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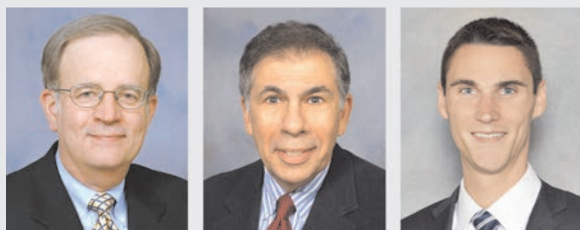
# Need a Determination Letter? A Declaratory Judgment Might Work

By Fred Oliphant, Gary Quintiere, and Nicholas Wamsley



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This article examines the implications of a recent announcement that the IRS intends to restrict the use of its determination letter program by ongoing individually designed retirement plans. The authors consider whether an employee seeking to implement a plan amendment can request a declaratory judgment under section 7476 if the IRS refuses to issue a determination letter, and they analyze the IRS's ability to block an employer from going to the Tax Court under section 7476.

## Introduction

The IRS may soon be closing the door to the use of its determination letter program by ongoing individually designed retirement plans. This would be an unfortunate turn of events for thousands of employers — predominantly major employers. Those employers, especially ones sponsoring defined benefit plans, will likely not see the options available under the IRS's preapproved plan program as adequate substitutes.

So what will sponsors of individually designed plans do? Will they risk making significant plan changes without IRS approval? That would seem to be an unpalatable option for major employers that for many years have relied on the determination letter program to provide them with enough confidence to support the frequent need to make market-based modifications to their plans.

Fortunately, the loss of the determination letter program may not require those employers to choose between shying away from plan modifications or accepting the risks associated with making a non-approved amendment. The declaratory judgment remedy of section 7476 may afford them a mechanism for obtaining assurance that is comparable to that previously provided by determination letters.

Virtually all major employers offer individually designed, "customized" plans that are written in their own words and that provide the flexibility to make discretionary changes. The alternative of moving to an IRS-approved master and prototype plan or volume submitter plan is not nearly as desirable because it involves generally being subject to the control of a mass-produced, one-size-fits-all plan that is written and effectively interpreted by others.

Despite widespread use by major employers, or perhaps because of it, individually designed plans are disfavored by the IRS. The IRS believes that their "individuality" presents greater challenges to determination letter specialists and auditors than do master and prototype or volume submitter plans. Consequently, the IRS began cutting back the scope of services offered to individually designed plans under the determination letter program.[1] In general, the IRS has rationalized those reductions in the program as being necessary to conserve scarce resources.[2] Unfortunately, that resource problem, while undoubtedly a legitimate concern for the IRS, has led to big problems for employers seeking to maintain individually designed plans in a world of increasing legal complexity.

In Announcement 2015-19,[3] the IRS has given notice of still further changes that it intends to make to the determination letter program. When implemented, these changes will pose a dilemma for employers amending their individually designed plans. As proposed, the IRS intends to issue determination letters to those plans only upon their

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[1]In Announcement 2011-82, 2011-52 IRB 1052, the IRS stated that it would no longer consider a plan's compliance with coverage and nondiscrimination requirements as part of its determination letter program. For a thorough discussion of how that affects plan sponsors, see C. Frederick Oliphant and Elizabeth Drake, "No Determination Letters of Coverage and Nondiscrimination Compliance — Now What?" *J. of Pension Planning and Compliance*, Vol. 39, No. 1 (2013).

[2]Matthew R. Madara, "IRS Official Offers More Details on Determination Letter Changes," *Tax Notes*, May 25, 2015, p. 892.

[3]Announcement 2015-19, 2015-32 IRB 157.



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establishment or termination. For an employer maintaining an individually designed plan, this announcement, for all practical purposes, amounts to a ''no determination letter'' policy for the life of the plan. That much is made clear by the IRS's statement that a determination letter application for an ongoing, individually designed plan will be accepted only ''in certain . . . limited circumstances that will be determined by Treasury and the IRS.''

But there may be hope for employers seeking certainty regarding the application of a seemingly ever-increasing array of complex regulations to their retirement plans. The provisions of section 7476 are a looming presence overshadowing the IRS's determination letter program and its actions in Announcement 2015-19, and they potentially offer employers a way out of the dilemma.

Even assuming that the IRS can exit the determination letter program permissibly under section 7476, it seems highly unlikely that the IRS can unilaterally cut off an employer's access to the declaratory judgment proceedings established by Congress in that section. Accordingly, if under the soon-to-be-modified program, the IRS refuses to issue a determination letter to an employer seeking to implement a plan amendment under the protection of a favorable letter, an employer might want to consider requesting a declaratory judgment by the Tax Court.

### Legislative History of Section 7476

The enactment of ERISA introduced a new remedy for addressing controversies involving the qualified status of retirement plans. ERISA added section 7476 to the code, opening the way for employers to *immediately* challenge not only an adverse determination by the IRS in connection with the qualified status of a plan but also the IRS's failure to make a determination after being requested to do so.

Before ERISA, an employer was unable to mount an immediate court challenge in response to an unfavorable determination regarding its plan's qualified status. At that time, the employer had only two choices, and both were bad: either agree with the IRS's conditions for granting qualified status or reject them and wait until the IRS denied its deductions for contributions made to the plan.[4] The legislative history makes clear that Congress did not wish to see that state of affairs continue. Congress considered the ability to obtain advance determinations as providing a strong inducement to employers agreeing to sponsor broad-based retirement plans. However, it viewed the then-existing determination letter program as offering an employer a ''take it or leave it'' bargain. Congress was rightfully concerned that if left undisturbed, the program would not provide the desired stimulus for employers to adopt new plans or enhance their current plans.

The House Ways and Means and Senate Finance committees had virtually identical views on how to re-balance the determination letter process to give employers a greater edge. The House report, repeated almost verbatim in the Senate report, included the following statement:

> As a practical matter, there is no effective appeal from a Service determination (or refusal to make a determination) that a proposed pension plan fails to qualify for the special tax benefits. In these cases, although there may be a real controversy between the employer and the Service, present law permits the employer to go to court only after he has made contributions to the plan, deducted them, and had those deductions disallowed. The long time period and the related uncertainty, coupled with the threat of the ultimate loss of the tax deduction, almost always causes the employer to go along with the Service, even if he disagrees with the Service's position. In addition the determination letter procedure does not permit employees, or their unions, to question the qualification of plans.
>
> Your committee believes that both employers and employees should have the right to court adjudication in the situation described above.[5]

Congress had the right idea, but until now, most employers have not been willing to take their determination letter issues to the Tax Court. When effective, the ''no rule'' policy described in Announcement 2015-19 might be the trigger that changes their views about those actions.

