A Wellness Prescription for Qualified Retirement Plans

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I. Introduction

Almost none of you were alive in 1921 when Congress cut taxes and enacted the first federal income tax preference for qualified retirement plans. It is more likely than not that the IRS issued determination letter rulings to qualified retirement plans before you were born. Some remember ERISA and the Tax Reform Act of 1986; others do not, for one reason or another.

Today, however, we are together experiencing a different era. This is a time in which partisan congressional factions are sparring but not doing — with the exception of slashing the IRS’s budget. It is a time in which the IRS has had to eliminate the determination letter program for individually designed qualified plans with a prior determination letter ruling. This era may see a comprehensive overhaul of the Internal Revenue Code of 1986, as amended. And it may see the significant legally required changes and plan design changes likely to follow from it.

This report provides an analytical framework to help plan sponsors and practitioners preserve the tax-qualified status of individually designed retirement plans without the determination letter program. Section II analyzes an effect of Rev. Proc. 2016-37, 2016-29 IRB 136, which eliminated the determination letter program for individually designed qualified plans with a prior determination letter ruling. Plan sponsors and third parties may rely
on a plan’s last determination letter ruling only for provisions in the plan document that are not modified or affected by a change in law. The IRS established a remedial amendment system under section 401(b) to help plan sponsors with the transition, and it reformulated the Employee Plans Compliance Resolution System (EPCRS) under Rev. Proc. 2016-37. Section III explores the foundational principles for applying section 401(b). The construction of section 401(b) and reg. section 1.401(b)-1 identifies the main limits of relief available. A plan sponsor may cure a disqualifying provision by adopting a retroactive amendment during the applicable remedial amendment period. The analysis yields general principles to help understand and apply the IRS’s curative and corrective mechanisms available under section 401(b) and the three EPCRS correction programs (the self-correction program, the voluntary correction program, and the audit closing agreement program (audit CAP)).

The elimination of the determination letter program makes section 401(b) more important than ever to plan sponsors and those who counsel them on preserving tax-qualified status. Section IV reviews the IRS’s new section 401(b) remedial amendment system under Rev. Proc. 2016-37. The IRS extended the remedial amendment period for curing a disqualifying provision. The transition rule extends the remedial amendment period to December 31, 2017, for a disqualifying provision with an open remedial amendment period as of December 31, 2016. Plan sponsors can no longer depend on an additional 91-day remedial amendment period extension because of the elimination of the determination letter program. The IRS also exercised its discretion to extend the remedial amendment periods for curing a disqualifying provision caused by a qualification requirement change and a disqualifying provision caused by a discretionary plan amendment. Curing a disqualifying provision during the remedial amendment period prevents an EPCRS qualification failure from occurring when the period ends.

EPCRS correction programs are unavailable while and to the extent that a plan sponsor may use section 401(b) to conform plan provisions to plan administration and comply with the law. Section V analyzes the availability of curative relief under section 401(b) and the correction programs under EPCRS. Each plays a role in the system, but at different times. Section 401(b) is generally available to cure a disqualifying provision during the applicable remedial amendment period. EPCRS is available after the remedial amendment period ends or to the extent section 401(b) is otherwise unavailable. Without periodic determination letter rulings, plan sponsors and practitioners must understand how to apply the section 401(b) remedial amendment system under Rev. Proc. 2016-37 and the reformulated EPCRS correction programs under Rev. Proc. 2016-51. That understanding is imperative if plan sponsors are to maintain tax-qualified plans or if the need arises to seek assurance that a plan provision modified or affected by a change in law satisfies the qualification requirements.

Despite the elimination of the determination letter program, the IRS will continue selecting plans for audits that can last several years. Section VI recommends internal controls and preventive measures that plan sponsors should implement as a form of tax-qualified wellness prescription for their individually designed qualified plans. The IRS created an incentive to establish and follow a program for satisfying the requirements under section 401(a). When selecting the size of the monetary penalty to impose for a qualification failure discovered on audit and corrected under audit CAP, the IRS will

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4 An analysis of the new extended remedial amendment periods and the IRS’s new required amendment and operational compliance lists should help plan sponsors and legal counsel remedy disqualifying provisions before they become qualification failures. See generally Rev. Proc. 2016-37, sections 9 and 10.
give weight to measures designed to satisfy the qualification requirements. Further, eligibility for the self-correction program is conditioned on having established practices and procedures designed to facilitate compliance with section 401(a) in form and operation. In the years ahead, a qualified plan wellness prescription will be an essential part of avoiding costly audit penalties and civil sanctions, and for providing assurance as to a plan’s tax-qualified status. Whether a plan sponsor implements a tax-qualified wellness prescription now greatly affects what the response will be to reasonably foreseeable events in the future.

The examples herein are for illustrative purposes. Unless otherwise stated, assume that the plan sponsor maintains an individually designed plan that has a prior determination letter ruling, and that section 411(d)(6) presents no problems.

II. A New Era

Congress conditions valuable employer and employee tax preferences (that is, immediate deduction for employers, no current taxes for employees, and tax deferral until retirement) on satisfying the qualification requirements under section 401(a) in form and operation. A form failure occurs when a plan document leaves out required language or terms. An operational failure occurs when (1) a plan, in operation, does not meet the section 401(a) requirements; and (2) a plan fails to follow the terms of the plan document. Failure to meet one of the section 401(a) requirements could result in plan disqualification and the IRS disallowing the employer plan sponsor’s deduction and the plan’s tax-exempt status.

The written plan document is the touchstone for determining whether a plan formally and operationally satisfies the qualification requirements under section 401(a). It is a qualification requirement to have a written plan document. The legal plan document must provide the terms applicable to participants and beneficiaries to satisfy the “definitely determinable benefit” qualification requirement.

The plan sponsor and its service providers must

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Failure to meet one of the section 401(a) requirements could result in plan disqualification and the IRS disallowing the employer plan sponsor’s deduction and the plan’s tax-exempt status. The written plan document is the touchstone for determining whether a plan formally and operationally satisfies the qualification requirements under section 401(a). It is a qualification requirement to have a written plan document. The legal plan document must provide the terms applicable to participants and beneficiaries to satisfy the “definitely determinable benefit” qualification requirement. The plan sponsor and its service providers must

12. See, e.g., DNA Pro Ventures Inc. v. Commissioner, T.C. Memo. 2015-195. The Tax Court has refused to accept the argument that the size of a plan affects its requirement to comply with all the qualification requirements, even if provisions that violate the qualification requirements never come into effect in operation. Pawlak, T.C. Memo. 1995-7; Christy & Susan Profit Sharing Plan v. Commissioner, T.C. Memo. 2011-62.

13. Reg. section 1.401-1(a)(2). Pawlak, T.C. Memo. 1995-7 (“A plan’s written provisions and operation must meet the statutory requirements under section 401(a) for a plan to be qualified. To be qualified, a plan must initially meet the formal requirements of section 401(a) and continually be amended to comport with subsequent changes to the statutory requirements.”) (internal citation omitted). But see Aero Rental v. Commissioner, 64 T.C. 331 (1975) (holding that section 401(b) was intended merely as a safe harbor and not the exclusive means of adopting a retroactive amendment without which plan amendments are given retroactive effect and by exercising reasonable diligence in filing a determination letter application). In later cases, however, the Tax Court has made it clear that the Aero Rental holding “is not to be expansively construed.” Pawlak, T.C. Memo. 1995-7; see also Bolinger v. Commissioner, 77 T.C. 1353, 1360-1361 (1981); Jack R. Mendenhall Corp. v. Commissioner, 68 T.C. 676, 681-682 (1977); Mills, Mitchell & Turner v. Commissioner, T.C. Memo. 1993-99; D.J. Powers Co. v. Commissioner, T.C. Memo. 1981-62; and Kollipara Rajeshkumar M.D. Inc. v. Commissioner, T.C. Memo. 1992-628.


operate the plan in accordance with the provisions in the plan document.\textsuperscript{16}

For over 70 years, the IRS has issued determination letter rulings to individually designed qualified plans.\textsuperscript{17} A determination letter gave plan sponsors and third parties an IRS ruling on a plan’s continued satisfaction of the tax qualification requirements. Determination letter rulings have served an important role in the qualified plan system. The retirement industry has become accustomed to relying on a plan’s determination letter ruling for assurance that it qualifies for substantial tax preferences. Plan auditors conducting the annual plan audit have relied on determination letters. Purchasers in corporate transactions have relied on determination letters. Third-party service providers, such as investment managers, have relied on determination letters. Banks making lending decisions have relied on determination letters. Determination letters have helped the retirement industry function efficiently by providing assurance to all that the plans are qualified.

