EDUCATION AND EXAMINATION COMMITTEE

OF THE

SOCIETY OF ACTUARIES

COURSE EA-2, SEGMENT A, STUDY NOTE

EXCERPT ON PLAN QUALIFICATION

2009 RPF-1 Course: Retirement Plan Fundamentals, Part 1
Reprinted with permission from ASPPA.

E2A-52-09 **Printed in U.S.A.**

Chapter 7: Plan Qualification

§7.01 Learning Objectives

- State the benefits of sponsoring and/or participating in a qualified plan.
- State ERISA's impact on retirement plans and describe its four titles.
- Identify the different types of issued guidance regarding qualified plans and their position in the hierarchy of authority.
- Define the role of the IRS, DOL and PBGC in the enforcement of laws affecting retirement plans.
- Differentiate among temporary, proposed and final regulations.

- Explain the concept of plan qualification including the general requirements for plan qualification.

§7.02 Introduction

The fundamental benefit granted by qualified plan status cannot be overstated: favorable tax treatment for the employer who sponsors the plan, the trust and the participants covered by the plan. Achieving and maintaining qualified status through compliance with the statutes of ERISA and the Internal Revenue Code are therefore essential to the success of any retirement benefit program desiring this favored tax status.

It also cannot be overemphasized that qualification is not a static state. In addition to meeting qualification standards at the time they are first established or adopted by an employer, plans must evolve to reflect any new legislation affecting qualified retirement plans or lose their qualified status. Therefore, both in written form and in the course of day-to-day operation, a plan must conform to current qualified plan requirements.

Fortunately, guidance is available on many fronts for both plan sponsors and retirement plan professionals to assist in the protection of a plan's qualification. All of the following serve as valuable aids when seeking and securing plan qualification under the Internal Revenue Code and ERISA:

- Understanding the history of retirement plans;
- Understanding the tax advantages available to qualified plans;
- Knowledge of the sources of legislation that dictate and surround qualified plan status; and
- Various forms of guidance those sources of legislation issue.

This chapter will cover the fundamental requirements for a plan to attain qualification and the advantages that qualified status bestows upon those involved in the plan. It also includes discussion of:

- ERISA and subsequent retirement plan law;
- Roles of various government agencies charged with overseeing retirement plans; and
- The hierarchy of guidance in the form of regulations, rules, procedures, notices and other letters and memoranda.

§7.03 Plan Qualification

[A] Benefits of Qualified Plan Status

The special characteristics of qualified retirement plans described in ERISA and the Internal Revenue Code must be adhered to in order for a plan to be tax-qualified, that is, to provide favorable tax treatment to:

- Plan sponsors;
- Plan trusts, which are the legal means under which funds or assets of the plan are held in trust (separate from the employer's assets); and
- Plan participants and their beneficiaries.

This favorable tax treatment is exhibited in four principal instances.

First, contributions made by the plan sponsor, within specific limits, are deductible as a legitimate business expense on the employer's tax return.

Second, interest income and investment gains on funds within the plan's trust are tax-exempt, so benefits under the plan typically accumulate on a tax-deferred basis.

Third, participants may reduce their current taxable income through elective deferrals as allowable, and participants and their beneficiaries are generally not taxed on their benefits under a qualified plan until those benefits are distributed from the plan.

Fourth, distributions from the plan may be subject to reduced tax rates, or payment of taxes in certain circumstances may be postponed by transferring (often called rolling over) the distributed amounts to an IRA or another employer's qualified plan. It's a win-win situation for all.

[B] Growth of Employer-Sponsored Plans

Historically, the origins of formal employer-sponsored plans in the United States lay more than one and a quarter century in the past. A scant few years after the American Express Company established its plan in 1875, the Baltimore and Ohio Railroad Company became the second sponsor of a retirement plan in 1880. Thereafter, railroad, banking and public utility employers led their industrial counterparts in the creation of several hundred plans during the next 50 years.

Insurance companies emerged as the first retirement plan service-providers in 1921, when the Metropolitan Life Insurance Company issued an annuity contract designed to provide benefits to a group of employees. In 1924, Equitable Life Assurance Society of the United States became Metropolitan Life's first competitor, and thus began the inklings of retirement plan professional as a designated career.

1. Pre-ERISA Regulatory Environment

The IRS's role as a regulator of retirement plans pre-dates ERISA and originates in the Revenue Acts of 1921 and 1926. These Acts granted tax advantages to employers and employees by allowing deductions from corporate income for retirement plan contributions, tax-deferred accumulation of investment income within the plan and deferral of taxation until benefits were distributed with the stipulation that plans attained minimum coverage and met employer contribution conditions.

Disclosure of information rules were added and more stringent participation standards established with the Revenue Act of 1942 as the nation's economy expanded, and the numbers of retirement plans grew significantly.

When legislation in 1959 was enacted empowering employees with monitoring ability over their employer plans to minimize the potential for abusive mismanagement of plan funds, the DOL joined the IRS as a regulatory agency regarding retirement plans, assuming its proper role as an advocate for employees as plan participants.

