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IRS Opens Determination Letter Program for Cash Balance Plans, Pension Equity Plans, and Certain Merged Plans

In 2017, the IRS eliminated the ability of sponsors of individually-designed qualified retirement plans to apply for favorable determination letters other than when a plan is first adopted or is terminated.

The IRS has recently announced that it will now accept determination letter submissions for cash balance and pension equity (PEP) plans during a 12-month window from September 1, 2019 through August 31, 2020. In addition, beginning on September 1, 2019, the determination letter program is being expanded on an ongoing basis to allow determination letter submissions for individually-designed plans that result from the merger of plans sponsored by previously unrelated employers following a corporate merger, acquisition, or similar business transaction, provided that both the plan merger and IRS submission occur within a limited timeframe following the business transaction.

Background

Individually-designed plans are plans that are intended to be tax-qualified retirement plans under the Internal Revenue Code but do not use template documents that have been pre-approved by the IRS. Instead, they are custom-drafted based on the design of the particular plan.

A determination letter is a letter issued by the IRS that states that the IRS has reviewed the plan documents and determined that plan terms meet the applicable requirements for tax-qualified retirement plans under Internal Revenue Code Section 401(a) and the related trust is tax-exempt under Internal Revenue Code Section 501(c).

Prior to 2017, the IRS determination letter program provided a system under which individually– designed plans could request a determination letter every 5 years (with the particular 5–year deadline determined based on the sponsor’s Employer Identification Number). Under that system, if plans were timely updated and submitted by the applicable 5–year deadline, a sponsor could generally correct without penalty any plan document errors that were related to qualification requirements becoming newly effective during that cycle.

The closing of the ongoing determination letter program was particularly troublesome for cash balance and PEP plans (also known as “hybrid” plans) because the IRS’s final regulations governing hybrid plans did not become fully effective until 2017 (later in the case of certain collectively bargained plans). Therefore, previously issued determination letters for these plans generally do not cover certain key qualification requirements addressed by these regulations. This IRS announcement is a welcome opportunity for a sponsor to obtain a determination letter that it can rely on to establish that the plan’s written terms meet all of the qualification requirements for hybrid plans.

Deadlines and Scope of Review

Cash Balance and Pension Equity Plans

Sponsors of individually–designed hybrid plans can submit their plans to the IRS during the 12–month period beginning September 1, 2019 and ending August 31, 2020.

The IRS’s review will be based on its 2017 Required Amendments List which includes, among other items, the final hybrid plan regulations. It will also take into account all Required Amendments Lists and Cumulative Lists issued prior to 2016.

(Prior to 2016, the IRS issued “Cumulative Lists” of qualification requirements that applied to individually–designed plans applying for determination letters under the 5–year cycle; in 2016, it began issuing a list annually known as a “Required Amendments List” that generally sets out new qualification requirements becoming effective during the applicable year.)

Merged Plans

Generally, a merger of plans will not result in an opportunity to apply for a new determination letter for an individually-designed plan that is the ongoing plan after the merger (the “Surviving Merged Plan”).

However, beginning on September 1, 2019, a Surviving Merged Plan can be submitted to the IRS for a determination letter if the following conditions are met:

- There is a corporate transaction such as a merger, acquisition or similar transaction that causes employers that were previously considered “unrelated” to become part of a common controlled group;
- The Surviving Merged Plan is an individually-designed plan that is formed by the merger of two or more plans of the previously unrelated employers and the merger is effective no later than the last day of the first plan year that begins after the plan year that includes the corporate transaction; and
- The determination letter submission for the Surviving Merged Plan is made no later than the last day of the first plan year that begins after the plan merger is effective.

Example: Company A acquired 100% of the stock of Company B on April 1, 2019. As of March 30, 2019, Company A sponsored Plan A and Company B sponsored Plan B. The plan year for both plans is a calendar year. In order to meet the requirements above, the plans must be merged by December 31, 2020 and the IRS determination letter submission for the Surviving Merged Plan must be made by December 31, 2021.

The IRS’s review will be based on the Required Amendment List issued during the second full calendar year before the submission is made and will also take into account all previously issued Required Amendments Lists and Cumulative Lists.

Note: The IRS will not begin accepting applications for review of Surviving Merged Plans until September 1, 2019 and there is no special extended deadline for cases where the corporate transaction or plan merger already occurred on a date that makes it impossible to meet the criteria above. In those cases, there is no

opportunity to submit the Surviving Merged Plan unless the plan is also a cash balance or PEP plan that can be submitted during the September 1, 2019 to August 30, 2020 hybrid plan window.

Before merging an acquired plan, nondiscrimination testing for all plans involved needs to be carefully considered because merging plans within the deadline above may result in an early end to the special transition period that otherwise may apply and that typically allows each separate plan to be tested separately.

In addition to new requirements for hybrid plans and plan provisions necessary to accomplish a plan merger in the case of a Surviving Merged Plan, the IRS will review all plan amendments since the last determination letter was issued for the plan being submitted and will consider all applicable qualification requirements. Therefore, prior to any plan submission, the plan and all amendments (including the plan or plans being merged into the Surviving Merged Plan) should be carefully reviewed.

What if the IRS identifies Plan Errors?

In its announcement expanding the determination letter program for these submissions, the IRS has also provided special rules related to penalties if it identifies errors in the review process.

With respect to cash balance and PEP plans, the IRS will allow correction with no penalty if it identifies any plan document error that relates to requirements under the final hybrid plan regulations. For errors unrelated to those regulations, the penalty will be equal to, or in some cases up to 250% of, the user fee that would apply if the error were identified by the sponsor and corrected under the IRS's Voluntary Compliance Program (VCP). The VCP user fee currently ranges from \$1,500 to \$3,500, depending on the assets of the plan.

With respect to Surviving Merged Plans, the IRS will allow correction with no penalty if it identifies any plan document error that relates to a plan provision that is included in the plan to effectuate the plan merger. For errors unrelated to provisions necessary to effectuate the plan merger, the penalty will be equal to, or in some cases up to 250% of, the user fee that would apply if the error were identified

by the sponsor and corrected under VCP.

For more information about IRS determination letters or other qualified retirement plan matters, please contact [Amy Crotty](#) or any attorney in [Frost Brown Todd's Employee Benefits Law](#) practice group.

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