

Self-Correction of Participant Loan Failures: A brand new world!

Q&As

- 1. In a situation where there are delinquent payments due to employer error, for example, is re-amortization prior to a true default at the end of the cure period permitted? Or must the plan require the participant to continue making loan payments through the due date and re-amortize after the expiration of the cure period? Note that this would only work if the loan term originally was less than five years. What if the loan term was five years? Would your suggestion be to then re-amortize prior to the expiration of the five-year term even if the loan is not technically defaulted?**

If the plan document or loan policy provides for a grace period, the plan should not proceed with correction (reamortization) until the grace period expires. With the cooperation of the participant, the IRS may not challenge a correction that begins before the grace period expires.

A plan may use the correction option of reamortization even if the original loan period was for five years. If there was a loan default with a 5-year loan, the plan may correct by adding the missed payments to the outstanding loan and reamortizing the loan over what's left of the 5-year repayment period.

- 2. Can a deemed distributed loan which was not 1099'd be self-corrected under EPCRS if the maturity date has passed?**

If the 5-year repayment period has expired, the employer cannot use the use the SCP correction methods (e.g., reamortization) that avoid the requirement to issue the Form 1099-R. However, the employer may use the SCP correction method that allows the employer to issue the Form 1099-R in the year of correction (as opposed to the year of failure).

- 3. Is there a method for calculating interest on the lump sum make-up payment?**

The plan should use the interest rate in the loan note to determine the employee's lump sum payment for the missed payments. The employer also has an obligation to make a contribution for the lost interest (or earnings) the loan payments would have generated if the amounts had been paid timely. The employer's interest amount is the greater of the loan interest rate or the rate of return under the plan.

- 4. If the employee originally takes a 2 year loan and misses loan repayments. Can they re-amortize up to the 5 year period or can they not go up to 5 years since their original loan was only for 2 years? Employee is worried about larger loan repayments if staying within the original 2 year period of the original loan**

If the original loan was for less than 5 years, the plan can reamortize the loan using the full 5 year repayment period (measured from the date the loan proceeds were provided to the participant).

- 5. For defaulted loans, if the loan has already been deemed and the participant got 1099'd and paid the taxes on the deemed distribution, the only thing we need to do is carry it on the**

books going forward until an event that would allow us to offset it, correct? No additional correction is necessary at that point, is that correct?

You are correct. The additional interest which accrues after the loan has been treated as a deemed distribution (and before offset) is relevant for top heavy and vesting purposes, but will never be reported on a Form 1099-R. That is why many referred to it as “phantom” interest.

6. Can you re-amortize inside the cure period or must you wait until the cure period ends? If you have to wait to re-amortize, why? Doesn't that argue for a shorter cure period in order to avoid accrued interest?

If the plan or the plan’s loan policy includes a grace period, the loan is not in default until the end of the grace period. However, if the participant concurred with a correction through reamortization before the end of the grace period, it is doubtful that the IRS would challenge the correction.

7. What if a loan defaulted, and the grace period passed, causing a 1099-R to be issued to the participant. Is there any way to subsequently issue a corrected 1099-R and move forward with self-correction?

As long as the Form 1099-R was issued after April 19, 2019 (effective date of the new EPCRS), you should be able to reverse the Form 1099-R and proceed with the EPCRS correction method.

8. The re-amortization example implies that the participant still pays the loan accrued interest that occurred during the period of no payments and the employer also funds a lost earnings payment to the participant’s account for the period of no payment. Is this correct?

You are correct. Under either the reamortization correction method or the lump sum payment correction method, the employer makes a payment for the interest (or earnings, if greater) that the missed payments would have generated within the plan if the amounts had been paid timely.

9. Just to confirm. Can an employer self-correct a loan that defaulted in 2018 after 4-19-2019, or only loans that default after that date?

The plan can correct a loan failure that occurred before or after April 19, 2019, as long as the employer has not already treated the loan failure as a deemed distribution prior to April 19, 2019. In other words, if the employer issued the Form 1099-R before April 19, 2019, I think it would be aggressive for the employer to reverse the Form 1099-R and use the new SCP correction methods.

10. Could you please go back to slide 15 and clarify when the employer has to pay taxes? You said only if the error was at the beginning. What does that mean?