Under the Welfare and Pension Plans Disclosure Act of 1959, sponsoring employers, including labor unions, had to make available to participants and their beneficiaries copies of plan descriptions and annual financial reports which were also filed with the government. Later in 1962, again to address mismanagement and abuse of plan funds, the Secretary of Labor was endowed with the power to interpret, investigate and enforce the retirement plan rules.

However, despite this history, the legislative environment for the 50 years prior to ERISA was comparatively very limited in scope and influence.

[C] ERISA

On September 2, 1974, Congress enacted the **Employee Retirement Income Security Act (ERISA)** as federal law. To say that retirement plan legislation as we know it effectively did not exist prior to ERISA would not be viewed by many as an understatement, for ERISA made sweeping and extensive changes affecting the legal, tax, investment, labor, reporting, disclosure, benefit and funding aspects of corporate and self-employed retirement plans.

ERISA was Congress's answer to public concerns regarding previous inadequacies in the law. Among them those that permitted loss of promised retirement benefits due to insufficient funding, early terminations of plans after employers deducted contributions but prior to paying benefits and lack of plan provisions dictating when employees were considered to own or have a non-forfeitable or vested right to part or all of their benefits.

Therefore, ERISA codified when an employee must be allowed to participate in a plan, how long an employee must wait before owning benefits, how much and how often an employer must contribute to the plan, what information about the plan must be disclosed to participants, rules of conduct for those administering the plan and its assets and avenues for enforcing these qualified plan rules. Additionally, ERISA established two new important concepts: plan termination insurance (administered by the PBGC), and IRAs for those taxpayers not covered by an employer's qualified retirement plan.

Notably, while ERISA does not apply to all employer-sponsored plans, as explained in Chapter 1, the broad reach of ERISA should not be underestimated. In general, federal laws such as ERISA will supersede state laws whenever they are in conflict.

1. ERISA Titles

ERISA consists of four numbered sections known as Titles. It is not unusual to encounter references to ERISA by title numbers, which are as follows:

- Title I relates to the protection of employee rights under employee benefit plans and is often thought of as containing the labor provisions. Included are requirements for:

    - reporting and disclosure of plan information;
    - the crediting or accrual of benefits;
    - the method and payment of benefits;
    - participation;
    - ownership or vesting;
    - funding;
    - standards of conduct for those empowered to administer the plan and handle plan assets; and
    - the enforcement of Title I.

  For example, Title I created the right of participants, beneficiaries and the DOL to file suit regarding retirement benefits.

- Title II applies only to qualified retirement plans and contains various amendments to the Internal Revenue Code, some of which were effected to create tax provisions which parallel and reflect the new labor law provisions of Title I. Included are specific conditions for tax qualification such as minimum coverage, maximum benefit limits, top-heavy compliance, provisions for deductibility of contributions and taxation of distributions.

- Title III concerns the jurisdiction, administration and enforcement of ERISA, including the coordination of regulatory authority between the IRS and DOL. Also included are provisions regarding educational requirements for actuaries, who as professionals in the area of statistical probability, perform certain required benefit and funding-related calculations for defined benefit plans.

- Title IV created the Pension Benefit Guaranty Corporation (PBGC) and established the termination insurance program for defined benefit plans.

[D] Subsequent Legislative History

In the absence of a national policy, Congress has repeatedly acted to protect the rights of participants and beneficiaries from sometimes real and sometimes perceived abusive employer practices. Post-ERISA legislation has been robustly pursued, and the body of employee benefits-related law is now substantial and under constant scrutiny for revision and expansion.

While a detailed history of the numerous laws enacted subsequent to ERISA is beyond the scope of this course, and indeed might decrease clarity of understanding since new laws often change, eliminate or make obsolete provisions contained in their predecessors, please refer to Exhibit 7-A in Section 7.08 for a summary of retirement plan legislation.

[E] The Order of Authority

Because laws quite often are broadly-stated, incomplete or unclear, supportive and clarifying guidance in various forms are issued from time to time that serve to explain and interpret these laws, providing employers and retirement plan professionals with a methodology when dealing in complicated and ambiguous areas.

There is an inherent order of authority or hierarchy of reliance that is created by the scope of application for a particular form of guidance. For example, the highest order of authority or reliance is placed on laws issued by Congress, for these apply to everyone in the land. At the lowest end of the hierarchy, with the smallest scope of application, would be that guidance issued at the private or specific request of an individual taxpayer, since the response is directed to and limited by that individual's particular circumstances.