Everything changed on June 29, 2016. On that day, the IRS eliminated the determination letter program for individually designed qualified plans.\textsuperscript{18} Only new and terminating plans may request an IRS ruling on their qualified status.\textsuperscript{19} The agency reserved the right to allow existing plans to request a new determination letter in “certain other circumstances.”\textsuperscript{20} Given its budgetary constraints, it is unlikely the IRS will reopen the determination letter program.\textsuperscript{21}

After Rev. Proc. 2016-37, plan sponsors and third parties can continue to rely on a plan’s final determination letter.\textsuperscript{22} None, however, can rely on a plan’s final determination letter for any plan provision that is either modified or affected by a change in law.\textsuperscript{23} Each post-determination-letter plan design change causes provisions in the plan document to lose their reliance on the final determination letter ruling.\textsuperscript{24} And each post-determination qualification requirement change that affects a plan causes provisions in the plan document to lose reliance on the final determination letter ruling.

This is a problem for plan sponsors. Plan sponsors can soon expect third parties to request assurance that their plans continue to satisfy the tax qualification requirements under section 401(a).

Some law firms have announced that they will offer plan sponsors a tax opinion letter to fill the void left by determination letter rulings. Those firms presumably intend to issue tax opinion letters to plan sponsors regarding whether plan provisions modified or affected by a change in law since the final determination letter rulings continue to satisfy the qualification requirements under section 401(a). A tax opinion letter could supplement a plan’s final determination letter ruling. Together, the determination letter and the tax opinion letter could assure third parties (for example, the plan auditor or a party to a corporate transaction) that a plan is tax qualified.

However, a tax opinion letter does not carry the same authoritative weight as a determination letter ruling issued by the IRS. Tax law gives the IRS discretion to determine whether a plan document satisfies the tax qualification requirements, and it grants the IRS enforcement authority. Unfortunately, those who intend to fill the determination letter void by offering an opinion on a plan document’s qualified status are not the IRS. Despite this shortcoming, plan sponsors and third parties in need of assurance could find a tax opinion letter useful.

\textsuperscript{16} Reg. section 1.401-1(b)(3) (“The law is concerned not only with the form of a plan but also with its effects in operation.”). In general, a qualification failure under section 401(a) is a continuing failure because allowing a plan to requalify in subsequent years would be to allow a plan “to rise phoenix-like from the ashes of such disqualification and become qualified for that year.” Pulver Roofing Co. v. Commissioner, 70 T.C. 1001, 1015 (1978); see also Martin Fireproofing, 92 T.C. 1173; and Fleming Cardiovascular PA v. Commissioner, T.C. Memo. 2015-224, at *481.

\textsuperscript{17} Tavannes Watch Co. v. Commissioner, 176 F.2d 211 (2d Cir. 1949), rev’g 10 T.C. 544 (1948); see also Announcement 2015-19, 2015-32 IRB 157, at section III n.1 (providing a history of IRS rulings on a plan’s tax-qualified status).

\textsuperscript{18} Rev. Proc. 2016-37, section 1.01.

\textsuperscript{19} Id.

\textsuperscript{20} Id.

\textsuperscript{21} Id. at section 4.03(3).

\textsuperscript{22} Id. at section 13.

\textsuperscript{23} Id. at section 13.03.

\textsuperscript{24} See id.
The utility of tax opinion letters, and the risks associated with issuing them, depend on properly and timely maintaining and amending the plan document. In the ordinary course of business, plan sponsors modify the design of their plans for business purposes and as required by law. Without the backstop of periodic determination letter rulings, the complexity and risks associated with changes to the plan design and the law increase. Plan sponsors will not have the opportunity to adopt retroactive amendments to cure disqualifying provisions within the 91-day extended remedial amendment period following the issuance of a determination letter ruling. As a result, law firms intending to issue a tax opinion letter must take extraordinary care in timely and compliantly modifying a tax-qualified plan document.

To aid those tasked with this endeavor, the IRS provided extended section 401(b) remedial amendment periods under Rev. Proc. 2016-37 and updated EPCRS under Rev. Proc. 2016-51. The extended remedial amendment periods allow plan sponsors to fix disqualifying provisions by adopting retroactive amendments effective as of the day a change in plan design or the law took effect. When the applicable extended remedial amendment periods end, a plan must have a perfect plan document (that is, a plan without a disqualifying provision). The actions that plan sponsors take during the extended remedial amendment period could affect their legal counsel’s ability to later issue a tax opinion. Once the extended remedial amendment period expires, a plan sponsor suffers the ills of a qualification failure that requires correction under EPCRS or results in IRS sanctions on audit.

III. Principles of Section 401(b)

Section 401(b) and reg. section 1.401(b)-1 provide the principles for applying the remedial amendment system under Rev. Proc. 2016-37. Congress created the first remedial system in 1942. At that time, there were only five requirements under what became section 401(a). In 1974 Congress amended section 401(b) by expanding the relief it provided from only four qualification requirements to all qualification requirements under section 401(a).

A. Statutory Construction

An individually designed plan must comply with the qualification requirements under section 401(a) every day. Section 401(b) provides a grace period during which a plan sponsor may cure a failure to satisfy a qualification requirement under section 401(a) by adopting an amendment during a prescribed remedial amendment period.

Section 401(b) provides:

Certain retroactive changes in plan. A stock bonus, pension, profit-sharing, or annuity plan shall be considered as satisfying the requirements of [section 401(a)] for the period beginning with the date on which it was put into effect, or for the period beginning with the earlier of the date on which there was adopted or put into effect any amendment which caused the plan to fail to satisfy such requirements, and ending with the time prescribed by law for filing the return of the employer for his taxable year in which such plan or amendment was adopted (including extensions thereof) or such later time as the Secretary may designate, if all provisions of the plan which are

27 Revenue Act of 1942, ch. 619, section 162(d), as amended by P.L. 511, section 2 (Dec. 20, 1944); see also 88 Cong. Rec. 7817, 8091 (Oct. 6, 1942); 90 Cong. Rec. 9043 (Dec. 6, 1942); 91 Cong. Rec. 6706 (June 26, 1945); and 555 Inc. v. Commissioner, 15 T.C. 671 (1950).
28 Revenue Act of 1942, ch. 619, section 162(a) (amending section 165(a) of the Revenue Act of 1942, which is now codified as section 401(a)).
29 P.L. 93-406, section 1023 (1974) (amending section 401(b) under Title II of ERISA). See American Bar Association, “Report of the Committee on Employee Benefits,” 24 Tax Law. 921-922 (1970) (recommendation to amend section 401(b) to apply retroactive relief to all qualification requirements under 401(a), as opposed to only four qualification requirements, and to prevent the IRS’s “arbitrary refusal” to allow a retroactive amendment).
30 Reg. section 1.401(b)-1(a); section 401(a) and (b).
31 Crow-Burlingame Co. v. Commissioner, 15 T.C. 738 (1950) (referring to the predecessor to section 401(b) as providing a “grace period”).

necessary to satisfy such requirements are in effect by the end of such period and have been made effective for all purposes for the whole of such period.

The Tax Court has noted that the text of section 401(b) is “highly confusing.” In general, section 401(b) provides relief for “certain retroactive changes” to cure the failure to satisfy the requirements under section 401(a). The statute establishes a period during which a plan sponsor may cure the failure by adopting an amendment that takes retroactive effect. The beginning and end dates of this period are set forth in the statute, and the Treasury secretary has discretion to extend the period for curing the failure. A retroactive amendment must put in the plan by the end of the period all provisions necessary to cure the failure, and it must make those provisions effective for the entire period.

As a general principle, if a plan is eligible for section 401(b) relief and the plan sponsor satisfies the conditions necessary for relief, the statute mandates that the plan be considered as satisfying the requirements of section 401(a). This is true regardless of whether the qualification requirement concerns the form or operation of the plan.

Section 401(b) does not distinguish between different types of qualification requirements. For example, the statute does not state that the IRS will treat a plan as satisfying the qualification requirements under section 401(a) for formal plan document compliance but not for operational compliance. The statute states that a plan that fulfills the conditions under section 401(b) “shall be considered as satisfying the requirements” of section 401(a).

B. Reg. Section 1.401(b)-1

Reg. section 1.401(b)-1 interprets the relief available to plan sponsors under section 401(b). The regulations state that a qualified plan that does not satisfy the requirements of section 401(a) on any day solely as a result of a disqualifying provision will be considered to have satisfied those requirements on that date if, on or before the last day of the remedial amendment period for that disqualifying provision, all plan provisions necessary to satisfy all requirements of section 401(a) are in effect and have been made effective for all purposes for the whole of that period.

The regulation identifies the situations to which section 401(b) applies. Section 401(b) applies only when a plan does not satisfy the requirements of section 401(a) on any day “solely as a result of a disqualifying provision.” Reg. section 1.401(b)-1(b) defines what causes a disqualifying provision. As explained below, it is the X factor.

For section 401(b) to apply to a particular situation:

- X must cause a disqualifying provision; and
- The disqualifying provision must cause a failure to satisfy a requirement under section 401(a).

