

# Global Rewards Update:

## United States – IRS Updates Correction Program for Retirement Plans

**June 2015**

### Background

The Internal Revenue Service (“IRS”) has long recognized that errors often arise in the administration of retirement plans, and that these errors can jeopardize the tax-advantaged status of these plans. To accommodate plan administrators who wish to remedy these errors, the IRS established the Employee Plans Compliance Resolution System (“EPCRS”) to allow plans to maintain their tax-favoured status. EPCRS was most recently restated pursuant to Revenue Procedure 2013-12.

There are two main ways under EPCRS for employers to correct failures voluntarily: the Self-Correction Program (“SCP”) and the Voluntary Correction Program (“VCP”). The primary difference is that VCP involves the submission of an application to the IRS to obtain specific IRS approval for the correction, but under SCP, the employer corrects the failure on its own, without involving the IRS. The benefit of a VCP submission over SCP is that it can provide explicit IRS approval of a proposed correction. VCP is also available for certain failures that are not eligible for SCP, and in some cases, VCP permits methods of correction that are not permissible under SCP.

In early 2015, the IRS published Revenue Procedures 2015-27 and 2015-28 to make certain modifications to EPCRS. Generally, these updates revise acceptable corrections for certain failures. These updates do not replace Revenue Procedure 2013-12, but simply modify certain provisions.

### Summary of Changes

Revenue Procedures 2015-27 and 2015-28 introduced a number of modifications to the existing correction procedures of Revenue Procedure 2013-12, including:

- Clarification of various approaches for correcting overpayment failures;
- Modification of the safe harbour correction method for failure to implement employee elective deferrals pursuant to an automatic contribution feature;
- Modification of the alternative safe harbour method for calculating earnings on certain automatic contribution failures;
- Modifications to encourage early correction of employee elective deferral failures;
- Modification of the period of time for certain corrections of excess annual additions under certain defined contribution plans;
- Reduction of the VCP fees for certain required minimum distribution and participant loan failures;
- Clarification of required forms for plan sponsors wishing to use the Model VCP Submission Documents;
- Clarification of provisions related to the requirement to submit a determination letter, including clarification concerning certain corrective amendments made to pre-approved plans; and
- A number of other miscellaneous modifications.

As this list is not exhaustive, we recommend reading through both recent Revenue Procedures in their entirety

for additional details.

## Updated EPCRS Provisions

Although a number of modifications and clarifications were made to Revenue Procedure 2013-12, there are a few that warrant particular mentioning:

- *Flexibility in correction of overpayment:* In some cases, an operational failure results in a participant receiving an overpayment of his or her plan benefits. Previous IRS guidance suggested that the overpayment could be corrected by obtaining repayment of the overpayment from the participant. Although the previous guidance provided alternatives, some plan sponsors interpreted the previous requirement as obligating them to seek repayment from participants. This imposed a hardship on plan participants in certain situations, particularly those involving elderly retirees who had been collecting benefits that included overpayments, for whom the repayment obligation would be particularly harsh. In the revised guidance, the IRS relaxed the requirement that the plan sponsor seek repayment of the overpayment from the participant, and clarified that in certain cases, it was permissible for the plan sponsor to reimburse the plan, rather than the participant. The guidance also clarifies that a retroactive amendment may also be appropriate, subject to rules governing the acceptability of retroactive amendments. The IRS is currently seeking comments on the specifics of this correction.
- *Extended relief for correcting excess annual additions:* Under Revenue Procedure 2013-12, a plan with repeated excess annual additions in violation of IRC Section 415(c) would be considered to have inadequate administrative procedures if such excesses were not corrected within 2½ months of the plan's limitation year. Under the self-correction eligibility requirements of EPCRS, a plan that lacks adequate administrative procedures is not eligible to self-correct significant failures, and would therefore be required to use VCP in all cases. Revenue Procedure 2015-27 modifies the EPCRS to extend the period of time to return elective deferrals to affected employees from 2½ months to 9½ months after the end of the plan's limitation year.
- *Reduced corrective contributions for certain corrections of employee elective deferral failures under an IRC 401(k) or 403(b) plan:* Generally, where a participant's deferral election has not been implemented, EPCRS correction procedures require a qualified non-elective contribution ("QNEC") equal to 50% of the participant's missed deferrals. Revenue Procedure 2015-28 reduces or eliminates the corrective QNEC in certain cases.

No QNEC required – The corrective QNEC is not required where the deferral election is implemented within three months of when the failure occurred.

Reduced QNEC – The corrective QNEC is reduced to only 25% of the missed deferrals if corrected more than three months after the failure occurred, but not later than the end of the second plan year following the plan year in which the failure occurred.

Special rules for correcting missed deferrals for eligible employees subject to an automatic contribution arrangement – Corrective relief is available for a failure to implement an automatic contribution feature for an affected eligible employee or failure to implement an affirmative election of an affected employee pursuant to such arrangement. No corrective QNEC is required if the correct deferral election is implemented no later than the end of the 9½-month period after the end of the plan year of the failure. This safe harbour correction is only available with respect to plan failures that begin on or before December 31, 2020. The IRS plans to assess whether to extend this relief beyond December 31, 2020.

In each case,

- The update does not eliminate the requirement for corrective matching contributions based on the full missed deferral (adjusted for earnings), if applicable, which must be made within the timing required for correcting significant operational failures under SCP.
- The affected participant(s) must be provided with a notice that includes a description of the error and the corrective steps that have been taken.
- The required timing for the correction may be accelerated if the affected participant notifies the

plan sponsor of the error.

These changes, among others, are meant to encourage voluntary correction and may ultimately reduce the cost of self-correction.

## Action

As the IRS has been actively auditing retirement plans, the EPCRS is meant to promote use of SCP and VCP in an effort to streamline the process. We can provide consulting assistance with respect to the implementation of a self-correction under SCP or with the preparation of a VCP application, with proposed corrections for review. As a practical matter, we suggest that plan administrators continue to review plan operations as a means to identify and correct plan failures. Correcting failures under the EPCRS may help avoid or reduce future monetary sanctions if a qualification issue were to be discovered upon audit.

Additionally, we are able to assist with a plan qualification self-compliance review as a pre-emptive means to proactively correct plan failures prior to being audited.

## People to contact

For assistance with this matter, or any other issue related to the operation of your global rewards plans, please contact your local Deloitte global rewards consulting services adviser or email us at [globalshareplans@deloitte.co.uk](mailto:globalshareplans@deloitte.co.uk), and a global rewards consultant will contact you.

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