

# Major EPCRS Changes: Revenue Procedure 2019-19

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# Major EPCRS Changes: Revenue Procedure 2019-19

• Co-hosts:

Chuck Gouge



Joanne Pecina



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# During the Webinar

- All attendees' lines are muted
- We will try to answer questions as we go. Send questions to all panelists.
- Slides and recording of webinar are available from [ERISApedia.com/webcasts](http://ERISApedia.com/webcasts).
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## Your Presenters Today

Ilene H. Ferenczy, JD, CPC, APA



S. Derrin Watson, JD, APM

Stephen W. Forbes



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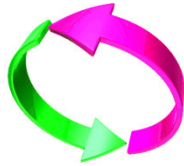
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## Three Major Changes

1. Self-correct plan loan failures
  - With 1099-R forgiveness
2. Self-correct plan document failures
  - If you're quick about it
3. Self-correct certain document issues relating to benefits, rights, and features



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## Requirements to Self-Correct (Anything)

- Plan must have in place practices and procedures “reasonably designed to promote and facilitate overall compliance in form and operation with applicable Code requirements”
- If failure is “significant”
  - Must correct by end of second plan year after year of failure (and before audit)
  - Must have “favorable letter”



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## Practices and Procedures

- If these requirements have always been there, what's the big thing?
  - The self-corrections permitted under the new procedures are more extensive in nature
  - It is possible (likely?) that the IRS will be more critical in reviewing self-corrections under audit
- What are practices and procedures regarding:
  - Plan documents?
  - Plan loans?



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## Practices and Procedures

- This is a huge opportunity for TPAs!
  - Help your clients establish internal policies with regard to the plan (improves compliance and sets up eligibility for self-correction)
  - Give your clients a “who to call” list so that they are primed to come to you when errors occur



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### Old Rules: Correction of Plan Loan Failures

- If you don't go through VCP or Audit CAP:
  - Plan must issue Form 1099-R for year of failure
- If you do go through VCP or Audit CAP, plan may:
  - Request no 1099-R for deemed distribution (if within five-year period)
  - Request 1099-R be issued for year of correction, rather than year of failure (if outside five-year period)
  - Use VCP compliance statement as basis of DOL VFCP filing regarding fiduciary breaches and prohibited transactions



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### New Rules: Guidance Issued for Specific Situations

- **Situation 1:** QJSA plan was required to get consent from spouse to make loan and failed to do so
  - Fix: Notify the participant and the spouse and get consent
  - If Cannot Get Consent: Talk to IRS under VCP or Audit CAP
- **Situation 2:** Plan limited number of loans to a participant but made loans to a participant in excess of that limit
  - Fix: Retroactively amend plan to conform to operations
- Both problems can be self-corrected
  - No deemed distribution or Form 1099-R



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### New Rules: Self-Correction of Defaulted Loan

- Situation
  - Loan terms comply with IRC §72(p)
  - Loan defaulted because of failure to timely pay
  - Corrected within maximum repayment period (normally five years)
- Fix
  1. If company's fault, company pays additional interest
  2. Employee must either:
    - Make lump sum payment to bring loan up to date, or
    - Reamortize loan and accrued interest over remaining loan term (or five-year limit), or
    - Combination of 1 & 2



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### New Rules: Self-Correction of Defaulted Loan (cont.)

- New rule: You can self-correct and avoid the deemed distribution
  - No Form 1099-R
  - Even if you don't self-correct, you can issue 1099-R for year of "correction"



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### Other Loan Failures

- You cannot self-correct (but must use VCP or Audit CAP):
  - Loans in excess of loan limits
  - Loan terms in excess of maximum repayment period (normally five years)
- Under VCP or Audit CAP:
  - Can ask for forgiveness of deemed distribution
  - If not, delay of Form 1099-R to year of correction is automatic
- You still cannot self-correct if you want to use DOL VFPC to correct fiduciary breaches/prohibited transactions
  - You must use IRS VCP if you want DOL VFPC



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### Case Study #1

- ABC Plan made a participant loan to Mary
- The loan was for \$60,000
- Mary's vested accrued benefit was \$200,000 at the time
- Can we self-correct?



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### Case Study #1

- Answer: Cannot use SCP
- Loan failures still must be corrected under VCP (i.e., cannot be self-corrected) if they relate to:
  - Excessive amounts
  - Excessive loan periods (i.e. > five years/reasonable time for home loan)
  - Failure to fully amortize
- If not corrected under VCP, employer liable for payroll taxes on \$10,000 and plan must issue Form 1099-R for \$10,000
- If corrected under VCP:
  - No payroll taxes
  - No 1099-R (or issued for year of correction)



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### Case Study #2

- ABC Plan made a participant loan to Sam
- The loan was for \$50,000 (and Sam's vested interest was sufficient to support that loan)
- Sam made three payments and then forgot to do more
- Can ABC self-correct to help Sam avoid taxation in year of default?



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### Case Study #2

- Answer: Yes
- The correction:
  - Sam must either make a payment equal to the principal and interest to bring him up to date; or
  - The loan may be reamortized over the remaining period of the loan (or up to five-year maximum)
- No Form 1099-R!



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### Case Study #3



- Same facts as Case #2 except that the reason why Sam's loan went into default is that there was a glitch in ABC's payroll program, and it ceased to take the payments out of Sam's paycheck
- Still self-correctable?