To assist in an awareness of the contextual application of existing guidance, some of which is discussed in the remainder of this chapter, the order of authority, in descending hierarchical reliance, may be summarized as follows:

- Laws as enacted by Congress (ERISA and the Internal Revenue Code);

- Court Decisions, since federal law generally preempts state law, (U.S. Supreme Court, Federal Courts of Appeal, Federal District or Tax Courts);
- Legislative History (Committee Reports, Blue Books);
- Treasury or Department of Labor Regulations - Final, Proposed and Temporary;
- Revenue Rulings;
- Revenue Procedures;
- Notices and Announcements – includes News Releases, General Counsel and Technical Advice Memoranda, Field Assistance Bulletins, Information Letters; and
- Private Letter Rulings and Advisory Opinions.

§7.04 Regulations Issued by the IRS and DOL

[A] Responsibility for Enforcement

The responsibility for enforcement of the Internal Revenue Code is placed with the Secretary of the Treasury (Secretary), who is empowered to prescribe rules and regulations. The IRS, with the approval of the Secretary, is responsible for interpreting statutory authority, administering the Internal Revenue Code and developing a uniform tax enforcement policy.

As the result of ERISA, Congress created the IRS's Office of Employee Plans and Exempt Organizations that was subsequently eliminated and succeeded by the **Tax Exempt and Government Entities division**. Within the IRS, the Tax Exempt and Government Entities division or Employee Plans division oversees retirement plans. In particular, it administers the Title II provisions of ERISA and provides a wealth of information via its Web site (www.irs.gov/ep).

The provisions of Title I of ERISA are administered by a separate agency within the DOL called the **Employee Benefits Security Administration (EBSA)**. (The EBSA Web site is www.dol.gov/ebsa.) Headed by an Assistant Secretary of Labor, EBSA's stated mission is to "assist workers in getting the information they need to exercise their benefit rights; assist plan officials to understand the requirements of the relevant statutes in order to meet their legal responsibilities; develop polices and regulations that encourage the growth of employment-based benefits; [and] deter and correct violations of the relevant statutes through strong administrative, civil, and criminal enforcement efforts to ensure workers receive promised benefits."

Because of the parallel provisions within Titles I and II of ERISA where the tax laws were amended to mirror the labor laws, there were areas of joint responsibility between the IRS and DOL. Subsequently, in 1978 the IRS became primarily responsible for the participation, funding and ownership or vesting rules, while the DOL assumed primary responsibility for the reporting, disclosure and standards of conduct requirements.

Responsibility for enforcement of Title IV of ERISA rests with the agency created by Title IV: the PBGC. Since the PBGC's termination insurance program applies only to defined benefit plans, further discussion of the PBGC is provided in RPF-2.

Given the complexities of the tax and labor laws, as well as the need to maintain uniformity in their application, both the IRS and the DOL have developed multifaceted administrative policies that include interpretation of statutory authority, drafting of regulations, rulings on substantive issues and disseminating information to the general public. Because the emphasis in this course is placed on gaining knowledge regarding qualification for purposes of tax advantages, the ensuing discussion will concentrate more fully on IRS issuances.

[B] Treasury or Labor Regulations (Treas. Reg. §1.xxx or Reg. §.xxx)

The pronouncements by the IRS and DOL that have the broadest impact are **Treasury Regulations** and **Labor Regulations**. Generally speaking, there are two types of Regulations: Legislative and Interpretative.

1. A **Legislative Regulation** is one issued under specific authority delegated by Congress to set standards or establish policy. Legislative Regulations are given the full force and effect of law unless the IRS or DOL goes beyond the scope of its delegated power.

2. An **Interpretative Regulation** is a statement of opinion on the meaning of ERISA or the Internal Revenue Code and, while not having the force and effect of law, such regulations are generally accorded great weight by the courts. Interpretative Regulations are subject to substantive judicial review as to whether the position adopted by the IRS or DOL correctly interprets the statute.

[C] Final, Proposed or Temporary Regulations

<u>1. What Does a Regulation Do?</u>

A regulation is a broad expression of the issuing agency's interpretation of a statutory provision under ERISA or the Internal Revenue Code. Regulations often contain examples of typical fact patterns to illustrate the narrative explanation and are binding on both the taxpayer and the IRS or DOL. However, a regulation is not meant to cover all situations. Employers and retirement plan professionals will therefore look to other forms of guidance offering increased specificity to supplement their understanding.

Regulations are designated as one of the following:

- **Final Regulations** must be published in the Federal Register and provide for adequate notice, comments and public hearing.
- **Proposed Regulations** must be published according to specific procedural requirements and are intended to become final regulations. Proposed regulations are issued to solicit public written comments, and public hearings are held if written requests are made.
- **Temporary Regulations** are published to provide guidance in an area of immediate concern or to cover a situation that may exist only for a short period of time.

All regulations must be issued in proposed form before being published in final form. A temporary regulation may also be designated as a proposed regulation if such regulation conforms to the procedural requirements.

It is common for the IRS and DOL to announce that reliance on a proposed regulation will not adversely affect the employer. Once a final regulation is issued time will be given either to conform retroactive transactions to the final regulation or an exception will be made for previously completed transactions under a process called grandfathering.