Even if section 401(b) applies to a particular situation, a plan sponsor can attain section 401(b) relief only by satisfying three conditions under section 401(b) and reg. section 1.401(b)-1(a):

See also ABA, supra note 29, at 921-922.
1. the plan sponsor must adopt an amendment to cure the failure to satisfy section 401(a) caused solely by the disqualifying provision;

2. the amendment must cause the plan to have all provisions necessary to cure that failure in effect before the end of the applicable remedial amendment period; and

3. the amendment must cause the plan to have all provisions necessary to satisfy section 401(a) made effective from the first day of the applicable remedial amendment period to the last day of the applicable remedial amendment period.

Section 401(b) relief, however, may be subject to additional limits in some cases. Reg. section 1.401(b)-1(a) offers guidance on when section 401(b) relief is not available:

Under some facts and circumstances, it may not be possible to amend a plan retroactively so that all provisions of the plan which are necessary to satisfy the requirements of section 401(a) are in fact made effective for the whole remedial amendment period. If it is not possible, the requirements of [section 401(a)] will not be satisfied even if the employer adopts a retroactive plan amendment which, in form, appears to satisfy such requirements.

The limitation set forth in the regulation is, unfortunately, vague. It tells us that relief may be unavailable under “some facts and circumstances.” It goes on to let us know that when those facts and circumstances are present, it may be impossible to cure a disqualifying provision for the whole remedial amendment period by adopting a retroactive amendment. Finally, it tells us that if it is impossible to cure a disqualifying provision for the entire remedial amendment period, the plan will fail to satisfy the qualification requirements under section 401(a).

In other words, section 401(b) relief is unavailable to a plan sponsor when a retroactive amendment cannot take effect for the entire remedial amendment period without causing a failure to satisfy a qualification requirement under section 401(a). For example, section 401(b) is generally unavailable when a retroactive amendment would cause the plan to violate the anti-cutback rule under section 411(d)(6) unless the IRS authorizes it. 42

1. Disqualifying provisions.

The first step in applying section 401(b) is to determine whether there is a disqualifying provision. Reg. section 1.401(b)-1(b) provides the general standards for what causes a disqualifying provision. For purposes of Rev. Proc. 2016-37 and the analysis in Section IV of this report, two types of disqualifying provisions are particularly important. The first is a disqualifying provision caused by a discretionary amendment under reg. section 1.401(b)-1(b)(1). The second is a disqualifying provision caused by a legally mandated qualification requirement change designated by the IRS under reg. section 1.401(b)-1(b)(3). These two disqualifying provisions have a different X factor.


Under reg. section 1.401(b)-1(b)(1), a disqualifying provision includes an amendment to an existing plan that causes the plan to fail to satisfy the code requirements applicable to qualification of the plan as of the date the amendment is first made effective. This type of disqualifying provision results from a plan sponsor implementing a discretionary plan design change, including a modification for an optional change in law. A discretionary plan design change generally causes a qualification defect because the plan is not operated in accordance with its terms when the change takes effect. Section 401(b) allows a plan sponsor to cure the defect by adopting a retroactive amendment.

A discretionary amendment can cause a disqualifying provision. However, the mere fact that a plan sponsor adopts a discretionary amendment does not result in a disqualifying

41 Rev. Proc. 2016-51, section 4.05(1).
43 Rajsheker, T.C. Memo. 1992-628.
provision. A disqualifying provision arises when a discretionary amendment causes a plan provision to fail to satisfy the requirements of section 401(a). A retroactive amendment can cause a disqualifying provision if, when an amendment is adopted, plan administration does not align with the modified provisions in the plan document.

This can occur in many ways.\textsuperscript{44} A discretionary amendment can cause a disqualifying provision when the plan terms as amended violate a qualification requirement. A discretionary amendment can cause a disqualifying provision when past, current, or prospective plan administration does not conform to the modified terms of the plan document. A discretionary amendment results in a disqualifying provision whenever an amendment causes a plan to fail to satisfy any qualification requirement as of the date it first takes effect.

**Example 1:**

1. The plan sponsor makes a discretionary plan design change that takes administrative effect on January 1, 2018. On August 15, 2018, the plan sponsor adopts a discretionary amendment effective as of January 1, 2018, to modify the terms of the plan document for the plan design change that took administrative effect on January 1, 2018.

2. On February 3, 2019, the plan sponsor discovers that a provision in the amendment adopted on August 15, 2018, which was effective as of January 1, 2018, does not satisfy a qualification requirement in form. The August 15, 2018, discretionary amendment caused a disqualifying provision effective as of January 1, 2018.

3. The plan sponsor may adopt an amendment on or before the end of the applicable remedial amendment period to cure the disqualifying provision caused by the August 15, 2018, amendment effective as of January 1, 2018.\textsuperscript{45}

**Example 2:**

1. The plan sponsor makes a discretionary plan design change that takes administrative effect on January 1, 2018. On September 12, 2018, the plan sponsor adopts a discretionary amendment effective as of January 1, 2018, to modify the terms of the plan document for the plan design change that took effect on January 1, 2018.

2. On October 23, 2019, the plan sponsor discovers that the amendment adopted on September 12, 2018, which was effective as of January 1, 2018, does not reflect plan administration effective as of May 1, 2018, and thus does not satisfy a qualification requirement. This resulted from a prospective change, effective May 1, 2018, in how the plan administered the design change that took effect on January 1, 2018.

   The plan properly administered the design change in accordance with the September 12, 2018, amendment from January 1, 2018, to April 30, 2018. The September 12, 2018, amendment, however, caused a disqualifying provision effective as of May 1, 2018.

3. The plan sponsor may adopt an amendment on or before the end of the applicable remedial amendment period to cure the disqualifying provision caused by the September 12, 2018, amendment effective as of March 1, 2018.

**Example 3:**

1. The plan sponsor adopts a discretionary amendment on January 17, 2018, to modify the terms of the plan document for a plan design change that will take effect on March 1, 2018.

2. On March 1, 2018, the plan design change takes administrative effect but

\textsuperscript{44} See Commissioner v. Produce Reporter Co., 207 F.2d 586, 587 (7th Cir. 1953), aff’g 18 T.C. 69 (1952).

\textsuperscript{45} IRS field service directive, supra note 15.
does not conform to the terms of the plan document as modified by the January 17, 2018, amendment that took effect on March 1, 2018. The plan does not satisfy a qualification requirement effective March 1, 2018. The January 17, 2018, amendment caused a disqualifying provision.

3. The plan sponsor may adopt an amendment on or before the end of the applicable remedial amendment period to cure the disqualifying provision caused by the January 17, 2018, amendment effective as of March 1, 2018.


A disqualifying provision under reg. section 1.401(b)-1(b)(3) includes the presence or absence of a plan provision the IRS in its discretion designates as a disqualifying provision that results in the failure to satisfy the qualification requirements because of a change in those requirements or that is “integral to a qualification requirement . . . that has been changed.”

The IRS must exercise discretion and identify a provision as a disqualifying provision for there to, in fact, be a disqualifying provision under reg. section 1.401(b)-1(b)(3).

Unlike a reg. section 1.401(b)-1(b)(1) disqualifying provision, a reg. section 1.401(b)-1(b)(3) disqualifying provision is not caused by the plan sponsor adopting an amendment. A reg. section 1.401(b)-1(b)(3) disqualifying provision is caused by a legally required qualification requirement change that applies to a plan.

A change to the qualification requirements that apply to a plan necessitates a change in plan administration. On the day a qualification requirement change takes effect, a plan to which it applies must change plan administrative practices to comply with the law. Not changing plan administration to comply with a legally required change in law results in a failure to satisfy the qualification requirements. Similarly, a plan document that is not modified effective as of the date a qualification requirement change takes effect has a disqualifying provision.

A retroactive amendment cures the disqualifying provision. Plan administration must comply with the change in law on the day the change in law takes effect. Similarly, plan administration must comply with any subsequent IRS guidance concerning the change in law, even if the guidance itself is not retroactive to the date the law change took originally took effect. The plan sponsor must cure any disqualifying provision caused by a qualification requirement change within the applicable remedial amendment period.

Section IV.C.2 of this report discusses the disqualifying provisions under reg. section 1.401(b)-1(b)(3) designated by the IRS in Rev. Proc. 2016-37.

Example 4:

1. On February 3, 2018, section 101 of the Tax Reform Act, which modifies an existing qualification requirement, takes effect. This qualification requirement change is legally required for the plan sponsor’s plan. After months of interpreting and analyzing TRA section 101, the plan sponsor modifies plan administration effective February 3, 2018, to comply with that new law. TRA section 101 causes the plan to have a disqualifying provision effective February 3, 2018.

2. On December 26, 2018, the IRS publishes guidance in the Internal Revenue Bulletin regarding TRA section 101 that takes prospective effect on June 13, 2019. The IRS’s guidance differs from how the plan administered TRA section 101 effective February 3, 2018. On June 13, 2019, plan administration prospectively changes to comply with the IRS guidance.

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46 Reg. section 1.401(b)-1(b)(3) and (c)(1). See Stepanowski v. Commissioner, 456 F.3d 520, 526 (3d Cir. 2006); aff’d 124 T.C. 198 (2005); and Rajshuker, T.C. Memo. 1992-628 (explaining that the secretary had not exercised discretion under reg. section 1.401(b)-1(b)(3) to designate “a plan’s failure to comply with changes promulgated by [the Deficit Reduction Act of 1984 and the Retirement Equity Act of 1984] as a disqualifying provision”).