### Basic Elements of Section 7476

The roadmap to seeking declaratory judgment is spelled out clearly in section 7476.[6] The threshold requirement for the petitioner is to prove the existence of an ''actual controversy'' involving the IRS's determination or failure to make a determination regarding the initial or continuing qualified status of the retirement plan. For a failure to make a determination regarding the continuing qualification of the plan, the controversy must relate to a

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[4]H.R. Rep. No. 93-779, at 105 (1974); S. Rep. No. 93-383, at 112-113 (1974).

[5]*Id.*

[6]For additional guidance on the practical application of these requirements, see reg. section 601.201(o) and Title XXI of the Tax Court Rules of Procedure.



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plan amendment or plan termination, meaning that operational issues are not covered.

Also, the petitioner must satisfy the following five procedural requirements: First, the petitioner must be among the authorized petitioners described in section 7476(b)(1), namely, the employer sponsor, the plan administrator, an employee who qualifies as an ''interested party,'' and the Pension Benefit Guaranty Corp.

Second, when applicable, the ''notice to interested parties'' requirement must be satisfied. Specifically, when the petition is filed by the employer or the plan administrator, there must be a showing that notice of the determination letter request was properly and timely given to interested parties.

Third, the petition must include factual assertions demonstrating that the petitioner exhausted those administrative remedies available to him within the IRS. Section 7476(b)(3) gives the IRS a 270-day grace period in this regard, stating that a ''petitioner shall not be deemed to have exhausted his administrative remedies with respect to a failure by the Secretary to make a determination with respect to initial or continuing qualification of a retirement plan before the expiration of 270 days after the request for such determination was made.''

Fourth, relating to the ''actual controversy'' requirement, there must be a real (as opposed to a hypothetical or theoretical) issue presented to the court. Section 7476(b)(4) requires that the ''plan'' (in a case involving initial qualification) or the ''amendment'' (in a case of continuing qualification) be ''put into effect'' before the filing of the petition. The statute suggests, however, that a plan or amendment subject to a contingency might nonetheless meet this requirement: ''A plan or amendment shall not be treated as not being in effect merely because under the plan the funds contributed to the plan may be refunded if the plan (or the plan as so amended) is found to be not qualified.''

Fifth, when the IRS sends a certified or registered notice of its determination, a petition must be filed before the 91st day following the notice. That timing requirement doesn't appear to apply to the IRS's failure to issue a determination.

Section 7476 provides that ''upon the filing of an appropriate pleading, the Tax Court *may* make a declaration'' regarding the qualification issue presented. The question that immediately arises is whether the word ''may'' gives the Tax Court discretion to refuse taking jurisdiction in the face of a well-pleaded petition. There is no inkling of that under the Tax Court rules and, looking at the Tax Court's opinions over the years, it seems that the sole instance in which declaratory judgment jurisdiction will not be afforded to an employer making an ''appropriate pleading'' is when a traditional remedy (that is, contesting a tax deficiency) is readily available.[7]

**Employers' Past Use of Section 7476**

It must be recognized that despite Congress's good intentions, major employers, by and large, have not fully embraced a declaratory judgment action as a viable strategy in dealing with failures or stalemates in the determination letter process. In the over 40 years since the passage of section 7476, only a very few major employers have sought the recourse in the Tax Court afforded by section 7476. This is surprising, given that major employer plans typically cover thousands of participants and that it is not all that unusual for those plans to be required to accept costly or burdensome conditions or correction procedures as the ''price'' for receiving a favorable determination. The likely explanations for this phenomenon are cost and risk avoidance. Rightly or wrongly, employers have likely viewed declaratory judgment proceedings under section 7476 as another form of expensive litigation. And, by litigating, the employer could risk antagonizing the very agency whose favorable determination it has been seeking.

Whatever the reason for employers' sparing use of the section 7476 declaratory judgment provisions, it should not be ascribed to the Tax Court's being inhospitable to employer petitions, at least not those presenting serious legal issues. It might appear that the track record is not all that good for employers seeking to overturn IRS determinations regarding their retirement plans by suing for a declaratory judgment in the Tax Court. On further

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[7]*See, e.g.*, *Shut Out Dee-Fence Inc. v. Commissioner*, 77 T.C. 1197 (1981). In that case, the employer adopted a retirement plan in 1973 and submitted a determination letter application in 1974 seeking the IRS's confirmation of the plan's qualified status. In 1980, six years after the determination letter application had been filed, the IRS sent the plan's retirement trust a notice of deficiency pertaining to the trust's tax years 1974 and 1975. Included with the deficiency notice was the following statement: ''It has been determined that you did not qualify as an organization exempt from tax under section 501 of the Internal Revenue Code.'' *Id.* at 1198. The employer then filed three timely petitions in the Tax Court — one for declaratory relief under section 7476 and two others, each challenging the notice of deficiency for the specific tax year involved. Although the court sided with the employer's argument that the IRS had never made a proper determination on the plan's status, it decided not to accept section 7476 jurisdiction on practical grounds. The court noted that the declaratory relief afforded to qualified petitioners under section 7476 was ''intended to facilitate a relatively prompt judicial review of the specified types of exempt organization issues'' but was not intended to supplant the normal avenues of judicial review, which in this case were already in process. *Id.* at 1201-1205.



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examination, one notices a more encouraging pattern: Employers presenting genuine legal issues on which reasonable parties may differ have so far fared reasonably well.[8] In contrast, employers making last-ditch, desperation arguments seeking to explain why their plans were amended late or why they permitted accruals or made distributions in excess of the section 415 limitations have, for obvious reasons, not fared well at all. In reviewing the declaratory judgment cases under section 7476, the message is fairly clear that a petitioner with a strong argument stands a good chance of obtaining a favorable result. The cases summarized below prove this assessment.

