



Correction Primer 2: Deeper Dive into SCP and VCP

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Your Presenters Today



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Agenda

- Session 1 Recap
- Self-Correction Under EPCRS
 - What Can Be Corrected?
 - What is an Eligible Inadvertent Failure?
 - Timing Requirements
 - How to Do It
 - Corrections
 - Documentation
 - Notifying Participants
 - Changing Procedures
- Voluntary Correction Program
 - How it Works
 - Why Use It?
 - How to Do It: VCP Submission Preparation
 - Common VCP Submissions
 - Dealing with the IRS
 - Operating the Plan in the Meantime
 - Compliance Statement



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Recap From Primer Session 1

- EPCRS is the consolidated program established by the IRS to correct qualification failures – i.e., things that could cause the plan to be disqualified (Rev. Proc. 2021-30, as augmented by SECURE 2.0 and Notice 2023-43)
- EPCRS contains three programs:
 - Self Correction Program (SCP) – **do it yourself** (i.e., no IRS involvement)
 - Voluntary Correction Program (VCP) – **do it with the IRS's assistance**
 - Audit Closing Agreement Program (Audit CAP) – **do it or else** – the IRS offers this as a means of resolving errors found in audit



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Self-Correction under EPCRS



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Self-Correction Program

- IRS permits certain qualification failures to be resolved by the plan and its sponsors without IRS involvement
 - If done right, discovery of the failure in a later IRS audit will not cause the plan to be disqualified
 - SCP is popular because you don't have to file with the IRS
 - BUT, you must follow proper procedures and maintain documentation in the plan's files



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What Can Be Corrected under SCP?

- SCP should only be used to correct an Eligible Inadvertent Failure
- Defined by the law to be:
 - A failure that occurs
 - Despite the existence of practices and procedures
 - That satisfies the standards of Section 4.04 of Rev. Proc. 2021-30 (which requires that the established practices and procedures be “reasonably designed to promote and facilitate overall compliance in form and operation with applicable Code requirements”)
- Note: manufactured failures are not “inadvertent”



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Not an Eligible Inadvertent Failure

- Eligible Inadvertent Failures do not include:
 - Egregious failures – EPCRS examples:
 - Plan that consistently and improperly covers only HCEs
 - Plan that provides more favorable benefits to owners based on purported collective bargaining agreement
 - DC plan where contributions for HCE are several times greater than \$415 limit
 - Diversion or misuse of plan assets; or
 - Failures related to an abusive tax avoidance transaction



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Not an Eligible Inadvertent Failure (cont.)

- Notice 2023-43 specifically excludes:
 - Failures to initially adopt a written plan or post-2008 403(b) plan
 - What about participating employers in CG/ASG plans?
 - Failures in orphan plans
 - Significant failures in terminated plans
 - BUT: does not define “terminated plans”
 - Failure involving excess contributions to a SEP or SIMPLE IRA where the correction leaves the excess in participant’s IRA



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Not an Eligible Inadvertent Failure (cont.)

- Notice 2023-43 specifically excludes (cont.):
 - Failures in SEP/SIMPLE that do not use model or prototype plan document
 - Does that mean they needed to be on model/prototype document when the failure happened or upon correction?
 - Failures under IRC §409 in ESOPs (and especially §409(p)) that involve tax consequences other than disqualification



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Time Window for Self-Correction

- Notice 2023-43 requires that the failure be corrected within a reasonable period after identification
 - “Reasonable period” is facts and circumstances determination
 - Notice provides that time is “deemed reasonable” if correction occurs by last day of 18th month following failure identification
 - This should be a “safe harbor”
 - This means you’re racing against the clock that the IRS won’t catch the plan



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If IRS Tags the Plan for Audit During SCP Process

- The IRS will permit completion of self-correction if the Plan Sponsor has demonstrated a “specific commitment” to self-correct
 - Plan Sponsor must be “actively pursuing correction of the specific identified failure”
 - What is enough?
 - Facts and circumstances determination by IRS



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What You Need To Do For SCP

1. You must correct the failure in a permissible fashion
 - How do you know what that is?
 - Wherever possible, follow the correction ‘recipes’ from EPCRS (See Sections 4 and Appendices A and B for common failures)
 - If you want to go into the gray areas, you should consider VCP
 - Nonamender Corrections:
 - Review IRS Employee Plans Newsletter May 23, 2022
 - Outlines requirements for nonamender corrections
 - Pre-approved plans become individually designed after end of RAP



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What You Need To Do For SCP (cont.)

