Employee Benefits Corner

IRS Expands Its Plan Correction Program with Two New Revenue Procedures

By Elizabeth Thomas Dold and David N. Levine

The Employee Plans Compliance Resolution System (EPCRS), set forth in Rev. Proc. 2013-12,[1] was recently expanded by two separate revenue procedures, Rev. Proc. 2015-27 and Rev. Proc. 2015-28,[2] providing plan sponsors additional tools to correct and maintain the tax-qualified status of their tax-qualified plans.

As more fully described below, these new procedures (1) provide additional flexibility for correcting automatic enrollment and elective deferral failures (including automatic escalation failures), (2) provide reduced filing fees for loan and minimum required distribution corrections, (3) provide helpful clarification that plan overpayments may, in certain circumstances, be corrected *via* a plan amendment or without having to seek repayment from the participant, (4) extend the self-correction period for repeated Code Sec. 415 violations, and (5) offer additional relief in other miscellaneous areas. The first provision is set forth under Rev. Proc. 2015-28 and is effective as of April 2, 2015, while the remaining provisions are set forth under Rev. Proc. 2015-27 and are generally effective July 1, 2015, but plan sponsors may, at their discretion, apply such provisions on or after March 27, 2015.

These new correction options are more favorable and cost-effective than prior preapproved correction methods, and therefore plan sponsors should remember to incorporate these new correction options into their arsenal for addressing plan operational failures going forward.

ELIZABETH THOMAS DOLD and **DAVID N. LEVINE** are Principals at Groom Law Group, Chartered in Washington, D.C.

Automatic Enrollment and Elective Deferral Failures (Rev. Proc. 2015-28)

Despite the plan sponsor's best intentions and due diligence, operational failures routinely arise with administering 401(k) and 403(b) plans. With the complex rules and strict timing provisions, these new correction procedures are a welcomed relief.

Under the existing preapproved correction methods, automatic enrollment and elective deferral failures (*e.g.*, failure to implement the participant actual or deemed election) are typically corrected *via* an employer contribution in the form of a qualified non-elective contribution (QNEC) equal to 50 percent of the "missed deferral opportunity" (*i.e.*, 50 percent of the proper deferral amount that should have been made by the participant), plus missed earnings, along with 100 percent of the missed match on such deferrals. Special rules also apply for missed after-tax, Roth and catch-up contributions, along with a limited exception for errors within the first three months of the plan year. The new guidance does not change any of these preapproved correction methods, but rather adds three new correction methods that may also be used, basically adding a participant notice provision to justify a reduction in the employer contribution (and thereby helping to address the windfall issue that always arises when correction is discussed—the employer is required to put money into the plan that represents money that the employee put in his pocket).

Method 1—Automatic Enrollment Plans Only

No QNEC is required for the missed elective deferral resulting from a failure to properly implement an automatic enrollment feature (EACA, QACA, ACA), including an affirmative election by an employee out of such feature and an automatic escalation feature, if the following three requirements are satisfied:

1. *Commencement of Elective Deferrals*: Correct deferrals must begin no later than the "deferral commencement date"—which is the earlier of (a) the first paycheck made on or after the last day of the nine-and-a-half-month period after the end of the plan year in which the failure occurred (October 15 for a calendar year plan), or (b) if the plan sponsor was notified by the employee, the first paycheck made on or after the last day of the month after the month of notification.
2. *45-Day Participant Notice*: Notice of the failure must be given to the affected employee no later than 45 days after the deferral commencement date (described in #1 above). The notice must contain all of the following information:
   - General information about the failure, such as the correct deferral percentage and the date the deferrals should have commenced (importantly, disclosure of the actual dollar amounts is not required)
   - Statement that appropriate amounts have begun (or will begin shortly) to be deducted from compensation and contributed to the plan
   - Statement that corrective contributions relating to the missed matching contributions have been made (or will be made) (but information on the date and amount of corrective contributions are not required)
   - Explanation that the participant may increase his or her deferral percentage to make up for the missed deferral opportunity, subject to the Code Sec. 402(g) limits.
   - Name of the plan and plan contact information (including the name, street address, e-mail address and phone number of a plan contact)
3. *Missed Matching Contributions*: Corrective contributions (adjusted for earnings) to make up for full missed matching contributions must be made no later than the end of the second plan year following the plan year in which the missed matching contribution occurred. The guidance clarifies that in addition to the existing guidance, if the employee has not made an investment election, the plan's default investment option can be used to calculate earnings. However, the earnings adjustment cannot result in a cumulative loss (*i.e.*, at least contribute the amount of the missed match).

