

Lesson 6

THE EMPLOYEE PLANS COMPLIANCE RESOLUTION SYSTEM

Revenue Procedure 98-22, 1998-12 I.R.B. 11 will be taught as a current development. The text of the revenue procedure is reproduced beginning on the next page.

Employee Plans CPE Technical Topics for 1998

PART I. INTRODUCTION TO EMPLOYEE PLANS COMPLIANCE RESOLUTION SYSTEM

SECTION 1. PURPOSE AND OVERVIEW

- .01 Purpose.
- .02 General principles underlying EPCRS.
- .03 Overview.
- .04 TVC program.
- .05 Further changes and request for comments.

SECTION 2. CHANGES TO PROGRAMS

- .01 Changes affecting all programs.
- .02 Changes affecting specific programs.

PART II. PROGRAM EFFECT AND ELIGIBILITY

SECTION 3. EFFECT OF EPCRS; RELIANCE

- .01 Effect of EPCRS.
- .02 Reliance.

SECTION 4. PROGRAM ELIGIBILITY

- .01 General program eligibility.
- .02 Effect of examination.
- .03 Favorable Letter requirement.
- .04 Established practices and procedures.
- .05 Plan amendments.
- .06 Egregious failures.
- .07 Diversion or misuse of plan assets.
- .08 Operational Failures in § 403(b) Plans.

Employee Plans CPE Technical Topics for 1998

PART III. DEFINITIONS, CORRECTION PRINCIPLES, AND RULES OF GENERAL APPLICABILITY

SECTION 5. DEFINITIONS

- .01 Qualification Failure.
- .02 Favorable Letter.
- .03 Maximum Payment Amount.
- .04 Qualified Plan.
- .05 § 403(b) Plan.
- .06 Under Examination.

SECTION 6. CORRECTION PRINCIPLES AND RULES OF GENERAL APPLICABILITY

- .01 Correction principles; rules of general applicability.
- .02 Correction.
- .03 Correction under statute or regulations.
- .04 Matters subject to excise taxes.
- .05 Confidentiality and disclosure.
- .06 No effect on other law.

PART IV. SELF-CORRECTION (APRSC)

SECTION 7. IN GENERAL

SECTION 8. SELF-CORRECTION OF INSIGNIFICANT OPERATIONAL FAILURES

- .01 Requirements.
- .02 Factors.
- .03 Multiple failures.
- .04 Examples.

SECTION 9. SELF-CORRECTION OF SIGNIFICANT OPERATIONAL FAILURES

Employee Plans CPE Technical Topics for 1998

- .01 Requirements.
- .02 Correction period.
- .03 Substantial completion of correction.
- .04 Example.

PART V. VOLUNTARY CORRECTION WITH SERVICE APPROVAL (VCR AND WALK-IN CAP)

SECTION 10. VCR PROGRAM

- .01 VCR requirements.
- .02 Identification of failures.
- .03 No concurrent examination activity.
- .04 Insufficient information.
- .05 Closing agreements with respect to the excise tax under § 4974.
- .06 Initial processing.
- .07 Processing of acceptable submission.
- .08 Failures discovered after initial submission.
- .09 Conference right.
- .10 Failure to reach resolution.
- .11 Concurrent processing of determination letter applications.
- .12 Special rules relating to SVP.
- .13 General description of compliance statement.
- .14 Compliance statement conditioned upon timely correction.
- .15 Compliance statement for new plans conditioned upon timely amendment.
- .16 Acknowledgement letter.
- .17 Verification.

SECTION 11. WALK-IN CAP

Employee Plans CPE Technical Topics for 1998

- .01 Walk-in CAP requirements.
- .02 Failures discovered after initial submission.
- .03 Failure to reach resolution.
- .04 Effect of closing agreement.

SECTION 12. APPLICATION PROCEDURES FOR VCR AND WALK-IN CAP

- .01 General rules.
- .02 Multiemployer and multiple employer plans.
- .03 Submission requirements.
- .04 Required documents.
- .05 Fee.
- .06 Signed submission.
- .07 Power of attorney requirements.
- .08 Penalty of perjury statement.
- .09 Checklist.
- .10 Designation.
- .11 VCR/SVP mailing address.
- .12 Walk-in CAP mailing address.
- .13 Maintenance of copies of submissions.