A proposed regulation or a temporary regulation has the same force and effect of law as a final regulation and is subject to the same judicial review. While not a common occurrence, proposed or temporary regulations may be withdrawn prior to becoming final regulations.

2. Regulation Citations

Citations to Treasury Regulations appear as “Treas. Reg. §1.” while Labor Regulations appear as “Reg. §.” Contained in the numbering system of both sets of regulations is a reference to the section of the Internal Revenue Code or ERISA (also referred to as the Act) that the regulation interprets. Please refer to Appendix B for a brief table with descriptions of the IRC Sections applicable to retirement plans by section number.

For example, IRC §401(a), which contains the requirements for plan qualification, is interpreted by Treas. Reg. §1.401(a), and IRC §401(k) has as its companion Treas. Reg. §1.401(k). (Of note: Treasury Regulation numbers always begin with “1.”)

With regard to citation examples of ERISA and Labor Regulations, Act §408(b) regarding loans made to certain participants under the plan, is interpreted by Reg. §2550.408b, while Act §503, regarding procedures pertaining to claims for plan benefits, should be read with Reg. §2560.503 at hand.

§7.05 Rulings, Procedures and Determination Letters

The IRS Rulings Program advises taxpayers in advance how the IRS will interpret the Internal Revenue Code and affiliated Regulations with regard to distinct factual situations. The program offers guidance in two categories:

1. Revenue Rulings; and
2. Private Letter Rulings.

[A] Revenue Rulings (Rev. Rul. yyyy-x)

Revenue Rulings are construed as an official interpretation by the IRS regarding how the law is applied to a particular subject using a specific set of facts. Although an individual Revenue Ruling would not apply to fact patterns that deviate from those stated within the Ruling, its purpose is to ensure that the issue it addresses will be handled uniformly throughout the country.

One might think of a Revenue Ruling as an explanation of the effect of the Internal Revenue Code or a Treasury Regulation upon a prescribed set of circumstances that have general application. Thus, Revenue Rulings may be relied upon by taxpayers, as long as any limits or factual prescriptions contained within the Rulings are met.

For example, Rev. Rul. 2004-11 explains the effect of a portion of the minimum coverage requirements upon the retirement plan of an employer who has experienced a company merger, acquired another company or sold part of itself during the 12-month period considered the plan year. Any employer who has undergone a similar merger, acquisition or sale conforming to the fact pattern established by Rev. Rul. 2004-11 could therefore rely on its guidance.

<u>1. Revenue Ruling Citations</u>

A Revenue Ruling citation contains the year it was issued and a number representing the order of its issuance. As an example, Rev. Rul. 2004-11 was the eleventh Revenue Ruling of 2004. Of note: Revenue Rulings issued prior to year 2000 exhibit only the last two digits of their issuance year. Therefore, the first Revenue Ruling issued in 1998 was Rev. Rul. 98-1.

[B] Revenue Procedures (Rev. Proc. yyyy-x)

Revenue Procedures use the same citation system as Revenue Rulings, which may at first glance allow a Ruling to be mistaken for a Procedure. However, the two are in form and content quite distinct. A **Revenue Procedure** is precisely what its name implies: it embodies an official statement of the procedural steps one must take to comply with the Internal Revenue Code, related statutes, tax treaties and other regulations.

By publishing a how to guide towards accomplishing compliance, the IRS ensures that what should be a matter of public knowledge has broad impact. Like Revenue Rulings, a Revenue Procedure has less force and effect than Treasury Regulations, but taxpayers are expected to conform to the Procedure's dictates. Indeed, Revenue Procedures represent extremely useful guidance as the explanations they contain are often undertaken in great detail.

For example, Rev. Proc. 2008-6 explains what information and forms must be provided to the IRS when requesting a favorable determination letter, how to withdraw an application, where to send the application, how to request a status conference, what will happen if an application submission is incomplete and even such minutia as what identifying information regarding an employer should be contained in the cover letter to the IRS if an employer is sponsoring more than one plan and wishes to submit all of its plan documents at the same time.

[C] Private Letter Rulings (PLR yyyywwxxx)

A **Private Letter Ruling (PLR)** is published in response to a request from an individual taxpayer wishing to ascertain the IRS's position with respect to the private set of facts presented. As such, a PLR issued to a taxpayer may be relied upon only by that taxpayer. To emphasize the specificity of its application, the PLR bears the legend: "This document may not be used or cited as precedent."

Inquisitive natures aside, those who peruse PLRs are often attempting to glean insight into how the IRS might be expected to respond to their own situations, and thus PLRs have their place in the hierarchy of available guidance. However, another taxpayer with the same or similar factual circumstances described in a published PLR must request a separate Private Letter Ruling to be assured of the same result. Also of note: PLRs are not issued as answers for questions regarding whether or not a plan is qualified.

1. PLR Citations

PLRs are identified by the year, week and issuance number. Hence, PLR 199938052 was the 52nd Private Letter Ruling issued in the 38th week of 1999. Prior to 1999, only the last 2 digits of the year were used as identifiers.