Notably, this correction method was intended to facilitate adoption of automatic enrollment plans and therefore shall expire on December 31, 2020, unless extended by the IRS (which presumably will require more wide-spread adoption of these types of plans).

Method 2—Elective Deferral Failures Corrected Within a Revolving Three-Month Period

This method (along with Method #3) applies to an "Employee Elective Deferral Failure," which is broadly defined to include: (1) a failure to implement elective deferrals correctly in a 401(k) or 403(b) plan pursuant to an affirmative election or pursuant to an automatic contribution feature (including auto escalation) under a 401(k) or 403(b) plan, and (2) a failure to provide an employee with the opportunity to make an affirmative election because the employee was improperly excluded from the plan.

No QNEC is required for the missed elective deferral resulting from an "Employee Elective Deferral Failure," if the following three requirements are satisfied:

1. *Timely Commencement of Elective Deferrals*: Correct deferrals must begin no later than the earlier of (i) the first paycheck made on or after the three-month period that begins when the failure first occurred for the employee, or (ii) if the plan sponsor was notified by the employee, the first paycheck made on or after the last day of the month after the month of notification.
2. *45-Day Notice*: Notice of the failure must be given to the affected employee no later than 45 days after the date on which correct deferrals begin. The notice must contain the following information:
   - General information about the failure, such as the correct deferral percentage and the date the deferrals should have commenced (importantly, disclosure of the actual dollar amounts is not required)
   - Statement that appropriate amounts have begun (or will begin shortly) to be deducted from compensation and contributed to the plan

- Statement that corrective contributions have been made (or will be made) (but information on the date and amount of corrective contributions are not required)
- Explanation that the participant may increase his or her deferral percentage to make up for the missed deferral opportunity, subject to the Code Sec. 402(g) limits
- Name of the plan and plan contact information (including the name, street address, e-mail address and phone number of a plan contact)

3. *Missed Matching Contributions (if any)*: Corrective contributions to make up for missed matching contributions (if any), adjusted for earnings, must be made no later than the end of the second plan year following the plan year in which the missed matching contribution occurred. The guidance again clarifies that earnings can be based off the plan's default investment fund if the participant has not made an investment election.

Method 3—Elective Deferral Failures Corrected Within Two-Year Period

A reduced QNEC is required—equal to 25 percent (rather than 50 percent) of the missed deferrals—for the missed elective deferral resulting from an "Employee Elective Deferral Failure" (as defined above), if the following three requirements are satisfied:

1. *Timely Commencement of Elective Deferrals*: Correct deferrals must begin no later than the earlier of (i) the first paycheck made on or after the last day of the second plan year following the plan year when the failure first occurred, or (ii) if the plan sponsor was notified by the employee, the first paycheck made on or after the last day of the month after the month of notification.
2. *45-Day Notice*: Notice of the failure (containing the information described in Method #2) is given to the affected employee no later than 45 days after the date on which correct deferrals begin.
3. *Corrective Contributions*: Corrective contributions (including the 25-percent QNEC, plus 100 percent of any missed matching contributions), adjusted for earnings, must be made no later than the end of the second plan year following the plan year in which the missed contribution occurred. The guidance again clarifies that earnings can be based off the plan's default investment fund if the participant has not made an investment election.

Changes to EPCRS Following Rev. Proc. 2015-27

Chart 1 summarizes the existing and new rules that are set forth in Rev. Proc. 2015-27, which largely focuses on replacing the existing rules with lower VCP filing fees and more favorable plan overpayment correction procedures.

ENDNOTES

1 Rev. Proc. 2013-12, IRB 2013-4, 313.

2 Rev. Proc. 2015-27, IRB 2015-16, 914; Rev. Proc. 2015-28, IRB 2015-16, 920.

CHART 1.

