

*Plan Corrections: Update on the
Employee Plans Compliance
Resolution System ("EPCRS")*

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Agenda

- EPCRS Overview
- Changes in the new revenue procedure: Rev. Proc. 2008-50

EPCRS Revenue Procedure

- Revenue Procedure 2006-27 is the current applicable document for EPCRS
- Revenue Procedure 2008-50 will supersede Rev. Proc. 2006-27 on January 1, 2009
- Optional use of Rev. Proc. 2008-50 from Sept. 2, 2008

EPCRS Programs

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

Types of Plans covered

- Qualified plans under IRC § 401(a)
- 403(b) plans
- SEPs and SARSEPs under IRC § 408(k)
- SIMPLE IRAs under IRC § 408(p)
- Eligible governmental IRC § 457(b) plans (outside of EPCRS)

EPCRS Objectives

- For qualified plans
 - Continued qualification of the plan under IRC § 401(a)
- For 403(b) plans, SEPs, and SIMPLE IRAs
 - Continued compliance with the provisions of IRC §403(b), 408(k), or 408(p), as applicable

Other possible goals

Excise/Income tax relief:

Income tax items - § 72(p) (EXPANDED),
72(t) (NEW)

Excise tax items - § 4972, 4973 (NEW),
4974, 4979

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))**

Rev. Proc. 2008-50 New items

Participant Loans

- Relief from reporting loans as deemed distributions under § 72(p). 72(p) provisions do not need to be in the plan. §4.01 Rev. Proc. 2008-50
- 50% reduction in VCP fee in certain instances (loan failure is sole failure; no more than 25% of employees affected in each year of the failure) §12.02(3) Rev. Proc. 2008-50
- Streamlined VCP application procedure available under certain circumstances. App. F & related Sch. 5 Rev. Proc. 2008-50; §11.03 RP 2008-50
- Provision for resolution of failure under Audit CAP. MPA increases. §§13.01, 14.01 Rev. Proc. 2008-50

Rev. Proc. 2008-50 New items

Availability of SCP

- Liberalized criteria for “substantial completion of correction” for significant failures, increasing potential for use of SCP § 9.04 of Rev. Proc. 2008-50
 - For criterion #1 - Correction can be completed within 120 days after the end of the correction period (previously limit was 90 days)
 - For criterion #2 - Correction with respect to 65% of the plan’s participants should have been completed by the end of the correction period. (previously correction for 85% of participants was required)

Rev. Proc. 2008-50 New items

Exclusion of Eligible Employees

- Failure to implement employee elections *App. A .05(5) Rev. Proc. 2008-50; Ex. 12 App. B*
 - Use employee's elected deferral percentage instead of ADP
- Failure to permit eligible participants to make catch-up contributions *App. A .05(4) Rev. Proc. 2008-50; Ex. 11 App. B*
 - Assume participant would have made catch-up contribution equal to half of the catch-up contribution limit
- Exclusion of employee from plan that also provides the employee with the ability to designate elective deferrals as Roth contributions. *App. A .05(3) Rev. Proc. 2008-50*
 - QNEC = 50% x ADP correction unchanged; Also does not change corrections for failure to implement employee elections; catch-up contributions. QNECs not treated as Roth contributions

Failure to implement employee election example

Amy's elective deferral election at the start of 2006 somehow was never processed by the employer's payroll system. As a result, Amy (a NHCE) received taxable compensation amounts that should have been contributed to the plan during the first six months of the year.

The facts in this situation include:

- plan's actual deferral percentage (ADP) for NHCEs of 5%
- Amy's election form agreeing to a deferral of 10% of pay
- Amy's compensation of \$20,000 for the six months that no deferrals were made.

Failure to implement employee election example contd.

- Correction:

- (1) Use Amy's elected deferral percentage (10%). Not ADP (5%);
 - (2) 50% factor applies. Replacing deferral opportunity not actual dollar amounts.
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- QNEC for MISSED DEFERRAL OPPORTUNITY=
50% x MISSED DEFERRAL (10% x \$20K)
= 50% x \$2,000 = \$1,000 (adjusted for earnings)

Failure to permit eligible ee to make catch-up contribution example

USG Inc. maintains a 401(k) plan. Plan permits employees to defer the maximum amount allowable under § 402(g). Plan also provided for catch-up contributions. In 2006, Mary, an employee age 55, made elective deferrals totaling \$15,000. Mary was not provided with the opportunity to make catch-up contributions. [2006 402(g) limit = \$15,000; catch-up contribution limit = \$5,000]

Failure to permit eligible ee to make catch-up contributions example contd.

