

*Plan Corrections: The
Employee Plans Compliance
Resolution System ("EPCRS")*

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Agenda

- EPCRS Update
- Plan Correction Issues

EPCRS Revenue Procedure

- Expected update to the Revenue Procedure
 - Sometime in 2010?
 - Primary Purpose: Update to reflect the written plan requirement under the final 403(b) regulations

Rev. Proc. 2008-50

Comments Requested

- 401(k) automatic enrollment
- Failure to provide safe harbor notice
- Designated Roth contributions

Availability of EPCRS or other correction programs for:

- What is the availability of EPCRS or other correction programs for:
- 457(b) eligible governmental plans
- 457(b) plans sponsored by tax exempt employers
- 5500 EZ non filers

EPCRS Programs

(Rev. Proc. 2008-50)

- EPCRS consists of three correction programs
 - Self-Correction Program (SCP)
 - Voluntary Correction Program (VCP)
 - Audit Closing Agreement Program (Audit CAP)

Correction Principles *ref: §6 of Rev. Proc. 2008-50*

- Full correction includes all taxable years, whether or not the taxable year is closed
- The correction method should restore the Plan and its participants to the position they would have been in had the failure not occurred.
- The correction should be reasonable and appropriate for the failure.
 - Appendix A/B - correction deemed to be reasonable
 - Other: Consistency with the IRC; provide benefits to NHCEs; keep assets in plan; **Consideration of corrections approved by another govt. agency (e.g., DOL's reg. for abandoned plans (new))**

SCP- Determining eligibility

- Employer sponsors a 401(k) plan and would like to use SCP to correct violations of compensation limits [§401(a)(17)] and the ADP test. The failure occurred for 6 years. Does the fact that the failure occurred for 6 years mean that the failure is significant?
- Consider: (1) Type of failure; Practices and Procedures before significance
- (2) Evaluate Factors
- Document rationale

SCP: Administrative practices

- Employer sponsors a 401(k) profit sharing plan. At the end of the year, employer makes a full profit sharing contribution and returns excess elective deferrals after the year end. This ensures that the participant keeps as much of employer contribution as possible.
- Does the plan have practices and procedures to ensure compliance with Code? **No. By design, plan violates 415 first and then corrects.**
- Is the plan now ineligible to correct the failure under SCP? **Yes. Plan does not have practices and procedures to facilitate compliance with Code requirements.**
Suggested alternative: Adjust P/S contributions and allocations at year end to ensure compliance with 415.

Failure to file a DL application on-cycle.

- Is VCP available to address the plan sponsor's failure to file an on-cycle DL application?
- No. The failure by a plan to file a DL application in its scheduled on cycle year is not a qualification failure that can be addressed under VCP.

Correction by Plan amendment under VCP and Determination Letter (DL) submissions. DL SUBMISSION REQ'D

- Nonamender failures
- Operational/demographic failures corrected by plan amendment and submission is made during the plan's on-cycle year
- Exception: Correction made by adoption of preapproved document with current opinion or advisory letter; IRS model amendment

Correction by Plan amendment under
VCP and DL submissions.

DL SUBMISSION NOT REQ'D

- Interim, discretionary amendments corrected using App. F schedule 1
- Operational/demographic failures corrected by plan amendment and submission is made in an off-cycle year.

Nonamender for GUST and EGTRRA (e.g. Cycle A).

- **Can correction be accomplished by retroactively adopting a single EGTRRA compliant document ? Or does the plan sponsor need to adopt two documents- a GUST compliant document and an EGTRRA compliant document?**
- **Adopting an EGTRRA compliant document alone would not be sufficient.**
- **The EGTRRA compliant document would not comply with applicable rules during the years that GUST was in effect.**
- **Possible correction options:**
 - **(1) Adopt a GUST compliant document, effective for years in which GUST rules applied and an EGTRRA compliant document for years in which EGTRRA rules took effect.**
 - **(2) Adopt a single document that includes GUST provisions for applicable years and EGTRRA provisions for applicable years.**

Failure to adopt good faith EGTRRA amendments before the expiration of the plan's extended remedial amendment period.

- Can a Cycle C plan submit a VCP application using App. F sch. 1 (\$375 fee) to address the failure to adopt good faith EGTRRA amendments?
- The issuance of a compliance stmt using App. F sch. 1 results in the corrective amendment being treated as if it had been timely adopted for purposes of determining the availability of the extended RAP.
- Cycle C extended RAP expired on January 31, 2009. The failure may no longer be limited to the failure to adopt interim amendments. The plan would be a nonamender for EGTRRA.
- Use App. F schedule 2 to address nonamender problem. 50% discount on regular VCP fee schedule may apply if submission made within one year of expiration of the extended RAP.

Exclusion of eligible employee

- Facts
- Plan year ends on December 31. Employee became eligible to participate in the 401(k) plan on April 1. The employee was provided with the opportunity to make elective deferrals on June 1. Upon entry, the employee elects to defer 5% of compensation.

Exclusion of eligible employee contd.. (Q/A 1)

- Q 1. Can we assume that the employee would have elected to defer 5% of comp. for the period April 1 through May 31?
- No. We would not look at elections made after the period of exclusion to estimate what a person would have deferred during the period of exclusion. Use ADP to estimate employee's deferrals for period of exclusion.

