

August 19, 2008

IRS Enhances Voluntary Correction Program for Retirement Plans

On September 2, 2008, the IRS will publish [Rev. Proc. 2008-50](#), updating and expanding the voluntary correction program for qualified retirement plans. This latest version of the Employee Plans Compliance Resolution Program (EPCRS) is effective January 1, 2009, though plan sponsors can elect to apply the new EPCRS as soon as September 2, 2008.

The new EPCRS retains the basic structure (and plethora of acronyms) of its predecessor, Rev. Proc. 2006-27. The program continues to have a self-correction program (SCP) available for minor errors and more significant, recent errors; a voluntary submission program (VCP) involving a submission to the IRS and a fixed fee for errors that cannot be corrected through SCP; and a correction program for errors discovered by the IRS on audit (Audit CAP).

Change and Enhancements. Rev. Proc. 2008-50 makes a number of technical revisions to Rev. Proc. 2006-27. The changes are mainly enhancements or expansions of the prior version of EPCRS. Some of the more significant changes include the following:

- Previously, if an employee elected a deferral percentage or dollar amount in a 401(k) plan, but the election was not actually implemented, the only correction method specified was for the employer to make a contribution to the employee's account based on 50% of the Average Deferral Percentage (ADP) of the group (non-highly compensated or highly compensated) to which the employee belonged. Many practitioners felt this correction was inappropriate because the employee's actual election provides evidence of what the affected employee wanted to elect. Apparently recognizing this inconsistency, the IRS added a new correction method in Rev. Proc. 2008-50 providing for an employer contribution equal to 50% of the amount elected by the employee but not contributed.
- The new version of EPCRS expands the correction method for the exclusion of eligible employees from a 401(k) plan to take into account catch-up contributions and Roth contributions.
- The prior version of EPCRS required that earnings rates for corrections generally had to be based on returns for plan investments, which is often one of the most complicated and expensive parts of making a voluntary correction. The prior version of EPCRS generally permitted reasonable estimates of investment returns in some situations, but this still required obtaining enough information regarding plan investment returns to enable an estimate. Finally, the prior version of EPCRS provided that if it is not feasible to make a reasonable estimate of investment returns, a "reasonable interest rate" may be used. The new version of EPCRS retains all of these rules, but also adds a specific statement that for purposes of the "reasonable interest rate," the Department of Labor's Online Calculator for interest in connection with its Voluntary Fiduciary Correction Program would be deemed to be reasonable. While many plan sponsors were hoping to be able to use the DOL's (DOL) Online Calculator in any situation, regardless of whether precise calculations or reasonable estimates of actual returns are feasible, the IRS did not go down that path.
- The new version of EPCRS increases the de minimis rule under which correction may not be necessary for individual corrective distributions from \$50 to \$75 per participant. Unfortunately, there continues to be no formal de minimis rule with respect to corrective contributions.

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- It is frequently the case that a plan error, such as an overpayment to a participant, results in the participant receiving a distribution and rolling over the amount into an IRA. Because the amount was improperly distributed from the plan, it is not eligible for rollover, and would generally be subject to the 6% penalty tax under section 4975 of the Internal Revenue Code for excess contributions to an IRA. The new version of EPCRS provides rules under which the 6% penalty tax would not apply, provided the participant removes the improperly rolled over amounts from the IRA.
- The prior version of EPCRS included reduced fees and streamlined application procedures for certain failures to amend plans on a timely basis. The new version of EPCRS significantly expanded the streamlined application procedures to include additional types of failures to amend (including for optional law changes), certain SEP and SIMPLE IRA failures, certain plan loan failures, certain failures related to employers adopting plans that they were not eligible to adopt, 402(g) failures and minimum required distribution failures. The fee for most plan loan failures is also reduced to 50% of the otherwise applicable fee. The streamlined procedures and reduced fees may make a plan loan correction through a VCP submission significantly more attractive than it had been previously.

