

IRS Eases Pain for Correcting Certain Plan Administration Errors

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To err is human; to forgive is divine, according to poet Alexander Pope. The IRS acknowledges that retirement plan administrators aren't infallible, and provides correction for certain administrative errors. Most recently, it reduced certain penalties and extended deadlines for fixing specified mistakes.

Some Background

In 2013, the IRS overhauled the Employee Plans Compliance Resolution System (EPCRS). One of the more significant changes involved benefit overpayment. If a plan inadvertently gives participants more than they're entitled to, the plan must recover those dollars. Plans can do this by having affected participants repay the excess, or, with a defined benefit plan, by adjusting the accrual rate for future benefits.

However, for many years before this change, the U.S. Department of Labor (DOL) recognized the need for discretionary exceptions when reclaiming excess benefits. For example, it made an exception when recovering the overpayment would cause financial hardship for aged participants and beneficiaries, particularly when the error was discovered long after it was made.

IRS and DOL Agree

After the 2013 update to the EPCRS, it wasn't clear whether the IRS agreed with the DOL's position. As a result, when confronted with such a situation, many plans followed the IRS stance and required repayment.

But in 2015 the IRS went on record as accepting the DOL position. Thus, "depending on the facts and circumstances," plans may not have to recover overpaid funds. An example offered by the IRS is when plan sponsors or third party administrators contribute the amount of excess funds to the plan from their own resources. The IRS also is accepting suggestions for examples of reasonable circumstances when it shouldn't require recoupment.

Plan Amendments and Determination Letters

The IRS also reminded plan sponsors that, if they need to amend their plans to address excess benefit payments, they can't opt to "self-correct" under its correction program. Plan sponsors must have the IRS approve such an amendment in advance by applying for an IRS determination letter seeking approval of the plan amendment needed to cure the problem.

However, other administrative errors may not require a determination letter. Under the new procedures, a determination letter isn't required if an amendment made to a preapproved plan isn't so substantial that it prevents the plan from being able to rely on the preapproved plan's advisory or opinion letter.

If a plan sponsor must apply for a determination letter (along with a correction filing) to approve a plan amendment fixing a problem, the sponsor now has the later of 150 days after the compliance statement, or 91 days after the issuance of a favorable determination letter, to adopt the corrective amendment. This doesn't apply, however, in cases where the plan has failed to adopt a change in the law.

Penalties Reduced

The 2015 EPCRS updates also reduced penalty amounts for certain errors, based on plan size. The previous policy caused some larger plans to think twice about coming clean on small mistakes that could perhaps be swept under the rug and quietly fixed. Now plans with up to 150 participants face a maximum penalty of \$500 for errors involving required minimum distributions, whereas, before, the cut-off point was 50 participants.

One Last Change

Defined contribution (DC) plans featuring only elective deferrals and nonelective employer contributions previously had 2½ months following the plan year to remedy excess DC plan annual additions. The IRS extended this deadline to nine months. However, this isn't applicable to DC plans that make matching contributions. Talk to your benefits advisor to learn more about how the reduced penalties and extended deadlines may affect your plan.

For more information on BPM's Employee Benefit Plan services, please visit our website page or contact Jenise Gaskin at 925-296-1040 or Mike Spence at 408-961-6300

Penalty Modified for Failing to Process Participant 401(k) Plan Deferrals

Until recently, the penalty associated with a plan's failure to start deducting and investing 401(k) plan participants' elective deferral amounts and any accompanying employer matches equaled 50% of those amounts. The IRS has changed that policy.

According to IRS Revenue Procedure 2015-28, that penalty now will no longer apply if certain conditions are met. What are those conditions? First, the correct deferral amounts begin the earlier of the first payday on or after the last day of the 9½ month period after the end of the first plan year in which the failure began — or, if the plan sponsor was notified of the failure by the affected eligible employee, the first payday on or after the last day of the month after the month of notification.

In addition, sponsors must notify affected employees of the error no later than 45 days after the date the correct deferrals begin. Finally, the plan must make corrective contributions for any matching contributions — and earnings on those contributions — the employee otherwise would have received.