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February 18, 2010

Internal Revenue Service  
Attention: SE:T:EP:RA:VC  
1111 Constitution Avenue NW  
Washington, D.C. 20244

Re: Suggestions for Improvements to EPCRS

The American Society of Pension Professionals & Actuaries (ASPPA) appreciates this opportunity to comment on future updates and enhancements to the Employee Plans Compliance Resolution System, currently published in Revenue Procedure 2008-50 (“EPCRS”).

ASPPA is a national organization of more than 6,500 retirement plan professionals who provide consulting and administrative services for qualified retirement plans covering millions of American workers. ASPPA members are retirement professionals of all disciplines, including consultants, investment professionals, administrators, actuaries, accountants and attorneys. Our large and broad-based membership gives ASPPA unique insight into current practical applications of ERISA and qualified retirement plans, with a particular focus on the issues faced by small- to medium-sized employers. ASPPA’s membership is diverse but united by a common dedication to the employer-sponsored retirement plan system.

### **Summary of Recommendations**

EPCRS is a great resource for employers that maintain qualified plans. We appreciate the Service’s efforts to continue to expand the standard corrections available under the program. The following is a summary of ASPPA’s recommendations for enhancements to the EPCRS program. More detail regarding each of these recommendations is included in the discussion section below:

1. Provide a standard self-correction for errors relating to automatic enrollment, including a reasonable grace period for certain violations.
2. Provide a standard self-correction for errors relating to Roth elections, including a reasonable grace period for certain violations.
3. Provide a single \$100 de minimis standard that applies to corrective distributions and contributions.

4. Add a thirty (30) day “grace period” for missed deferrals, where participants have at least thirty (30) days left in the plan year to change deferral elections.
5. Expand the Self-Correction Program to include certain loan errors caused by the employer (or its agents).
6. Add document corrections (and group procedures) for SEPs and SIMPLEs to the streamlined application process under VCP.
7. Expand the streamlined non-amender VCP program to include late discretionary amendments.
8. Revise the factors for determining the sanction amount under Audit Cap to include consideration of the economic condition of the plan sponsor.

## **Discussion of Issues**

### **1. Failures Related to Automatic Enrollment**

The Service requested comments relating to standard corrections for operational errors that occur within automatic enrollment plans. Specifically, the IRS requested comments relating to failures to implement automatic enrollment with respect to participants who do not make elections and failures to provide timely notice to participants.

#### **A. Failure to Implement Automatic Enrollment**

EPCRS currently provides standard corrections for situations where otherwise eligible employees were not offered the opportunity to defer and for failure to implement an employee election, including correction methods for a full or partial plan year.

*ASPPA recommends* establishing standard corrections similar to those already in EPCRS (*e.g.*, 50% missed deferral and 100% missed match), with the following special features:

- The missed deferral amount should be equal to the initial default percentage under the plan.
- The missed deferral opportunity (or required contribution to correct) should be 50% of the missed deferral amount.
- For a Section 401(k)(13) plan, the default percentage should be 3% or the greatest deferral rate in excess of 3% that would be entitled to a 100% match under the plan.

Encouraging the establishment of automatic enrollment plans and use of EPCRS by these plans requires availability of correction methods similar to those available for other plan designs.

*ASPPA further recommends* that a 30-day grace period be provided under EPCRS, provided that the applicable notice requirements were met. If an employer discovers a failure to implement automatic enrollment provisions and begins withholding deferrals within the first 30 days after a participant would otherwise have been deemed to have elected deferral contributions, no correction would be required. Special consideration is warranted for employers who convert to an automatic enrollment plan. This process involves substantial changes in the administration of salary deferral elections. Moreover, in light of the employer taking on the burden of beginning the salary reduction on the employees' behalf, which necessarily involves a greater chance of error, a reasonable grace period should be available before corrective contributions are required.

**B. Failure to Timely Provide Notice under Code Sections 401(k)(12), (13) or 414(w)**

*ASPPA recommends* that no penalty be imposed for a failure to timely provide notices under section 401(k)(12) [safe harbor], 401(k)(13) [automatic contribution arrangements], or 414(w) [withdrawals from eligible automatic withdrawal arrangements] of the Internal Revenue Code, as amended (the "Code"), provided that notice is provided within the first 90 days of the plan year. More specifically:

- The notice must clearly indicate how to receive the maximum employer contribution under the plan in light of the shortened deferral period.
- In the event of a Section 401(k)(13) Plan, where automatic enrollment was implemented, the notice would open a 90 day withdrawal period similar to the Section 414(w) period regardless of whether this feature is normally offered under the plan.

*ASPPA further recommends* that where the failure to send the notice is not corrected in the first 90 days, the employer may correct errors by sending the notice and treating and correcting the error as a missed deferral opportunity. This results in an additional 50% deferral by the employer (with no match) from the date the notice was required to the date notice was sent. In this event, the applicable safe harbor would still be available for the plan year.