*FLBA Asheville*[9] is the earliest employer victory, and it was remarkable given the difficult path that the employer was forced to take to attain a review on the merits and the high legal standard it was required to satisfy in order to reverse the IRS's adverse determination.[10]

The case involved a money purchase pension plan that the employer made available to all ''full-time employees,'' defined in the plan to include employees who worked over 20 hours per week and more than five months of the year. The plan did not extend automatic coverage. To participate, an employee was required to contribute 6 percent of base pay (via a salary reduction agreement) in which he was fully vested from the outset. For each eligible employee electing to participate, the employer was required to contribute 3 percent of the employee's base pay, in which the employee would vest at the rate of 20 percent per year.

The issue before the court was whether the plan's coverage, during its first year of operation, satisfied the nondiscriminatory classification test under then-section 401(a)(3)(B).[11] During that year, the employer had 23 eligible employees — nine highly paid and 14 lower-paid — but only two elected to participate: one from the highly paid group and the other from the lower-paid group. The IRS issued an adverse determination letter based on its conclusion that the plan's first-year coverage did not satisfy the ''fair cross-section test,'' and therefore, it failed to meet the nondiscriminatory classification test under then-section 401(a)(3)(B). The fair cross-section test required broad participation over all salary levels, a standard that the plan's two out of 23 coverage could not meet.

This case presented a challenge for the employer because in making its adverse determination, the IRS had exercised discretion that was expressly granted to it under then-section 401(a)(3)(B). For the employer to prevail, it was necessary to convince the Tax Court that the IRS's determination was arbitrary, unreasonable, or an abuse of its discretion. Although it decided some collateral issues against the employer, the Tax Court held favorably for the employer on the ultimate issue, resting its opinion heavily on the relevant facts and circumstances, all of which favored the employer's contention that its plan was not discriminatory: the plan was open to all full-time employees meeting nominal service requirements; the 6 percent salary reduction contribution was not burdensome; the 3 percent employer contribution vested at a reasonable rate; and the plan's first-year coverage (one employee from each of the highly paid and lower-paid groups) did not reflect a favoring of the highly paid group. Based on these facts, the court held: ''We must conclude that petitioner's plan did not discriminate in favor of the prohibited group and should not have been disqualified for the initial year it went into effect.''

The taxpayer victory in *FLBA Asheville* was not a fluke. Other significant victories followed. In *Calfee*,[12] several different employers sought a declaratory judgment after the IRS had determined that their respective pension and profit-sharing plans failed to qualify under section 401(a), all, in the IRS's view, failing for the same reason: Each plan permitted a reversion of contributions to the employer under limited circumstances explicitly sanctioned by ERISA but not the code. The IRS argued that the ERISA provision was part of the fiduciary standards in Title I of ERISA and that those standards did not govern the qualification requirements under applicable sections of the then-existing code and those added by Title II of ERISA. The Tax Court rejected that argument and held for the employers on the grounds that Title I and Title II were drafted ''in concert'' and should therefore be construed harmoniously.

In *Sutherland*,[13] the IRS refused to qualify the petitioner's two retirement plans on the grounds that they failed the coverage requirements. In reaching its determination, the IRS considered the employees working for the petitioner's lumber

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[8]For cases in which the Tax Court has sided with or against the taxpayer, see the Appendix.

[9]*Federal Land Bank Association of Asheville v. Commission,* 74 T.C. 1106 (1980).

[10]On first hearing, the Tax Court dismissed the case for lack of jurisdiction, holding that declaratory relief under section 7476 was not available to the petitioner for the tax year at issue. 67 T.C. 29 (1976). The Fourth Circuit reversed and remanded the case to the Tax Court for a hearing on the merits. 573 F.2d 179 (4th Cir. 1978).

[11]Section 401(a)(3)(B) is now section 401(a)(5)(B).

[12]*Calfee, Halter & Griswold v. Commissioner*, 88 T.C. 641 (1987).

[13]*Sutherland v. Commissioner*, 78 T.C. 395 (1982).



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business employees along with the employees of two failing aviation businesses that the petitioner owned in partnership with others. The IRS found the lumber company and the two aviation companies to be part of the same controlled group. The Tax Court viewed this finding as an overly harsh reading of the controlled group rules given that one of the aviation companies went out of business before the IRS's issuance of the adverse determination letters and the other one failed shortly thereafter. In arriving at this conclusion, the Tax Court stated:

> [The IRS's] harsh position does nothing to advance the purpose Congress had in mind in enacting section 414(c), but does plenty to subvert the overriding purpose of Congress to encourage the establishment of pension plans for employees. The owner of one healthy and two dying businesses has enough impediments to the establishment of a pension plan for the viable concern. If he has to carry two near corpses — possibly finishing them off in the process — he may simply decline to do anything, with the employees of the viable concern being the losers.

*Halliburton*[14] represents another successful effort by an employer to obtain a declaratory judgment in the Tax Court. In that case, the Halliburton Company convinced the court that its layoff of thousands of employees, made necessary by a sharp decline in the company's oil field services business, did not result in a partial termination of its profit-sharing plan. This victory was hard-fought because before it could present its case on the merits, Halliburton had to overcome two motions to dismiss — one for failure to exhaust administrative remedies[15] and a second for failure to notify interested parties.[16] After a thorough and comprehensive review of the facts and applicable law, the Tax Court held in favor of Halliburton.

In its opinion resolving the substantive part of the case — whether the layoffs resulted in a partial termination of the plan — the court signaled early that its decision would not be based on a mechanistic or formulaic analysis. It gave substantial weight to the severity of the economic downturn that the company had to deal with when it noted that "Halliburton was faced with two options: Cut costs or go out of business." It also noted that Halliburton had no "improper or bad motive for terminating the participants," that its actions "resulted from emergency measures designed to reduce costs," and that the company, rather than continuing on with a diminished workforce once the recovery started, rehired "a significant number of [the] laid-off employees." Those and other factors contributed heavily to the court's agreeing with Halliburton that even though almost 20 percent of the plan's participants were involuntarily terminated, a partial termination had not occurred.[17]

More recently, in 2001, the trustees of a multiemployer pension fund persuaded the Tax Court to overturn the IRS's determination to disqualify their plan. In *Sheet Metal Workers*, the fund's trustees were notified that their amendment ceasing cost of living adjustment benefits for some retirees constituted a prohibited cutback and needed to be corrected.[18] Instead of conceding, the trustees petitioned for a declaratory judgment under section 7476. The IRS made several alternative arguments in defense of its position: The COLA represented an accrued benefit, it was a retirement-type subsidy, or, based on a "pattern or practice" theory, it had become a permanent part of the plan. The Tax Court rejected all of those arguments and held that the trustees' amendment did not constitute a cutback.