Treas. Reg. §1.72(p)-1, Q-15 provides that: “To the extent a loan, when made, is a deemed distribution ... the amount includible in income is subject to withholding. ... If a deemed distribution of a loan ... results in income at a date after the date the loan is made, withholding is required only if a transfer of cash or property (excluding employer securities) is made to the participant or beneficiary from the plan at the same time.” In other words, a loan that violates the amount limitation, the time period requirement or the level amortization would violate the Code §72(p) when the loan is made and would be subject to income tax withholding. On the other hand, if the violated Code §72(p) at a later date (e.g., loan defaults because of a failure to withhold loan payments), the withholding requirement is inapplicable. Of course,

if the plan uses an SCP or VCP correction method that avoids the issuance of the Form 1099-R, the withholding issue does not apply.

11. Full-time participant is making loan payment regularly and then changes to PRN status. Loan payments become sporadic, for instance, maybe 2 of six required payments made during the quarter, one in January and one in March. Participant does not make up missed loan payments in between the various payroll deductions. When does the clock start ticking when payments are missed sporadically?

In general, once a payment is missed the clock starts. However, the IRS permits a plan to apply a payment to a previous month to avoid default. For example, in your situation, assuming the plan applied the maximum grace period, the employer could apply the March payment to February and then the May payment could cover the March payment. This approach can work for a while, but if the participant does not get on a steady repayment schedule, there will be a payment that is not made up by the end of the grace period. In that situation, you have a loan default and a deemed distribution. The plan will need to correct or issue a Form 1099-R.

12. Do the required policies and procedures need to be specific to the sponsor's situation? Are there any prototype examples of these against which the Service would review them?

Practices and procedures do not have to be tailored to the sponsor but may be. The IRS does not provide a prototype for practices and procedures; only examples. Under EPCRS §4.04, the IRS provides example - operating manual with steps for performing tests. The IRS also states that the plan document alone is not sufficient to establish that the plan has practices and procedures.

13. I have a situation where a loan was taken in December 2017, to be paid off by November 2018. We just found out. If we were to self-correct and re-amortize, do we just go out 1 year?

No, you can reamortize the loan over a 5-year repayment period measured from December, 2017.

14. Is there any grace period for the 5 year amortization schedule, example if the 5 years is exceeded only by a month or 2?

No. Neither the Code nor the regulations provide an extension of the 5-year repayment period (other than for military leaves of absence). In other words, if the loan exceeds the 5-year repayment period by one or two months, the loan violates the requirement and the loan is a deemed distribution. However, in practice, an IRS agent may choose not to enforce the rule strictly.

15. Regarding the effective date of using the new SCP loan correction for defaulted loans. Are you saying that for a significant error, the new rules only apply to significant errors looking forward from April 19, 2019 and not those that may have occurred during the last two years? If your answer is that the new SCP loan correction may be used for significant errors that occurred during the last two years, then why would the new SCP rules not allow a correction of insignificant errors that occurred before April 19, 2019?

EPCRS §2.02 provides: "Beginning April 19, 2019, Plan Sponsors that satisfy the eligibility requirements of SCP may use the procedures under this revenue procedure to correct certain Operational Failures or Plan Document Failures under SCP." Any loan failure (whether it occurred before or after 4/19/19) that has not been corrected by April 19, 2019, can be corrected under the new EPCRS procedure, including

the self-correction options. If the plan treated a loan failure as a deemed distribution and issued a Form 1099-R prior to April 19, 2019, the new EPCRS correction options probably are unavailable. The effective date of the new EPCRS procedure does not affect the issue as to whether the failure is significant or insignificant.

16. What if a participant requests a home loan for 10 years, then you discover the participant either (1) didn't go through with purchasing a house or (2) lied about purchasing a house? Would you re-amortize to 5 years under SCP or VCP? (Record keeper processes loans and administrator has to collect proof of home purchase after the loan is processed.)

You describe two different situations that will result in different resolutions. If a plan issues a home loan with a 10-year repayment period and the purchase does not occur, that fact pattern does not result in a loan failure if the employer promptly reamortizes the loan over a 5-year period. If the plan does not reamortize the loan, the employer would need to file under VCP to avoid issuing the Form 1099-R. With respect to the second situation, if the employer establishes that the participant misrepresented the purpose of the loan to obtain the longer repayment period, the employer should correct the failure under VCP to avoid issuing a Form 1099-R.

17. For a loan that exceeds 5 years, can the participant just payoff the loan prior to the period exceeding 5 years?

If the loan exceeded the 5-year repayment period when made, the loan is a deemed distribution from the beginning. If the employer wants to avoid issuing a Form 1099-R, the correction is under VCP. To correct, the employer would need to reamortize the loan over the 5-year period. Alternatively, the employer may issue a Form 1099-R in the year of correction, but the deemed distribution amount is the entire loan since it never complied with Code §72(p).