47 Hollen, T.C. Memo. 2011-2 (The employee stock ownership plan “is therefore not qualified under section 401(a) because the required provisions failed to be effective for the whole of the remedial amendment period.”).

3. The plan sponsor may adopt an amendment on or before the end of the applicable remedial amendment period to cure the disqualifying provision caused by TRA section 101. The amendment must conform the plan terms to plan administration effective on and after February 3, 2018, and on or before June 12, 2019, and effective on and after June 13, 2019.

Example 5:

1. On February 3, 2018, TRA section 1064, which modifies an existing qualification requirement, takes effect. That section sets minimum standards that plans must meet; however, plans may satisfy this requirement by exceeding the minimum standards. The qualification requirement change is legally required for the plan sponsor’s plan. The plan sponsor modifies plan administration effective February 3, 2018, to comply with TRA section 1064. Administratively, the plan exceeds the minimum standards of TRA section 1064. TRA section 1064 causes the plan to have a disqualifying provision effective February 3, 2018.

2. On June 12, 2018, the IRS publishes guidance in the Internal Revenue Bulletin regarding TRA section 1064 that takes immediate effect. The guidance does not affect how the plan has administered TRA section 1064 since February 3, 2018.

3. The plan sponsor may adopt an amendment on or before the end of the applicable remedial amendment period to cure the disqualifying provision caused by TRA section 1064. The amendment must conform the plan terms to plan administration effective February 3, 2018.

2. Remedial amendment periods.

The second step in applying section 401(b) is to identify the remedial amendment period. Reg. section 1.401(b)-1 gives the IRS broad discretion to extend the remedial amendment period for curing a disqualifying provision. Section IV of this report examines the extended remedial amendment periods under Rev. Proc. 2016-37 for curing a disqualifying provision caused by a discretionary amendment and for curing a disqualifying provision caused by a qualification requirement change.

IV. Remedial Amendment System

Rev. Proc. 2016-37 clarified, modified, and superseded Rev. Proc. 2007-44. Under Rev. Proc. 2016-37, the IRS exercised discretion under section 401(b) and reg. section 1.401(b)-1 to extend the remedial amendment period and to designate disqualifying provisions.

Rev. Proc. 2016-37 establishes extended remedial amendment periods, including a transitional remedial amendment period extension. The transition relief applies to a disqualifying provision with an open remedial amendment period under Rev. Proc. 2007-44 as of December 31, 2016. Without the extended remedial amendment period transition relief, a disqualifying provision that had an open remedial amendment period under Rev. Proc. 2007-44 would end on December 31, 2016. The transition relief extends the remedial amendment period until December 31, 2017. On or before December 31, 2017, plan sponsors must adopt all retroactive corrective amendments for any disqualifying provision with an open remedial amendment period under Rev. Proc. 2007-44 as of December 31, 2016. On or before December 31, 2017, the plan sponsor should adopt a retroactive amendment to cure any disqualifying provision subject to the extended remedial amendment period transition rule.

Separate from the transition rule, the IRS designated specific provisions as disqualifying provisions and established extended remedial amendment periods.
amendment periods and amendment deadlines. The new rules apply to disqualifying provisions that are first effective on or after January 1, 2016. To help preserve tax-qualified status in the wake of the elimination of the determination letter program, the IRS plans to issue an annual required amendment list and a periodically updated operational compliance list.  

**A. This Bird Has Flown**

Before January 1, 2017, Rev. Proc. 2007-44 supplied rules for curing disqualifying provisions during the remedial amendment period under section 401(b). The extended remedial amendment period thereunder did not expire until the end of the applicable five-year remedial amendment cycle for requesting a determination letter. By requesting a determination letter, a plan sponsor could further extend its remedial amendment period to the 91st day after the IRS issued a determination letter ruling. The extended period allowed plan sponsors to adopt retroactive amendments to cure a disqualifying provision with IRS approval. The IRS conditioned the extended remedial amendment period on the prior adoption of a timely interim amendment, which generally required plans to adopt retroactive amendments by a specified deadline that occurred during the remedial amendment period. During the determination letter review process, the plan sponsor could submit proposed amendments to the IRS, at the agency’s request, for adoption after the IRS issued the determination letter. The plan sponsor had to adopt the proposed retroactive amendments before the end of the 91-day remedial amendment period extension. Timely adoption of the retroactive amendments was a condition for relying on the determination letter ruling.

A plan’s determination letter also specified the scope of the IRS’s review of the plan as amended. Each year the IRS published a cumulative list of required qualification requirement changes, which included optional changes in law. Before each determination letter filing cycle opened, the IRS specified which year’s cumulative list it would use to review the plan document in connection with a ruling request. When the IRS ultimately issued a plan’s determination letter ruling, the letter stated which year’s cumulative list the agency reviewed the terms of the plan document against.

A determination letter ruling effectively ended one remedial amendment period and started a new one. The IRS ended the remedial amendment period for potential disqualifying provisions that became subject to the determination letter ruling. Subsequent changes in design and law became subject to a new extended remedial amendment that coincided with the new five-year determination letter filing cycle.

**B. Transition Rule**

Rev. Proc. 2016-37 eliminated interim amendments, the five-year remedial amendment cycle, and periodic determination letters for individually designed plans as provided under Rev. Proc. 2007-44. Plan sponsors and third parties can rely on a plan’s final determination letter only with respect to the plan terms reviewed by the IRS. They cannot rely on a final determination letter for any changes first included in a cumulative list that was published after the cumulative list that the IRS referenced in the final determination letter. Nor can they rely on a final determination letter for any provision modified or affected by a change in law that has an open remedial amendment period as of December 31, 2016 under Rev. Proc. 2007-44.

Any law changes listed on the 2016 required amendment list, which is discussed in Section

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56. Id. at sections 3.01(9) and (10).
57. Rev. Proc. 2007-44, section 5.03.
58. Id. at section 7.
59. Section 401(b)(1)(c)(1), K.H. Co. LLC Employee Stock Ownership Plan v. Commissioner, T.C. Memo. 2014-31 (discussing the 91-day remedial amendment period extension). The table at the end of Section IV of this report provides additional information on the remedial amendment cycle applicable to a plan.
61. Rev. Proc. 2016-37, sections 1.05 and 3.
62. Id. at section 6. A plan must have adopted a timely interim amendment for a disqualifying provision caused by a qualification requirement in order for the extended remedial amendment period transition rule to apply. Id. at section 11, Example 7.
IV.D.2 of this report, are not subject to the extended remedial amendment period transition rule. They are subject to the new rule discussed in Section IV.C.1 of this report.

Before the transition period expires on December 31, 2017, plan sponsors should have their qualified plans reviewed for compliance with the cumulative lists not covered by the final determination letter ruling, and any modifications not subject to the final determination letter. This could provide an opportunity to cure a disqualifying provision on or before December 31, 2017, identified by the IRS in connection with an ongoing plan audit. Although plan sponsors’ third parties will be unable to gain determination letter ruling reliance for any provisions subject to the extended remedial amendment period transition relief, they could procure assurance from others willing to provide it in the form of a tax opinion letter.

The transition relief is particularly important to plan sponsors and those who intend to issue tax opinion letters. The first audit for which a plan sponsor can reasonably expect a plan auditor to request assurance that a plan continues to satisfy the tax qualification requirements in form will occur in 2018 for the 2017 plan year Form 5500, “Annual Return/Report of Employee Benefit Plan.”

Example 6:

1. The last digit of the plan sponsor’s employer identification number is 2. The plan sponsor maintains a plan assigned to Cycle B under Rev. Proc. 2007-44. During the second Cycle B, the plan sponsor filed a determination letter application on January 31, 2012, and included the plan as amended and restated effective January 1, 2012, as well as four amendments adopted before the restatement. The IRS will review the plan and amendments for compliance with the 2011 cumulative list of required changes.

2. On August 15, 2013, the plan received a determination letter ruling. The determination letter ruling references the plan restatement and four prior amendments, the 2011 cumulative list of required changes, and an expiration date.

The IRS did not condition the determination letter on the adoption of a proposed amendment.

3. On February 2, 2015, the plan sponsor adopted an amendment to merge in a plan acquired in an acquisition. On June 15, 2015, the plan sponsor adopted an amendment to add a Roth contribution feature.

4. On January 4, 2016, the IRS announced in Notice 2016-3, 2016-3 IRB 278, that expiration dates on determination letters issued before January 4, 2016, are no longer operative. The plan’s August 15, 2013, determination letter is no longer subject to an expiration date.

5. On July 21, 2015, the IRS announced the elimination of the five-year determination letter remedial amendment cycle. The plan cannot request a new determination letter ruling. The plan sponsor and third parties can rely on the determination letter only regarding the provisions reviewed by the IRS and the law changes listed in the 2011 cumulative list. None may rely on the plan’s August 15, 2013, determination letter for law changes added to the 2012, 2013, 2014, and 2015 cumulative lists.

