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View From Groom: DOL's Revised VFCP Should Provide an Opportunity to Submit Comments

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The Department of Labor ("DOL") Voluntary Fiduciary Correction Program ("VFCP") and the related Prohibited Transaction Class Exemption ("PTE") 2002-51 provide for the rare opportunity to obtain retroactive excise tax relief on prohibited transactions. While only certain types of transactions are covered under the VFCP — and a narrower set is covered under PTE 2002-51 — for the right type of transaction, retroactive exemptive relief can be obtained for an unlimited number of prohibited transactions. Even for those transactions covered under the VFCP but not under PTE 2002-51, filing a VFCP application could result in a "no action" letter from the DOL. Thus, any revisions to the VFCP to make its use more attractive would be a welcome development.

While the DOL is undoubtedly busy with its fiduciary rule proposal, the DOL's regulatory agenda includes publishing a revised VFCP this fall as an interim final rule. While this may be delayed, once the interim final rule is published, interested persons should have an opportunity to submit public comments on the VFCP. Some changes that would make the VFCP more attractive are:

- Requiring a simplified application that would lower the cost of preparing VFCP applications;
- Allowing the correction amount due to a plan to be reduced by any payments the plan received during a prohibited transaction period; and
- Allowing an alternative method of calculating lost earnings.

We discuss why these changes would be beneficial below.

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The VFCP Should Require a Simplified Application Based on the Applicant's Representations

Perhaps the most onerous part of preparing a VFCP application is collecting the numerous required documents. While applicants should be required to describe the prohibited transactions and the correction method followed, the VFCP requires much more: it generally requires applicants to submit a transaction-by-transaction calculation of the required correction amount and proof of payment (such as a copy of a cashed check or bank statement for the plan's account). While this approach may be feasible for a small number of transactions, it is unduly burdensome for large correction projects involving hundreds or thousands of transactions.

In contrast, the DOL has taken a different approach with prohibited transaction exemption applications. For exemption applications, the DOL grants relief based on the applicant's representations. There is no compelling reason why the DOL should not similarly grant relief under the VFCP based on the applicant's representations concerning how correction amounts were calculated and paid. For clarity, DOL could require applicants to include an example of how it calculated correction amounts, but requiring applicants to include every correction amount calculation is not necessary to protect the interests of plan participants and beneficiaries.

Removing the requirements to provide transaction-by-transaction calculations and proofs of payment would significantly lower the cost of preparing VFCP applications. This change, if implemented, would go a long way to making the VFCP more attractive.

Correction Amount Should Be Reduced by any Payments the Plan Received During the Prohibited Transaction Period

One type of transaction covered under the VFCP is the purchase of an asset by a plan from a party in interest. VFCP § 7.4(a). One possible way to correct this type of transaction under the VFCP is for the plan to retain the asset and receive the ''Lost Earnings'' (*i.e.*, interest) on the amount the plan paid for the asset, ''but only to the extent that such Lost Earnings . . . exceeds the difference between the [fair market value] of the asset . . . and the original purchase price.'' VFCP § 7.4(a)(2)(ii). This means that the correction amount (here, the Lost Earnings) that the party in interest has to pay to the plan is allowed to be reduced by the *unrealized* gain — the increase in the fair market value of the asset — that the plan could realize from owning the asset.

This VFCP correction method, however, does not permit the reduction of the correction amount by any *realized* payments (such as bond interest or dividend payments) the plan received from owning the asset. This is a key shortfall of the VFCP when a party in interest is faced with correcting the sales of stocks or bonds to plans that resulted in the plan receiving significant stock dividend or bond interest payments. To the extent the DOL desires to promote the filing of VFCP applications, the correction method required under the VFCP should result in a fair outcome for both the plan and the party in interest.

Alternative Method for Correction Amount Calculation

The DOL should recognize that it is not feasible to use its online calculator to calculate correction amounts for a large number of transactions. While some applicants will be able to efficiently calculate correction amounts for a large number of transactions through computer spreadsheets or programs, all applicants would benefit from an alternative method for calculating correction amounts.

The VFCP generally requires Lost Earnings (interest) to be calculated using quarterly adjusted interest rates under Section 6621(a)(2) of the Internal Revenue Code, where the interest must be compounded daily. Allowing applicants to calculate Lost Earnings as a simple interest for the entire period of the prohibited transaction using a single interest rate would greatly simplify the required correction amount calculation. The DOL could prescribe the method for determining the required single interest rate — which could be based on the Section 6621(a)(2) interest rates in effect during the prohibited transaction period — in such a way that using the alternative correction amount calculation method will always result in a slightly higher correction amount due to the plans. Thus, while the plans would not be negatively affected by this change, the VFCP would become much easier to use. This change would likely have the most beneficial impact when large numbers of prohibited transactions involving small amounts are discovered.

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DOL staff has indicated to us a few years ago that it had a running list of potential improvements to the VFCP. So we are eagerly anticipating the DOL's publication of the revised VFCP. It is possible that the revised VFCP would address the issues discussed in this article. If not, the opportunity to submit public comments may prove useful.