The foregoing cases and others[19] demonstrate compellingly that the Tax Court is no rubber stamp for the IRS and is not afraid to overturn a determination by the IRS as to the qualified status of a plan.

**Curtailing Determination Letter Program Impact**

Announcement 2015-19 puts a new variable into the mix for employers. If the IRS moves ahead as planned, determination letters will no longer be issued in the normal course to ongoing, individually designed plans. This will mean that employers wishing to amend those plans will need to figure out whether it is better to adopt the amendment without a letter, scrap the amendment entirely, or consider other options.

One option might be to seek to convince the IRS that the amendment falls into the now-undefined category of "limited circumstances" worthy of a determination letter. However, given that the IRS has already announced its general reluctance to

[14]*Halliburton Co. v. Commissioner*, 100 T.C. 216 (1993), *aff'd*, 25 F.3d 1043 (5th Cir. 1994) (per curiam).

[15]*Halliburton Co. v. Commissioner*, 98 T.C. 88 (1992).

[16]*Halliburton Co. v. Commissioner*, T.C. Memo. 1992-534. The Tax Court also denied a government motion to compel discovery to supplement the administrative record.

[17]*Halliburton* may represent the high-water mark in partial termination cases. The discussion is illustrative only of the evenhanded treatment that an employer seeking a declaratory judgment in the Tax Court might expect in connection with a matter heavily dependent on a review of the facts and circumstances.

[18]*The Board of Trustees of the Sheet Metal Workers' National Pension Fund v. Commissioner*, 117 T.C. 19 (Dec. 4, 2001).

[19]*See* the Appendix.



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issue determination letters in those cases, it would appear that, in most instances, this option is destined to fail. Another option may be to pursue a strategy designed to obtain a determination from the Tax Court at the inception of the amendment.[20]

Before turning to how the declaratory judgment procedure might work in the face of the IRS's refusal to entertain a determination letter request, it is worth asking whether the IRS even has the legal authority to close the determination letter program for ongoing qualified plans. Clearly, the structure of section 7476 assumes that a determination letter program exists and, while the IRS generally has authority to regulate its own affairs, there is at least reason to question whether it can dispense with a program that is so intertwined with a statutory declaratory judgment provision. One might infer from the statute that the IRS must provide a determination letter program so that the declaratory judgment provisions will work the way Congress intended.

That conclusion appears to be shared by other practitioners. In June 2010 the IRS Advisory Committee on Tax-Exempt and Government Entities (ACT) issued a report that included a white paper titled "Analysis and Recommendations Regarding the IRS's Determination Letter Program."[21] The white paper included the following statement, which strongly supports the belief that the IRS may not unilaterally cease issuing determination letters to ongoing plans:

> While nothing in the Code compels a plan sponsor to seek a determination letter, IRC section 7476 provides the Tax Court with the power to issue a declaratory judgment with respect to the qualification of a retirement plan if the IRS fails to make a determination regarding the plan's qualification provided the petitioner has exhausted administrative remedies within the IRS. *Such statutory requirement thus mandates the Service to issue determination letters upon request.*[22] [Emphasis added.]

Because this article focuses on an employer's use of the declaratory judgments provisions, we will assume for our purposes that the IRS may legally decline to issue determination letters on the qualified status of plans or on various aspects of those plans. Accordingly, we will turn to the related question whether a refusal to issue determination letters impairs or limits an employer's ability to seek a declaratory judgment.[23]

The IRS might offer several arguments to support the view that if it exits the determination letter program, an employer may not seek a declaratory judgment on an issue that the IRS has refused to rule on, or alternatively may not seek a declaratory judgment until the Service subsequently makes a determination on that issue (that is, upon audit). Those arguments appear weak.

Whatever the scope of the IRS's authority in making changes to its determination letter program — assuming those changes result in the failure to issue determinations regarding the qualified status of retirement plans — we think a court would be hard-pressed to conclude that the IRS's exercise of its discretionary authority was powerful enough to override a statutory right granted to taxpayers by Congress. Section 7476 expressly provides for a declaratory judgment remedy in cases where the IRS fails to issue a determination on a qualification issue. The plain language of that provision has no exceptions: failures based on policy, budget, personnel, or similar reasons are still failures.

Further, as noted above, it is clear that Congress viewed advance determinations as a strong inducement to employers agreeing to sponsor broad-based retirement plans. It is also clear that Congress wanted to adjust the scales of the determination letter program to provide greater leverage to the employer. The declaratory judgment remedy does

[20]Of course, the employer could also adopt the amendment and wait and see if it were ever audited and then pursue the declaratory judgment procedure at that time. The downside to that approach is that if the employer cannot prevail, there would be no alternative to disqualification other than paying the high audit cap sanctions.

[21]ACT, "Report of Recommendations: Analysis and Recommendations Regarding the IRS's Determination Letter Program" (June 9, 2010).

[22]*Id.* It should be noted that the IRS's own regulations appear to exempt *retirement plan* determinations from the general rules that afford the IRS the discretion to decline to issue determination letters. Those regulations provide as follows:

> Where such a determination cannot be made, such as where the question presented involves a novel issue or the matter is excluded from the jurisdiction of the district director by the provisions of paragraph (c) of this section, a determination letter will not be issued. *However, with respect to determination letters in the pension trust area, see paragraph (o) of this section.* Treas. Reg. section 601.201(a)(3). [Emphasis added.]

[23]This article analyzes the IRS's ability to block an employer from going to Tax Court under section 7476 when the IRS refuses to issue determination letters, but we recognize that in the IRS's prior actions to curtail its determination letter program, there has been little or no acknowledgement by the IRS of an employer's rights under section 7476. For that reason, it is difficult to know precisely what the IRS thinks about the scope of the employer's rights. One might infer from its silence that the IRS would in fact accept the view that any failure on its part to issue a determination letter, regardless of the reason, provides an employer with the necessary predicate for filing a petition for a declaratory judgment. Or, as more likely may be the case, the IRS may just be opting to "play its cards close to the vest," choosing to deal with those petitions as they may arise.



