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# Employee Benefits Corner

## *A Look at the Expanded Plan Correction Procedures Under SECURE 2.0*

By Elizabeth Thomas Dold and David N. Levine

In order for a qualified retirement plan to maintain its favorable tax-qualified status, the plan terms must comply with the Internal Revenue Code, and any Internal Revenue Service (IRS) guidance thereunder, and the terms of the plan must be followed in operations. With hundreds of very complex rules in play, it is common for a qualification failure to occur. The good news is that the IRS has a special correction program—Employee Plans Compliance Resolution System (EPCRS), currently set forth in Rev. Proc. 2021-30—to allow plan sponsors to correct these failures and maintain the tax-qualified status of the plan.

As wonderful as EPCRS is, with the Consolidated Appropriations Act, 2023 (Setting Every Community Up for Retirement Enhancement (SECURE) 2.0) that was enacted on December 29, 2022, it just got even better! Specifically, SECURE 2.0 made a number of changes to the correction procedures that plan sponsors (and their recordkeepers) need to be aware of. These provisions cover the following three failures, some of which are effective immediately:

- inadvertent benefit overpayment (Section 301 of the Act, effective immediately),
- eligible inadvertent failures (Section 305 of the Act, effective upon IRS guidance), and
- automatic enrollment failures (Section 350 of the Act, effective in 2024).

Notably, there are also detailed overpayment correction procedures set forth in EPCRS, and it is important to apply consistent correction procedures for similarly situated participants.

### **I. Inadvertent Benefit Overpayment**

#### **A. ERISA Covered Plans**

For the purposes of Title I of Employee Retirement Income Security Act of 1974 (ERISA), SECURE 2.0 provides that an inadvertent benefit overpayment (not defined) will not give rise to a breach of fiduciary duty for not seeking recovery of the overpayment, provided that (1) for an individual account plan, any impermissible forfeiture arising in connection with the overpayment is restored, (2) for a defined benefit pension plan, failure to recover the overpayment would not materially affect the plan's ability to pay benefits due under the plan, and

(3) the plan has established prudent procedures to prevent and minimize overpayment of benefits and these policies were followed.

Moreover, this fiduciary relief is still available if (1) future benefit payments are reduced to the correct amount going forward, or (2) the plan fiduciary seeks recovery from the person(s) responsible for the overpayment.

Lastly, if recoupment is sought from the participant or beneficiary, the following conditions generally apply (with exceptions for culpable participants or where the overpayment is material):

- No interest or other fees are sought with the overpayment;
- For a non-decreasing annuity, reduction of future payments are capped at 10% of the overpayment each calendar year, and not more than 10% reduction in the periodic payment;
- No threat of litigation or use of a collection agency;
- No collection of a participant's overpayment from a beneficiary;
- No collection for payments if the first overpayment was made more than three years before written notice is provided of the error (unless fraud or misrepresentation); and
- The claims procedures are available to contest the recoupment. (The participant's hardship as a result of the recoupment can also be taken into account in determining the amount to recover.)

## B. Internal Revenue Code Provisions

Similarly, the Code was amended to provide that the plan is not disqualified as a result of an inadvertent benefit overpayment not being repaid, or the plan sponsor amends the plan to increase past, or decrease future, benefit payments in order to adjust for such prior overpayments.

This relief is still available if the plan (1) reduces future benefit payments to the correct amount going forward, or (2) seeks recovery from the person(s) responsible for the overpayment. This does not impact the plan sponsor's obligations to (1) comply with minimum funding requirements, (2) otherwise prevent or restore an impermissible forfeiture, (3) correct 401(a)(17) compensation limit failures, and (4) correct Code Sec. 415 failures. Moreover, the Act provides that the IRS may issue guidance specifying how benefit overpayments and their recoupment (or non-recoupment) are taken into account for various Code purposes.