1. You must correct the failure in a permissible fashion (cont.)
 - Earnings must be added to contributions, allocations, refunds for the period between the failure occurring and the correction being made
 - **Note:** DOL Online Calculator is NOT your default for earnings – very rarely permitted
 - Refer to EPCRS, Appendix B, Section 3 for most earnings information
 - In general, use the rate that the participant would have earned had the plan been administered properly (i.e., actual rate of return on funds)
 - Can usually use highest earning fund option during the period for additions being made to NHCE accounts, if details about actual rate are unavailable
 - Sometimes, may use weighted average rate of return on all fund options



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What You Need To Do For SCP (cont.)

1. You must correct the failure in a permissible fashion (cont.)
 - Earnings must be added to contributions, allocations, refunds (cont.)
 - Other than correcting for late deposits of deferrals, you can generally apply losses (yes, 2022, I'm looking at you) and Auto Enroll Matching Contributions
 - Automatic Enrollment failures have their own earnings methods (EPCRS, Appendix A.05(8)(b))
 - If participant has made no investment election, may use QDIA rate (but not if there is a loss)



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What You Need To Do For SCP (cont.)

2. Document the Correction
 - We use SCP “Memo” to the file to meet documentation requirements
 - SCP Memo Elements:
 - Section 1: Explanation of the failure
 - What the failure is
 - Dates of when the failure was occurred (i.e., affected plan years)
 - Date on which the failure was identified and how it was discovered
 - Number of employees affected (HCE/NHCE)
 - Description of procedures in place to avoid the failure and why they were ineffective



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What You Need To Do For SCP (cont.)

2. Document the Correction (cont.)

– SCP Memo Elements (cont.):

- Section 2 – Explain how the correction was done
 - Cite EPCRS basis for correction methods, including earnings
 - Attach calculations of any dollar adjustments to accounts, payouts, contributions, etc. and other supporting materials
 - » Include details on number of affected participants (HCE/NHCE), dollar amount of correction, amount of earnings
 - How earnings were calculated
 - Include dates when correction steps were taken (especially including when corrective deposits and payouts are made)



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What You Need To Do For SCP (cont.)

2. Document the Correction (cont.)

– SCP Memo Elements (cont.):

- Section 2 – Explain how the correction was done (cont.)
 - For nonamender failures, need to confirm why plan satisfied any IDP requirements (or how any failures were corrected)
- Section 3 – Identify any missing participants and how they will be tracked down
 - Launch the tracking process as soon as the participants requiring correction are identified



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What You Need To Do For SCP (cont.)

2. Document the Correction (cont.)

– SCP Memo Elements (cont.):

- Section 4 – What new procedures will be implemented to prevent this failure from recurring in the future?



– Spoiler Alert: Mere engagement of a TPA is not sufficient

– Must be something that the Plan Sponsor will now do to prevent further failures

» E.g., agreement to meet annually with service providers

» E.g., implementation of written internal procedure for transmission of deferrals to financial institution

– Procedure should address the specific failure

» E.g., compensation failure should be resolved with proper review/coding



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Voluntary Correction Program (VCP)



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Voluntary Correction Program

- VCP filing must be submitted to the IRS for approval (EPCRS Sections 10-11)
 - Filings must be done electronically through www.pay.gov
 - Filing should contain all necessary forms and exhibits based on the type of failure
 - Forms available on IRS website
 - Must pay the required User Fee
 - User fees are announced annually by the IRS, usually in Rev. Proc. 20XX-4
 - Current fee schedule (based on assets at the end of the prior year – pull from Form 5500):

– \$0 - \$500,000	\$1,500
– \$500,001 - \$10m	\$3,000
– \$10m+	\$3,500



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Voluntary Correction Program

- At end of process, IRS issues a Compliance Statement, reflecting the facts of the situation and the required correction
 - The Compliance statement includes the Form 14568 that the taxpayer (or its representative) filed at the submission, with the narrative explaining the facts of the case and the correction



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Why Use VCP instead of SCP?

- Missing all plan documents
- Not allowed to correct this failure under SCP
 - E.g., no practices/procedures
- Desired correction method doesn't fit in nicely with approved corrections under EPCRS Appendices A & B
 - Coloring outside of the lines = VCP
- Client likes a conservative approach
- Plan is being merged with another or the plan sponsor is being acquired and buyer demands VCP assurances



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VCP Features That May Cause Concern

- Plan Sponsor is required to fully correct the failure for all years
 - Includes “closed” years
 - There are only very rare exceptions to fully correcting the failure
 - If the Plan Sponsor is not prepared to fully correct (either emotionally or financially), need to consider whether to file or not
 - Read the Penalty of Perjury statement carefully – cannot make misrepresentations as to the failure period in VCP filing



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VCP Features That May Cause Concern (cont.)