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just that. Under these circumstances, the IRS must either issue determination letters upon request or accept as a consequence that its failure to make a determination justifies an employer's right to seek a declaratory judgment in the Tax Court.

The IRS might also try to block an employer's access to the Tax Court on other procedural grounds. Reg. section 601.201(o)(10)(i)(a) provides that one of the necessary steps for satisfying the exhaustion of administrative remedies requirement is the filing of a ''completed application with the appropriate district director pursuant to paragraphs (o)(3)(iii) through (xii).''[24] That paragraph suggests that where a noncompliant determination letter application is filed, the IRS may return it to the applicant and, if this occurs, the 270-day period described in section 7476(b)(3) will be tolled and will not recommence until a compliant application is filed.

Based on the foregoing, the IRS could conceivably take the position that an application that seeks a determination on a question that falls under a previously announced ''no rule'' policy or is made by a plan that is barred from requesting a determination on any question (for example, an individually designed plan that applies after the program has been closed), is a noncompliant application. Based on that premise, the IRS could assert that the 270-day period never begins, and therefore, the applicant is never able to meet the jurisdictional requirement of section 7476(b)(3).

We think that any argument along those lines would be rebuffed summarily by the Tax Court on the grounds that its obvious intent would be to deny a retirement plan sponsor the right to seek a declaratory judgment in a case where the IRS has refused to make a determination on a plan qualification issue. Such a case would fall squarely within the remedial provisions afforded by section 7476. In simple terms, without an amendment to section 7476 that allows the IRS to refuse to issue determinations in the pension trust area *for policy reasons*, the Tax Court should continue to apply the plain meaning of the words ''failure by the [IRS] to make a determination'' and therefore not deny a petitioner the right to the judicial remedy established by Congress in 1974.[25]

Given Congress's desire to spare the taxpayer the need to endure ''the long time period'' between plan adoption (here, the adoption of plan amendments) and the potential disallowance of deductions and ''the related uncertainty'' associated with the ''threat of the ultimate loss'' of such deductions, it seems inconceivable that the Tax Court would deny jurisdiction based on the ''policy'' argument described above.[26] As written, section 7476 provides for a declaratory judgment in the event of any controversy between the employer and the IRS regarding a plan or amendment that is put into effect before the filing of a petition. In those circumstances, a controversy arises whenever the IRS either issues an adverse determination or fails to issue any determination. If the IRS is permitted to carve out an exception, that is, avoid the consequences of section 7476, based on policy reasons, employers sponsoring retirement

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[24]*See also* Rev. Proc. 2015-6, 2015-1 IRB 194, sections 20.01 and 20.02.

[25]A related point arises when the IRS issues a determination letter but refuses to rule on certain aspects, such as the application of the discrimination rules. While we are not aware of cases in which an employer has attempted to seek a declaratory judgment when the IRS has issued a caveated determination letter, there is reason to believe that an employer would have recourse to the declaratory judgment proceeding if the IRS does not respond *fully* to the determination letter request.

Support for that assertion can be found in declaratory judgment cases brought by tax-exempt organizations under section 7428. Courts have deemed section 7428 a ''counterpart'' to section 7476. *E.g.*, *McManus v. Commissioner*, 93 T.C. 79 (1989); *Loftus v. Commissioner*, 90 T.C. 845 (1988); and *Gladstone Found. v. Commissioner*, 77 T.C. 221 (1981). In *Friends of Society of Servants of God v. Commissioner*, the taxpayer requested a definite ruling regarding its status as a church under section 170(b)(1)(A)(i). 75 T.C. 209, 210 (1980). The IRS instead issued the taxpayer an advance ruling letter stating that it could reasonably expect to be considered a non-private foundation under sections 509(a)(1) and 170(b)(1)(A)(vi), but that it was ''not now making a final determination of [the taxpayer's] foundation status under section 509(a).'' *Id.* at 210-212. The taxpayer sought a declaratory judgment under section 7428 regarding its status. The court stated that ''all petitioner really got was a trial period within which to demonstrate that it was publicly supported. . . . At best, respondent's ruling constitutes a failure to make a determination which itself would support jurisdiction under section 7428(a)(2).'' *Id.* at 217. *Friends* demonstrates that courts do not consider just any IRS response a determination for purposes of section 7428, and by extension section 7476. Instead, the IRS's response must address the taxpayer's request in order to foreclose a judicial remedy.

(Footnote continued in next column.)

[26]*Federal Land Bank Association of Asheville v. Commissioner*, 573 F.2d 179 (4th Cir. 1978) (explaining that absence of declaratory judgment remedy often ''operated to coerce a taxpayer in agreeing with the IRS's determination of disqualification''); *Halliburton Co. v. Commissioner*, 98 T.C. 88, 100-101 (1992) (listing considerable costs that would result from refusing to grant jurisdiction, including administrative difficulties and participants' hampered ability to plan for retirement); and *Efco Tool Co. v. Commissioner*, 81 T.C. 976, 982 (1983) (placing importance on ''speedy resolution of the dispute'').

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plans would be put back in the same position they were before section 7476 was enacted. Unless Congress sanctions this result by modifying section 7476 to accommodate the IRS's policy reasons argument, it is difficult to think that the Tax Court will accept that argument.

**Seeking Declaratory Judgment: Practical Aspects**

While we do not think that the IRS can prevent an employer adopting a plan amendment from obtaining a declaratory judgment under section 7476 simply by refusing to issue a determination letter, we recognize that the IRS's withdrawal from the determination letter program poses practical questions for an employer that wishes to pursue the option of seeking a declaratory judgment. If there is no prescribed procedure for requesting a determination letter for the plan amendment, how does an employer demonstrate to the Tax Court as a practical matter that it has exhausted its administrative remedies? And how does it show that it has complied with the requirement to give notice to interested parties?