SECTION 13. FEES

- .01 Rev. Proc. 98-8 modified.
- .02 VCR fee.
- .03 Establishing number of plan participants.
- .04 SVP fee.
- .05 Walk-in CAP compliance correction fee.

Employee Plans CPE Technical Topics for 1998

PART VI. CORRECTION ON AUDIT (AUDIT CAP)

SECTION 14. DESCRIPTION OF AUDIT CAP

- .01 Audit CAP requirements.
- .02 Payment of sanction.
- .03 Additional requirements.
- .04 Failure to reach resolution.
- .05 Effect of closing agreement.
- .06 Other procedural rules.

SECTION 15. AUDIT CAP SANCTION

- .01 Determination of sanction.
- .02 Factors considered.

PART VII. CHRONOLOGY, EFFECT ON OTHER DOCUMENTS, AND EFFECTIVE DATE

SECTION 16. CHRONOLOGY

- .01 APRSC.
- .02 VCR program.
- .03 Walk-in CAP.
- .04 Audit CAP.

SECTION 17. EFFECT ON OTHER DOCUMENTS

- .01 Revenue procedures modified and superseded.
- .02 Revenue procedure 98-8 modified.
- .03 APRSC modified.
- .04 Audit CAP modified.

SECTION 18. EFFECTIVE DATE

SECTION 19. PAPERWORK REDUCTION ACT RAFTING INFORMATION

- APPENDIX A
- APPENDIX B

Employee Plans CPE Technical Topics for 1998

PART I. INTRODUCTION TO EMPLOYEE PLANS COMPLIANCE RESOLUTION SYSTEM

SECTION 1. PURPOSE AND OVERVIEW

.01 Purpose. This revenue procedure provides a comprehensive system of correction programs for sponsors of retirement plans that are intended to satisfy the requirements of § 401(a) or § 403(a) of the Internal Revenue Code (the "Code"), but that have not met these requirements for a period of time. This system permits plan sponsors to correct these qualification failures and thereby continue to provide their employees with retirement benefits on a tax-favored basis. The Internal Revenue Service (the "Service") previously established several programs allowing correction of qualification failures, including the Administrative Policy Regarding Self-Correction ("APRSC"), the Voluntary Compliance Resolution ("VCR") program, the Walk-in Closing Agreement Program ("Walk-in CAP"), and the Audit Closing Agreement Program ("Audit CAP").

This revenue procedure modifies these programs and consolidates them into a coordinated Employee Plans Compliance Resolution System ("EPCRS"). In response to requests by practitioners, this revenue procedure sets forth and assembles in one place the specific rules and procedures applicable to the programs, including illustrative examples.

.02 General principles underlying EPCRS. EPCRS is based on the following general principles:

- Sponsors of tax-qualified retirement plans should be encouraged to establish administrative practices and procedures that ensure that plans are operated properly in accordance with the tax qualification requirements.
- Sponsors of tax-qualified retirement plans should maintain plan documents satisfying the tax qualification requirements.
- Plan sponsors should make voluntary and timely correction of any plan qualification failures, whether involving discrimination in favor of highly compensated employees, plan operations, or the terms of the plan document. Timely and efficient correction protects participating employees by providing them with their expected retirement benefits, including favorable tax treatment.
- Voluntary compliance is promoted by providing for limited fees for voluntary corrections approved by the Service, thereby reducing employers' uncertainty regarding their potential liability.
- Sanctions for qualification failures identified on audit should be reasonable in light of the nature, extent, and severity of the violation.
- Administration of EPCRS should be consistent and uniform.
- Taxpayers should be able to rely on the availability of EPCRS in taking corrective

Employee Plans CPE Technical Topics for 1998

actions to maintain the qualified status of their plans.

.03 Overview. EPCRS includes the following basic elements:

- **Self-correction.** A plan sponsor that has established compliance practices and procedures may, at any time, correct insignificant operational failures without paying any fee or sanction. In addition, where a plan is the subject of a favorable determination letter from the Service, the plan sponsor generally may correct even significant operational failures within a two-year period without payment of any fee or sanction. (APRSC)
- **Voluntary correction with Service approval.** In the case of any other qualification failure, a plan sponsor, at any time before audit, may pay a limited fee and receive the Service's approval for the correction. (VCR and Walk-in CAP)
- **Correction on audit.** If a qualification failure (other than a failure corrected as described above) is identified on audit and corrected, the sanction imposed will bear a reasonable relationship to the nature, extent and severity of the failure, taking into account the extent to which correction occurred before audit. (Audit CAP)