*ASPPA further recommends* that if the error is significant and the notice described above is not sent in 90 days, the employer can correct the error by providing late notice (as described above) and completing the applicable nondiscrimination testing for the plan. The employer would still be required to meet all other safe harbor conditions for the plan year under this correction, including making the applicable employer contribution.

**2. Failures Relating to Designated Roth Contributions**

The Service requested comments regarding correction of failures related to designated Roth contributions, including comments on the correction methods proposed by the Service.

**A. Salary Deferrals Withheld, but Treated as Pre-Tax 401(k) Deferrals (Not as Designated Roth Contributions)**

Revenue Procedure 2008-50 set forth several possible correction methods for the operational defect that occurs when a designated Roth contribution is erroneously treated as a pre-tax deferral.

*ASPPA recommends* that the correction be made by a transfer (at the participant's election) of the contribution (with earnings) to a Roth account and inclusion of the amount so transferred in the participant's compensation in the year of the transfer. If the participant elects (either affirmative or negative election) to retain the pre-tax status of the prior deferrals and simply have the Roth election become effective prospectively, no transfer would be required. The benefits of a correction method that recharacterizes the contribution back to the year of the deferral would be substantially outweighed by the expense of correcting and the burden on the participant of having to file an amended income tax return. Moreover, ASPPA's recommended approach would allow the participant to account for changes in his or her personal tax planning since the date of the error. If the participant elects the transfer, the five-year period for qualifying Roth distributions should begin as of the date the first deferral should have been made, rather than the date of correction, to restore the participant to where he or she would have been absent the error.

*ASPPA further recommends* that a 30-day grace period be provided under EPCRS, similar to the grace period described in 1.A above. If the employer discovers the error within 30 days and makes the necessary system changes going forward, the employer should be able to just apply the Roth election prospectively.

**B. Failure to Implement Participant's Roth Election**

EPCRS currently contains standard corrections for failure to implement after-tax and pre-tax contributions, but does not address what correction is appropriate if the plan also includes Roth deferrals.

*ASPPA recommends* applying the 50% rule to calculate the missed deferral opportunity. The employer should be permitted to include the contribution as taxable income to the employee at the time of the corrective contribution and allow the participant to treat the five-year period for distributions as beginning when the first deferral should have been made, rather than the date of correction, in order to restore the participant to where he or she would have been absent the error.

*ASPPA further recommends* that the special rule for brief exclusion from elective deferrals, set forth in Revenue Procedure 2008-50, Appendix B, §2.02(1) should apply.

*ASPPA further recommends* that where a participant is excluded from making designated Roth contributions for a brief period, the rule proposed under (4) below should apply.

### **C. Failure to Provide Notice of Opportunity to Make Designated Roth Contributions**

As noted above, EPCRS currently contains standard corrections for failure to make available after-tax and pre-tax contributions, but does not address what correction is appropriate if the plan fails to offer Roth deferrals (while still offering pre-tax or after-tax deferrals).

*ASPPA recommends* that the employer be permitted to correct by providing a notice to all affected employees and providing a 90 day election period for participants to elect to recharacterize pre-tax deferrals during the period of failure as designated Roth contributions, similar to the method proposed in 2.A above.

*ASPPA further recommends* that the same 30-day grace period described in Section 2.A above be applied. However, if the error results in discrimination in favor of Highly Compensated Employees, the employer should correct by making a “missed deferral opportunity” corrective contribution for the period of the delay in providing notice, as described in 1.B above.

### **3. Uniform De Minimis Threshold**

Establishing and maintaining small account balances can be expensive. Many third party administrators charge a distribution fee between \$25 and \$50, as well as other per account fees to cover operational costs. As a result, a significant portion of a small account balance may be applied to pay administrative fees.

In EPCRS, the Service recognizes these challenges and provides various relief from corrective actions:

- Delivery of small benefits of \$75 or less, if the costs would exceed benefit.
- Recovery of small overpayments of \$100 or less.
- Distribution or forfeiture of small excess amounts of \$100 or less.

There is currently no de minimis exception for corrective contributions.

*ASPPA recommends* that the Service establish a universal \$100 or less de minimis threshold, without regard to the costs of correction, which would apply to corrective contributions and distributions.

### **4. Special Rule for Brief Exclusion from Elective Deferrals**

EPCRS includes a special rule for brief exclusion from elective deferrals. Under this rule, an employer is not required to make up elective deferrals if the opportunity to make contributions was available to the employee for at least the last nine months of the plan year, but the employer is required to make up missed matching contributions (the “nine month rule”). However, the

nine-month rule only applies to participants who become eligible during the first three months of the plan year. The current rule has no applicability to employees who miss an opportunity to defer for a couple weeks in the 4<sup>th</sup> month of a plan year. We strongly believe that a participant has a reasonable opportunity to defer for a plan year if the participant can make the contribution he or she intended by increasing contributions for the balance of the plan year, after missing deferrals for a short period.