6. During 2017 the plan sponsor reviews the plan document to determine whether any amendments require a section 401(b) curative amendment before the extended remedial amendment period ends on December 31, 2017. The review includes the changes in law listed in the 2012, 2013, 2014, and 2015 cumulative lists, any modified plan provision for which a timely interim amendment was adopted that has an open remedial amendment period, any plan provisions modified since the determination letter ruling request, and administrative changes since the determination letter.
7. Legal counsel responsible for the transition review discovered several disqualifying provisions. On December 28, 2017, the plan sponsor adopts a retroactive plan amendment to cure them.

8. On January 1, 2018, the extended remedial amendment period under the transition relief closed (that is, the plan sponsor can no longer cure a defect under section 401(b)).

9. On August 15, 2018, the plan auditor asks the plan sponsor for assurance that the plan, as amended on February 2, 2015, June 15, 2015, and December 28, 2017, continues to satisfy the qualification requirements under section 401(a).

The table at the end of Section IV of this report describes key features of the five-year determination letter remedial amendment cycle under Rev. Proc. 2007-44. The table includes each cumulative list of required changes a plan sponsor, based on its plan’s prior determination letter filing cycle, should include in the extended remedial amendment period transition review.

C. New Rule

Effective January 1, 2016, the IRS designated disqualifying provisions and established extended remedial amendment periods and amendment deadlines for individually designed qualified plans with a determination letter. The Cycle B plan in Example 6 is thus subject to two different extended remedial amendment periods: the transition and new extended remedial amendment periods.

Id. at sections 2.01, 2.08, 3.01, 5.01, 5.02, 5.03, 5.04, and 5.05.
Plan sponsors must classify each plan provision modified or affected by a change in law to determine which type of disqualifying provision could arise. Classification is necessary to determine the applicable amendment deadline and the end of the extended remedial amendment period under Rev. Proc. 2016-37. Classification also affects the procedure for curing a disqualifying provision under section 401(b) within the extended remedial amendment period.

1. Reg. section 1.401(b)-1(b)(3) disqualifying provision caused by a qualification requirement change.

The IRS exercised its authority under reg. section 1.401(b)-1(b)(3) to designate a provision in a plan as a disqualifying provision if its presence in or absence from the plan document (1) results in the plan’s failure to satisfy the code’s qualification requirements because of a change in those requirements that is effective after December 31, 2001, or (2) is integral to that disqualifying provision. A change in qualification requirements, for this purpose, includes a statutory change or a regulatory change or other guidance published in the Internal Revenue Bulletin.

The amendment deadline and last day of the remedial amendment period occur on the same day. The IRS extended the remedial amendment period to the end of the second calendar year that begins after the IRS adds a legally required qualification requirement change to the required amendment list. This is also the deadline for adopting a timely plan amendment. A statute, regulation, or other guidance can change the amendment deadline and extended remedial amendment period for a particular change in law.

2. Reg. section 1.401(b)-1(b)(1) disqualifying provision caused by a discretionary amendment.

Under reg. section 1.401(b)-1(b)(1), a plan sponsor causes a disqualifying provision by adopting a discretionary amendment that does not satisfy the qualification requirements. Adopting a discretionary amendment does not cause a disqualifying provision if it complies with the qualification requirements.

The default amendment deadline for an individually designed plan is the end of the plan year in which the plan sponsor operationally puts the plan amendment into effect. For purposes of determining the amendment deadline, a change is operationally put into effect when the plan is administered in a manner consistent with the intended plan amendment (rather than existing plan terms). The IRS provides two illustrative examples. First, the deadline for adopting a discretionary amendment for a calendar-year plan that increases participants’ accrued benefits is operationally put into effect during 2018 is December 31, 2018. Second, the deadline for adopting a discretionary amendment for a calendar-year plan that is operationally put into effect during 2018 to provide a new right or benefit as of January 1, 2011, for participants with same-sex spouses is December 31, 2018.

The deadline for timely adopting a retroactive amendment for a disqualifying provision that

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64 Id. at section 5.03(1), n.1 ("As provided in section 5.01 of Rev. Proc. 2007-44, December 31, 2001, was the date after which all changes in qualification requirements were designated as disqualifying provisions by the [commissioner] in order for those changes to be eligible for the remedial amendment period available with respect to disqualifying provisions.").
65 Id. at sections 5.02, 5.03, and 5.04; Stepnowski, 456 F.3d at 326 (interpreting “integral to” as the term is used in reg. section 1.401(b)-1).
67 Id. at section 8.01.
68 Id. at section 5.05(3).
69 Id. at section 8.01.
70 Id. at section 5.03(1), n.1 ("As provided in section 5.01 of Rev. Proc. 2007-44, December 31, 2001, was the date after which all changes in qualification requirements were designated as disqualifying provisions by the [commissioner] in order for those changes to be eligible for the remedial amendment period available with respect to disqualifying provisions.").
71 Id. at section 5.02. In general, discretionary amendments are any type of change to the plan that is not legally required. Id. at section 5.05(2).
72 Id. at sections 5.02, 8.02.
73 Id. at section 8.02(1). A different amendment deadline applies to an individually designed governmental plan under section 414(d): the later of the end of the plan year in which the plan amendment is operationally put into effect or 90 days after the close of the second regular legislative session of the legislative body with the authority to amend the plan that begins on or after the date the plan amendment is operationally put into effect. Id. at section 8.02(2).
74 Id. at section 8.02(1).
causes a discretionary amendment is the end of the extended remedial amendment period.\textsuperscript{75} The IRS extended the remedial amendment period to the end of the second calendar year following the calendar year in which the amendment is adopted or effective, whichever is later.\textsuperscript{76} A plan sponsor generally may cure a disqualifying provision caused by a discretionary amendment by adopting a second retroactive amendment (or, if necessary, a third, fourth, etc.) during the extended remedial amendment period.

The amendment deadline or extended remedial amendment period for a particular type of design change might be altered by statute or in regulations or other guidance. For example, the IRS could designate a different extended remedial amendment period date for an optional law change.

D. IRS Lists

The IRS will issue two new lists to help preserve an individually designed plan’s tax-qualified status in form and operation: the required amendment list and the operational compliance list.\textsuperscript{77}

1. Operational compliance list for legally required qualification requirement changes and optional changes.

A plan must administratively comply with a qualification requirement change on the date the change becomes effective.\textsuperscript{78} To add plan sponsors and practitioners, the IRS plans to periodically update the operational compliance list on its website.\textsuperscript{79} The operational compliance list will include legally required qualification requirement changes and optional law changes. The IRS does not intend for the operational compliance list to be a comprehensive list of every item of IRS guidance or new legislation for a year that could affect a particular plan. Plan sponsors must comply with all laws and qualification requirements, even if a qualification requirement change does not appear on, or is not timely added to, the operational compliance list. Each time the IRS updates the operational compliance list, an analysis is necessary to determine whether a provision applies to a particular plan’s design.

The operational compliance list should be only one part of plan compliance reviews. Continued monitoring of changes in law is necessary, and plan sponsors must monitor plan design and administrative changes.

2. Required amendment list for legally required qualification requirement changes.

The IRS intends to publish a required amendment list in the Internal Revenue Bulletin annually.\textsuperscript{80} The required amendment list includes only those qualification requirement changes that a plan must adopt to maintain its qualified status.\textsuperscript{81} These are legally required amendments for a qualification requirement change, not optional law changes.

In general, the annual required amendment list includes a qualification requirement only after the IRS publishes regulations or other guidance in the Internal Revenue Bulletin.\textsuperscript{82} The IRS, however, retains discretion to include an item on the required amendment list in other circumstances. For example, the IRS may include a qualification requirement change on the required amendment list when it does not anticipate issuing guidance regarding a newly enacted statute.\textsuperscript{83}

Example 7:

1. Enacted July 1, 2017, TRA section 101, a legally required qualification requirement change, becomes effective August 15, 2017. On July 18, 2017, the IRS adds TRA section 101 to the operational compliance list. The plan sponsor determines that TRA section 101 applies to its plan after analyzing the updated operational compliance list and the plan design and terms. On August 15, 2017, TRA section 101 is operationally put into effect by the

\textsuperscript{75} Id. at section 8.01.
\textsuperscript{76} Id. at section 5.05(3).
\textsuperscript{77} Id. at sections 9, 10.
\textsuperscript{78} Id. at section 10.
\textsuperscript{79} Id.
\textsuperscript{80} Id. at section 9. The IRS published the 2016 required amendment list as Notice 2016-80, 2016-52 IRB 918.
\textsuperscript{81} Rev. Proc. 2016-37, section 9.
\textsuperscript{82} Id.
\textsuperscript{83} Id.
plan sponsor following several weeks of designing new administrative practices. The plan has a disqualifying provision as of August 15, 2017.