.04 TVC program. This revenue procedure does not incorporate or modify the Tax Sheltered Annuity Voluntary Correction program ("TVC"). TVC enables a sponsor of a § 403(b) Plan to voluntarily disclose to the Service certain operational defects it has discovered in its § 403(b) plans and pay both a fixed fee and a monetary sanction negotiated with the Service. The TVC program procedures under Rev. Proc. 95-24, 1995-1 C.B. 694, continue to apply, pending future modifications to the TVC program (which may include consolidation with EPCRS).

.05 Further changes and request for comments. The Service believes it is important to update EPCRS periodically to reflect changing circumstances and make other improvements. Accordingly, it is anticipated that EPCRS will continue to be monitored and improved in light of experience and comments from those who use it, and that this consolidated revenue procedure will be revised periodically for that purpose. The Service specifically solicits comments or suggestions relating to this revenue procedure and the administration of EPCRS. In particular, the Service requests (1) comments regarding the extent to which a fixed (as opposed to an indefinite) self-correction period encourages prompt, voluntary correction, (2) suggestions for items that should be included in forthcoming guidance on permissible correction methods, and (3) comments on possible improvements to the TVC program.

It is requested that comments or suggestions be submitted by June 21, 1998, addressed to CC:DOM:CORP:R (Rev. Proc. 98-22), Room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, comments may be hand-delivered between the hours of 8 a.m. and 5 p.m. to CC:DOM:CORP:R (Rev. Proc. 98-22), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC. Alternatively, taxpayers may transmit comments electronically via the Service's Internet site at http://www.irs.ustreas.gov/prod/tax_regs/comments.html

SECTION 2. CHANGES TO PROGRAMS

Employee Plans CPE Technical Topics for 1998

.01 Changes affecting all programs. This revenue procedure makes the following changes affecting all of the programs comprising EPCRS:

- provides a uniform set of correction principles;
- clarifies that there may be more than one appropriate method of correcting Qualification Failures;
- permits, in appropriate circumstances, the use of reasonable adjustments in making corrections; and
- permits taxpayers to rely on the availability of EPCRS in correcting Qualification Failures.

.02 Changes affecting specific programs. This revenue procedure makes the following specific changes to the APRSC, VCR, Walk-in CAP, and Audit CAP correction programs:

(1) APRSC. APRSC enables a sponsor of a Qualified Plan or a § 403(b) Plan to self-correct Operational Failures it discovers in its plans. The provisions of APRSC are modified and restated to:

- incorporate the recent extension of the period for correcting significant Operational Failures from the end of the first plan year following the plan year in which the Operational Failure occurred to the end of the second plan year following the plan year in which the Operational Failure occurred, as set forth in Announcement 97-121, 1997-50 I.R.B. 62;
- clarify that, for purposes of correcting a failure to satisfy the actual deferral percentage ("ADP") or actual contribution percentage ("ACP") test, the two-year correction period begins after the expiration of the statutory correction period; and
- permit correction of an Operational Failure to be completed after the end of the correction period if correction was substantially completed by the end of the correction period.

(2) VCR. The VCR program enables a sponsor of a Qualified Plan to voluntarily disclose to the Service Operational Failures it has discovered in its plans and to pay a fixed fee to the Service. The provisions of VCR are modified to:

- reduce the specificity required in the calculations supporting plan sponsors' proposed correction methods;
- revise the circumstances under which closing agreements will be entered into with respect to the excise tax under § 4974 (applicable to the failure to satisfy the minimum distribution requirements under § 401(a)(9));
- extend the time period within which corrections are to be effected to 150 days;

Employee Plans CPE Technical Topics for 1998

- clarify and simplify permissible correction methods under the Standardized VCR Procedure (SVP) (see Appendix A of this revenue procedure); and
- provide a checklist for use by plan sponsors in preparing VCR and SVP requests (see Appendix B to this revenue procedure).