Given our belief that the Tax Court will not allow the IRS's ''no rule'' position to thwart an employer's ability to obtain a declaratory judgment, we would anticipate that in time, the Tax Court will answer these questions, either by decision or by amending its procedural rules.[27] In the meantime, however, employers attempting to seek declaratory judgments will have to fashion their own approach to these issues. For example, to the extent that the IRS has defined the limited circumstances in which a determination letter would be issued for a plan amendment and indicated the procedures to be followed in those circumstances, an employer with a plan amendment falling outside the stated circumstances might consider following those procedures, including requesting that the IRS exercise its discretion to consider the particular plan amendment and giving notice to interested parties in the normal course. To the extent that the IRS has not defined the circumstances in which it will entertain a determination letter on a plan amendment, the employer might consider filing under the procedure for newly adopted plans, including a request that the IRS exercise its discretion to consider the plan as modified by the amendment.

There is the related practical question of what will make up the administrative record if the IRS refuses to act on a determination letter request. As a general proposition, a declaratory judgment case will be decided by the court on the basis of the administrative record associated with the determination letter application, unless the court accedes to a request by the IRS to supplement the record.[28] This means that there will likely be no pretrial discovery and no trial requiring the preparation and presentation of witnesses. It also means that from the employer's standpoint, most of the legwork would have been done by the time it files a petition for a declaratory judgment. Here, it is reasonable to assume that the employer, which initiated the determination letter application and is seeking to bring the process to a favorable conclusion, would have placed in the record its best and most articulate arguments in support of the plan amendments, anticipating any arguments that the IRS might make. The IRS, on the other hand, may choose not to respond substantively to the employer's arguments if the primary basis for its refusal to respond is merely administrative, for example, ''We don't issue determination letters anymore.'' If, during the determination letter process, the IRS fails to engage the employer on the question for which a determination is being requested, the IRS will need to rely on the discretion of the Tax Court to permit its substantive arguments to be added to the administrative record.[29]

Employers will also want to consider how to ensure that the actual controversy requirement is satisfied. The question arises whether the requirement that the employer put the amendment into effect is met if the employer adopts the amendment contingent on approval by the IRS or the Tax Court. As noted above, the fact that the statute treats the reservation of the right to recover contributions if the plan is not qualified as not undermining the effectiveness of the plan's or amendment's adoption, suggests that such a contingency might not defeat the ''actual controversy'' requirement.[30]

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[27]It is too early to predict what the reaction of the Tax Court might be to these practical questions, particularly if there is a significant uptick in declaratory judgment petitions under section 7476 where the IRS has not expressed any view on the qualification of the plan.

[28]*See* Tax Court Rule of Procedure 217(a); *see also Stepnowski v. Commissioner*, 124 T.C. 198, 205-206 (2005), *aff'd*, 456 F.3d 320 (3d Cir. 2006) (applying that rule to a case involving the continuing qualification of a plan).

[29]The employer would be well-advised to make the administrative record as complete as possible, anticipating any possible counterarguments, before petitioning the Tax Court. As noted, the Tax Court may permit the IRS to supplement the record to add its views but may not permit the employer to respond to any arguments raised by the IRS in its supplemental submission but not addressed by the employer.

[30]*See* H.R. Rep. No. 93-779, at 106 (1974) (''In the case of a plan amendment or plan termination, the proposed action by the employer or plan trustee also may be put into effect on a conditional basis.''); *see also* S. Rep. No. 93-383, at 115 (1974). Also, even if the amendment does not include such a condition, there is the possibility that the amendment might still be

**(Footnote continued on next page.)**



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Finally, employers that are considering seeking a declaratory judgment will undoubtedly want to consider the cost of litigation as well as whether doing so would antagonize the IRS. As a general proposition, the cost of pursuing a declaratory judgment in the Tax Court should not be nearly as high as engaging in conventional litigation. And when doing the cost-benefit analysis, it should become apparent that, given the history of section 7476, the Tax Court does not defer unduly to the IRS on qualification issues. As noted above, major employers who have sought a declaratory judgment under section 7476 and have presented well-considered arguments have fared quite well in the Tax Court.

Further, if Announcement 2015-19 is implemented as written, there should be less concern about antagonizing the IRS because seeking a declaratory judgment should not be perceived as seeking to overturn an adverse determination by the IRS. When the IRS refuses to issue a determination letter to an employer sponsoring an individually designed plan, there is no IRS decision to *review* and the Tax Court becomes the *only authority* available to issue a determination on the merits.

## Conclusion

The IRS's recent move to close the determination letter program to ongoing, individually designed retirement plans should motivate employers to reconsider the declaratory judgment benefits afforded by section 7476. If an employer does not wish to amend its individually designed plan without the protection previously afforded by a determination letter, it should consider adopting an approach to place the amended plan before the Tax Court. That approach might entail notifying interested parties and filing a customized request for determination. If the filing were made after Announcement 2015-19 becomes effective, the IRS would likely refuse the request. In that case, it seems that the employer would need only to supplement the administrative record with an explanation for why the amendment would not undermine the plan's qualified status, wait the necessary 270 days, and file a petition. Assuming the IRS remains unbending in its decision not to issue a determination, those steps should give the employer access to the Tax Court's declaratory judgment powers, thus affording the employer an opportunity to protect its plan with a favorable determination.