[D] Determination Letters

Assurance that a plan in written form constitutes a document compliant with qualification requirements remains the domain of IRS Determination Letters rather than PLRs. Upon submission of the plan documents to the IRS for review, a request for determination letter process is initiated to culminate in receipt of a letter illustrating approval of the plan's provisions. This is known as a **favorable determination letter**.

As part of the quest for a favorable letter, during the approval process, any deficiencies in the plan documents are identified and corrected. In the event of a legislative change, plan documents may be updated in response and later resubmitted for a current determination letter that cites approval of the plan document in its present form.

Understandably, plans that have enjoyed a lengthy history often have several determination letters: the current, most recently dated determination letter conferred upon the last application to the IRS and previous letters that applied at various stages in the evolution of the plan.

It is important to take heed of a cautionary tale: if a favorable determination letter is issued to a qualified plan but the plan is found to operate in a manner which does not comply with its written provisions, it may be disqualified since the determination letter does not guarantee qualified status of the plan.

§7.06 News Releases, Notices, Announcements, Information Letters and Advisory Opinions

There is an abundance of additional guidance from the IRS and DOL available to keep the public informed, albeit communicated via different techniques and of varying degrees of application.

The IRS uses **News Releases, Notices** and **Announcements**

- To inform the public of current developments;
- To present information of general interest; and
- To summarize new tax law or to publicize procedural matters.

Principally, the material contained within the News Release, Notice or Announcement does not present a question of fact or involve an issue of reliance or substantive interpretation of the Internal Revenue Code. For example, a Notice may relate what a Regulation will say in situations where issuance of the Regulation is pending and not expected in the near future.

Announcements are intended to have only immediate or short-term value: thus, an announcement may be made to remind taxpayers of approaching deadlines for filing or conforming a transaction to a new statute. However, as noted in Rev. Rul. 87-138, these communications are intended to be relied on by taxpayers and are the equivalent of revenue rulings and revenue procedures.

The DOL also offers News Releases regarding retirement and labor issues. The IRS and DOL employ non-binding **Information Letters** to call attention to well-established principles or interpretations as part of their general service to the public.

The DOL will also provide an **Advisory Opinion**, something akin to a Labor Department version of the PLR, in answer to inquiries from individuals and organizations regarding the application of the Act to a restricted set of facts. In addition, both agencies advertise "contact us" technical assistance via their respective Web sites and phone lines.

In retrospect then, plan sponsors and retirement plan professionals have several avenues to explore when searching for guidance regarding the obtainment of plan qualification under the Internal Revenue Code and ERISA. The listing above is by no means exhaustive. Consequently, the ability to research, identify and ultimately grasp the legal underpinnings of retirement plan rules and their accompanying guidance, as well as the authority and breadth of their application, will serve to strengthen awareness and understanding of the basic and fundamental requirements for plan qualification as set forth in these laws.

§7.07 Qualification Requirements

[A] Fundamental Requirements

It only makes good business sense for an employer to select the plan design which best meets the employer's objectives. Although plans can be established which are not tax-qualified and do serve to uphold certain business criteria, the tax savings of a qualified plan usually argue convincingly and successfully for its adoption as the employer's optimal choice. In this light, there are four fundamental requirements for any plan to be considered qualified for tax purposes:

1. The plan must be established and maintained by the employer for the exclusive benefit of its employees or their beneficiaries;
2. The employer must intend that the plan be permanent;
3. The plan must be in writing; and
4. The plan must be communicated to the employees.

[B] Qualification in Form

In addition, IRC §401(a) contains the basic requirements for qualified plans. Among the more notable of these are:

- Contributions made or benefits under the plan must not disproportionately favor the highly compensated; that is, the plan must not discriminate against lower-paid employees [IRC §401(a)(4)].
- The plan must not require a participant to work more than a maximum period of time before being granted ownership of benefits. Benefits once owned may not be taken away and returned to the employer [IRC §401(a)(7)].

- Plans under which a specified majority of the benefits has been credited to a key group of employees, called top-heavy plans, must satisfy additional requirements concerning faster vesting and minimum contributions or benefits [IRC §401(a)(10)(B)].
- A plan must provide for the payment of benefits in the form of a qualified joint and survivor annuity. That is, the plan should normally pay retirement benefits to a married participant for the participant's lifetime and then continue payments (the payment amount may be reduced) to the surviving spouse for the remainder of the spouse's lifetime [IRC §401(a)(11)]. There are exceptions for certain profit sharing plans.
- The plan must provide that on merger or consolidation of the plan with another plan each participant shall be entitled to a benefit after the merger that is no less than the participant's benefit before the merger [IRC §401(a)(12)].
- The plan must specify that benefits earned by a participant may not be assigned or alienated. They may not be granted to another party or attached by outside parties such as the participant's creditors [IRC §401(a)(13)].
- Unless the participant elects otherwise, the plan must provide that the payment of benefits shall commence no later than 60 days after the end of the 12-month period designated as the plan year in which the latest of three dates occur: 1) reaching the plan's usual or normal retirement age, 2) the tenth anniversary of the date the employee became a plan participant, or 3) the date the participant terminated service with the employer [IRC §401(a)(14)].
- The plan must not allow the level of contributions or benefits provided to a participant to exceed certain maximum amounts [IRC §415].
- The plan must cover or provide benefits for a required minimum number of employees of the employer [IRC §410(b)].
- The plan must limit the amount of an individual's compensation that can be taken into account for determining contributions and benefits to $230,000 (as indexed for cost of living adjustments in 2008) [IRC §401(a)(17)].
- Defined benefit plans must specify what assumptions will be used in calculating and converting benefits from one payment form to another so that an employer may not change them at will [IRC §401(a)(25)].