Provision	Old EPCRS (Rev. Proc. 2013-12)	Revised ECPRS (Rev. Proc. 2015-27)
Loan Failures	VCP Filing Fee—based on the number of participants in the plan. A 50-percent reduced VCP fee available if: (1) VCP submission involves a loan error corrected in accordance with the prescribed correction methods, (2) the failure does not affect more than 25 percent of the plan sponsor's participants in any year in which the failure occurred, and (3) this is the only failure.	VCP Filing Fee—if loan failure meets the same three requirements, the VCP filing fee is based on the number of participants affected and not the number of participants in the plan:
Required Minimum Distribution (RMD) Failures	VCP Filing Fee—reduced VCP compliance fee of $500 for RMD failures if there are 50 or fewer participants affected by the failure, provided that: (1) no other failures are included in the submission, and (2) the failure would result in the imposition of the 50-percent excise tax under Code Sec. 4974 (imposed on the participant who should have received the RMD).	VCP Filing Fee—if the RMD failure meets the same two requirements, the VCP fee is $500 if as many as 150 participants are affected, and $1,500 if 151 to 300 participants are affected. If more than 300 participants are affected, the regular VCP fee based on the total plan population will apply.

Number of Participants with Loan Failures	Compliance Fee
13 or fewer	$300
14 to 50	$600
51 to 100	$1,000
101 to 150	$2,000
Over 150	$3,000

CHART 1.

Provision	Old EPCRS (Rev. Proc. 2013-12)	Revised ECPRS (Rev. Proc. 2015-27)
Plan Overpayments	To correct an overpayment from a defined benefit plan, the plan sponsor should, along with other requirements, take reasonable steps to have the overpayment, with appropriate interest, returned by the participant to the plan. A similar requirement applies for correcting overpayments from defined contribution plans and 403(b) plans.	For defined benefit and defined contribution (including 403(b) plans) overpayments, depending on the nature of the failure, it may be permissible to (1) have the employer or another person contribute the amount of the overpayment (with appropriate interest) to the plan, instead of first asking the participant to repay it, or (2) adopt a retroactive amendment to conform the plan document to the plan's operations through VCP or Audit CAP. The guidance also indicates that comments are welcomed (by July 20, 2015) on whether: ■ make-whole contributions should be required to be made by the employer rather than being sought from participants and beneficiaries, ■ guidance should be provided on overpayments due to benefit calculation errors and whether the correction methods should follow rules similar to PBGC rules for recoupment of overpayments (providing for an actuarial reduction of future benefit payments, without interest, generally capped at a 10-percent reduction in the participant's monthly benefit), ■ further guidance is needed on the calculation of interest on benefit calculation errors, and ■ there is a need for other overpayment changes or guidance (including guidance on any unusual circumstances in which full correction should not be required).
Repeated 415 Violations	A plan that provides for elective deferrals and nonelective employer contributions (and no matching contributions) will be eligible for self-correction if it corrects Code Sec. 415(c) violations (*i.e.*, excess annual additions) by returning elective deferrals to the affected participant within two and a half months after the end of the plan's limitation year. This permits certain plans to avoid monitoring the 415 limits during the year.	The two-and-a-half-month correction period is replaced with a nine-and-a-half-month correction period after the end of the plan's limitation year. So now these plans have until October 15 (for a calendar-year limitation year) rather than March 15 to make the correction.
Model VCP Submission Documents and Other Miscellaneous Changes	A VCP applicant may use the Model Compliance Statement format in Appendix C of Part I of Rev. Proc. 2013-12 and the schedules set forth in Part II. Currently, Schedules 1 through 9 provide streamlined submission formats for correcting common qualification failures using standardized correction methods. To obtain an acknowledgement letter, the plan sponsor must submit the "Acknowledgement Form" in Appendix D of Rev. Proc. 2013-12.	Appendix C (Model VCP Submission Documents) has been replaced with official IRS forms: Form 14568, *Appendix C Part I, Model VCP Submission Compliance Statement*, and Form(s) 14568-A through 14568-I, comprising the Schedules. Appendix D (Acknowledgement Letter) has been replaced with IRS Letter 5265. The guidance also provides additional clarifications regarding when a determination letter is required to be submitted for certain plans, and other minor updates to the program (such as elimination of the reference to the SSA letter forwarding service, which was previously eliminated).