average plan size for all 401(k) plans. However, certain aspects of the current procedure still result in pre-approved plans seeking favorable determination that many practitioners feel could be avoided.

One type of filing that revised procedures could eliminate is the filing to make use of Bankruptcy Code exemptions for qualified plans. The Bankruptcy Code provides certain protections from creditors for funds held in a qualified plan. However, for the protection to apply, Section 522 of the Bankruptcy Code requires that the qualified plan must have "received a favorable determination under Section 7805 of the Internal Revenue Code of 1986, and that determination is in effect as of the date of the filing of the petition in a case." In order to preserve these bankruptcy exemptions, many practitioners advise clients to make a protective Form 5307 filing to ensure that the plan has a favorable determination under IRC Section 7805. If the pre-approved program procedures made it clear that reliance on an advisory/opinion letter was the same as a determination under Section 7805, many unnecessary Form 5307 filings would be avoided (provided bankruptcy courts recognized the IRS position). A sample of language that should satisfy bankruptcy code requirements is found in Section 5.01(4) of Rev. Proc. 2008-50.

Another situation in which practitioners make "protective" filings is in an attempt to provide a cut-off date before which IRS reviewers and/or auditors will not request prior documents and amendments. It appears that the current practice of IRS personnel, when performing an audit or processing a determination letter request, is to request copies of all required and optional plan amendments and restatements that were executed after the plan's last individual favorable determination letter. In reaction to this practice, some practitioners submit protective filings in order to prevent a request to produce documents that predate the date of the favorable determination letter. The IRS practice, and the practitioner reaction to it, has caused an increase in the number of otherwise unnecessary Form 5307 filings, which is another drain on IRS and practitioner resources.

General Recommendations for Practitioners

An overall recommendation to practitioners is the old principle "Keep It Simple, Stupid" (KISS). Several options available across plan types tend to create administrative hassle without sufficient rewards. Most pre-approved plan documents provide a wide array of options for various plan provisions and individually drafted documents provide nearly unlimited flexibility in drafting. The fact that many options are offered does not mean they should be chosen in all situations. Some options, while offering potential cost savings to adopting employers, often result in operational failures if difficult or impossible

to follow in practice. Several plan options to avoid—break-in-service rules, use of elapsed time and 415 "safe harbor" definitions of compensation—are discussed below under "General Drafting Tips." Finally, we discuss a few drafting tips for particular plan types.

General Drafting Tips

Break-in-Service Rules—Don't Use Them

The eligibility and service rules permit a plan to forfeit or delay recognition of service after a predetermined break in service. These break-in-service rules have the potential to save adopting employers money; however, if such rules are actually written into the plan, they must be applied to all participants and not only in selective situations. This means that in the case of every rehired employee an analysis must be conducted to determine whether or not the break-in-service rules apply. In order to do so, the party servicing the plan must ensure that the adopting employer is providing complete and accurate information on past service. In the small plan context, the time to analyze and audit the quality of data is usually not available. Eliminating the break-in-service rules greatly simplifies plan administration and prevents inadvertent operational failures where the break-in-service rules are not actually applied.

Use Hours of Service—Not Elapsed Time

On the surface, the elapsed time method of calculating service is quite straightforward. However, in actual practice it can get quite complicated. This is particularly true when (1) a break in service occurs, (2) less than a year of service is required by the plan, and (3) when calculating service for allocation purposes in a defined contribution plan. Many benefit administrators do not understand that service is treated as being continuous even in situations where an employee is absent for up to a year; they tend to only count the period of service actually worked. For example, an employee who terminates on January 2 and is rehired on December 31 of the same year will earn a full year of service in the calendar year under the elapsed time method. Determining partial years of service using the elapsed time method can also become quite complicated for the same reason.

A few pre-approved documents on the market generate some confusion by stating that the plan uses elapsed time for eligibility but then requiring continuous service with a 1,000-hour fail-safe provision. This language can lead practitioners to believe elapsed time may require continuous service, but this option is only permissible if the plan has a 1,000-hour fail-safe (which requires counting hours in any event).

Further, use of elapsed time to determine eligibility for allocations in a defined contribution plan can become quite complex, especially when an employee terminates at or just prior to the end of the year. Reviewing just the plan year in question (the current year), the participant may not have earned a year of service. However, if he or she is rehired before the first anniversary of termination, he or she will be recognized as having completed a year of service in the current year.