18. Can you explain the "level amortization" rule? It's not new, but I'm still not clear on what it really means. I understand that it means that an amortization schedule with level payments need to be produced, but some practitioners think that this also means unscheduled prepayments of some principal balance are not allowed unless it's for the full principal balance. And, some don't believe that. What do you think?

The regulations do not address the impact of prepayments on the level amortization rule. My feeling is that as long as the loan repayment schedule provides for level payments, the plan may allow prepayments. However, the plan may want to charge additional fees for prepayments (unless it is a complete payoff of the loan) because it adds to the administrative costs of loan administration.

19. As a follow-up...what technical authority limits the use of currently effective Rev. Proc. 2019-19 correction methods only to errors occurring on or after April 19, 2019? Doesn't the nature of the SCP correction rules for insignificant errors allowing for correction of prior years' issues necessarily allow a plan to correct prior years' issues under newly issued SCP rules?

See the response to question 15.

20. Do you recommend that if you are doing a retroactive amendment that you add language to amendment such as 'Pursuant to Revenue Proceeding 2019-19, the plan is amended effective.....'?

There are many ways to phrase a retroactive amendment. The phrasing you propose would be appropriate.

21. When a participant fails to make a loan payment because out on maternity leave is the employer responsible to pay the accrued interest when the loan is re-amortized?

No. Assuming the loan policy permits suspensions, this is not a loan failure so the plan does not need to correct. The accrued interest would be the responsibility of the participant. Generally, the plan reamortizes the loan with the accrued interest over what is left of the 5-year repayment period.

22. Regarding the 5 year max amortization for a personal loan, I believe you said that the loan duration clock starts the day the participant receives the loan check. How would we know when they actually received the loan check? I would think that it would be reasonable to make the 1st loan payment beginning on the next available payroll within a reasonable time based on the request/processing date. Especially true with balance forward plans.

A more accurate statement would be the 5-year period starts with the date the loan proceeds are distributed by the plan. I will concede that regulations do not address this rule as clearly as they should. However, legally, the loan (or debt) starts when the proceeds are distributed. I suspect you may find IRS agents that do not impose the rules strictly. However, it is a gamble that I wouldn't want to take.

23. What attachment to the 5500 for late deposit of loans if you correct but do not go through VFCP?

Actually, you use the attachment whether you use VFCP or self-correct. See the instructions to question 4a of Schedules H and I. The instructions provide a sample of the attachment.

24. Shouldn't you use the greater of the actual rate of return of the plan during the period a deposit should have been paid to the plan vs. the 6621(a) (2) rates?

The correction for a late deposit of deferrals or loan repayments is for the employer to deposit the deferrals or loan repayments, plus the greater of the lost earnings to the plan or restoration of the profits received by the employer for the use of the money. However, under VFCP, the employer may determine lost earnings by using the Code §6621(a)(2) interest rate. The DOL has provided an online calculator to determine lost earnings under the Code §6621(a)(2) interest rate. The DOL's position is that employer's only should use the online calculator it files under VFCP. However, many practitioners who self-correct use the online calculator.

25. Example - loan issued 11/2017. No payment to date has been made. Discovery in 5/2019. No 1099R issued yet. Option still exist to self-correct through catching up or re-amortizing?

Yes.

26. You indicated that technically you can only use the DOL calculator for calculating lost earnings if you file through the VFCP, however most people use it anyway because it is easier.

That's correct.

27. This may be off topic, but what are the ramifications if the Plan's loan program is limited to only active employees, i.e., does not allow a former employee that is a party-in-interest to request a loan?

A participant loan is a prohibited transaction unless it satisfies all of the statutory exemption requirements, including the requirement to make loans available on a reasonably equivalent basis. A loan program that excludes former employees violates this requirement. DOL Advisory Opinion 89-30. However, a plan may limit loans to former employee participants who are parties in interest. In the situation you describe, you violate the prohibited transaction exemption requirement and your loan program is a prohibited transaction. The plan needs to amend its loan program to comply with the exemption requirements.

28. You indicated that technically you can only use the DOL calculator for calculating lost earnings if you file through the VFCP, however most people use it anyway because it is easier. Is it ok to use the DOL calculator if not going through VFCP? That would save a lot of time and maybe money to the client.