## Appendix: Tax Court Opinions in Declaratory Judgment Actions

### A. Cases Decided in Favor of the Taxpayer

**1. The Tax Court has sided with the taxpayer on the merits in declaratory judgments cases several times.** *E.g.*, *Sheet Metal Workers*, 117 T.C. 220 (2001), *aff'd*, 318 F.3d 599 (4th Cir. 2002) (holding that COLAs do not constitute accrued benefits, so elimination does not violate anti-cutback rule); *Shedco Inc. v. Commissioner*, T.C. Memo. 1998-295 (rejecting plan disqualification for plan loan to a business that later defaulted, finding that facts and circumstances show that loan violated prudent investor standard but did not rise to a sufficient level of imprudence to violate exclusive benefit rule); *Halliburton Co. v. Commissioner*, 100 T.C. 216 (1993), *aff'd*, 25 F.3d 1043 (5th Cir. 1994) (per curiam) (finding for petitioner on significant partial termination issue); *Calfee, Halter & Griswold v. Commissioner*, 88 T.C. 641 (1987) (finding the plans not disqualified for reversion permitted under ERISA but not the code); *J.G. Kern Enterprises Inc. v. Commissioner*, T.C. Memo. 1987-580 (finding the plan qualified and excusing late amendments when taxpayer, despite ''imperfect action'' concerning determination letter filing, was diligent in attempts to properly comply); *Sutherland v. Commissioner*, 78 T.C. 395 (1982) (rejecting the IRS's determination that petitioner failed coverage requirements because of alleged controlled group); *Francis Jungers Sole Proprietorship v. Commissioner*, 78 T.C. 326 (1982) (agreeing with taxpayer that the IRS adopted an overly restrictive interpretation of exception to impermissible assignment of benefits rules under section 401(a)(13)); *Standard Oil Co. of California v. Commissioner*, 78 T.C. 541 (1982) (rejecting IRS's challenge to taxpayer's alternate method of calculating service); *Del. Valley Anesthesia Associates v. Commissioner*, T.C. Memo. 1982-89 (finding plan qualification requirements satisfied when employers were not members of a controlled group); *BBS Associates Inc. v. Commissioner*, 74 T.C. 1118 (1980) (agreeing with taxpayer's construction of qualified joint and survivor annuity requirement); *Garland, M.D. F.A.C.S. PA v. Commissioner*, 73 T.C. 5 (1979) (rejecting the IRS's attempt to aggregate

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changed retroactively depending on the application of the remedial amendment rules. Reg. section 1.401(b)-1(e)(3) extend the remedial amendment for a case in which the employer files a determination letter request under section 601.201(s) of the Statement of Procedural Rules. In Announcement 2015-19, the IRS has asked for comments on what changes should be made to these regulations. It is possible that under existing or revised regulations, the IRS may adopt an interpretation that does not allow for an extension of the remedial amendment period if an employer attempts to go to the Tax Court in the face of a ''no-rule'' position. How a court might view the IRS's refusal to extend the remedial amendment period in those circumstances is unclear, but as a policy matter, if, in fact, the IRS cannot block outright an employer's ability to seek declaratory judgment relief, it seems anomalous to allow it to obstruct that action at the administrative level by refusing to extend the remedial amendment period for the employer.

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employees of affiliated entities and finding plan qualified); and *Federal Land Bank Association of Asheville v. Commissioner*, 573 F.2d 179 (4th Cir. 1978) (rejecting the IRS's determination that the plan failed the nondiscrimination classification test).

**2. The Tax Court has also decided cases in favor of the taxpayer on procedural issues, dismissing the IRS's arguments that a taxpayer failed to satisfy specific procedural prerequisites under section 7476.** *E.g.*, *RSW Enterprises Inc. v. Commissioner*, 143 T.C. 21 (2014) (holding in a case involving a controlled group issue that when material facts are in dispute, the Tax Court presumes that parties did not intend to restrict court to the administrative record in revocation cases); *Halliburton Co. v. Commissioner*, 98 T.C. 88 (1992) (holding that unresolved section 7805(b) request does not establish taxpayer's failure to exhaust administrative remedies); *Halliburton Co. v. Commissioner*, T.C. Memo. 1992-534 (finding that taxpayer satisfied notice requirement under section 7476 by mailing notice containing all required information to last known address of participants); *Efco Tool Co. v. Commissioner*, 81 T.C. 976 (1983) (finding that taxpayer that received final revocation letter exhausted its administrative remedies because the purpose of the requirement was satisfied despite the fact that the taxpayer failed to perfectly satisfy procedural rules); and *Tipton & Kalmbach Inc. v. Commissioner*, T.C. Memo. 1982-260 (finding that administrative remedies were exhausted when the taxpayer failed to appeal to the IRS Appeals Office before filing for declaratory judgment because the IRS had delayed for 24 months after petitioner made qualification request and ''has attempted to buy time by turning back the administrative clock through the reissuance of an identical proposed adverse determination letter'').

### B. Cases Decided Against the Taxpayer

**1. The Tax Court has sided with the commissioner in cases that generally involve taxpayers using the section 7476 procedures as a last-ditch effort to combat clear errors in plan design or operation.** *E.g.*, *K.H. Co. LLC Employee Stock Ownership Plan v. Commissioner*, T.C. Memo. 2014-31 (upholding the IRS's post-audit decision to disqualify the plan because of the taxpayer's numerous failures); *Churchill Ltd. Employee Stock Ownership Plan & Trust v. Commissioner*, T.C. Memo. 2012-300 (upholding disqualification for failure to timely amend, among other deficiencies); *Michael C. Hollen DDS PC v. Commissioner*, T.C. Memo. 2011-2 (upholding disqualification when the plan, among other deficiencies, failed to timely amend because provisions were not effective by the required date); *Christy & Swan Profit Sharing Plan v. Commissioner*, T.C. Memo. 2011-62 (finding a failure to timely amend, rejecting taxpayer's argument that amending was not necessary because statutory changes did not affect plan operation); *Yarish Consulting Inc. v. Commissioner*, T.C. Memo. 2010-174 (upholding disqualification when taxpayer failed to properly indicate that it was a member of a controlled group on its determination letter application); *Beals Bros. Mgmt. Corp. v. Commissioner*, T.C. Memo. 2001-234, *aff'd*, 300 F.3d 963 (8th Cir. 2002) (finding that employers were members of controlled group and thus failed to satisfy the minimum participation requirement); *Van Roekel Farms Inc. v. Commissioner*, T.C. Memo. 2000-171 (holding that the taxpayer's plan violated specific section 415 limits because the participant was an independent contractor and thus had no ''compensation''); *Westchester Plastic Surgical Assocs. PC v. Commissioner*, T.C. Memo. 1999-369 (upholding plan disqualification for exclusive benefit violation when sole shareholder of taxpayer used plan account as ''a checking account''); *Steel Balls Inc. v. Commissioner*, T.C. Memo. 1995-266, *aff'd*, 89 F.3d 841 (8th Cir. 1996) (finding that employee pretax deferrals are not included in compensation, causing plan to violate section 415 limitations); *Pawlak v. Commissioner*, T.C. Memo. 1995-7 (holding that petitioner failed to timely amend when petitioner failed to exercise reasonable diligence in maintaining the plans); *Ada Orthopedic Inc. v. Commissioner*, T.C. Memo. 1994-606 (upholding disqualification when plan violated exclusive benefic rule for, among other reasons, making exclusively unsecured loans that violated plan terms and not pursuing delinquent payments, allowing plan to be used as ''personal bank account''); *Hamlin Development Co. v. Commissioner*, T.C. Memo. 1993-89 (upholding revocation of plan for noncompliance with TEFRA when no attempt to amend was made); *Mills, Mitchell & Turner v. Commissioner*, T.C. Memo. 1993-99 (finding plan disqualified because of late amendments when the taxpayer failed to use reasonable diligence in obtaining a determination letter); *Kollipara Rajsheker MD Inc. v. Commissioner*, T.C. Memo. 1992-628 (upholding disqualification for late amendments because of taxpayer's lack of diligence and fact that IRS did not contribute ''in any way'' to the delay); *Stark Truss Co. v. Commissioner*, T.C. Memo. 1991-329 (upholding disqualification when taxpayer attempted to rely on careless and piecemeal earlier-in-time plan document as proof of timely compliance amendments); *Basch Engineering Inc. v. Commissioner*, T.C. Memo. 1990-212 (upholding disqualification of the plan for failure to timely amend); *Peter M. Boruta MD PC v. Commissioner*, T.C. Memo. 1988-172 (rejecting the taxpayer's good-faith defense to partial termination issue because of the substantial quantity of employees terminated and specific evidence suggesting potential bad faith); *Pecora v. Commissioner*, T.C. Memo. 1988-104