- Mary's missed deferral on account of the plan's failure to offer the opportunity to make catch-up contributions is \$2,500 (or one half of the limitation on catch-up contributions for 2006)
- Mary's missed deferral opportunity is \$1,250 (or 50% of \$2,500)
- Required QNEC for Mary's missed deferral opportunity relating to catch-up contributions in 2006 is \$1,250 adjusted for earnings

Roth contribution question

Would our corrections in the examples above change, if the plan also provides employees with the ability to designate all or a portion of their elective deferrals as Roth contributions?

Roth contribution answer

- No change to the corrective QNEC
- The corrective QNEC cannot be contributed or allocated to a Roth account
- When corrective QNEC is distributed, it is taxable to the employee

Rev. Proc. 2008-50 New items

Excess Allocations *(ref: §6.06;5.01(3) of Rev. Proc. 2008-50)*

Provision of correction mechanism for excess allocations in cases where code/regs. do not provide for a specific method of correction (e.g., plan limits):

- Excess employer contribution:
 - Correction mechanism based on plan provisions.
 - Reallocation among other participants; OR
 - Reallocation to unallocated account to be used to reduce Employer contributions
- Excess elective deferrals or after-tax employee contributions:
 - Distribute excess (plus earnings) to employee. Report as income in year of distribution. See section 3 of Rev. Proc. 92-93.
- 415 ordering rules

Excess Allocations (Plan terms) example

Plan limits deferrals to 15% of comp. In 2007, Jane defers 20% of comp. Excess deferral is \$1,000. Could the plan sponsor:

- (a) Forfeit the \$1,000 from Jane's account and compensate Jane outside of the plan?
- (b) Transfer \$1,000 to an unallocated account and credit it towards Jane's 2008 deferral? (s.t. 2008 limits)
- (c) Distribute the \$1000 (adj for earnings) in 2008 and report on 1099-R for 2008, as if it was a returned excess ADP / 415 excess deferral for 2008?

Answer: (c)

Rev. Proc. 2008-50 new items

Excess Allocations (415 limits)

If annual additions include after-tax employee contributions, elective deferrals, employer contributions correction should be made in the following order:

- Unmatched after-tax employee contributions, elective deferrals;
- Matched after-tax employee contributions, elective deferrals and forfeiture of related match
- Forfeiture of other employer contributions

Excess Allocations 415 limits example

2006 415 limit on annual additions for Richard: \$44,000. Plan provides for 100% match of first \$7,000 deferred.

2006 Elective Deferral:	\$15,000
Matching Contribution:	\$ 7,000
Profit-sharing contribution:	\$35,000
2006 annual addition:	\$57,000
Excess annual addition:	\$13,000

Excess Allocation 415 limits example

\$13,000 excess annual addition is corrected by?

- a) Distributing \$13,000 from elective deferrals; OR
- b) Distributing \$6,500 from elective deferrals and forfeiting \$6,500 from matching contributions; OR
- c) Distributing \$10,500 from elective deferrals and forfeiting \$2,500 from matching contributions; OR
- d) Forfeiting \$6,000 in profit sharing contributions and \$7,000 from matching contributions

Excess Allocation 415 limits

Correct answer (c).

- (1) First distribute unmatched elective deferral. \$8,000. (Only first \$7,000 matched. Total deferral \$15,000. Unmatched amount \$8,000)
- (2) Amount of excess remaining \$5,000. Distribute \$2,500 elective deferral and forfeit corresponding match of \$2,500.
- (3) Total elective deferral distributed: \$10,500. Match forfeited: \$2,500.