(3) Walk-in CAP. Walk-in CAP enables a sponsor of a Qualified Plan to voluntarily disclose to the Service Qualification Failures it has discovered in its plans and to pay a compliance correction fee. The provisions of Walk-in CAP are modified to:

- discontinue the use of 40% (or any other percentage) of the Maximum Payment Amount as the basis for calculating sanctions (except for egregious failures);
- provide for greater predictability and consistency by replacing the prior sanction structure with a limited range of compliance correction fees, with the lowest fees provided for small plans; and
- provide a checklist for use by plan sponsors in preparing Walk-in CAP requests (see Appendix B to this revenue procedure).

(4) Audit CAP. Audit CAP, a program established in the key district offices that is available on examination of a Qualified Plan, enables the plan sponsor to negotiate a monetary sanction. The provisions of Audit CAP are modified and restated to:

- clarify that the sanction imposed under Audit CAP will not be excessive and will bear a reasonable relationship to the nature, extent, and severity of the failure; and
- provide assurance that correction made before audit, even for failures corrected outside of the APRSC, VCR, and Walk-in CAP programs, will be an important factor in reducing the potential sanction under Audit CAP.

PART II. PROGRAM EFFECT AND ELIGIBILITY

SECTION 3. EFFECT OF EPCRS; RELIANCE

.01 Effect of EPCRS. If the eligibility requirements of section 4 are satisfied and the plan sponsor corrects a Qualification Failure in accordance with the requirements of APRSC in section 7, the VCR program in section 10, Walk-in CAP in section 11, or Audit CAP in section 14, the Service will not treat the plan as disqualified on account of the Qualification Failure.

.02 Reliance. Taxpayers may rely on this revenue procedure, including the relief described in section 3.01.

Employee Plans CPE Technical Topics for 1998

SECTION 4. PROGRAM ELIGIBILITY

.01 General program eligibility. EPCRS includes three specific voluntary correction programs and an audit correction program for Qualified Plans. The voluntary correction programs are APRSC and VCR, both of which are available for Operational Failures, and Walk-in CAP, which applies to Plan Document and Demographic Failures and to Operational Failures that are not eligible for APRSC and VCR. APRSC is a voluntary employer-initiated procedure that generally does not involve Service approval, whereas VCR and Walk-in CAP are voluntary employer-initiated procedures that involve Service approval. The audit correction program is Audit CAP, which is available for all types of Qualification Failures found on examination that cannot be corrected under APRSC. Additional, specific rules are set forth below.

.02 Effect of examination. If the plan or plan sponsor is Under Examination, the VCR and Walk-in CAP programs are not available; insignificant Operational Failures can be corrected under APRSC; and significant Operational Failures can be corrected under APRSC in limited circumstances. See section 9.

.03 Favorable Letter requirement. The VCR program and the provisions of APRSC relating to significant Operational Failures (see section 9) are available only for a plan that is the subject of a Favorable Letter.

.04 Established practices and procedures. In order to be eligible for APRSC, the plan sponsor or administrator of a plan must have established practices and procedures (formal or informal) reasonably designed to promote and facilitate overall compliance with the requirements of § 401(a) or § 403(b). For example, the plan administrator might use a check sheet for tracking allocations and indicate on that check sheet whether a particular employee was a key employee for top-heavy purposes. A plan document alone will not constitute evidence of established procedures. These established procedures must have been in place and routinely followed, but through an oversight or mistake in applying them, or because of an inadequacy in the procedures, an Operational Failure occurred.

.05 Plan amendments.

(1) Correction by plan amendment not permitted in APRSC or VCR. Neither APRSC nor the VCR program is available for a plan sponsor to correct an Operational Failure by a plan amendment that conforms the terms of the plan to the plan's prior operations. Thus, if loans were made to participants, but the plan document did not permit loans to be made to participants, the failure cannot be corrected under VCR by retroactively amending the plan to provide for the loans. Nevertheless, if a plan sponsor corrects under APRSC or VCR, it may amend the plan to the extent necessary to reflect operational correction. For example, if the plan failed to satisfy the ADP test required under § 401(k)(3) and the employer must make qualified nonelective contributions not already provided for under the plan, the plan may be amended to provide for qualified nonelective contributions. The issuance of a compliance statement does not constitute a determination as to the effect of any plan amendment on the qualification of the plan.

Employee Plans CPE Technical Topics for 1998

(2) Limited availability of correction by plan amendment in Walk-in CAP. In appropriate circumstances, a plan sponsor may use Walk-in CAP to correct an Operational Failure by a plan amendment to conform the terms of the plan to the plan's prior operations, provided that the amendment complies with the requirements of § 401(a), including the requirements of §§ 401(a)(4), 410(b), and 411(d)(6). Future guidance will be issued regarding circumstances under which correction of an Operational Failure through plan amendment may be appropriate under Walk-in CAP.