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(dismissing the taxpayer's defense that specific nondiscrimination requirements, which its plans failed, were unconstitutional); *Professional & Executive Leasing v. Commissioner*, 89 T.C. 225 (1987) (upholding disqualification of the plan because workers were not employees of the company); *William Bryen Co. v. Commissioner*, 89 T.C. 689 (1987) (upholding the IRS's determination that taxpayer's advance contributions disqualified plan); *Feichtinger v. Commissioner*, 80 T.C. 239 (1983) (upholding disqualification for improper actuarial assumptions when taxpayer ''took the risk of disregarding the revenue ruling''); *Seekonk Lace Co. v. Commissioner*, T.C. Memo. 1983-127 (upholding disqualification when data revealed significant plan discrimination in favor of highly compensated employees); *Gross Distrib. Co. v. Commissioner*, T.C. Memo. 1982-264 (upholding disqualification when the taxpayer was on notice of qualification issues and took no action); *Fujinon Optical Inc. v. Commissioner*, 76 T.C. 499 (1981) (rejecting the taxpayer's position that all members of controlled group need not be grouped for purposes of section 410(b) antidiscrimination provisions); *Ralph Gano Miller PLC v. Commissioner*, 76 T.C. 433 (1981) (approving stock bonus plan regulations as consistent with congressional intent and finding the plan in violation); *G&W Leach Co. v. Commissioner*, T.C. Memo. 1981-91 (upholding disqualification of the plan when there was scant evidence of a written plan and no qualified trust); *Trustees of the Taxicab Industry Pension Fund v. Commissioner*, T.C. Memo. 1981-651 (upholding disqualification of the plan when the plan failed to provide a nonforfeitable vested benefit at normal retirement age); *Tamko Asphault Prods. Inc. of Kan. v. Commissioner*, 71 T.C. 824 (1979), *aff'd*, 658 F.2d 735 (10th Cir. 1981) (addressing issue of rapid turnover discriminating in favor of longtime employees and highly compensated because they would benefit from substantial forfeiture allocations); *Oakton Distribs. Inc. v. Commissioner*, 73 T.C. 182 (1979) (upholding retroactive revocation when the taxpayer misstated a material fact in its determination letter application); *Caterpillar Tractor Co. v. Commissioner*, 72 T.C. 1088 (1979) (rejecting taxpayer's ''semantical analysis'' of section 411(a) in finding the plan disqualified); *Automated Packaging Sys. Inc. v. Commissioner*, 70 T.C. 214 (1978) (rejecting the taxpayer's arguments, including its argument that the Department of Labor lacked authority to define ''year of service,'' stating that cited evidence constituted mere opinions); and *Hill, Farrer & Burrill v. Commissioner*, 67 T.C. 411 (1976) (finding plan disqualified because of the existence of ''owner-employees,'' although several judges supported the taxpayer's position).

**2. The Tax Court has also refused jurisdiction under section 7476 because of various procedural failings on the part of the taxpayer.** *E.g.*, *Calvert Anesthesia Associates v. Commissioner*, 110 T.C. 285 (1998) (refusing jurisdiction when the taxpayer, which must file a declaratory judgment suit no later than 91 days after the issuance of a final revocation letter, sued 94 days after such an issuance); *Clawson v. Commissioner*, T.C. Memo. 1993-174 (finding a failure to exhaust administrative remedies when the taxpayer did not appeal to the Appeals Office or request that the matter be referred to the IRS National Office); *Dr. Erol Bastug Inc. v. Commissioner*, T.C. Memo. 1989-262 (refusing jurisdiction when no reason excused the taxpayer's failure to properly raise evidence in time for it to enter the administrative record); *Sack v. Commissioner*, 82 T.C. 741 (1984) (dismissing case because the taxpayer requested a ruling on proposed amendments, which were not ''put into effect'' for purposes of jurisdictional requirements); *Steffen Insurance Agency Ltd. v. Commissioner*, T.C. Memo. 1981-276 (refusing jurisdiction when parties who could have ''easily'' been notified were not given notice, but explaining that the individual with the greatest interest in the plan had alternate recourse available); *Shut Out Dee-Fence Inc. v. Commissioner*, 77 T.C. 1197 (1981) (refusing jurisdiction on practical grounds because the taxpayer had access to judicial review through other means); *McManus v. Commissioner*, 93 T.C. 79 (1981) (finding a failure to exhaust administrative remedies when the taxpayer's representative knew the plans were defective yet remained uninvolved, neglecting to correct them throughout application process, leading to the plan's failure to qualify); *Prince Corp. v. Commissioner*, 67 T.C. 318 (1976) (finding a failure to exhaust administrative remedies even though more than 300 days had elapsed since filing for determination letter when the IRS had not acted in an unusually dilatory fashion); and *Sheppard & Myers Inc. v. Commissioner*, 67 T.C. 26 (1976) (refusing jurisdiction based on section 7476 legislative history when the plan was not amended or terminated, and thus did not satisfy statutory requirements for jurisdiction).

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