Rev. Proc. 2008-50 New items Determination Letter submissions

- Submission Required
 - Nonamenders (VCP and Audit CAP)
 - On-cycle corrections by plan amendment (VCP and Audit CAP)
 - SCP corrections by plan amendment to be submitted in next determination letter cycle
- Submission not required
 - Correction of interim amendments, discretionary amendments relating to optional law changes prior to expiration of cycle
 - Off-cycle corrections by plan amendment (VCP and Audit CAP)
Note - amendments to be submitted in next determination letter cycle
- Submission optional
 - Situations described in section 14.02 or 14.03 of Rev. Proc. 2007-44 e.g. urgent business need

Rev. Proc. 2008-50 New items DOL VFCP online calculator

VFCP online calculator can be used to calculate earnings adjustments in situations where it is not feasible to determine an actual earnings adjustment. This may occur because either:

- Actual data cannot be obtained or
- The probable difference in the use of actual data, instead of the estimate, is small and the cost associated with obtaining actual data would exceed the probable difference.

See § 6.02(5)(a) of Rev. Proc. 2008-50

Rev. Proc. 2008-50 New items Distribution of small amounts

- If the total corrective distribution is \$75 or less, the plan sponsor is not required to make a corrective distribution if the reasonable direct costs of processing and delivering the distribution to the participant or beneficiary would exceed the amount of the distribution (previously distribution amount was \$50 or less)

See §6.02(5)(b) of Rev. Proc. 2008-50

Rev. Proc. 2008-50 New items

VCP: IRC 4973 relief

- IRS may agree not to pursue IRC 4973 excise tax if improper rollovers to IRA are returned (with earnings) to plan; or in certain cases (e.g., excess elective deferrals) distributed (with earnings) to the employee *see §6.09(5) of Rev. Proc. 2008-50*
- Relief must be requested *see §6.09(5) of Rev. Proc. 2008-50*
- Rev. Proc. provides relief from IRC 4973 when an ineligible employer failure is corrected under VCP. *see §6.03(4) of Rev. Proc. 2008-50*

Rev. Proc. 2008-50 New items

VCP: IRC 72(t) relief

- IRS may agree not to pursue additional income tax under IRC 72(t) if amounts distributed, in the absence of a distributable event, are returned (with earnings) to the plan.
- Relief must be requested.

Ref: §6.09(6) of Rev. Proc. 2008-50

Rev. Proc. 2008-50 New items Comments requested

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

Ref: §2.02 of Rev. Proc. 2008-50

Rev. Proc. 2008-50 New items Streamlined VCP application procedures

Appendix F:

Schedule 1 - Interim amendments or discretionary amendments relating to the implementation of optional law changes.

Schedule 2 - Other nonamender failures

Schedule 3 - SEPs/SARSEPs

Schedule 4 - SIMPLE IRAs

Schedule 5 - Loan failures

Schedule 6 - Ineligible employer failure: 403(b) or 401(k) plan

Schedule 7 - Elective deferrals in excess of § 402(g)

Schedule 8 - Failure to make required minimum distributions under §401(a)(9)

Schedule 9 - Failures corrected by plan amendments allowable under SCP

Appendix D - Sample format for submissions not covered by

Appendix F

Submission choices: Streamlined VC submissions

- Appendix F streamlined procedures. Employer can complete Appendix F and applicable schedules. Appendix F includes enforcement resolution. If good - IRS can complete and execute the enforcement resolution in Appendix F. Compliance stmt. would consist of completed Appendix F and applicable schedules.
- IRS can request additional information
- IRS can issue streamlined/ nonstreamlined compliance statements, if the App. F itself does not work.

Also see §11.03 of Rev. Proc. 2008-50

Submission choices: Non streamlined VC submissions

- Use Appendix C and submit all items required under Appendix C.
- If Appendix D used, Part I of Appendix C need not be completed.
- Some of the items in the checklist (e.g., narrative of failures, proposed corrections, revisions to admin. procedures) will be satisfied when Appendix D is used.
- The Appendix D includes an enforcement resolution. If good - IRS can complete and execute the enforcement resolution. Appendix D (incl. executed enforcement resolution) would be the compliance statement.
- App. D: Streamlined/Nonstreamlined compliance stmts can still be issued. Supplemental information requests can still be made.

Also see § 11.02 of Rev. Proc. 2008-50