.06 Egregious failures. Neither APRSC nor the VCR program is available to correct Operational Failures that are egregious. For example, if an employer has consistently and improperly covered only highly compensated employees or if a contribution to a defined contribution plan for a highly compensated individual is several times greater than the dollar limit set forth in § 415, the failure would be considered egregious.

.07 Diversion or misuse of plan assets. The APRSC, VCR, Walk-in CAP and Audit CAP programs are not available for Qualification Failures relating to the diversion or misuse of plan assets.

.08 Operational Failures in § 403(b) Plans. APRSC is also available to correct an Operational Failure in a § 403(b) Plan (other than a failure that would result solely in income inclusion for affected employees). Thus, Operational Failures involving contributions to a § 403(b) Plan in excess of the § 415 limit and the maximum exclusion allowance (failures that result solely in the inclusion in income for affected participants) are not eligible for APRSC.

PART III. DEFINITIONS, CORRECTION PRINCIPLES, AND RULES OF GENERAL APPLICABILITY

SECTION 5. DEFINITIONS

The following definitions apply for purposes of this revenue procedure:

.01 Qualification Failure. A Qualification Failure is any failure that adversely affects the qualification of a plan. There are three types of Qualification Failures: (1) Plan Document Failures, (2) Operational Failures, and (3) Demographic Failures.

(1) Plan Document Failure. The term "Plan Document Failure" means a plan provision (or the absence of a plan provision) that, on its face, violates the requirements of § 401(a) or § 403(a). Thus, for example, the failure of a plan to be amended to reflect a new qualification requirement within the plan's applicable remedial amendment period under § 401(b) is a Plan Document Failure. For purposes of this revenue procedure, a Plan Document Failure includes any Qualification Failure that is a violation of the requirements of § 401(a) or § 403(a) and that is neither an Operational Failure nor a Demographic Failure.

(2) Operational Failure. The term "Operational Failure" means, with respect to a Qualified Plan,

Employee Plans CPE Technical Topics for 1998

a Qualification Failure that arises solely from the failure to follow plan provisions.

A failure to follow the terms of the plan providing for the satisfaction of the requirements of § 401(k) and § 401(m) is considered to be an Operational Failure. A plan does not have an Operational Failure to the extent the plan is permitted to be amended retroactively pursuant to § 401(b) or another statutory provision to reflect the plan's operations. However, if within an applicable remedial amendment period under § 401(b), a plan has been properly amended for statutory or regulatory changes, and, on or after the later of the date the amendment is effective or is adopted, the amended provisions are not followed, then the plan is considered to have an Operational Failure.

An Operational Failure with respect to a § 403(b) Plan is a failure that would result in the loss of the exclusion allowance under § 403(b).

(3) Demographic Failure. The term "Demographic Failure" means a failure to satisfy the requirements of § 401(a)(4), § 401(a)(26), or § 410(b) that is not an Operational Failure.

The correction of a Demographic Failure generally requires a substantive corrective amendment to the plan adding more benefits or increasing existing benefits (see, for example, § 1.401(a)(4)-11(g) of the Income Tax Regulations).

.02 Favorable Letter. The term "Favorable Letter" means a current favorable determination letter for an individually designed plan (including a volume submitter plan), a current favorable opinion letter for a plan sponsor that has adopted a master or prototype plan, or a current favorable notification letter for a plan sponsor that has adopted a regional prototype plan. A plan has a current favorable determination letter, opinion letter, or notification letter if either (1), (2), or (3) below is satisfied:

(1) The plan has a favorable determination, opinion, or notification letter that considers the Tax Reform Act of 1986 ("TRA '86").

(2) The plan has a favorable determination, opinion, or notification letter that considers the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA"), the Deficit Reduction Act of 1984 ("DEFRA"), and the Retirement Equity Act of 1984 ("REA"), and the § 401(b) remedial amendment period for TRA '86 has not yet expired. (The remedial amendment period for TRA '86 may not have expired either because the plan has a timely submitted, pending request for a determination, opinion, or notification letter that considers TRA '86, or because the plan is an adoption of a master or prototype plan, regional prototype plan, or volume submitter plan, described in section 3 of Rev. Proc. 95-12, 1995-1 C.B. 508; a governmental plan described in Notice 96-64, 1996-2 C.B. 229; or a plan maintained by a tax-exempt organization, including a non-electing church plan, described in Notice 96-64.)