2. On February 3, 2018, the IRS publishes guidance in the Internal Revenue Bulletin for TRA section 101 that takes immediate effect. After analyzing the IRS’s guidance, the plan sponsor modifies the plan administration of TRA section 101 to comply with the guidance, retroactively effective as of February 3, 2018. The plan has a disqualifying provision as of August 15, 2017, with an administrative change effective February 3, 2018, that will require compliant plan terms reflective of the change required by the guidance. The plan has a disqualifying provision.

3. In November 2018 the IRS adds TRA section 101 to the 2018 required amendment list. The extended remedial amendment period for TRA section 101 ends on December 31, 2020. The plan continues to have a disqualifying provision.

4. In December 2019 a legally required plan amendment is designed and adopted to reflect the administration of TRA section 101 as of August 15, 2018. The retroactive amendment includes a provision effective on August 15, 2017, and before September 3, 2018, and a provision effective on and after September 3, 2018. The retroactive amendment corrects the disqualifying provision that resulted from TRA section 101.

V. Curative and Corrective Relief

Both section 401(b) and EPCRS are important for preserving a plan’s tax-qualified status. Section 401(b) cures and EPCRS corrections are available for different purposes and at different times. Any action taken under section 401(b) or EPCRS cannot violate another qualification requirement, such as section 411(d)(6).

A. Mutual Exclusivity

Plan sponsors cannot use EPCRS when section 401(b) is available. Rev. Proc. 2016-51, section 6.08, states:

Correction under statute or regulations. Generally, none of the correction programs are available to correct failures that can be corrected under the Code and related regulations. For example, as a general rule, a Plan Document Failure that is a disqualifying provision for which the remedial amendment period under section 401(b) has not expired can be corrected under provisions of the Code through retroactive remedial amendment.

Section 401(b) and EPCRS are available at different times:

• section 401(b) is available during the applicable remedial amendment period; and
• EPCRS correction programs are available after the applicable remedial amendment period ends and during the applicable remedial amendment period if section 401(b) is unavailable.

Section 401(b) allows a plan sponsor to cure a disqualifying provision within the applicable remedial amendment period so that it does not become a qualification failure. After the applicable remedial amendment period or if section 401(b) is unavailable, the IRS permits the plan sponsor to correct qualification failures under EPCRS. In those cases, plan sponsors may use EPCRS’s three correction programs: the self-correction program, the voluntary correction program, or audit CAP. The type of qualification failure and the time at which a plan sponsor attempts to correct it determine which of the three programs is available.

As discussed in Section V.B of this report, EPCRS illustrates this principle with an example in section 6.08 of Rev. Proc. 2016-51 and under the definitions

84 As defined in Rev. Proc. 2016-51, section 5.01(2).
for operational failure and plan document failure. The IRS states, as an example, that a plan document failure that could be cured under section 401(b) cannot be corrected under EPCRS. This principle applies to an operational failure as well.

B. EPCRS

The IRS allows plan sponsors to correct qualification failures under EPCRS. Effective January 1, 2017, Rev. Proc. 2016-51 defines a qualification failure as “any failure that adversely affects the qualification of a plan,” and it enumerates several types of failures, including plan document failures and operational failures. The EPCRS-defined terms “plan document failure” and “operational failure” work in concert with the prohibition against using the correction programs if section 401(b) curative relief is available. When section 401(b) relief is unavailable, these definitions provide the standard for diagnosing the type of qualification failure and determining which of the correction programs a plan sponsor may use to correct it.

As a rule, the IRS allows a plan sponsor to correct an operational failure under the self-correction program, the voluntary correction program, and audit CAP, as applicable. A plan sponsor may correct plan document failures under the voluntary correction program or audit CAP. An analysis of what constitutes a plan document failure and an operational failure sets boundaries for a plan sponsor’s use of the EPCRS correction programs.


For purposes of EPCRS, a plan document failure is a “plan provision (or the absence of a plan provision) that, on its face, violates the requirements of section 401(a).” This includes “any qualification failure that is a violation of the requirements of section 401(a) . . . and that is not an Operational Failure.” In general, this is the textbook example of a plan document with (or without) a provision that violates section 401(a).

EPCRS identifies a non-amender failure as a type of plan document failure. A non-amender failure is the failure to cure a “disqualifying provision described in section 1.401(b)-1(b) within the remedial amendment period.” This includes a disqualifying provision caused by a discretionary amendment or qualification requirement change. A discretionary amendment adopted in the year a change is put into effect is not a disqualifying provision if it satisfies the qualification requirements. A discretionary amendment that satisfies the qualification requirements does not result in a plan document

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85 As defined in Rev. Proc. 2016-51, section 5.01(2)(b).
86 As defined in Rev. Proc. 2016-51, section 5.01(2)(a).
87 Rev. Proc. 2016-51, section 6.08. Neither section 401(b) nor the regulations discriminate between types of failures. See section 401(b); and reg. section 1.401(b)-1.
88 Rev. Proc. 2016-51, sections 1.01, 4.01, and 6.08.
89 Id. at section 5.01(2). Demographic failures and employer eligibility failures are also considered qualification failures under EPCRS. They are not essential to the analysis herein because neither definition references section 401(b) or disqualifying provisions. Id. at section 5.01(2)(c) and (d).
90 For example, a qualification failure that is an operational failure cannot be a plan document failure. Id. at section 5.01(2)(a)(i).
91 In three limited situations, however, EPCRS allows a plan sponsor to adopt a retroactive amendment to correct a failure. Id. at Appendix B, section 2.07. Those situations involve failures that could cause a violation of section 411(d)(6) or harm participants through a quasi-cutback.
92 Id. at section 4.01(1), (2), and (3).
93 Id. at section 4.01(2) and (3).
94 Regardless of whether a plan sponsor should use section 401(b) or EPCRS in a particular situation, a section 401(b) cure or EPCRS correction method should not violate another qualification requirement, including section 411(d)(6).
95 Rev. Proc. 2016-51, section 5.01(2)(a)(i).
96 Id.
97 Id. at section 5.01(2)(a)(ii)(C). EPCRS also cites the failure to adopt a good-faith amendment or an interim amendment as plan document failures. Id. at section 5.01(2)(a)(i), (ii)(A), and (ii)(B). Rev. Proc. 2016-37 eliminated interim amendments for individually designed plans effective January 1, 2017. Rev. Proc. 2016-37, sections 3.01(1) and 4.02; Rev. Proc. 2016-51, section 5.01(2)(a)(i) and (ii)(B).
98 Rev. Proc. 2016-51, section 5.01(2)(a)(i) and (ii)(C) (emphasis added).
99 Id. See discussion in Section III.
100 In other words, not adopting a discretionary amendment by the end of the plan year in which the plan amendment is operationally put into effect does not result in a plan document failure under EPCRS. Rev. Proc. 2016-51, section 5.02(2)(a)(i) (referencing section 8.02 of Rev. Proc. 2016-37 and section 5.05(2) of Rev. Proc. 2007-44); Rev. Proc. 2016-37, section 8.02(1). A plan document failure results from failing to adopt an amendment that corrects a disqualifying provision within the applicable remedial amendment period. Rev. Proc. 2016-37, sections 5.05(2) and 8.01(2); Rev. Proc. 2016-51, section 5.01(2)(a).

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failure for purposes of EPCRS. Section V.B.2 of this report explains that a discretionary amendment that is not timely adopted is an operational failure, not a plan document failure.

a. Plan document failure resulting from a disqualifying provision caused by a discretionary amendment.

Whether a plan document failure occurs under EPCRS is a question of causation and timing. Under EPCRS, a plan document failure occurs if a plan sponsor does not cure a disqualifying provision caused by a discretionary amendment during the remedial amendment period. A plan sponsor can use EPCRS to fix this type of plan document failure. A sponsor cannot use EPCRS to correct a discretionary amendment that did not cause a disqualifying provision because no plan document failure occurred.

In general, two issues require analysis before one can conclude that a plan document failure exists and can be corrected under EPCRS. The first inquiry is whether a discretionary amendment caused a disqualifying provision under reg. section 1.401(b)-1(b)(1). The second inquiry, which is necessary only if a discretionary amendment caused a disqualifying provision, is whether the plan sponsor may cure the disqualifying provision under section 401(b). EPCRS is available only if section 401(b) is unavailable to cure the disqualifying provision. If a plan sponsor could cure a disqualifying provision under section 401(b), a retroactive amendment should be adopted during the extended remedial amendment period to avoid a plan document failure that must be corrected under EPCRS.

EPCRS is expensive for plan sponsors (as well as the IRS). A plan document failure corrected under EPCRS requires a costly voluntary correction program filing fee or monetary sanctions imposed by the IRS under audit CAP.

The failure to cure the disqualifying provision during the remedial amendment period causes either a plan document failure or operational failure under EPCRS, as determined by what caused the disqualifying provision. There are other expenses (including time) incurred under the voluntary correction program and audit CAP.

b. Plan document failures resulting from a disqualifying provision caused by legally required qualification requirement change.