*ASPPA recommends* that no correction should be required where there is a failure to implement a participant election for up to 30 days, so long as the affected participants have at least 30 days left to make additional deferrals in the same plan year and have the opportunity to change their deferral elections after receiving notice of the failure. This correction should also be available for automatic contribution arrangements and designated Roth contributions.

## **5. Self-Correction of Loan Failures**

Errors relating to the payroll deduction of loan payments and similar administrative errors can cause a loan that satisfied Section 72(p) when made to go into default. Under EPCRS, there is no self-correction for errors of this nature. Many times these errors occur early in the life of the loan, making reamortization within the original loan term a reasonable solution for the participant who wants to avoid tax consequences related to the loan default. Errors can also arise when participants terminate employment and cease making payroll deductions, but defer taking a distribution from the plan, or other similar circumstances that result in a loan default. Generally, these errors are the result of a vendor or employer error, rather than an unwillingness to pay on the part of the participant.

*ASPPA recommends* adding two standard self-corrections for insignificant loan errors caused by an employer or vendor, involving Non-Highly Compensated Employees:

- A standard correction allowing (a) a lump sum repayment equal to any missed payments, plus interest; or (b) reamortization of the loan balance, including accrued interest, over the remaining loan term (or over the maximum period permitted under Code §72(p)(2)(B), measured from the original loan date); or any combination of (a) and (b).
- A standard correction allowing late reporting of loan defaults/deemed distributions in the year of correction, not the year of default, to avoid the burden on participants to file amended tax returns.

## **6. Document Corrections for SEPs and SIMPLEs**

EPCRS includes streamlined application procedures under VCP using Appendix F. These procedures include a method for correcting document or nonamender failures by qualified plans and methods for correction of certain errors in SEPs and SIMPLEs. Through the Pension Protection Act, Congress specifically charged the Service to improve and expand EPCRS to meet the needs of small employers. We understand that the most common corrections completed

under EPCRS are plan amendment corrections.

*ASPPA recommends* that the Service expand the streamlined VCP application procedure to assist small employers who adopt SEP and SIMPLE plans:

- SEPs and SIMPLEs are generally adopted by use of form documents and the Service periodically publishes Lists of Required Modifications for these plans. As a result, document failures in these plans are compatible with the streamlined approach of Appendix F.
- Adopters of SEPs and SIMPLEs generally rely more heavily on third parties, such as their investment custodian, to maintain their documents making these plans more susceptible to group errors. We therefore also recommend addition of a streamlined application and reduced filing fee for group submission of document errors for these types of plans.

## **7. Nonamender Failures Relating to Voluntary Amendments**

Failures in plan documents and amendments are the most common types of errors. Even with established procedures and professional vendors and consultants, many employers fail to timely execute discretionary amendments (which may not become apparent until a determination letter application is filed for the plan).

*ASPPA recommends* that the Service add discretionary amendments to its non-amender filing program. The filing would be substantially similar to a failure to adopt an interim amendment, with a reduced filing fee (\$375.00), where this is the only error being corrected under VCP.

## **8. Audit-CAP Sanction Factors**

EPCRS includes a list of factors that the Service may consider in determining the amount of the sanction under the Audit-CAP Program, but the factors do not include consideration of the plan sponsor's economic condition.

*ASPPA recommends* that the factors considered in determining the sanction amount under Audit-CAP be revised to include consideration of the plan sponsor's economic condition. This will encourage the establishment of employer-sponsored retirement plans and is consistent with the directive to the Service to take into account the special circumstances faced by small employers and to assure that sanctions are not excessive. The Audit-CAP sanction should take into account the ability of a plan sponsor to pay and still maintain its plan, including any employer contributions made (or to be made) under its plans.

## **9. Corrections For Errors Under Code §§430 And 436**

There is a reasonable probability that operational errors under Code §§430 and 436 and applicable regulations and guidance are occurring or will occur. ASPPA believes it is very

important to address these issues and to provide reasonable correction methods under EPCRS for operational errors that are likely to occur. ASPPA will be submitting comments and recommendations for additional improvements to EPCRS relating to Code §§430 and 436 in a separate letter.

\* \* \*

These comments were prepared by the IRS and 401(k) Subcommittees of the ASPPA Government Affairs Committee, and were primarily authored by Michelle Ueding. Please contact us if you have any comments or questions regarding the matters discussed above. Thank you for your consideration of these comments.

Respectfully submitted,

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