(3) The plan is initially adopted or effective after December 7, 1994, and the plan sponsor timely submits an application for a determination, opinion, or notification letter within the plan's remedial amendment period under § 401(b).

.03 Maximum Payment Amount. The term "Maximum Payment Amount" means a monetary

Employee Plans CPE Technical Topics for 1998

amount that is approximately equal to the tax the Service could collect upon plan disqualification and is the sum for the open taxable years of the:

- (1) tax on the trust (Form 1041),
- (2) additional income tax resulting from the loss of employer deductions for plan contributions (and any interest or penalties applicable to the plan sponsor's return), and
- (3) additional income tax resulting from income inclusion for participants in the plan (Form 1040).

For purposes of determining the maximum compliance correction fee applicable under section 13.05(3), relating to egregious failures under Walk-in CAP, paragraph (2) above is modified to exclude interest or penalties applicable to the plan sponsor's return, and paragraph (3) above is modified to include only the additional income tax resulting from income inclusion for highly compensated employees, as defined in § 414(q).

.04 Qualified Plan. The term "Qualified Plan" means a plan intended to satisfy the requirements of § 401(a) or § 403(a).

.05 § 403(b) Plan. The term "§ 403(b) Plan" means a plan intended to satisfy the requirements of § 403(b).

.06 Under Examination. The term "Under Examination" means: (1) a plan that is under an Employee Plans examination (that is, an examination of a Form 5500 series or other Employee Plans examination), or (2) a plan sponsor that is under an Exempt Organizations examination (that is, an examination of a Form 990 series or other Exempt Organizations examination).

A plan that is under an Employee Plans examination includes any plan for which the plan sponsor, or a representative, has received verbal or written notification from the Employee Plans Division of an impending Employee Plans examination, or of an impending referral for an Employee Plans examination, and also includes any plan that has been under an Employee Plans examination and is now in Appeals or in litigation for issues raised in an Employee Plans examination. A plan is considered to be Under Examination if it is aggregated for purposes of satisfying the nondiscrimination requirements of § 401(a)(4), the minimum participation requirements of § 401(a)(26), or the minimum coverage requirements of § 410(b), or the requirements of § 403(b)(12), with a plan(s) that is Under Examination. In addition, a plan is considered to be Under Examination with respect to a failure of a qualification requirement (other than those described in the preceding sentence) if the plan is aggregated with another plan for purposes of satisfying that qualification requirement (for example, § 402(g), § 415, or § 416) and that other plan is Under Examination. For example, assume Plan A has a § 415 failure, Plan A is aggregated with Plan B only for purposes of § 415, and Plan B is Under Examination. In this case, Plan A is considered to be Under Examination with respect to the § 415 failure. However, if Plan A has a failure relating to the spousal consent rules under § 417 or the vesting rules of § 411, Plan A is not considered to be Under Examination with respect to the § 417 or § 411 failure. For purposes of this revenue procedure, the term aggregation does not include consideration of benefits provided by various plans for purposes of the average benefits

Employee Plans CPE Technical Topics for 1998

test set forth in § 410(b)(2).

An Employee Plans examination also includes a case in which a plan sponsor has submitted a Form 5310, Application for Determination of Qualification Upon Termination, and the Employee Plans agent notifies the plan sponsor, or a representative, of possible Qualification Failures, whether or not the plan sponsor is officially notified of an "examination." This would include the case where, for example, a plan sponsor has applied for a determination letter on plan termination, and an Employee Plans agent notifies the plan sponsor that there are partial termination concerns.

A plan sponsor that is under an Exempt Organizations examination includes any plan sponsor that has received (or its representative has received) verbal or written notification from the Exempt Organizations Division of an impending Exempt Organizations examination or of an impending referral for an Exempt Organizations examination and also includes any plan sponsor that has been under an Exempt Organizations examination and is now in Appeals or in litigation for issues raised in an Exempt Organizations examination.

SECTION 6. CORRECTION PRINCIPLES AND RULES OF GENERAL APPLICABILITY

.01 Correction principles; rules of general applicability. The following general correction principles and rules of general applicability apply for purposes of this revenue procedure.