If the plan administrator or adopting employer does not want to count actual hours of service, the equivalency method is a straightforward substitute. The plan can achieve nearly the same effect as elapsed time by using the monthly equivalency, i.e., 190 hours credited for each month in which an employee works at least one hour.

Use W-2-Based Definitions of Compensation

There are several safe harbor definitions of compensation that automatically satisfy the nondiscrimination rules under IRC Section 414(s). Three of these definitions are commonly used in pre-approved documents: (1) Box 1 (gross wages) on Form W-2, (2) income subject to withholding on Form W-2, and (3) "safe harbor" Section 415 compensation. There is a misconception among some practitioners that use of Section 415 compensation is preferable over the two definitions based on W-2 wages. The definition of Section 415 compensation is found in Treasury Regulation Sections 1.415(c)-2(b) and (c) is approximately 700 words in length. There are few plan administrators or adopting employers that parse the meaning of these regulations at the end of each plan year when performing compliance testing and allocations. It is virtually impossible to ensure that the plan sponsor is providing correct amounts for compensation when using Section 415 compensation. On the other hand, gross wages or wages subject to withholding on form W-2 are generally very straightforward and easy for plan sponsors to manage.

ERISA and the Internal Revenue Code Are Not the Only Laws That Apply to Qualified Plans

Many practitioners are quite comfortable that a plan document complies with all applicable laws once it receives a favorable determination letter from the Internal Revenue Service. Note, however, that determination letters include a caveat that expressly disclaims the letter covering any law other than the Internal Revenue Code. Other laws that impact qualified plans

include the Americans with Disability Act ("ADA") and the Age Discrimination in Employment Act ("ADEA").

A plan provision that could violate the ADA is providing more restrictive contribution allocation requirements in defined contribution plans in situations where a participant is disabled. For example, some plans may be drafted so that a participant who is not employed on the last day of the plan year due to a regular termination of employment will receive an allocation but a participant who is not employed on the last day of the plan year due to disability will not receive an allocation.

Violations of the ADEA occur when certain plan features do not apply to individuals who are over age 40. For example, some defined benefit plans have been drafted so that benefit accruals cease upon attainment of age 65 (which obviously also violates IRC Section 411(b)(1)(H)). In addition, care must be exercised when designing allocation groups in cross-tested plans to ensure that those designed to receive lower allocations are not based on age.

Beware of Plaintiff's Attorneys

Most small plans do not have enough assets to attract the interest of a contingent-fee plaintiff's attorney. However, there are numerous situations in which an employment termination gone wrong can generate lawsuits, even in small plans. Receipt of an IRS favorable determination letter does not automatically guarantee the plan document could not be interpreted in a way that is adverse to the adopting employer and in favor of a plaintiff-participant. This is particularly true in defined benefit plans. A poorly drafted plan may result in unintended benefits being awarded in a litigation situation.

Interim Amendments

Do not prepare and distribute/execute required interim amendments early in the plan year even if you are reasonably certain that you have taken into account all statutory/regulatory changes. In years past, many conscientious practitioners have been stuck doubling their workload when the IRS released guidance later in the year indicating an amendment was required for certain guidance despite general belief to the contrary.

Drafting Tips for Specific Types of Plans

401(k)—Use Volume Submitter Prototype Format

Under the prior revenue procedures, the principal reasons for choosing a prototype document over a volume submitter document were: (1) the ability of the pre-approved plan sponsor to amend on behalf of the adopting employer, (2) the requirement that adopting employers file Form 5307 for all volume submitter plans, and (3) the readability of a prototype document over a volume submitter document. Under the current procedure, these distinctions between prototypes and volume submitters have been virtually eliminated. While many practitioners still use prototype plans out of habit, more and more practitioners now believe that the pendulum has swung in favor of volume submitter documents for the following reasons:

- Volume submitter documents are largely available in a prototype format, i.e., with an adoption agreement, greatly improving readability;
- Volume submitter documents allow use of unlimited allocation groups in cross-tested plans;
- Volume submitter documents may now be amended by the pre-approved sponsor;
- Volume submitter documents may be used for MEPs; and
- Volume submitter documents may be submitted using Form 5307 if minor changes are made; otherwise, the adopting employer should be able to rely on the advisory letter.

