Comments Regarding Revenue Procedure 99-13

July 12, 1999

Ms. Carol Gold
Internal Revenue Service
POB 7604, Room 5228
Ben Franklin Station
Washington, DC 20004
CC:DOM:CORP:R (Rev. Proc. 99-13)

Re: Comments Regarding Revenue Procedure 99-13

Dear Ms. Gold:

The American Society of Pension Actuaries ("ASPPA") offers the following comments to the Internal Revenue Service in regard to Revenue Procedure 99-13.

ASPPA is a national organization of approximately 3,700 members who provide actuarial, consulting, administrative, legal and other professional services for about one-third of the qualified retirement plans in the United States, the majority of which are maintained by small businesses. ASPPA's mission is to educate pension actuaries, consultants, administrators, and other benefits professionals and to preserve and enhance the private retirement system as part of the development of a cohesive and coherent national retirement income policy.

I. General Comments.
ASPPA commends the Service for expanding and refining the scope of correction programs and procedures for 403(b) Plans which have failed to satisfy the requirements of Internal Revenue Code ("Code") Section 403(b). ASPPA especially welcomes the new availability of relief for the Plan of an Ineligible Employer, the availability of Audit CAP for 403(b) Plans, the expansion of relief for Operational Failures under APRSC, and the simplification of the fee structure under TVC.

Our comments in this letter are intended to assist the Service in improving EPCRS as it applies to 403(b) Plans, to obtain clarification regarding certain features of Revenue Procedure 99-13, and to communicate to the Service the concerns of 403(b) Plan sponsors and participants and benefit plan practitioners regarding Revenue Procedure 99-13.

II. Standardized TVC Procedure.
In Revenue Procedure 95-24, which established TVC, the Service indicated it would consider comments with respect to possible standardized correction methods for specified defects.

In our August 23, 1996 comment letter to the Service regarding TVC, ASPPA encouraged the Service to establish a standardized TVC procedure and proposed specific defects, methods of correction and a fee structure to be included as features in such a procedure. Revenue Procedure 99-13 does not include such a standardized procedure, except for correction of Excess Amounts.

We again encourage the Service to establish a standardized correction procedure under TVC. The procedure should be similar to SVP under EPCRS, but with variations appropriate in light of the differences between qualified plans and 403(b) programs and the differences between VCR and TVC. Like SVP, the standardized procedure would provide relief on an expedited basis for certain types of defects if correction of the defect is made according to a standardized method. Like SVP, the procedure would be optional, and the employer could still seek non-standardized TVC relief for a defect through a non-standardized method of correction, even if that defect is eligible for the standardized correction procedure.

We propose that the following defects, methods of correction and fee structure be included in the standardized procedure:

A. Failure to satisfy the actual contribution percentage test set forth in Code Section 401(m)(2) (as

required by Code Section 403(b)(12)(A)(i)).

The standard correction method for the failure to satisfy the average contribution percentage ("ACP") test should be either of the following, at the employer=s option, to the extent necessary to satisfy the ACP test: (1) for the employer to make a qualified non-elective contribution (AQNEC@) or a qualified matching contribution (AQMAC@), at the employer=s option, on behalf of non-highly compensated employees or (2) to reduce the allocations of matching contributions, or refund after-tax employee contributions, as the case may be, of highly compensated employees.

Any QNECs or QMACs should be made on behalf of all non-highly compensated employees (to the extent that the limits of Code Sections 403(b)(2) and 415 would not be exceeded) eligible to receive a matching contribution or to make an employee after-tax contribution under the terms of the 403(b) Plan. QNECs or QMACs should be either the same flat amount, percentage of compensation, or percentage of deferrals for each eligible non-highly compensated employee.

B. Failure to timely distribute elective deferrals in excess of the applicable dollar limits under Code Section 402(g) (in contravention of Code Sections 401(a)(30) and 403(b)(1)(E)).

The standard correction method would be to distribute the excess deferrals to the employee. Amounts so distributed would be taxable both in the year of deferral and in the year of distribution to correspond to the treatment of excess deferrals under SVP. See Appendix A, Section .04 of Revenue Procedure 98-22. Distributed elective deferrals would have no impact on nondiscrimination testing, as they do under SVP, because there is no ADP-type requirement for elective deferrals under a 403(b) Plan.

C. Failure to meet the universal eligibility requirement of Code Section 403(b)(12)(A)(ii) for elective deferrals.

We suggest that the method of correction for this defect should be to provide each improperly-excluded employee the opportunity to make special, additional elective deferrals under the 403(b) Plan for a period of years commensurate with the period of improper exclusion.

We recognize this method of correction may not always place the 403(b) Plan in exactly the position it would have been in had the defect not occurred. For example, improperly excluded employees who have terminated employment will not be able to make special additional deferrals. We also recognize that correction under this method might have to take into account the limitations of Code Sections 402(g), 403(b)(1)(E), 403(b)(2) and 415. Nevertheless, we believe this method will enable most improperly-excluded employees to generally achieve the tax-favored savings they would have accumulated had they not been improperly excluded, without undue expense to the employer.