.02 Correction. Generally, a Qualification Failure is not corrected unless full correction is made with respect to all participants and beneficiaries, and for all taxable years (whether or not the taxable year is closed). In the case of an Operational Failure, correction is determined taking into account the terms of the plan at the time of the failure. Correction should be accomplished taking into account the following principles:

(1) Restoration of benefits. The correction method should restore the plan to the position it would have been in had the Qualification Failure not occurred, including restoration of current and former participants and beneficiaries to the benefits and rights they would have had if the Qualification Failure had not occurred.

(2) Reasonable and appropriate correction. The correction should be reasonable and appropriate for the Qualification Failure. Depending on the nature of the Qualification Failure, there may be more than one reasonable and appropriate correction for the failure. Any standardized correction method permitted under SVP (see Appendix A) is deemed to be a reasonable and appropriate method of correcting the related Qualification Failure. Whether any other particular correction method is reasonable and appropriate is determined taking into account the applicable facts and circumstances and the following principles:

(a) The correction method should, to the extent possible, resemble one already provided for in the Code, Income Tax Regulations, or other guidance of general applicability. For example, the defined contribution plan correction methods set forth in § 1.415-6(b)(6) would be the typical means of correcting a failure under § 415. Likewise, the correction method set forth in § 1.402(g)-1(e)(2) would be the typical means of correcting a failure under § 402(g).

Employee Plans CPE Technical Topics for 1998

(b) The correction method for Qualification Failures relating to nondiscrimination should provide benefits for nonhighly compensated employees. For example, the correction method set forth in § 1.401(a)(4)-11(g) (rather than methods making use of the special testing provisions set forth in § 1.401(a)(4)-8 or 1.401(a)(4)-9) would be the typical means of correcting a failure to satisfy nondiscrimination requirements. Similarly, the correction of a failure to satisfy the requirements of § 401(k)(3), 401(m)(2), or 401(m)(9) (relating to nondiscrimination) solely by distributing excess amounts to highly compensated employees would not be the typical means of correcting such a failure.

(c) The correction method should keep plan assets in the plan, except to the extent the Code, regulations, or other guidance of general applicability provide for correction by distribution to participants or beneficiaries or return of assets to the employer or plan sponsor. For example, if an excess allocation (not in excess of the § 415 limits) was made for a participant under a plan (other than a cash or deferred arrangement), the excess should be reallocated to other participants or, depending on the facts and circumstances, used to reduce future employer contributions.

(d) The correction method should not violate another applicable specific requirement of § 401(a) (for example, § 401(a)(4) or 411(d)(6)).

(3) Principles regarding corrective allocations and corrective distributions. The following principles apply where an appropriate correction method includes the use of corrective allocations or corrective distributions.

(a) Corrective allocations under a defined contribution plan should be based upon the terms of the plan and other applicable information at the time of the Qualification Failure (including the compensation that would have been used under the plan for the period with respect to which a corrective allocation is being made) and should be adjusted for earnings and forfeitures that would have been allocated to the participant's account if the failure had not occurred. The corrective allocation need not be adjusted for losses. For administrative convenience, in the case of corrective allocations, if the plan permitted directed investments for the years at issue, and thus had a number of funds, the plan would be permitted to use the highest rate earned in the plan for a particular year as the rate used for all corrections, provided that most of the employees receiving the corrective allocations are nonhighly compensated employees. Similar rules apply with respect to corrective distributions.

(b) A corrective allocation to a participant's account because of a failure to make a required allocation in a prior limitation year will not be considered an annual addition with respect to the participant for the limitation year in which the correction is made, but will be considered an annual addition for the limitation year to which the corrective allocation relates. However, the normal rules of § 404, regarding deductions, apply.

(c) Corrective allocations should come only from employer contributions (including forfeitures if the plan permits their use to reduce employer contributions).

(d) In the case of a defined benefit plan, a corrective distribution for an individual should be

Employee Plans CPE Technical Topics for 1998

increased to take into account the delayed payment, consistent with the plan's actuarial adjustments.

(4) Special exceptions to full correction. In general, a Qualification Failure must be fully corrected. Although the mere fact that correction is inconvenient or burdensome is not enough to relieve a plan sponsor of the need to make full correction, full correction may not be required in certain situations because it is unreasonable or not feasible. Even in these situations, the correction method adopted must be one that does not have significant adverse effects on participants and beneficiaries or the plan, and that does not discriminate significantly in favor of highly compensated employees. The exceptions described below specify those situations in which full correction is not required.