A plan document failure resulting from a disqualifying provision caused by a qualification requirement change is similar to a disqualifying provision caused by a discretionary amendment. The main difference between these disqualifying provisions is the cause — the X factor. A disqualifying provision caused by a legally required qualification requirement change first occurs when the change in law takes effect. A plan sponsor’s action is irrelevant.

2. Operational failures.

Under EPCRS, a qualification failure cannot be a plan document failure if it is an operational failure. An operational failure is “a Qualification Failure . . . that arises solely from the failure to follow plan provisions.” The word “solely” in the definition is important. It illustrates the distinction between plan document and operational failures under EPCRS.

The textbook case of an operational failure is the failure to adopt a timely discretionary amendment (that is, plan not amended) that “arises solely from the failure to follow plan provisions” and is treated as an operational failure by Rev. Proc. 2016-51. The situation occurs when those in charge of administering the plan intentionally or unintentionally fail to follow the terms of the legal plan document (maintained for purposes of complying with the tax-qualification requirements and Title I of ERISA). The failure

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101 Compare Rev. Proc. 2016-51, section 5.02(2)(a)(i) (“Failure to adopt a discretionary plan amendment by the plan amendment deadline set forth in section 8.02 of Rev. Proc. 2016-37 (or section 5.05(2) of Rev. Proc. 2007-44) is not considered a plan document failure.”), with Rev. Proc. 2016-51, section 5.02(2)(a)(ii)(C) (“Nonamender Failure’ means a failure to adopt an amendment that corrects a disqualifying provision described in section 1.401(b)-1(b) within the applicable remedial amendment period.”).


104 See Rev. Proc. 2016-51, section 5.01(2)(a)(i), (ii)(B), and (b).

105 Rev. Proc. 2016-51, section 5.01(2)(b) (emphasis added). EPCRS cites the “failure to follow the terms of the plan providing for the satisfaction of the requirements of section 401(k) and (m)” as an example of an operational failure. Id.
neither involves nor is related to a change in law or change in plan design or administration. It occurs when administrators fail to follow the plan document or plan administration is changed, without informing legal counsel. Had counsel been informed or involved with the change, they could have provided advice on whether the change administratively violates the qualification requirements, and they could have helped prepare a discretionary amendment, which resolves the issue before the plan inures the significant expenses of the IRS or Labor Department discovering it on audit.

In general, two conditions must be present for an operational failure to occur that a plan sponsor can correct under EPCRS. First, a provision in the plan document is not followed administratively. Second, the failure to follow plan provisions must not result from a disqualifying provision that the plan sponsor may cure by adopting a retroactive amendment during the applicable remedial amendment period under section 401(b).

Regarding the first condition, the IRS — as demonstrated by case law, EPCRS, and other guidance — demands relatively strict administrative compliance with the provisions in the plan document. Strict administrative compliance arises from the qualification requirement that a plan be a “definitely determinable benefit” under section 401(b). This is a long-standing requirement dating to the 1940s — decades before ERISA’s enactment.\(^\text{111}\) Strict administrative compliance also arises from the qualification requirement to provide a “definitely determinable benefit” under the plan document.\(^\text{112}\) A plan document must provide a definitely determinable benefit; the exercise of administrative discretion when none exists can result in an operational failure.\(^\text{113}\)

Regarding the second condition, the EPCRS correction programs are unavailable to correct failures that can be corrected under the code and related regulations.\(^\text{114}\) As explained, this includes section 401(b). The IRS authorizes plan sponsors to use section 401(b) as the cure for failing to follow plan terms as a result of a disqualifying provision by adopting a retroactive amendment, which also has prospective effect, during the applicable remedial amendment period to conform the plan document to administration.\(^\text{115}\) The extended remedial amendment periods under Rev. Proc. 2016-37 generally align with the self-correction period under EPCRS, which applies in the textbook operational failure case.\(^\text{116}\)

C. Section 401(b)

Section 401(b) is available in two different situations. The first situation is a disqualifying provision under reg. section 1.401(b)-1(b)(1) caused by an amendment to an existing plan that results in the failure to satisfy the requirements under section 401(a), which can occur regarding form or operation. The second situation is a disqualifying provision under reg. section 1.401(b)-1(b)(3) caused by a plan sponsor’s failure to cure the plan’s failure to adopt a retroactive amendment during the extended remedial amendment period that applies to a particular qualification requirement change.

\(^{106}\) See generally Rev. Proc. 2016-51, section 5.01(2)(b). An operational failure also cannot occur if the failure is an employee eligibility failure under EPCRS.

\(^{107}\) Id. at section 5.01(2)(b).

\(^{108}\) Id.

\(^{109}\) IRS field service directive, supra note 15; see also Gladewell v. Reinhart, 477 Fed. App’x 510 (10th Cir. 2012); and Christy & Swan, T.C. Memo. 2011-62.

\(^{110}\) Reg. section 1.401-1(a)(2); Rev. Rul. 74-466, 1974-2 C.B. 131; GCM 37609 (July 19, 1978); see Christy & Swan, T.C. Memo. 2011-62. Administrative compliance with the terms of the plan document is a condition for both the employer and employees’ eligibility for the tax preferences afforded to a qualified plan. This position creates a code-based requirement parallel to ERISA section 404(a)(1)(D)/Y’s requirement to follow the terms of the plan document. While ERISA relies on the stick of civil enforcement backed by sanctions and equitable remedies, the code relies on the carrot of tax preferences. See generally Brian A. Benko, “The Regulatory Systems for Employee Benefits,” 63 Tax Law 239, 261-276 (2010). Statutory and civil litigation precepts determine who may enforce ERISA Title I’s remedial measures. The IRS, however, is the master of tax preference eligibility.

\(^{111}\) Engineered Timber Sales Inc. v. Commissioner, 74 T.C. 808 (1980); G&W Leach Co. v. Commissioner, T.C. Memo. 1981-91; Nelson H. Jones, 51 T.C. 651 (1969); unofficially released IRS technical advice memorandum (dated July 28, 1999) (stating that the written plan qualification requirement “first appeared in Reg. 103, Sec. 19.1655(a)(1)-1(a), which was added by T.D. 5278, for taxable years beginning after December 31, 1941”).

\(^{112}\) IRS field service directive, supra note 15.

\(^{113}\) TEGE-04-0417-0014, supra note 15.

\(^{114}\) Rev. Proc. 2016-51, section 6.08.

\(^{115}\) See Greenhalgh, 140 F.3d 427.

\(^{116}\) Compare section 401(b); reg. section 1.401(b)-1; and Rev. Proc. 2016-51, section 5, with Rev. Proc. 201651, section 9.02.
In those situations, section 401(b) permits the plan sponsor to (1) adopt plan amendments to cure a disqualifying provision caused by (i) a legally required qualification requirement change or (ii) an amendment to an existing plan provision (including an amendment for a discretionary change in design or administration or for an optional change in law); (2) during the applicable remedial amendment period that; (3) take effect as of the first day of the applicable remedial amendment period; (4) to conform the terms of the plan document to administration and; (5) remain in effect through the last day of the applicable remedial amendment period; (6) as long as any such amendment does not result in the failure to satisfy section 401(a).

VI. The Wellness Prescription

Plan sponsors must adapt to the new regulatory landscape by establishing new internal compliance systems and controls. An effective compliance system cures disqualifying provisions before they become qualification failures. An effective compliance system uses EPCRS to correct any failures that a plan sponsor does not (or cannot) cure with section 401(b). Without periodic determination letter rulings, the best of all possible compliance systems has the effect of reducing the risks of IRS sanctions on audit and costly litigation. Plan sponsors should heed the call and adopt the following wellness prescription.

A. The Principles

The foundation of the wellness prescription is the legal plan document. Plan sponsors must timely and compliantly incorporate administrative and legally required changes into the plan document. The plan document drives administration because a plan must operate in accordance with its terms. Whether by retroactive or prospective amendment, plan terms must evolve with administration.

Operational noncompliance is generally the result of failing to evolve with a change in circumstance. Legally required or discretionary changes usually cause noncompliant administration. A failure to comply with established terms in the legal plan document does occur; however, it is often caused by the initial implementation of the change. Administrative changes go into effect and affect participants as time passes. Failures happen. The law states that a plan must satisfy the qualification requirements under section 401(a) in form and operation.

A disconnect between what the plan says and what the administrator does is conceptually analogous to the effect of music on people. Three rooms illustrate the point. A person looks at a gathering of people standing still in a room filled with the sounds of Paul’s Boutique. The beat elicits no reaction (for some reason unbeknownst to logic and reason). That same person looks at a second room with people dancing the jitterbug while listening to Da Funk. They are not in time or in step with the music. The third and final room observed has people dancing to the beat and harmony of Good Vibrations. They dance as the composer intended.