We understand that the method of correction under SVP for the erroneous exclusion under a cash or deferred arrangement is for the employer to make a QNEC-type contribution on behalf of the employee that is equal to the average deferral percentage for the employee=s group (either highly compensated or non-highly compensated).

This approach is not appropriate for 403(b) Plans for a number of reasons. First, employers which sponsor 403(b) arrangements generally have never made non-elective contributions under the arrangements, and historically have had little or no involvement in the arrangement. These employers generally will be reluctant to expend their own funds to provide benefits when they have not done so before. Second, employers which sponsor 403(b) Plans are tax-exempt organizations which simply cannot afford to make corrective contributions on behalf of all improperly-excluded employees. Third, the area of nondiscrimination in 403(b) Plans and the universal eligibility rule has long been confusing to both employers and practitioners, and a violation of that rule usually has resulted from misunderstanding rather than intentional noncompliance. An employer should be able to correct violations caused by such uncertainty on an expedited basis and at a minimal cost. Sponsors of 403(b) Plans are typically organizations with limited financial resources, uncertain funding and budget constraints.

We also request that, if the universal eligibility rule has been violated in a 403(b) Plan which includes a matching contribution feature, the employer should not be required to make a matching contribution on behalf of all improperly-excluded employees; employer matching contributions would have to be made on behalf of such employees only to the extent necessary for the matching feature to comply with the applicable nondiscrimination requirements of Code Section 403(b)(12)(A)(i). There is no universal eligibility rule for matching contributions, and had an employer included the improperly-excluded employees in the elective deferral arrangement, it could have excluded those employees from the matching features as long as the requirements of Code Section 403(b)(12)(A)(ii) were met.

D. Fees.

We propose the compliance correction fee be $350 in all cases, which is the same compliance fee as under SVP.

III. Permitting Termination of Plan of an Ineligible Employer.
Revenue Procedure 99-13, Section 4.03, relating to the correction of a Plan of an Ineligible Employer, requires that the assets of such a plan not be distributed earlier than the occurrence of one of the distribution events described in Code Section 403(b)(7) (to the extent the assets are held in custodial accounts) or Code Section 403(b)(11) (for those assets invested in annuity contracts that would be subject to Code Section 403(b)(11) restrictions if the employer were eligible).

Because plan termination is not a distribution event described in either Code Section 403(b)(7) or in Code Section 403(b)(11), it appears that a Plan of an Ineligible Employer may not be corrected through termination of the plan and distribution of its assets.

We urge the Service to modify the permitted method of correction of a Plan of an Ineligible Employer so as to permit plan termination and distribution of assets upon termination. Requiring the continuation of a Plan of an Ineligible Employer until there has been a distribution event with respect to all participants prolongs the existence of a plan which came about through error. For such plans which are subject to Title I of ERISA, reporting, disclosure, fiduciary and other requirements would otherwise have to continue to be met until all assets have been distributed, even though the plan cannot receive any additional contributions on behalf of any participants.

IV. EP/EO Examination of Employer Should Not Render Plan Ineligible for APRSC or TVC Relief.

Section 5.01 of Revenue Procedure 99-13 403(b) and Section 5.06 of Revenue Procedure 98-22 render a 403(b) Plan ineligible for APRSC or TVC if the plan sponsor is under examination by the Service, even if the 403(b) Plan itself is not.

We strongly oppose the denial of APRSC or TVC relief to a 403(b) Plan because the employer is under an Exempt Organizations examination. There is no comparable ineligibility rule for non-tax-exempt employers under Walk-in CAP or VCR. 403(b) Plans lack many of the compliance and guidance resources (such as determination letters and pre-approved plan documents) available to plans which are tax-qualified under Code Section 401(a). Consequently the "ineligible-because-under-examination rule" already places 403(b) Plans at a disadvantage compared to qualified plans, and the broadening of that rule aggravates the effect of that disadvantage. Furthermore, the operation of a 403(b) Plan (particularly a 403(b) arrangement) generally has little or no connection with the other activities of the sponsoring employer. It would be inappropriate and unjust to deny relief to a 403(b) Plan simply because its sponsor is under examination for another, unrelated reason.

V. Plan of an Ineligible Employer Not To Be Considered a Severe Failure.

Although Revenue Procedure specifically identifies a Plan of an Ineligible Employer as a failure and provides a specific method of correction for that failure, that failure is still subject to the "range" fee structure set out in Section 8.04 of Revenue Procedure 99-13. Section 8.04 lists a Plan of an Ineligible Employer as a factor affecting the amount of the compliance correction fee, but does not specify how so, i.e., whether a Plan of an Ineligible Employer is to be considered a "severe" failure.

We request that the Service state that a Plan of an Ineligible Employer will not, absent other circumstances, weigh

in favor of a compliance correction fee in excess of the applicable presumptive amount set out in Section 8.04.

We appreciate the opportunity to provide these comments, and we would be pleased to discuss them with you further.

Sincerely,

Theresa Lensander, C.P.C., Q.P.A.
Chair, Tax-Exempt and Governmental Plans Committee

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