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IRS Issues New EPCRS Revenue Procedure

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On August 14, 2008, the IRS issued Revenue Procedure 2008-50 (the Procedure) (<http://www.irs.gov/pub/irs-drop/rp-08-50.pdf>), the updated procedure for resolving plan compliance failures under the Employee Plans Compliance Resolution System (EPCRS). The Procedure, which has plenty to love and some parts to at least dislike, is effective on January 1, 2009. However, a taxpayer may choose to make submissions under the Procedure anytime on or after September 2, 2008.

▲ What's New and Good

Simplified Submissions Including Expanded Streamlined Procedure under Appendix F. The Procedure simplifies submissions under the Voluntary Compliance Program (VCP) by providing formats to use for the submission. Appendix C to the Procedure is an updated VCP checklist; Appendix D is a normal VCP submission form; and Appendix F is an expanded streamlined submission form.

The expanded use of Appendix F is a clear advantage of the Procedure. Under the old EPCRS, the Appendix F process was available only for plans that failed to adopt interim amendments between GUST and EGTRRA. The Procedure now permits use of this streamlined process for:

- All nonamendment failures, including interim mandatory and optional amendments, as well as failures to restate (going all the way back to ERISA),
- Plan loan failures related to exceeding the IRC §72(p) limitations or defaulting on loan repayments (particularly when the employer was at fault),
- Failures to distribute deferrals in excess of the IRC §402(g) limit (i.e., \$15,500 for 2008),
- Failures to pay required minimum distributions under IRC §401(a)(9),
- Correction by retroactive plan amendment of a failure to limit compensation under IRC §401(a)(17), permitting hardships or loans without a plan provision

so authorizing, and permitting employees to participate before completing the eligibility requirements. The retroactive amendments in these situations have very specific provisions that are required,

- Eligible employer failures under IRC §401(k) and §403(b) plans, and
- Certain SEP, SARSEP, and SIMPLE IRA failures.

While ASPPA's Government Affairs Committee (ASPPA GAC) encouraged the IRS to permit use of the Self-correction Program (SCP) for many of these errors, the streamlined VCP procedure is certainly a step in the right direction of reducing the burden of EPCRS-based compliance.

The streamlined procedure has an additional benefit: the user fee may be lower than under normal VCP. The streamlined filing fee varies, depending on the type of compliance problem being addressed. The \$375 user fee for interim nonamenders has been retained, as has the 50% reduction in fees for nonamenders discovered and submitted within one year of the normal deadline.

Expanded Participant Loan Corrections. Responding to the difficulties of participant loan errors, particularly those due employers' missteps, the IRS has provided means under VCP to resolve loan failures while avoiding income and excise taxation. These methods are not available under SCP; nor can EPCRS correction take place if the maximum period for loan repayment (generally 5 years) has expired.

Roth Contribution Adjustments. The Procedure deals with corrections of excess deferrals and contributions when designated Roth contributions are involved.

Determination Letter Changes. The Procedure aligns its rules with the new structure for IRS favorable determination letter (FDL) submissions, generally requiring that EPCRS-related amendments be included in the proper cycle submissions

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of plans, rather than having the FDL submission as part of the EPCRS application.

Earnings Rate. The Procedure permits the use of the VFPC calculator for determining earnings on corrective contributions, distributions, and allocations when it is not feasible to make a reasonable estimate of actual earnings. ASPPA has encouraged both the IRS and DOL to permit use of the VFPC calculator for all earnings calculations; needless to say, the Procedure falls short of that aspiration, but is still progressive.

Definition of Substantial Correction Liberalized. If an error has been substantially corrected under the SCP when an audit notice is received, the IRS will permit the self-correction to be completed without requiring the payment of a closing agreement sanction. The Procedure has expanded the definition of “substantial correction,” thereby increasing the situations in which an intervening audit does not result in a sanction being levied. In general, an error is considered to be substantially corrected if the correction is completed within 120 days (as opposed to 90 days under the old rules) after the last day of the correction period or if correction is completed during the correction period with regard to 65% (as opposed to 85% under the old rules) of all affected participants, with correction as to the remaining participants being completed diligently thereafter.

More Detailed Preapproved Corrections. The Procedure outlines more failures and preapproved corrections for those failures. Furthermore, the Procedures states that, when there is a failure that is not detailed in the Procedure but is analogous to something that is reflected in the Procedure, an analogous correction is likely appropriate. Appendices A and B outline several types of qualification failures and permitted corrections, and should be referenced by a practitioner anytime an error is to be addressed. While the preapproved corrections are not the only permitted ways to deal with a noted failure, they are instructive, and provide assurances in a self-correction setting of what the IRS will approve. If other correction methods are to be used, a VCP filing may be warranted. (**Important note:** the correction methods for §415-related failures that used to be in the old §415 regulations, but were removed from the latest regulations, appear intact in the Procedure.)

Increased Threshold Amounts for Required Corrective Distributions. Under the old procedure, a corrective distribution to a terminated participant could be disregarded if the amount was \$50 or less and the cost of making the distribution exceeded the amount to be paid. The Procedure increases this to \$75.

Waiver of Excise Tax. The Procedure includes some provisions for waiver of excise taxes in addition to the §4974 tax on failure to make required minimum distributions (which was in the old procedure). The Procedure includes a possible

waiver of excise taxes under IRC §§4972 (nondeductible contributions, if they are required to make plan contribution), 4979 (late correction of ADP or ACP failures when tests were timely performed but data was incorrect), and 4973 (excess deposits to an IRA – generally in relation to situations in which excess payments were made to participants and rolled over).

Expanded Corrections for Improperly Excluded Employees. Under the prior procedure, we received guidance of how to correct the failure to get deferral elections improperly excluded employees. In this Procedure, we are provided with how to handle missed Roth deferral and after-tax employee contribution opportunities, as well as when the improper exclusion involves only a partial year.

▲ What's Not So Good

There are two areas of the new Procedure that are disappointing.

Still No Self-correction of Scriveners' Errors. First, the IRS has not added any substantial provision for self-correction of what practitioners call a “scrivener’s error” (which the IRS calls “correction of an operational failure through plan amendment”). This is not surprising, as ASPPA GAC has had several discussions on this topic with IRS representatives, and the IRS remains concerned regarding the potential for abuse in permitting these types of amendments. Nonetheless, a plan that has experienced a scrivener’s error and can demonstrate through extrinsic evidence that the provision at issue was included in the plan in error may be able to obtain the desired result through VCP.

Formalization of Sanctions for Nonamenders. The Procedure contains a chart identifying the sanctions to be charged if a nonamender situation is discovered on plan audit (or as part of a FDL submission), rather than being identified by the plan sponsor. The amount of the user fees vary depending on which required amendment is at issue (older amendments cost more), and how many participants are involved. While predictability and consistency throughout the country is a good thing, the amount being charged for relatively small plans may be considered by some to be disproportionate. For example, a plan that has 51-100 participants that failed to adopt an amendment in relation to the final regulations under §401(a)(9) may expect a sanction on audit of \$9,000 *for that failure alone*. In our experience, this already has resulted in higher sanctions for some of our audit clients than we have seen in previous months. The maximum nonamender sanction for a plan with more than 10,000 employees (which is for a plan that has not been amended for ERISA) is \$80,000. While that is not an insignificant amount of money, one ponders whether such a large employer feels the pain of \$80,000 as much as a smaller employer feels \$9,000 or more.