401(k)—Avoid Multiple Match Formulas in Safe Harbor Plans

One of the requirements to meet the ACP safe harbor is that the ratio of all matching contributions (not just safe harbor contributions) made on behalf of an HCE cannot be greater than the ratio of matching contributions that would apply with respect to any NHCE [Treas. Reg. § 1.401(m)-3(d)(4)]. The plan will not satisfy this requirement if an additional matching contribution is subject to a 1,000-hour requirement, last day rule, or other limitation that could apply to at least one NHCE but not apply to at least one HCE. For example, if a plan has a requirement that a participant be employed on the last day of the plan year to receive an allocation of non-safe harbor matching contributions, the plan loses reliance on the ACP safe harbor if at least one otherwise eligible HCE is employed on the last day of the plan year and at least one otherwise eligible NHCE is not. When drafting plans to provide matching contributions in addition to regular safe harbor contributions, care must be exercised to ensure that this requirement is met.

Cross-Tested Plan Design

Another cross-testing design technique is to remove any age or service requirements for eligibility and any

hour or last day requirements for allocations in combination with placing each participant in his or her own allocation group. Using a separate allocation group for each participant does not mean that each employee must actually receive a different allocation rate, rather a service-provider may place operational limitations of two to three allocation groups that the adopting employer may use. While removing age/service requirements may seem counter-intuitive and expensive, this method provides maximum flexibility and will likely result in cost savings to the plan sponsor, as explained below.

Plans with specified allocation groups can oftentimes cause an inadvertent failure of non-discrimination testing. Common causes of these failures include, (1) the unintended inclusion of a young HCE in the plan (e.g., young child of an owner), and (2) the allocation of top-heavy minimum and/or safe harbor non-elective contributions to participants who are not eligible to receive any other non-elective contributions. However, if each participant is in his or her own allocation group, the young HCE may be excluded from the allocation, which, in most cases, will rescue the test. Likewise, participants receiving unplanned top-heavy minimums and/or safe harbor non-elective contributions may be placed in their own allocation groups and receive an additional allocation that meets the minimum gateway contribution requirement.

In addition, a young NHCE with fewer than 1,000 hours of service or who terminates prior to the last day of the plan year may otherwise be excluded from an allocation with adverse results. Please note that typical eligibility and allocation requirements may still be imposed on the plan in operation by excluding from an allocation those participants who otherwise would not be eligible under typical age, service, and employment requirements. However, care must be exercised to ensure that an initial eligibility requirement of more than 1,000 hours in a plan year is not imposed in practice when determining participant allocation rates. Also, as discussed above, the ADEA rules prohibit lower allocation rates based on a participant's age in excess of 40 years.

Cash Balance Plans

It appears there is disagreement among IRS personnel on appropriate post-Pension Protection Act ("PPA") language for cash balance plans. All IRS personnel seem to agree that the definition of accrued benefit cannot be the balance in the hypothetical account even though IRC Section 411(a)(13)(C)(i) provides "[t]he term 'applicable defined benefit plan' means a defined benefit plan under which the accrued benefit (or any portion thereof) is calculated as the balance of a hypothetical account maintained for the participant or as an accumulated percentage of the participant's final average compensation."

If we accept the IRS position that the definition of accrued benefit was not changed by PPA, the IRS seems to be uncertain as to the ramifications of defining the accrued benefit as the annuity benefit payable at normal retirement age. In a recent IRS phone forum, an IRS actuary stated that the accrued benefit must be calculated by converting the hypothetical balance to the annuity starting at normal retirement age using the plan's interest crediting rate. While this reflects the understanding of the cash balance rules by many practitioners prior to PPA, the application of this conversion formula is suspect under new cash balance regulations permitting an interest-crediting rate to be tied to an index, which can be negative. The question then remains whether a participant's accrued benefit can be reduced in a plan year if the interest-crediting rate is less than (or even negative) the prior year's rate. In addition, the proposed cash balance regulations that are still pending indicate that a plan may determine the value of a participant's annuity benefit as the value of the hypothetical account converted to an annuity using the plan's reasonable actuarial assumptions. A possible remedy to this situation is for the plan to use a fixed safe harbor interest-crediting rate that is also used as the plan's interest assumption for determining actuarial equivalence.