  For example, a plan may use an investment rate of return assumption and an estimated lifetime assumption (or mortality assumption) to offer a terminating participant the following choice: $1,000 per month for the rest of your lifetime with payments to begin when you reach age 65, or what has been determined as an equivalent amount: a lump sum payment of $100,000 right now.

The plan document must provide these basic requirements at a minimum in order to become a qualified plan.

[C] Qualification in Operation

It also is necessary for the plan to operate in compliance with its written requirements; in other words, the plan must exhibit qualification in operation. Even though a plan document may have been approved by the IRS as a qualified plan in form, the plan may still be disqualified if it is administered contrary to the provisions of either its document or current law.

§7.08 Exhibits

Exhibit 7-A Summary of Significant Legislation Affecting Retirement Plans

ERISA	Employee Retirement Income Security Act of 1974
ERTA	Economic Recovery Tax Act of 1981
TEFRA	Tax Equity and Fiscal Responsibility Act of 1982
DEFRA	Deficit Reduction Act of 1984
REA	Retirement Equity Act of 1984
COBRA	Consolidated Omnibus Budget Reconciliation Act
OBRA’86	Omnibus Budget Reconciliation Act of 1986
TRA’86	Tax Reform Act of 1986
OBRA’87	Omnibus Budget Reconciliation Act of 1987
TAMRA’88	Technical and Miscellaneous Revenue Act of 1988
OBRA’89	Omnibus Budget Reconciliation Act of 1989
OBRA’90	Omnibus Budget Reconciliation Act of 1990
UCA’92	Unemployment Compensation Amendments of 1992
FMLA	Family and Medical Leave Act of 1993
OBRA’93	Omnibus Budget Reconciliation Act of 1993
GATT or	Uruguay Round of the General Agreement on Tariffs and Trade

RPA'94	The Retirement Protection Act of 1994 was attached to the GATT bill.
USERRA	Uniformed Services Employment and Reemployment Rights Act of 1994
SBJPA	Small Business Job Protection Act of 1996
TRA'97	Taxpayer Relief Act of 1997
RRA'98	IRS Restructuring and Reform Act of 1998
CRA'00	Community Renewal Tax Relief Act of 2000
EGTRRA	Economic Growth and Tax Relief Reconciliation Act of 2001
JCWAA	Job Creation and Worker Assistance Act of 2002
SOA'02	Sarbanes-Oxley Act of 2002
SCRA	Service Members Civil Relief Act of 2003
PFEA	Pension Funding Equity Act of 2004
PPA	Pension Protection Act of 2006

§7.09 Key Terms

Advisory Opinion: The DOL version of a private letter ruling.

Announcement: Issued by the IRS to inform the public of current developments, present information of public interest, summarize new tax law and publicize procedural matters.

Employee Benefits Security Administration (EBSA): The division under the Department of Labor which administers the nontax (regulatory and administrative) provisions of ERISA such as the reporting, disclosure and standards of conduct provision of Title I of ERISA. The EBSA issues opinion letters and other pronouncements, and requires certain information forms to be filed with it by plan sponsors.

Employee Retirement Income Security Act (ERISA): The basic labor law covering qualified plans, it incorporates both the pertinent Internal Revenue Code provisions by reference and labor law provisions.

Favorable Determination Letter: A letter illustrating approval of the plan's provisions regarding form for qualification purposes.

Final Regulation: Must be published in the Federal Register and provide for adequate notice, comments and public hearing.

Information Letter: A nonbinding letter that calls attention to well-established principles or interpretations of the law.

Interpretive Regulation: A statement of opinion on the meaning of ERISA or the Internal Revenue Code.

Labor Regulation: Regulations interpreted by the DOL.

Legislative Regulation: Issued under specific authority delegated by Congress to set standards or establish policy.

News Release: Issued by the IRS to inform the public of current developments, present information of public interest, summarize new tax law and publicize procedural matters.

Notice: Issued by the IRS to inform the public of current developments, present information of public interest, summarize new tax law and publicize procedural matters.

Private Letter Ruling (PLR): A private ruling issued by the IRS in response to a request from a taxpayer as to the tax consequences of a proposed or completed transaction. Private letter rulings are published informally by several publishers. They are not considered as precedent for use by taxpayers other than for the individual who requested the ruling, but they do give an indication of the IRS' current attitude as to a particular type of transaction.