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### Case Study #3

- Answer: Yes
- In this case, the employer should pay the increased interest due to the fact that payments stopped
- Sam is still responsible for making up the late principal payments, either in a lump sum or by reamortizing the loan



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### Case Study #4



- DEF Plan made a loan to Frank for \$50,000
- Frank had sufficient vested interest to cover the loan
- Unfortunately, the DEF Plan does not permit loans



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### Case Study #4

- Plan is subject to disqualification
- Lucky for DEF, EPCRS permits this to be self-corrected through a retroactive amendment
- DEF amends its plan to permit loans, effective as of the date that Frank took the loan
- BUT, what if Frank is an HCE?
  - Can't be used if it predominantly benefits HCEs



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Failure

### Self-Correcting Plan Document Failures



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### Correcting Plan Document Failures: Old Rules

- Plan document failures cannot be self-corrected
  - At all
  - Ever
- Must use VCP or Audit CAP
- Plan document failure:
  - Plan provision or absence of provision that, on its face, disqualifies plan
    - Includes failure to timely adopt required interim amendment
- Failure to adopt discretionary amendment is not plan document failure (it's an operational failure)



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### New Rules: Some Plan Document Failures Still Need VCP

- VCP and Audit CAP still needed for failure to adopt plan
- Qualified plan example:
  - Employer establishes 401(k) plan effective 7/1/2019 and begins accepting deferrals
  - Employer doesn't adopt written plan document until 2020
  - Cannot self-correct
- 403(b) plan example
  - Employer has been operating 403(b) plan since 2007
  - First written plan document signed in 2018
  - Must file under VCP



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### New Rules: You May Self-Correct Many Plan Document Failures ... If You Don't Dawdle

- Primary issue: Failure to timely adopt interim amendment
- Self-correction limitations:
  - It is treated as a "significant" failure
    - Must self-correct by end of second plan year after adoption deadline
    - If IRS audits you first, it's too late
  - You must have a "favorable letter"
  - Plan must have practices and procedures



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### Favorable Letter: What Does That Mean?

- Individually Designed Plan: IRS has issued determination letter to the plan
  - It doesn't matter how recent
- Preapproved Plan: Favorable opinion letter issued with respect to "most recently expired" six-year cycle
  - DC:
    - PPA Cycle ended 1/31/2017
    - Cycle 3 ends 1/31/2023
    - Expected that restatement deadline will be 4/30/2022
  - DB:
    - PPA Cycle ends 4/30/2020; same as restatement deadline



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### Case Study #5



- Congress passes the Garbage Retirement Act of 2020 (GRA20)
- All plans must be amended to conform to the provisions of the GRA20 by 12/31/2022
- JKL Corp. fails to amend its plan by the due date
- The failure is discovered during 2023



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### Case Study #5

- The GRA20 amendment is an interim amendment
- Failure to adopt subjects the plan to disqualification
- JKL may self-correct this error by adopting the amendment, retroactive to when it was supposed to be effective
- Because this is a plan document failure, the correction must happen within the self-correction period (i.e., by 12/31/2024, assuming the JKL plan is a calendar year plan)



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### Case Study #6



- Employer is late in adopting PPA defined benefit restatement
  - Signs restatement 5/15/2020
- DB PPA Cycle ended 4/30/2020
  - Plan no longer has a “favorable letter”
- Can only correct through VCP
  - We are checking with IRS to see if this is their intention



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### Case Study #7

- Individually designed calendar year DB plan erroneously amended in 2019 to permit hurricane distributions
- Plan has favorable determination letter and practices and procedures
- Employer can self-correct by retroactively repealing amendment by 12/31/2021

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### Wait! There's More!

### Expanded Correction of Operational Failures by Plan Amendment






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### New Self-Correction Retroactive Amendment to Conform to Plan Operations

- Conditions:
  - Normal self-correction requirements (not necessarily "significant")
  - Satisfy three requirements:
    - a) Plan amendment results in increase of a benefit, right, or feature,
    - b) The increase in the benefit, right, or feature is available to all eligible employees; and
    - c) Providing the increase in the benefit, right, or feature is permitted under the Code and satisfies the correction principles of EPCRS, including:
      - Reasonable and appropriate
      - Keep assets in the plan
      - Not violate another specific rule

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### Case Study #8

- 401(k) Plan document does not allow in-service distributions
- Operationally, plan has been allowing all participants to take distributions at age 59½
  - Not predominantly HCEs
- Plan can self-correct by retroactively amending plan to add age 59½ distribution option



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### Case Study #9

- Plan document does not permit individual direction of investment
- Operationally, plan has permitted participants over age 45 to direct investments
  - Assume this is nondiscriminatory
- Cannot retroactively amend under new procedure:
  - Amendment wouldn't apply to all participants
  - If employer expands amendment to cover all participants, it wouldn't conform to prior operations
  - File under VCP



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### Other Issues

- Expect more examples of insignificant failures on IRS website:

“The IRS plans to provide additional examples illustrating whether an Operational Failure is insignificant. The additional examples will be provided on the IRS.gov website. It is expected that a link to these examples will appear on the ‘Correcting Plan Errors’ webpage on the IRS.gov website.”
- IRS still considering practitioner comments on correcting Overpayments



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## Questions?






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## CE Credit

- ERPA/ASPPA/NIPA
  - Will receive certificate by email in several days
  - ERPA will take longer (please be patient)
  - Please check spam folder
- Any questions, email: [support@erisapedia.com](mailto:support@erisapedia.com)




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## Contact Information

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