Exclusion of eligible employee contd... (Q/A 2)

- Q 2. Can we assume that no correction is required, since the participant's exclusion is similar to the situation described in the brief period of exclusion provision in App. B section 2.02(1)(a)(ii)(F)?
- No. The brief period of exclusion provision cannot be adapted to other situations. In this case, the employee will not have at least 9 months remaining in the plan year to make elective deferrals up to the maximum amount allowed under the terms of the plan.

Correction for failure to provide notice in a safe harbor 401(k) plan?

- Depends on the impact on individual participants.
 - If failure to provide notice results in an employee not being able to make elective deferrals to the plan, then the failure to provide notice would result in the erroneous exclusion of an eligible employee. Corrective contributions on behalf of the employee would be required.
 - If employee otherwise informed and able to make elective deferrals, then correction may involve revising practices and procedures going forward.

Correction for failure to implement automatic enrollment provisions?

- Rev. Proc. 2008-50 asked for comments.
- Some ideas:
 - Correction would be determined by cause of failure.
 - Example: Failure occurred because the eligible employee did not receive enrollment materials. The employee was effectively excluded when eligible. Correction would be similar to the method of correction for erroneously excluded employees (i.e. use of ADP to determine missed deferral).

Correction for failure to implement automatic enrollment provisions?

Contd..

- Example: Failure occurred when employee received enrollment materials, and did not make an affirmative election. The employee is deemed to make an election equal to the plan's automatic enrollment percentage. However, payroll did not withhold any amounts from employee's pay check. Correction is similar to the failure to implement employee's election (in this case the automatic enrollment percentage)

Participant Loans: 72(p) relief for owner participants?

- Appendix F schedule 5 is not available for VCP applications in cases where the affected participant is also the owner of the business. Does this mean 72(p) relief is not available for an owner?
- No. But more facts are needed before a decision can be made. These could include answers to questions such as: Was the loan itself a bonafide loan? Or is it a withdrawal that is being recharacterized as a loan? Were there reasonable attempts to make payments on the loan? How long did the problem occur before attempts at correcting the missed payments were made? Why did the problem occur and what steps are being taken to ensure that the problem does not occur again?
- These details can be addressed in a VCP application using the format under Appendix D in Rev. Proc. 2008-50.

Defaulted Loan- Employer payment

- Section 6.02(6) of Rev. Proc. 2008-50 states that if a loan is being corrected under EPCRS, the employer should pay the portion of the correction payment equal to the interest that accumulates as a result of the failure. When is employer payment required?

Defaulted Loan- Employer payment contd..

- Participant's responsibility to make payments on the loan- both principal and interest. However, employer payments could be required under certain circumstances e.g.:
 - Failure occurred because of employer actions
 - Rate of return on plan investments exceeded plan loan rate.

Defaulted Loan.. Reamortization correction

- If a defaulted loan is being corrected under EPCRS through reamortization, is it permissible to use an interest rate that is different from the interest rate used at the time the loan was made?
- Assuming the interest rate on the loan complied with plan terms at the time the loan was made, it is expected that the correction would be made using the interest rate on the loan.

Failure to suspend deferrals

- 401(k) plan provides that upon receiving a hardship distribution, the participant is prohibited from making elective deferrals for 6 months. In operation, plan fails to suspend deferrals. Correction?

Failure to suspend deferrals contd..

- Option 1- Can plan return the improper elective deferrals (adjusted for earnings) to employee? **Yes.** This would put the participant in the same position he or she would have been in had failure not occurred.
- Option 2- Can plan suspend elective deferrals for a six month period going forward? **Possibly.** However, this may not put the participant in the same position. E.g. Matching contribution levels for the six month period going forward could be different than what they were during suspension period. Participant may quit employment before expiration of 6 month period.

Failure to suspend deferrals contd..

- Option 3- Take no action. Revise administrative procedures going forward? No. The failure will not have been corrected.

Use of forfeitures to make corrective QNECs

- Can a plan use forfeitures to make QNECs for correcting a failed ADP test?
- No. See QNEC definition in IT Reg. 1.401(k)-6. It requires that the QNEC come from nonelective contributions that satisfy vesting (100%) and distribution requirements under 401(k) when contributed to the plan. Forfeitures are derived from contributions that were not fully vested when made.
- Will the Service permit the use of forfeitures to provide for the employer contribution in the case of:
 - Employees improperly excluded from making elective deferrals to the 401(k) plan? Yes, if employee is fully vested and the 401(k) distribution restrictions apply when the contribution is allocated.

Web resources

- Visit www.irs.gov/ep and click on “Correcting Plan errors”. See:
 - Fillable VCP applications (e.g. App. F, related schedules)
 - Revenue Procedure 2008-50
 - Links to fix it guides [401(k), SIMPLE, SEP]
 - Articles on current issues (see article on Nonamenders and Voluntary Correction Program); Questions and Answers; Top 10 failures etc.

Web resources contd..

- Visit www.irs.gov/ep and click on Newsletters. You can subscribe electronically to Employee Plan News and Retirement News for Employers. Also view past issues.
- Retirement News for Employers has a section entitled “Fixing Common Plan mistakes”. See for example, article on failure to implement automatic enrollment provisions in the Summer 2009 issue. Or you can browse the archives and see for example, article on the failure to provide safe harbor notice in the Fall 2008 issue.

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- Questions?