The DOL's position is that a plan only may use the online calculator if the plan files under VFCP. Nevertheless, many practitioners that self-correct use the online calculator. If the DOL investigated your plan and challenged your use of the calculator, the worse the DOL could do would be to: (1) have the plan calculate and contribute the difference between the actual earnings and what the calculator determined, and (2) assess a 20% penalty on the additional earnings contribution. Frequently, the amount is not significant so plans are willing to take the risk.

29. Does the IRS accept the DOL VCP Calculator for these late deposits as EPCRS says that you use actual investment rate of return?

The IRS has no responsibility with respect to the late deposit of loan repayments (other than the prohibited transaction excise tax) and EPCRS does not address the failure. This failure is the responsibility of the DOL.

For the various corrective contributions required under EPCRS, the IRS requires the plan to adjust the corrective contributions for earnings. Generally, the employer would use one of the earnings calculation methods set out in Appendix B of EPCRS. However, in certain situations, the IRS will permit the employer to use the VFCP calculator to determine earnings. See EPCRS §6.02(5)(a).

30. What about an excise tax of 20 cents? Do you still file 5330?

The instructions to Form 5330 do not provide for a de minimis exception. The employer might round the tax up to \$1.00. I would pay the minimal excise tax so I could report that I followed all of the correction steps.

31. Current loan provision permit for a maximum of 5 loans...one participant has exceeded the limit by several loans. We can amend the whole plan retroactively or can we amend the plan indicating that unlimited loans were made for this one participant only (participant is a NHCE)? Would we need to change back to just 5 loans? Plan Sponsor does not want to make permanent change to unlimited loans. Currently we are in the process of paying off loans with lowest balances while keeping the 5 year spam of the loan in mind.

Since the participant who exceeded the loan limit is a NHCE, you can limit the retroactive amendment to that individual. The amendment should remain in effect for the balance of the plan year plus an additional plan year.

32. Could employer deposit 15% excise tax to participants in plan vs. send tiny check to IRS?

If you file under the DOL's Voluntary Fiduciary Correction Program and satisfy the requirements for paying the excise tax to the plan, the employer can contribute the excise tax to the plan.

33. There are still large record keepers who start the 5-year loan term based on the scheduled 1st payment of the loan rather than the date of the loan origination. We are a TPA and have many arguments with these record keepers who site loan rules from many, many years ago. Are there any official sites that discuss the 5-year term beginning on the date of the loan origination we can provide the record keepers?

I also have had discussions with recordkeepers regarding this issue. Generally, when I have asked them to provide a written indemnification to the employer if the IRS challenges their interpretation of the 5-year repayment rule, they decline which demonstrates to me their position is not that strong.

The IRS's 401(k) Plan Fix-It Guide states:

"The **loan terms** should require the participant to make level amortized payments at least quarterly.

- Each payment should include an allocation of principal and interest.
- The loan must be repaid within five years unless the participant uses the loan to purchase his or her main home. The five year repayment period is determined from date the loan was made."

I am not certain what "old" loan rules to which they are referring. I would love to know the citation. I know that some institutions cite some legislative history that states a reasonable delay in the start of the loan repayments will not violate the level amortization requirement, but that legislative history is not discussing the 5-year repayment rule. Also see response to question 22.

34. Should we file the Form 5330 for the 15% excise tax if the excise tax is \$0?

If the excise tax is \$0, you would not need to file a Form 5330.

35. Talking about Form 5330 that must be filed even if a couple of bucks. For 2018 lots of plans had negative earnings, so we used Federal short term rates - pretty low. In several cases, we've seen Forms 5330 with \$0 due with it (the Form 5330 can have rounding on or off). Would you file a Form 5330 with \$0 penalty?

See response to Question 34.

36. If a loan is issued and the participants goes on maternity leave, family leave or disabled with no loan payments, comes back to work and the payments go out further than the maturity date. Is this a problem? How to correct??

Yes it is a problem. Assuming the original loan was for 5 years, the loan would violate the 5-year repayment period requirement. The plan may avoid issuing a 1099-R by correcting under VCP. The correction would be to reamortize under the correct repayment period.

37. If we got a letter about fling through VFCP and we self-corrected. Do you advise us to go through VFCP?

That's a judgment call that needs to be made by the plan's attorney. You might contact the DOL office that issued the letter and discuss it with them.

38. Under VFCP you can get out of filing the 5330 if the total excise tax is less than \$100 and the excise tax is allocated to affected employees. Correct?

There is an exception that permits an employer to contribute the excise tax to the plan. The plan must file under VFCP and satisfy certain requirements. PTE 2002-51.