- VCP takes time
 - IRS may go radio silent for over a year (IRS is currently reviewing submissions from September 2022)
- Negotiations and responses need to be handled timely and carefully
 - IRS will reject filing if you don't meet deadlines
 - Correction must be made within 150 days of receipt of final Compliance Agreement
- The filing itself needs to be carefully prepared and professional fees will be incurred
 - Note: it may look easy, but it needs to be comprehensive
- Anonymous submissions no longer permitted, so there is some vulnerability if the IRS does not like proposed correction (but see below re: presubmission conferences)



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How to Prepare a VCP Submission

- You must be an ERPA, attorney, enrolled actuary, or CPA to do a filing for a client and be on the Form 2848
 - Otherwise, need to include a Form 8821, which will give you copies of correspondence, but you won't be able to work directly with IRS
- VCP Submissions are filed through www.pay.gov
 - Entire package must be a single PDF no bigger than 15MB
 - Once filed through pay.gov, Control Number will be issued which will be needed for all future correspondence or amendments to VCP



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Presubmission Conference

- If you want to VCP but have questions about issue not addressed in the EPCRS Rev. Proc., can request a presubmission conference with the IRS
 - No fee for conference
 - Informal: Conference occurs in a phone call and IRS will not provide anything in writing about what was discussed (only that conference took place), including its agreement to a correction procedure
 - No reliance (although no reports so far of practitioner dissatisfaction)
 - Need to submit Form 8950 to IRS with detailed explanation of failure, correction, earnings method, plan provisions, other information – in other words, pretty similar to a full VCP submission



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How to Prepare a VCP Submission

- Typical submission package will need:
 - Cover letter
 - Form 2848 or Form 8821
 - Penalty of Perjury Statement
 - Form 8950 (complete as PDF, but you won't be uploading this)
 - Form 14568
 - Attachment to Form 14568 (your narrative)
 - Additional Form 14568 sub-form(s) (-A through -I) for common failures
 - Exhibits supporting correction



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Form 14568 Attachment: The Narrative

- Relates to Sections II, III, IV, and V of the Form 14568
 - What the failure is
 - How it is being corrected
 - How you will find and notify former participants or beneficiaries
 - How you will change the administrative procedures for the plan
- This is where the IRS reviewer gets their first impression of what you are trying to do, and makes their first judgment as to whether they are sympathetic to the client's situation



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Form 14568 Attachment: The Narrative (cont.)

- This is the meat of your application
 - Use your creative writing skills
 - This should be where the majority of your time preparing the submission should be spent
- As mentioned above, this will be part of IRS's Compliance Statement, so it is common that the IRS will request that you make changes to this form as the review progresses ... expect this, regardless of how much time you put into it
- Must include the basic elements discussed re SCP memo: years affected, numbers of HCEs/NHCEs affected, dollars involved



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Form 14568 Attachment: The Narrative (cont.)

- Do not undervalue the importance of this part of the submission
 - Common for TPAs to be too succinct, too dismissive
 - Particularly if you are using an unusual correction, this is where you convince the IRS that your client deserves sympathy, empathy, leniency, and the correction it is requesting
 - Explain why the correction you are using fits into the EPCRS correction principles (Rev. Proc. 2021-30, Section 6)
 - Explain why this is fair or even additionally beneficial to NHCEs
 - Describe procedures in place and how the failure inadvertently occurred



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Form 14568 Attachment: The Narrative (cont.)

- More suggestions:
 - Be well organized
 - For example, if you have multiple failures, remember to number them "Failure #1," "Failure #2," etc.
 - Make sure you have a very clear explanation of what happened and why
 - Tip: have a colleague unfamiliar with the situation read it – if they can't understand what happened, the IRS won't either



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Form 14568 Attachment: The Narrative (cont.)

- More suggestions:
 - If using unusual correction, be compelling as to why the IRS should approve it
 - Always cite sections of EPCRS that direct or support the correction you are using



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Common VCP Submissions

- Nonamender Failures (use VCP if there are no documents or plan has no policies/procedures)
 - Need to prepare missing restatements and interim amendments and have client sign before submission
 - Will also need to include Form 14568-B
 - If documents that are missing are old and master templates can no longer be accessed, can use a later document template and date it for the missing restatement
 - E.g., if missing GUST, but only have an EGTRRA document, use the EGTRRA document and use effective date 1/1/2003



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Common VCP Submissions (cont.)

