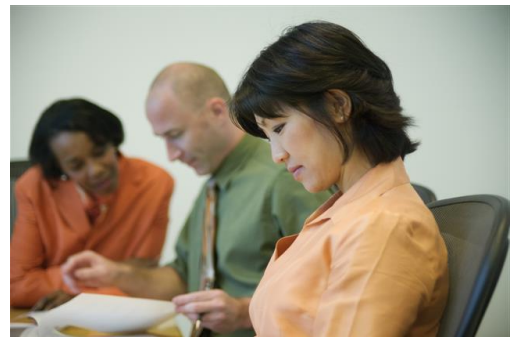


## IRS Updates Plan Corrections Procedure

IRS issued a new revenue procedure, effective January 1, 2017, governing employee plan corrections that takes into account the major changes to the IRS determination letter program. It also sets forth a “facts and circumstances” test for determining Audit CAP sanctions that will replace the current negotiated percentage of the maximum payment amount approach. Additionally, the VCP user fee has been relocated; beginning in 2017, user fees will be published in the annual user fee revenue procedure.

### Background

Since the 1990s, the IRS’ Employee Plans Compliance Resolution System (EPCRS) has been in place to encourage employers to establish strong compliance procedures, “self-discover” plan qualification violations, and correct these violations either independently or with IRS approval. EPCRS has three components: an option for self-correction (SCP), voluntary correction with IRS approval (VCP), and correction while under audit and in the case of certain loan errors (Audit CAP). IRS last restated the revenue procedure governing EPCRS in 2013. (See our [January 31, 2013](#) *For Your Information*.)



In 2015, IRS modified EPCRS to increase plans’ flexibility in correcting overpayment failures, reduce certain compliance fees, increase the time period within which a defined contribution plan can distribute excess deferrals, and add new options for making corrections. (See our [April 2, 2015](#) and [April 8, 2015](#) *For Your Information* publications.)

Earlier this year, IRS formally eliminated its staggered five-year remedial amendment cycle for individually designed plans, effective January 1, 2017. (See our [July 8, 2016](#) *For Your Information*.) Changes to EPCRS were expected to follow suit, given that the 2013 revenue procedure required a determination letter for a plan to access EPCRS in certain circumstances.

## Overview of Changes

In [Revenue Procedure 2016-51](#), the IRS modified and replaced the prior revenue procedure with a new one that incorporates the 2015 EPCRS guidance and sets forth several other key changes.

### Modifications to Reflect Curtailed Determination Letter Program

In light of the changes to the program, under the new guidance, a plan will not submit a determination letter application to the IRS when correcting qualification failures that require a plan amendment. The guidance further provides that, for qualified individually designed plans, a determination letter need not be current to satisfy the “Favorable Letter” requirement for certain SCP corrections of significant failures.

The guidance also deletes several other, now irrelevant, provisions of the 2013 version — including the procedure for filing a determination letter application with a VCP submission.

### New Approach for Determining Audit CAP Sanctions

The new revenue procedure changes the method for determining sanctions in the context of Audit CAP. When IRS identifies a qualification failure upon audit, the plan sponsor must correct the failure, pay a sanction, and enter into a closing agreement. Previously, the amount of the sanction was a negotiated percentage of the maximum tax IRS could collect if the plan were to be disqualified for all open tax years (known as the “maximum payment amount”) — which could result in a large sanction. The new revenue procedure establishes a more flexible “facts and circumstances” determination that considers the maximum payment amount, but no longer sets it as the base for negotiation. Nine other factors will also be considered, including the number and type of employees affected by the failure and the reason for the failure. Audit CAP sanctions generally will not be less than the VCP user fee applicable to the plan, however.

**Comment.** The IRS may have been motivated to change its approach to determining Audit CAP sanctions because individually designed plans will no longer have the opportunity for IRS review at regular increments. However, the Audit CAP user fee applicable to the plan could still be a large sum — so it is not clear that the new approach will result in lower sanctions.

For a failure to timely adopt a required amendment (a “nonamender failure”), IRS will consider additional factors, including the plan’s internal controls for ensuring timely adoption of required amendments. IRS also lowered the user fee from \$1,000 to \$750 when (1) a nonamender failure is the sole failure, and (2) the required amendment is adopted within three months of the end of the applicable remedial amendment period.

### User Fees Relocate

The new revenue procedure eliminates the “user fee” section for VCP submissions. Instead, beginning in 2017, IRS will publish user fees and rules about user fees in the annual revenue procedure on user fees — the current version of which is [Rev. Proc. 2016-8](#). Going forward, plan sponsors should refer to the annual revenue procedure in effect at the time of a VCP submission to determine the appropriate user fee.

## Effective Date

The new revenue procedure is effective January 1, 2017. Plan sponsors may not apply its provisions before that time.

## In Closing

It remains to be seen if the increased flexibility in determining Audit CAP sanctions will generally result in lower sanctions. Meanwhile, the IRS is continuing to solicit comments on expanding EPCRS rules to provide additional guidance on recovery of overpayments — the current revision does not include changes to respond to comments received on the overpayment guidance in Rev. Proc. 2015-27.

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