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Employee Benefits Update

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IRS Changes Rules for Correcting Common 401(k) & 403(b) Plan Errors

The IRS recently released additional guidance to the Employee Plans Compliance Resolution System (EPCRS). Revenue Procedures 2015-27 and 2015-28 modify and improve the previous Revenue Procedure 2013-12 and describe new IRS rules for correcting several of the more common errors in qualified retirement plans. The IRS correction guidance provides increased flexibility when making certain corrections as well as reduced fees designed to encourage plan sponsors to participate in the voluntary correction programs (VCPs).

Plan Loans & Required Minimum Distributions

The IRS greatly reduced the filing fees for loans in violation of Internal Revenue Code Section 72(p) and for late minimum required distributions (MRD). For example, the previous filing fee could be as high as $12,500, depending on the plan's size and if loan failures were the only compliance errors. The new fees are based on the number of participants with loan or MRD failures rather than the total number of plan participants.

Participants With Loan Failures	VCP Filing Fee
13 or fewer	$300
14 to 50	$600
51 to 100	$1,000
101 to 150	$2,000
Over 150	$3,000

Participants With MRD Failures	VCP Filing Fee
150 or fewer	$500
151 to 300	$1,500
Over 300	Standard VCP fee applies

Clarified Rules for Overpayment Corrections

Under Rev. Proc. 2013-12, when plan participants and beneficiaries receive overpayments from the plan, the employer is required to take reasonable steps to obtain repayment. If the overpayment is not returned to the plan, the employer in many situations is required to contribute the amount of the overpayment to the plan. IRS guidance now provides that in appropriate situations the employer can make payment to the plan, with accrued interest, without seeking recovery from the plan participants and beneficiaries. Alternatively, the employer could amend the plan retroactively to conform the plan to what was done in operation.

New Rules for Correcting Automatic Contribution Arrangements & Elective Deferral Errors

The IRS added a correction method for elective deferral failures in plans with automatic contribution arrangements and also reduced the cost to correct all deferral errors if they are discovered and corrected quickly.

Prior Correction Method

Previously, in Rev. Proc. 2013-12, the IRS required a plan sponsor to make a contribution in an amount equal to 50 percent of what the participant would have deferred if the elective deferral or automatic contribution provisions were not implemented properly. The sponsor was also required to contribute an amount equal to the full matching contribution that would have been made if the intended deferrals were contributed properly (adjusted for lost earnings on both the elective deferrals and matching contributions). According to public comments, these correction methods resulted in a "windfall" to participants who received both their regular pay and the 50 percent corrective contributions, and in plan

sponsors' reluctance to establish automatic enrollment arrangements due to the challenges of implementing and maintaining such arrangements. Rev. Proc. 2015-28 provides welcome relief to plan sponsors by eliminating the employer contribution for missed deferrals (but not the corrective contribution for missed matching contributions) and making the required corrections less onerous when made soon after they are discovered.

New Correction Method for Deferral Errors in Automatic Contribution Arrangements

For failures to implement automatic enrollments or automatic increases, **no corrective contribution** is required if the failure to automatically enroll or increase the participant's deferrals is found and corrected by the earlier of:

- The first payroll period after 9 1/2 months following the end of the plan year (Form 5500 due date)

  or

- The last day of the month following the month in which the plan sponsor learned of the error from the plan participant

The safe harbor provision for automatic contribution arrangements will sunset after 2020. The IRS will then evaluate whether it achieved the goal of increasing automatic contribution arrangements and if the availability of this safe harbor provision should be extended.

New Correction Method for Elective Deferral Errors *Not Exceeding* Three Months

For failures to implement deferral elections discovered within three months, **no corrective contribution** is required if the deferrals are restarted by the first payroll period after the three-month anniversary of the failure. However, if the participant advises the plan sponsor of the error, the deferrals must begin by the last day of the month following the month in which the plan sponsor learned of the error. Elective deferral errors include failure to implement a participant's deferral election and failure to permit an eligible participant to make a deferral election.

New Correction Method for Elective Deferral Errors That *Exceed* Three Months

The IRS created a new safe harbor for failures to implement deferral elections when the error is found after three months. In these cases, the **corrective contribution is reduced** from the historic 50 percent down to 25 percent of the employee's missed deferral as long as the error is corrected by the last day of the second plan year following the plan year in which the failure occurred. This deadline aligns with the current two-year correction period for significant operational errors. If the deadline is missed, the corrective contribution amount reverts to 50 percent of the missed deferral.

For each of these new correction methods to be effective, the plan sponsor must also:

- Provide the full matching contribution the participant would have received if the elective deferrals were processed correctly.
- Contribute lost earnings on the corrective contribution. Earnings are calculated using the same method as applicable to the participant's original elections. As an alternative safe harbor to calculate earnings for plans with automatic contribution arrangements, if the participant did not make an affirmative election, the IRS clarified that the plan's default investment can be used to determine earnings. The plan sponsor may also use the earnings calculation method in Appendix B, Section 3 of Rev. Proc. 2013-12.
- Provide the affected employee with notice of the error within 45 days after restarting the correct deferrals.

Generally, the new rules apply immediately. The new guidance provides welcome relief for plan sponsors by providing less burdensome procedures and reduced compliance fees. Plan sponsors should consider consulting legal counsel to discuss this new guidance and best practices for correcting any compliance concerns.

FOR MORE INFORMATION

For more information, please contact any member of our Employee Benefits & Executive Compensation group.

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