Proposed Regulation: Must be published according to specific procedural requirements and are intended to become final regulations.

Revenue Procedure: Issued by the IRS, a Revenue Procedure is similar to a revenue ruling. However, it focuses on procedural matters or details the requirements to be followed in connection with various dealings with the IRS. Revenue Procedures also may set forth guidelines that the IRS follows in handling certain tax matters.

Revenue Ruling: Issued by the IRS, these rulings express the IRS' views as to the tax results that apply to a specific problem.

Tax Exempt and Government Entities division: The IRS agency that administers the participation, funding and ownership or vesting provisions of Title I of ERISA. It also administers Title II provisions of ERISA.

Temporary Regulation: Published to provide guidance in an area of immediate concern or to cover a situation that may exist for a short period of time.

Treasury Regulation: Regulations interpreting the Internal Revenue Code are technically Treasury regulations. The IRS is a part of the Treasury Department.

§7.10 Review of Key Concepts

- A qualified plan receives favorable tax treatment by allowing
    - the plan sponsor to receive a deduction for contributions to the plan;
    - the trust to defer taxes on investment gains; and
    - participants to reduce their current taxable income through elective deferrals, defer taxes until benefits are distributed and possibly pay taxes at a reduced rate.

- ERISA established significant guidelines for employer-sponsored retirement plans, including extensive reporting and disclosure rules.

- ERISA established two new important concepts: plan termination insurance, administered by the PBGC, and IRAs for those taxpayers not covered by an employer's qualified retirement plan.

- Congress creates tax statutes or laws. The Internal Revenue Code contains these tax laws. Supportive and clarifying guidance is issued from time to time that serves to explain and interpret these laws.

- The IRS has responsibility for the enforcement and interpretation of the Internal Revenue Code, the issuance of Regulations and other rulings and provision of guidance with respect to application of the Internal Revenue Code.

- The DOL has primary responsibility for the enforcement of the reporting, disclosure and standards of conduct requirements of ERISA.

- The fundamental benefit of a qualified plan is favorable tax treatment for plan sponsors, the trust and the participants.

- Temporary regulations provide guidance in an area of immediate concern, while proposed regulations are intended to become final regulations.

- In order to be tax-qualified, a retirement plan must meet certain basic requirements found in the Internal Revenue Code, such as the plan must be established and maintained by the employer for the exclusive benefit of its employees or their beneficiaries.

§7.11 Review Questions

[A] True or False

______ 1. A plan must exhibit qualification in operation and maintain a qualified written document to be assured of its qualified status.

______ 2. The IRS is responsible for interpreting statutory authority, administering the Internal Revenue Code and developing uniform tax enforcement policy.

______ 3. EBSA is responsible for assisting workers in obtaining information they need to exercise their benefit rights.

______ 4. Tax deferral is a major reason to maintain a qualified plan.

______ 5. Title IV of ERISA created the PBGC.

[B] Multiple Choice

6. All of the following statements regarding ERISA are **TRUE, EXCEPT**:

   A. It provided rules to determine when a participant is vested in benefits.
   B. It established plan termination insurance.
   C. It established IRAs.
   D. It established educational requirements for actuaries.
   E. It mandated retirement benefits for all workers.

7. All the following can be issued by the IRS, **EXCEPT**:

   A. Legislative regulations
   B. Corrective regulations
   C. Temporary regulations
   D. Final regulations
   E. Proposed regulations

8. All of the following are general requirements that must be met for a plan to be qualified, **EXCEPT**:

   A. It must be communicated to employees
   B. It must be established for all employees
   C. It must be permanent
   D. It must be in writing
   E. It must be for the exclusive benefit of the employees

9. All of the following statements regarding proposed regulations are **TRUE, EXCEPT**:

   A. Proposed regulations are issued at the specific request of an individual taxpayer.
   B. A proposed regulation may be withdrawn prior to becoming a final regulation.
   C. All regulations must be issued in proposed form prior to being published in final form.
   D. Proposed regulations are issued to solicit public comments.
   E. A proposed regulation has the same force and effect as a final regulation.

§7.12 Answers

1. **True.** A plan must exhibit qualification in operation and form (written document) to be assured of its qualified status. §7.07

2. **True.** The IRS is responsible for interpreting statutory authority, administering the Internal Revenue Code and developing uniform tax enforcement policy. §7.04 [A]

3. **True.** EBSA is responsible for assisting workers in obtaining information they need to exercise their benefit rights. §7.04 [A]

4. **True.** Tax deferral is a major reason to maintain a qualified plan. §7.03 [A]

5. **True.** Title IV of ERISA created the PBGC. §7.03 [C]

6. The correct answer is **E.** §7.03 [C]

   A. Incorrect. This statement is true because ERISA provided rules to determine when a participant is vested in benefits.
   B. Incorrect. This statement is true because ERISA established plan termination insurance.
   C. Incorrect. This statement is true because ERISA established IRAs.
   D. Incorrect. This statement is true because ERISA established educational requirements for actuaries.
   E. Correct. This statement is false because ERISA did not mandate retirement benefits for all workers.