39. Since filing the excise tax removes statute of limitations, would that impact thinking on filing for 20 cents?

Filing the Form 5330 and paying the excise tax does start the statute of limitations.

40. How is the accumulated deemed distribution interest treated when a participant ultimately takes distribution?

After the plan treats the loan as a deemed distribution (but the loan has not been offset), interest continues to accrue until it is offset. However, the interest is often referred to as "phantom" interest because it is not reported on a Form 1099-R.

41. Is SCP available for loans implemented prior to 2019 such as a missed first payment being withheld from 2016 payroll on a still active loan? This would allow for no 1099R in 2016 or 2019? Does it matter if it is not active?

Yes, an employer may correct a 2016 loan failure under EPCRS. However, since the failure occurred more than two years ago, a plan only may self-correct if the failure is insignificant.

42. If your amortization schedule is a week or two over 5 years from the date the participant received the loan, do you need to re-amortize? Or, can you leave it alone since the final repayment would still be within the grace period?

You need reamortize the loan over the 5-year repayment period. Since the loan violated the rules from the beginning, the IRS probably will not accept the grace period argument.

43. Can you clarify how you indicate that the late contributions have been corrected on the 5500? Our clients are required to file schedule I.

The instructions to line 4a of Schedule I describe the attachment to be included to report the correction.

44. What is the correction method if a loan is issued at a higher interest rate than what the Plan Document states it should be?

The DOL prohibited transaction rules require the plan to use a reasonable interest rate. Most plans tie it to a published interest rate (e.g., prime +). Assuming the plan's rate satisfied the DOL's requirement, the plan should comply with its terms. The correction would be to reamortize the loan using the correct interest rate.

45. I have a client that self-corrected and just got a letter last week from the Philly DOL office because they saw late deferrals reported on the 2018 Form 5500-SF. It is not threatening, like the Chicago letter, but still suggests that they file through the VFCP. They already self-corrected with lost earnings and the filing of a 5330. Should I be concerned if we do NOT file with the DOL VFCP? Do you expect we will get many of these letters this year? I thought the DOL would stop sending them after the feedback that they received last year.

The DOL letter for late deposit of deferrals and loan payments is common. Many practitioners respond to the letter outlining the correction methods they employed. Generally, this satisfies the DOL. However, you should run this past the plan's attorney.

46. Can the re-amortization correction for missed loan repayments extend the loan repayment period only for the number of loan repayments missed (as opposed to the full 5 years) for a loan that was originally taken for a less than 5 year term?

Yes. The plan may reamortize a loan over a period that is less than the original 5-year repayment period.

47. A plan's loan interest rate is prime plus 1% but the plan used varying interest rates of prime plus 2%, prime plus 1% for a few plan years. Would they be eligible to self-correct? This was identified in this year's audit that is in progress.

EPCRS does not address this failure directly. However, the failure you identify is an operational failure (failure to comply with plan terms) that the plan should be able to correct under SCP. The correction would be to reamortize the loan using the correct interest rate.

48. We have had a few clients recently receive a letter from the DOL (Philadelphia office) regarding reporting of late deposits per 5500 - and there seems to be additional language (when we compare this year's letter to what clients have received in the past) that is "encouraging" plan sponsors to file and specifically says that just correcting is an informal process and doesn't protect the plan from potential audit. We kind of took that to mean clients should file; your opinion?

See my response to question 45.

49. To clarify the taxation on a deemed distribution. If a loan should have been deemed 3/31/2012, is it your opinion that interest accrues for tax purposes until the date in the year of taxation? For example, if the loan is deemed 6/30/19, interest would accrue from 2012-2019?

Yes. If the loan is not offset or treated as a deemed distribution, the loan will continue to accrue interest.

50. Can you utilize the allowable IRS cure period to "cure" a loan not paid in full by the end of the statutory 5-year term?

A plan that issued a loan that exceeded the 5-year repayment period by a couple of months cannot use the grace period to avoid having the loan treated as a deemed distribution. However, I have heard IRS officials verbally state that if a participant misses a payment in the final quarter of a 5-year loan, the plan could take advantage of the grace period.

51. What about loans to seasonal employees who are off from May 15 to Oct 15 every year.

This issue has been posed to the IRS and they have never provided any exceptions for seasonal employees. So, employer would need to make arrangements for the seasonal employees to make payments (e.g., ACH) during the periods when they are "off." Alternatively, if the plan can pass the nondiscrimination requirements, they could exclude the seasonal employees from loans.

52. If someone is on leave of absence and returns, can you extend the length of the repayment period, as long as it isn't beyond the 5 year limit?