Yet, there is an important distinction between tax-qualified plans and one’s dance to a beat. People react differently to the sound of music. There is technically no wrong way to dance. However, qualified plans are not subject to such freedom. The terms of the plan limit the actions parties charged with plan administration — often third parties — may take. What the plan says and what the administrator does must conform.\textsuperscript{117}

It is true that administration may not always conform to the plan terms.\textsuperscript{118} A plan sponsor may change administrative practice to comply with law as of its effective date but not adopt an amendment. A plan sponsor may adopt an amendment for a discretionary plan change before it takes effect. A plan sponsor may change administration but not adopt an amendment. In those cases, the plan sponsor is legally required to take action to conform plan terms to operation as of the date the administrative change takes effect.

For a legally required change in law, the plan sponsor must take action by adopting an amendment to cure a disqualifying provision caused by a change in law. The amendment must

\textsuperscript{117}Hollen, T.C. Mem. 2011-2 (“The ESOP fails to qualify under section 401(a) because it did not properly vest in operation in accordance with the schedule required by the plan. See section 1.401-1(b)(3), Income Tax Regs. (stating that ‘The law is concerned not only with the form of a plan but also with its effects in operation.’).”).

\textsuperscript{118}See, e.g., id.
conform to administrative practice as well as satisfy the qualification requirements. An amendment that does not comply with the law causes a plan document failure if not cured by the end of the remedial amendment period. An amendment that does not comply with past (or prospective) administrative practice causes an operational failure if not cured before the remedial amendment period ends, even if it is compliant with law. When the applicable remedial amendment period ends, section 401(b) eligibility ceases. Any disqualifying provision becomes either a plan document failure or operational failure and eligible for EPCRS.

As for a discretionary change, the plan must take action to conform the plan terms to plan administration. A timely amendment must conform plan terms to operation as well as satisfy the qualification requirements. Any amendment that does not do one or both of these things constitutes an amendment that does not satisfy the qualification requirements. By definition, such an amendment causes a disqualifying provision that the plan sponsor may generally cure during the remedial amendment period. Unless the plan sponsor adopts a curative amendment, the disqualifying provision becomes a qualification failure when the remedial amendment period ends. More specifically, a disqualifying provision becomes an operational failure unless the plan terms on their face fail to satisfy the qualification requirements under section 401(a). At that point, the plan sponsor may correct the qualification failure using EPCRS.

B. The Four Components

The wellness prescription meets the demands of the seismically changed regulatory landscape. Plan sponsors should use it beginning in 2017 and annually thereafter. The prescription has four components. Each plan year, the plan sponsor should apply each of the components, which cover different periods and different aspects of formal and administrative compliance. The components function to protect the plan sponsor from the risks associated with maintaining a plan without a current determination letter ruling. Individually, a component’s purpose is to protect against a particular type of noncompliance that can occur during a plan’s life cycle. Together, the components comprise the prescription for preserving a plan’s tax-qualified status. The wellness prescription is designed to help plan sponsors that may need assurance that their plans satisfy the qualification requirements under section 401(a) in form.

1. Legally required and discretionary changes effective during the plan year.

The first component of the prescription concerns legally required and discretionary plan changes that take effect during the plan year. Implementing any plan change requires careful planning during the design stage. In the long run, planning can prevent challenges that could arise in the future. The risks are reasonably foreseeable.

Designing a change in plan design or law can be challenging. Administrative systems may be unable to implement a change. An act of Congress may take effect but lack IRS guidance for quite some time. A plan sponsor’s intent or chosen design may not be administered accurately.

Legally required changes must take effect on a particular date. Using the IRS’s new operational compliance list is a useful tool for identifying provisions that a plan sponsor must implement. However, the IRS offers no guarantee that the operational compliance list will be updated timely or include all new changes in law. Plan sponsors must rely on their trusted advisers to fill the gap.

For each change in law, plan sponsors must determine whether it affects their plans. This is important because the operational compliance list includes both required and optional changes in law provisions. Distinguishing which law changes are required and which are discretionary is important for maintaining a plan. The IRS mandates that plans comply with all the qualification requirements in form and in operation. This includes a qualification requirement change that does not currently apply to a plan but could do so at some point in the future.\footnote{Christy & Swan, T.C. Memo. 2011-62.}

In many cases, the plan sponsor may not know the deadline for adopting a legally required amendment for quite some time. The length of the
wait depends on when the IRS adds the change in law to the required amendment list. In some cases, years may pass before the IRS issues guidance and adds an item to that list.

The objective of the first component is to timely and compliantly implement changes in law. By doing this, the plan sponsor has made the task of amending the plan terms easier because of the reduced risk of adopting language that does not conform to administration.

Discretionary amendments have a separate set of concerns. A plan sponsor may generally select the effective date for a discretionary plan change. The effective date of the change is the date that plan operation changes from what was done in the past. Whenever there is a change, the plan sponsor must adopt an amendment by the end of the plan year. An amendment that does not comply with its past administration generally causes a disqualifying provision, which is curable under section 401(b).

A plan sponsor can best avoid unfortunate disqualifying provisions by having its trusted legal adviser who drafts amendments and restatements work closely with those who administer it. If this does not occur and a disqualifying provision results, the plan sponsor may adopt a curative amendment during the extended remedial amendment period. However, it is preferable to avoid this headache with the wellness prescription.

2. Changes effective in a prior plan year with an open remedial amendment period.

The second component of the tax-qualified wellness prescription deals with changes to the plan that were effective in a prior plan year but have an open remedial amendment period. For provisions subject to the second component, the plan sponsor must ask several questions in evaluating whether the plan complies with changes that took effect in a prior plan year.

These questions include the following: Has the IRS issued guidance on a change in law that requires a change in administration (and, if so, as of what date is the change effective)? Has the IRS added a legally required qualification requirement change to the required amendment list and thus defined the last date of the extended remedial amendment period? Have discretionary modifications to the plan caused a disqualifying provision and thus created a remedial amendment period? Has the plan sponsor properly administered discretionary plan changes that were timely and compliantly adopted and took effect during the prior plan year?

The plan sponsor should take appropriate action if the answer to any of these questions is yes. This is important because disqualifying provisions subject to the second component of the wellness prescription still have an open remedial amendment period. Disqualifying provisions are curable. A plan sponsor must adopt a curative amendment that takes retroactive effect as of the first day the qualification requirement change took effect.\(^\text{120}\)

3. Changes with a remedial amendment period ending in the prior plan year.

The third component concerns disqualifying provisions with a remedial amendment period that closed in the immediately preceding plan year. Legally required and discretionary changes are no longer eligible for section 401(b) relief. Any noncompliant terms or conduct not cured during the first two components of the wellness prescription, as the components were applied in prior years, became qualification failures when the remedial amendment period closed. A plan sponsor may use EPCRS to correct plan document and operational failures discovered in the third component.

This component of the wellness prescription is exceptionally important because it covers the time when a plan sponsor is most likely to suffer the scrutiny of an IRS audit. Plan sponsors are advised to implement appropriate internal controls to discover failures and correct them. Doing so will effectively mitigate the risk of audit sanctions for individually designed plan sponsors — which are typically large employers, the kind mostly likely to be selected for an IRS audit.

4. Plan terms in effect in a prior plan year.

The fourth component applies to all plan terms that are not subject to the first three components of the wellness prescription. These plan terms do not have an open remedial amendment period and are

\(^{120}\) See Churchill, T.C. Memo. 2012-300.
more than one year beyond the end of the remedial amendment period that applied when the plan sponsor first adopted them. Plan terms established long ago are likely to be administered according to practices implemented years ago. Errors occurring in prior years continue to taint the plan without the protection of a statute of limitations. \(^\text{121}\) The taint of a qualification failure never ends until it is corrected. \(^\text{122}\)

Plan sponsors should rely on their trusted advisers for designing and implementing the procedures for maintaining qualified status and reducing the risk associated with IRS sanctions and a court judgment. Various factors, including the plan type and size, may dictate the type of compliance procedures. The procedures should diagnose, with surgical precision, the areas that pose the greatest risk of discovery on audit. EPCRS is available to correct any failures discovered. The question is whether the plan sponsor will correct the failure using the self-correction program, the voluntary correction program, or audit CAP.

VII. Conclusion

A healthy plan is a tax-qualified plan. Plan sponsors and their advisers should adapt to the change in circumstance if they wish to avoid contracting qualification infections. The wellness prescription provides the system for preventing IRS sanctions and civil suits caused by qualification failures. The cornerstone of the prescription is the thoughtful implementation of changes in plan design and law. When a plan sponsor suffers the unfortunate ills of a disqualifying provision, a section 401(b) curative amendment is the available remedy. The failure to cure under section 401(b) causes either a plan document or operational failure that may be correctable under EPCRS. If a plan sponsor desires or requires assurance that its plan satisfies the labyrinth-like qualification requirements under section 401(a), it needs a wellness prescription. An ounce of prevention is worth a pound of cure. Think about it.


\(^{122}\) See, e.g., DNA Pro Ventures Inc. Employee Stock Ownership Plan v. Commissioner, No. 16-1168 (8th Cir. May 9, 2017) (slip opinion), aff'd T.C. Memo. 2015-195; and Clendenen v. Commissioner, T.C. Memo. 2003-32, aff'd, 345 F.3d 568 (8th Cir. 2003).