7. The correct answer is **B.** §7.04 [B] and §7.04 [C]

   A. Incorrect. This statement is true because the IRS issues legislative regulations.
   B. Correct. This statement is false because the IRS does not issue corrective regulations.
   C. Incorrect. This statement is true because the IRS issues temporary regulations.
   D. Incorrect. This statement is true because the IRS issues final regulations.
   E. Incorrect. This statement is true because the IRS issues proposed regulations.

8. The correct answer is **B.** §7.07 [A]

   A. Incorrect. This statement is false because a qualified plan must be communicated to employees.
   B. Correct. This statement is true because a qualified plan need not be established for all employees.
   C. Incorrect. This statement is false because a qualified plan must be permanent.
   D. Incorrect. This statement is false because a qualified plan must be in writing
   E. Incorrect. This statement is false because a qualified plan must be for the exclusive benefit of the employees

9. The correct answer is **A.** §7.04 [C]

   A. Correct. This statement is false because private letter rulings, not proposed regulations are issued at the specific request of an individual taxpayer.
   B. Incorrect. This statement is true because a proposed regulation may be withdrawn prior to becoming a final regulation.
   C. Incorrect. This statement is true because all regulations must be issued in proposed form prior to being published in final form.
   D. Incorrect. This statement is true because proposed regulations are issued to solicit public comments.
   E. Incorrect. This statement is true because a proposed regulation has the same force and effect as a final regulation.

Appendix B:
A Guide to IRC Sections Affecting Retirement Plans

IRC §401(a) - Requirements for qualification

- (4) & (5) - General nondiscrimination rules
- (9) - Required distributions
- (10) - Top-heavy rules must be stated in plan document
- (11) - Requirement for a joint and survivor annuity and pre-retirement survivor annuity (QJSA and QPSA)
- (17) - Compensation limits
- (25) - Actuarial assumptions must be specified
- (26) - Minimum participation requirements
- (27) - Contributions to profit sharing plans need not be based on profits
- (28) - Employee Stock Ownership Plan (ESOP) requirements
- (31) - Optional direct transfer of eligible rollover distributions

IRC §401(b) - Retroactive changes in plan

IRC §401(c) - Rules relating to self-employed individuals and owner-employees

IRC §401(d) - Plans benefiting owner-employees

IRC §401(h) - Medical benefits for retirees

IRC §401(k) - Cash or deferred arrangement

IRC §401(l) - Integrating plan benefits with Social Security (Permitted Disparity)

IRC §401(m) - Nondiscrimination test for employer matching contributions and after-tax employee contributions

IRC §402(a) -Taxability of beneficiary of exempt trust

IRC §402(b) -Taxability of beneficiary of non-exempt trust

IRC §402(c) - Rules applicable to rollovers from exempt trusts

IRC §402(d)	- Tax on lump-sum distributions
IRC §402(f)	- Written explanation to recipients on distributions eligible for rollover treatment
IRC §402(g)	- Limit on elective deferrals
IRC §402(h)	- Rules for Simplified Employee Pensions (SEP)
IRC §403(a) and (b)	- Tax-sheltered annuity (TSA) rules
IRC §404	- Deduction of contribution rules
IRC §408	- Individual Retirement Accounts (IRA)
IRC §410(a)	- Minimum participation standards
IRC §410(b)	- Minimum coverage requirements
IRC §411(a)	- Vesting schedules
IRC §411(b)	- Accrued benefit requirements
IRC §411(d)(6)	- Anti-cutback rules
IRC §412	- Minimum funding standards
IRC §413	- Collectively-bargained plans
IRC §414(a)	- Service for predecessor employer
IRC §414(b)	- Employees of controlled group corporations
IRC §414(c)	- Employees under common control
IRC §414(d)	- Governmental plans
IRC §414(m)	- Affiliated service group
IRC §414(n)	- Employee leasing
IRC §414(p)	- Qualified Domestic Relations Order (QDRO)
IRC §414(q)	- Highly Compensated Employee (HCE)

IRC §414(r)	- Qualified Separate Lines of Business (QSLOB)
IRC §414(s)	- Nondiscriminatory definition of compensation
IRC §414(u)	- Veteran's Rights under Uniformed Services Employment and Reemployment Rights Act of 1994 (USERRA)
IRC §414(v)	- Catch-up contributions for individuals age 50 or over
IRC §415(b)	- Defined benefit limitations
IRC §415(c)	- Defined contribution limitations
IRC §416(g)	- Top-heavy plan defined
IRC §416(l)	- Key Employee definition
IRC §417(a)	- Restrictions on cash-out payments
IRC §417(b)	- Other special rules and definitions regarding survivor annuities