Lastly, and perhaps most importantly for lump sum overpayments, SECURE 2.0 treats the inadvertent benefit overpayment as an eligible rollover distribution

(provided it would have been one absent the fact that it was an overpayment). This avoids the 6% excise tax for individual retirement accounts (IRAs) (and permits the amounts to be retained into the receiving plan) and facilitates the tax-free return of these funds to the plan in the event recoupment is sought.

These new rules are effective beginning from December 29, 2022. A reasonable good faith standard of the then existing rules applies for overpayment corrections (and determinations thereon) before such date.

## II. Eligible Inadvertent Failures

SECURE 2.0 also provides relief for "eligible inadvertent failure" (defined below) to comply with the Code qualification rules that may be self-corrected under EPCRS, provided that (1) such failure was not identified by the IRS prior to such actions which demonstrate a specific commitment to implement a self-correction, and (2) the self-correction is completed with a reasonable period after such failure is identified. Specifically, the applicable period of self-correction is indefinite, except as provided under the Code, regulations, or other guidance.

The IRS shall update EPCRS within two years regarding the applicable correction methods for these failures. An "eligible inadvertent failure" is defined as a failure that occurs despite the existence of practices and procedures which (1) satisfy the standards set forth in section 4.04 of Rev. Proc. 2021-30 (or successor) (or satisfy similar standards in the case of an IRA), and (2) does not include failures which are egregious, relate to the diversion or misuse of plan assets, or is directly or indirectly related to an abusive tax avoidance transaction.

### A. Loan Failures

In the case of an eligible inadvertent failure related to loans, the failure may be self-corrected in accordance with the rules of EPCRS (Section 6.07 of Rev. Proc. 2021-30). The Department of Labor (DOL) shall treat such corrections as meeting the requirements of the DOL's Voluntary Fiduciary Correction Program (VFCP), but it may impose reporting or other requirements for this relief. This has the result of permitting self-correction of all plan loan violations (including loans in excess of the 72(p) limit that was previously subject to VCP filing).

### B. IRA Failures

The IRS is directed to expand EPCRS to address eligible inadvertent failures with respect to an IRA, including (1) waivers of excise tax on late required minimum distributions, and (2) distributions to nonspouse

beneficiaries that due to an inadvertent error by a service provider, the beneficiary had reason to believe that the distribution could be rolled over without taxation (as indirect rollovers are not permitted to be made to an inherited IRA). Although simplified employee pension (SEP) and savings incentive match plan for employees (SIMPLE) IRAs have been covered under EPCRS, this is a brand-new world for IRAs that have never had a self-correction program!

### III. Elective Deferral Failures

SECURE 2.0 adds a permanent correction method for missed automatic enrollment/escalation failures substantially similar to the relief set forth in EPCRS—resulting in no make-up of missed deferrals—which is set to expire on December 31, 2023. However, this one is even better as it extends to terminated employees and applies even if raised by the IRS in audit, but it looks like we need to make sure the eligible automatic contribution arrangement (EACA) (414(w)) rules are followed (which brings in the 90-day withdrawal right).

This covers a reasonable administrative error made in implementing automatic enrollment/escalation (or affirmative election by a covered employee), or by failing to offer an affirmative election due to the employee's improper exclusion from the plan. The error must be corrected in accordance with an EACA

and within 9½ months of the end of the plan year in which the error first occurred (or the date of the first payment of compensation on or after the last day of the month following the month the employee notifies the plan sponsor of the error, if earlier).

The details of the requirements are pending additional guidance (and until issued a reasonable good faith standard applies), but are anticipated to track closely the existing EPCRS rules regarding timing of matching contributions, notice requirements, earnings calculations, *etc.* Moreover, this correction must be applied to all substantially similar participants in a nondiscriminatory manner.

This optional relief is effective for any errors with respect to which the date that is 9½ months after the end of the plan year during which the error occurred is after December 31, 2023.

### IV. Conclusion

Plan sponsors and their recordkeepers should review their existing correction procedures, particularly for plan overpayments and the repayment procedures, and update the process to ensure compliance with these rules. This will also impact reporting and withholding procedures for plan overpayments as a result of the rollover change (which is very welcomed!).

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