SELF-CORRECTION OF OPERATIONAL DEFECTS IN A QUALIFIED RETIREMENT PLAN

When a qualified plan experiences one or more operational defects in the operation of the plan, the plan risks losing its tax exempt status. A plan can avoid being disqualified if it is corrected under the IRS’s voluntary compliance program known as the Employee Plans Compliance Resolution System (“EPCRS”).

Eligibility for Self-Correction under EPCRS (“SCP”)

Under EPCRS, some errors, in some plans, may be self-corrected without IRS involvement. However, not every plan is eligible for self-correction. In order to be eligible to self-correct, the plan must meet each one of the following requirements:

1. The plan must have a current favorable determination letter or equivalent;
2. The plan must have established practices and procedures reasonably designed to promote and facilitate overall compliance with applicable requirements;
3. The errors must be operational (not document) errors and (with a few exceptions) may not be corrected via a plan amendment, but only operationally;
4. The errors must be corrected within very specific limited timeframes or must be “insignificant” based on all of the facts and circumstances. In determining if an error is insignificant, all facts and circumstances should be considered, including the following:
   a. Whether other failures occurred during the period being examined;
   b. The percentage of plan assets and contributions involved in the failure was minimal relative to the total amount of the plan’s assets;
   c. The number of plan years during which the failures occurred was minimal;
   d. The number of participants affected was minimal relative to the total number of Participants;
   e. The number of participants affected was minimal relative to the total number of Participants who could have been affected;
   f. Correction was made within a reasonable time after discovery of the failure; and
   g. The reason for the failures.

Correction Method and Documentation

The IRS has prescribed certain safe harbor correction methods for some types of plan errors. However, not every type of error is covered under a safe harbor and, unless the plan is submitted to the IRS under their voluntary correction program (“VCP”), there is no guarantee that the IRS will agree that the defects are eligible for self-correction or that the method of self-correction used is sufficient to preserve and restore the tax-qualified status of the Plan. All self-correction steps taken, including eligibility for SCP, should be clearly and carefully documented and those records should be retained pursuant to the plan’s records retention policy.

If you would like more information regarding self-correction of a qualified plan, or other employee benefits matters, please contact us: www.boutwellfay.com.