Traditional Defined Benefit Plans

When choosing among pre-approved plan documents, the volume submitter in prototype format appears to be the clear choice versus the prototype document. As mentioned above for 401(k) plans, one of the main reasons for using volume submitter documents is that minor modifications may be made without taking the plan out of pre-approved status. If any modifications are made to the volume submitter document, the favorable determination letter will be requested using Form 5307 rather than Form 5300. On the other hand, if any modifications are made to a prototype document, the plan will no longer be pre-approved and will be placed on the five-year restatement cycle.

ESOPs

While ESOPs may not use pre-approved documents, it does not mean the format of the document must be individually designed rather than prototype-formatted. Therefore, for ease of use, it may make more sense to place an ESOP on a prototype-style document (adoption agreement and basic plan document).

In the small employer arena, it is common to find employers that have adopted an ESOP and a separate 401(k) plan. In many cases, the ESOP is no longer leveraged and is more similar to a regular profit sharing plan. In this situation, it may be advisable to combine the plans into a single 401(k)/ESOP otherwise known as a "KSOP." Since many document vendors provide a KSOP document, implementation of such a document can be done in a cost-effective manner. Combining the plans on a document vendor's document does not negate the advisability of having a qualified ERISA attorney review the document.

In 2009 and early 2010, the IRS released a number of technical advice memoranda dealing with ESOPs, which should be reviewed prior to drafting an ESOP document. The memoranda are available on the IRS Web site at http://www.irs.gov/retirement/article/0,,id=225834,00.html and address the following topics:

- Response to Technical Assistance Request #1 (Nov. 3, 2009). Concludes that ESOP provisions providing for a distribution of stock that is subject to immediate, mandatory resale are consistent with IRC Section 409(h).
- Response to Technical Assistance Request #2 (Nov. 3, 2009). Discusses plan language defining "qualified participant" under IRC Section 401(a)(28)(B)(iii).
- Response to Technical Assistance Request #3 (Dec. 9, 2009). Discusses the required timing and substance of IRC Section 409(p) amendments.
- Response to Technical Assistance Request #4 (Feb. 23, 2010). Discusses qualification issues presented by plan provisions concerning the mandatory transfer of employer securities to and from participant plan accounts.
- Response to Technical Assistance Request #5 (Oct. 8, 2010). Discusses qualification issues presented by plan provisions concerning the mandatory transfer of employer securities to and from participant plan accounts designed to prevent the occurrence of a non-allocation year (within the meaning of IRC Section 409(p)(3)).

DB(k)

The IRS recently provided guidance on obtaining favorable determination letters for the new DB(k) plan, which was authorized by PPA. While it was the apparent intent of PPA that the DB(k) plan would provide an easy and convenient way to offer a defined benefit plan in conjunction with a 401(k) plan, the favorable determination letter procedures appear to be the "nail in the coffin" of DB(k) plans. The procedures indicate that DB(k) plans must be individually designed and further provide that two Form 5300 filings (each at the high user fee) are required to obtain favorable determination letters. Based on an informal survey, it would appear that fewer than 100 DB(k) plans have been implemented at this time because of this recent guidance.

Conclusion

The IRS has made many improvements to pre-approved plan procedures. We recommend that they continue to work with document vendors, practitioners, and sponsors to ensure that procedures continue to reflect actual plan demographics and needs. We submit that the interim amendment procedures are largely a solution in search of a problem, and a new approach that will save resources on all sides should be considered. Pre-approved plan documents have proven to be useful to the majority of plans in the marketplace (most of which are small plans). Simplifying, while also expanding the plan types eligible for this largely successful program, makes sense for the IRS, plan practitioners, and plan sponsors.

Practitioners need to be aware that many of the differences between pre-approved documents have largely disappeared. While transitioning to a new document can certainly be a painful process, the flexibility that a volume submitter provides may be worth the effort to the average practitioner. At the same time, we caution practitioners not to choose every option simply because it is available. Certainly not every plan should use a cross-tested formula. However, having the plan already on a volume submitter with flexible cross-tested formulas could certainly be a useful option in the future. ■

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