- Nonamender Failures (cont.)
 - If no documents can be located, you will still need to provide evidence of contemporaneous intent to form the plan
 - This can be account applications, email correspondence, etc.
 - If Forms 5500 were done, first submission can also be used
 - With no documents, the question has to be asked – how was the plan operated?
 - Could lead to other failures such as safe harbor failures, eligibility failures, compensation issues, etc.



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Common VCP Submission (cont.)

- Operational Failures
 - Definition: failure to follow the terms of the plan
 - “Normal” correction: fix operations to match what the plan says
 - Must show calculations comparing what participants got under original operations, and what the impact is of the correction
 - If correction covers multiple years, permitted to submit only a sample of calculation if it is uniform for all years



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Common VCP Submission (cont.)

- Operational Failures (cont.)
 - Option: amend plan with retroactive effective date to match actual administration
 - Once rarely approved, but now widely available, but only if:
 - You are matching what was actually done
 - The effect of the amendment does not decrease the benefits or rights of anyone
 - If using retroactive amendment, highlight why the proposed amendment is more favorable to the NHCEs than the provisions as originally written



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Common VCP Submission (cont.)

- Operational Failures (cont.)
 - Option: amend plan with retroactive effective date to match actual administration (cont.)
 - Identify original document provision and explain why the amendment complies with the principles of EPCRS and IRC, where applicable
 - Again, citations are always needed
 - Still need to show calculations and who benefits
 - Must include the proposed amendment with the submission, but NEVER have the client sign it until the IRS approves it (remember: not true for nonamender failures – for that, client signs before you file)



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What To Do When the IRS Surfaces

- Once a real, live IRS reviewer picks up the submission, they often have questions or requested changes to Form 14568
 - Request for Information (RFI) will arrive either by fax or U.S. Mail
 - Immediately look at the due date for the response
 - Usually, you are given 21 days to respond
 - One extension may be given by the reviewer, but you must request the extension long before your current due date (waiting until day 21 is not cool!)
 - If there is a legitimate hardship that impedes the ability to respond to the RFI after the extension is given, the reviewer may grant another extension, but be prepared to prove your hardship (this is not something to be used in general)



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How Do We Operate in the Meantime?

- Regardless of the VCP status, the moment an operational failure is detected, amend or change procedures to match the plan prospectively to stop the bleeding
 - Example: the Client thought that the eligibility was 1 YOS. In reality, it was 6 months of service. Amend the plan immediately prospectively to reflect the 1 YOS to match the plan to the provision the client wants going forward
- Avoiding terminating the plan should be avoided unless the correction has no impact on participant balances (hard to accommodate IRS-requested changes to allocations when the accounts are already paid out)
 - Example 1 – VCP is being filed for being a non-amender
 - Example 2 – VCP is being filed because required minimum distributions were missed in the prior year



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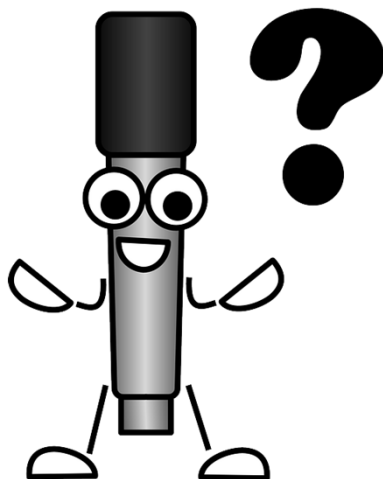
Compliance Statement

- Once all of the negotiations back-and-forth are completed and both sides are happy with the outcome (or if you're lucky enough to be fast-tracked and no negotiations were needed), six weeks later, you will receive your Compliance Statement
 - Make sure that you read the Compliance Statement very carefully
 - Is it for the right client?
 - Is the correct narrative attached?
 - Are all of the requested excise tax waiver boxes checked?
- If your correction must still be executed, the clock starts ticking and you have 150 days to complete
 - All proposed retroactive amendments need to be signed and dated



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**OUR FINAL THOUGHTS
AND
YOUR QUESTIONS**



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A Few Reminders

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- Go to ERISApedia.com WEBCAST tab to retrieve previous certificates.
- After the webcast you will be presented with a short google forms survey. Please let us know how we are doing.
- Joanne Pecina will demonstrate how to find more information on today's topic from the ERISApedia.com resources



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