Yes.

53. If an employee has terminated and has a loan balance and remaining funds in the plan but has not initiated a distribution of their plan, should the balance of the loan be offset or considered a deemed distribution?

If the participant has terminated employment, the plan can effect a loan offset (distributable event) even if the participant does not initiate distribution with respect to the balance of his/her account.

54. In other webinars and seminars, it was stated that the DOL calculator cannot be used for lost participant earnings unless there was VFCP filing or if the calculator interest rate is higher than the actual return. I had an IRS agent question the use of the calculator during an audit and we demonstrated that this was permissible because actual earnings was a loss. Did I understand you correctly that the calculator can be used if it is "difficult" to calculate earnings?

For a late deposit of loan repayments, see the discussion under Questions 24.

For corrective contributions under EPCRS, the IRS permits the employer to use the online calculator:

(a) Reasonable estimates. If either (i) it is possible to make a precise calculation but the probable difference between the approximate and the precise restoration of a participant's benefits is insignificant and the administrative cost of determining precise restoration would significantly exceed the probable difference or (ii) it is not possible to make a precise calculation (for example, where it is impossible to provide plan data), reasonable estimates may be used in calculating appropriate correction. If it is not feasible to make a reasonable estimate of what the actual investment results would have been, a reasonable interest rate may be used. For this purpose, the interest rate used by the Department of Labor's Voluntary Fiduciary Correction Program Online Calculator is deemed to be a reasonable interest rate. The calculator can be found on the internet at <http://www.dol.gov/ebsa/calculator>. EPCRS §6.02(5)(a).

55. If loan last payment made 10/27/16 and they have cure period which would be 12/31/16 end of quarter following quarter stopped making pmt. Balance at 10/27/16 say is 18,000 and balance at 12/31/16 is 13,000. What is the 1099 R issued for? 18,000 plus interest through 12/31/16 or the 12/31/16 total loan balance. The loan continues on through 2019.

I am having a difficult time following the fact pattern. You might call me to discuss.

56. On Slide 13, you indicate that EPCRS says that the employer pays the interest that accumulates as a result of such failure and I see that requirement in Section 6.02(6) of Rev. Proc. 2019-19. However, I'm confused about this requirement..... Slide 13 also indicates that one of the approved correction methodologies is for the loan and accrued interest to be

reamortized. If that is the case, isn't the participant already paying the accrued interest as part of the reamortized loan repayments? If so, why should the employer also pay or does the employer pay the accrued interest to the participant rather than the plan? I'm probably just missing something here but I'd appreciate hearing your thoughts on this.

Let me see if I can illustrate it with an example. Steve took out a 5-year loan with monthly payments of \$100 (principal) and \$5 (interest). Let's assume that Steve missed 10 monthly payments. If the plan selected the reamortization correction method, the plan would add \$1,050 to the remaining loan balance and reamortize it over the remaining portion of the 5-year repayment period. Alternatively, the plan could correct by having Steve make a lump sum payment of \$1,050 and pick up with making the regular loan repayments of \$105/month. However, to complete the correction under either method, EPCRS requires the employer to make a payment of the interest (determined at the greater of the loan interest interest or the plan's rate or return) that accumulates as a result of the failure. In other words, if the loan repayments had been made timely, the repayments would have in the plan generating interest (earnings) for the plan (or participant) up until the correction. For example, if Steve failed to make a January 31, 2018 loan repayment and it was not corrected until November 30, 2018, the employer would need to make a payment of the interest (earnings) that would have been generated over the 10-month period. Generally, the interest payment the employer makes is nominal.

57. Beginning in July 2018, payments for an existing loan continued to be withheld from pay, but were not remitted to the Trust account. A Form 1099-R was issued in January 2019 on the "defaulted" loan. The error was discovered in March 2019 and all loan payments were forwarded to the Trust on 3/25/19. Does the Plan Sponsor need to file through BOTH VCP and VFCP, along with a Form 5330? Should they issue a revised Form 1099-R for 2019 or 2018?

If loan repayments were withheld but not deposited, the plan does not have a 72(p) failure (i.e., payments were timely made to a fiduciary of the plan). Therefore, no EPCRS correction needs to be made. However, the failure to deposit the loan payments timely is both a prohibited transaction and a breach of fiduciary duty. You may resolve the failure under VFCP. Some practitioners use the VFCP methodology for correction but do not file. In such a case, the employer should note the correction on its 5500 filing. As for the 1099-R filing, the employer should reverse the 1099-R.