Request for Comments. Rev. Proc. 2008-50 indicates that the IRS intends to continue enhancing EPCRS over time (as has been mandated by the Pension Protection Act), and the IRS invites comments on EPCRS generally. The IRS also specifically asks for comments in the following areas:

- Section 401(k) automatic enrollment, including the failure to implement automatic enrollment for a plan that provides for it, and the failure to provide a safe harbor notice for various types of safe harbor plans.
- Roth contributions, including methods of correction for Roth contributions improperly made on a pre-tax basis, and the failure to notify employees of their right to make Roth contributions in a plan that allows such contributions.

Also, the IRS has previously suggested that it may incorporate into EPCRS additional corrections for section 403(b) programs to reflect the July 2007 final regulations, which were not included in this update.

Scope of SCP and VCP. With the enhancements and subject to the conditions and procedures specified in Rev. Proc. 2008-50, the following plan failures are generally eligible for correction under the SCP and VCP.

Defect	401(a)		403(b)	SEP/ SIMPLE
	Program	Standard correction		
Operational failure				
Insignificant operational defect	SCP	Varies with defect	SCP	SCP
Recent, significant operational defect:				
Related to plan assets transferred in corporate combination in prior plan year	SCP	Varies with defect	SCP	VCP
ADP/ACP violation in prior two plan years following 401(k)/(m) 12-month correction period	SCP	Varies with defect	SCP	VCP

Defect	401(a)		403(b)	SEP/ SIMPLE
	Program	Standard correction		
Other significant operational defect in prior two plan years	SCP	Varies with defect	SCP	VCP
Significant operational defects not covered above:				
Minimum top-heavy contribution/benefit	VCP	Make minimum contribution/accrual for non-key employees	N/A	N/A
ADP test	VCP	Make QNEC	VCP	VCP
Universal availability			VCP	
ACP test	VCP	Make QNEC	VCP	VCP
Undistributed §402(g) excess deferrals	VCP	Distribute/report as taxable	VCP	VCP
Improperly excluded employees:				
Employer provided contributions/benefits	VCP	Make contribution/accrual	VCP	VCP
Elective/catch-up/Roth contribution; failure to implement employee election	VCP	Make QNEC = 50% missed deferral (or 100% of safe harbor contribution as applicable)	VCP	VCP
After-tax contribution	VCP	Make QNEC = 40% missed contribution	VCP	VCP
Matching contribution	VCP	Make QNEC keyed to correction above	VCP	VCP
Required minimum distribution	VCP	Make distribution	VCP	VCP
Participant/spousal consent	VCP	Consent to actual distribution or receive QJSA	N/A	N/A
§415 limit/DC plan	VCP	Prior to 2009: move excess to unallocated account. After 2008: credit to other participants or move to unallocated account	VCP	N/A
Other failure to follow terms of plan	VCP	Varies depending on failure	N/A	N/A
Distribution restrictions (403(b)(7) or 403(b)(11))	N/A	N/A	VCP	N/A
Incidental death benefit rule (403(b)(10))	N/A	N/A	VCP	N/A
Direct rollover rules	N/A	N/A	VCP	N/A
Other §403(b) qualification failures	N/A	N/A	VCP	N/A
Demographic failure				
Nondiscrimination defect that is not an operational failure	VCP	Corrective plan amendment adding new benefits or enhancing existing benefits	VCP	N/A
§410(b) coverage	VCP		VCP	N/A
§401(a)(26) participation	VCP		VCP	N/A
Employer eligibility failure				
Adoption of §401(k)/403(b) plan by ineligible employer	VCP	Cessation of all contributions and distribution upon an applicable event	VCP	VCP
§401(g) nontransferability requirement	N/A	N/A	VCP	N/A

Defect	401(a)		403(b)	SEP/ SIMPLE
	Program	Standard correction		
Failure to establish/maintain §403(b)(7) custodial account	N/A	N/A	VCP	N/A
Failure to purchase appropriate §403(b) vehicle	N/A	N/A	VCP	N/A
Plan document failure				
Plan provision that violates §401(a)/403(a) or is not timely amended for change in law	VCP	Varies depending on failure	N/A	VCP
Plan loans				
Loan in excess of §72(p) limit	VCP	Repay excess to plan	VCP	N/A
Incorrect repayment schedule	VCP	Reamortize over remaining repayment period	VCP	N/A
Defaulted loan	VCP	Repay defaulted installments or reamortize remaining balance over remaining repayment period	VCP	N/A



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