(a) Reasonable estimates. If it is not possible to make a precise calculation, or the probable difference between the approximate and the precise restoration of a participant's benefits is insignificant and the administrative cost of determining precise restoration would significantly exceed the probable difference, reasonable estimates may be used in calculating appropriate correction.

(b) Delivery of very small benefits. If the total corrective distribution due a participant or beneficiary is \$20 or less, the plan sponsor is not required to make the corrective distribution if the reasonable direct costs of processing and delivering the distribution to the participant or beneficiary would exceed the amount of the distribution.

(c) Locating lost participants. Reasonable actions must be taken to find all current and former participants and beneficiaries to whom additional benefits are due, but who have not been located after a mailing to the last known address. In general, such actions include use of the Internal Revenue Service Letter Forwarding Program (see Rev. Proc. 94-22, 1994-1 C.B. 608) or the Social Security Administration Reporting Service. A plan will not be considered to have failed to correct a failure due to the inability to locate an individual if either of these programs is used; provided that, if the individual is later located, the additional benefits must be provided to the individual at that time.

(5) Reporting. Any distributions from the plan should be properly reported.

(6) Additional guidance. The Service may publish additional rules regarding appropriate correction methods.

.03 Correction under statute or regulations. Generally, none of the correction programs are needed to correct failures that can be corrected under the Code and related regulations. For example, as a general rule, a Plan Document Failure that is a disqualifying provision for which the remedial amendment period under § 401(b) has not expired can be corrected by operation of the Code through retroactive remedial amendment.

.04 Matters subject to excise taxes. Excise taxes and additional taxes, to the extent applicable, are not waived merely because the underlying failure has been corrected or because the taxes result from the correction. Thus, for example, the excise tax on certain excess contributions under § 4979 is not waived under these correction programs.

Employee Plans CPE Technical Topics for 1998

The correction programs are not available for events for which the Code provides tax consequences other than plan disqualification (such as the imposition of an excise tax or additional income tax). For example, funding deficiencies (failures to make the required contributions to a plan subject to § 412), prohibited transactions, and failures to file the Form 5500 cannot be corrected under the correction programs. However, if the event is also an Operational Failure (for example, if the terms of the plan document relating to plan loans to participants were not followed and loans made under the plan did not satisfy § 72(p)(2)), the correction programs will be available to correct the Operational Failure, even though the excise or income taxes generally still will apply. (In limited circumstances, as described in section 10.05, if the failure involves the failure to satisfy the minimum distribution requirements of § 401(a)(9), the Service may enter into a closing agreement, as part of the VCR program, with respect to the excise tax under § 4974 applicable to plan participants.)

.05 Confidentiality and disclosure. Because each correction program relates directly to the enforcement of the qualification requirements, the information received or generated by the Service under the program is subject to the confidentiality requirements of § 6103, and is not a written determination within the meaning of § 6110.

.06 No effect on other law. Compliance under these programs has no effect on the rights of any party under any other law, including Title I of the Employee Retirement Income Security Act of 1974.

PART IV. SELF-CORRECTION (APRSC)

SECTION 7. IN GENERAL

The requirements of this section are satisfied with respect to an Operational Failure if the plan sponsor satisfies the requirements of section 8 (relating to insignificant Operational Failures), or section 9 (relating to significant Operational Failures).

SECTION 8. SELF-CORRECTION OF INSIGNIFICANT OPERATIONAL FAILURES

.01 Requirements. The requirements of this section are satisfied with respect to an Operational Failure if the Operational Failure is corrected and, given all the facts and circumstances, the Operational Failure is insignificant. This section is available for correcting an insignificant Operational Failure even if the plan or plan sponsor is Under Examination.

.02 Factors. The factors to be considered in determining whether or not an Operational Failure under a plan is insignificant include, but are not limited to: (1) whether other failures occurred during the period being examined (for this purpose, a failure is not considered to have occurred more than once merely because more than one participant is affected by the failure); (2) the percentage of plan assets and contributions involved in the failure; (3) the number of years the failure occurred; (4) the number of participants affected relative to the total number of participants in the plan; (5) the number of participants affected as a result of the failure relative to the number of participants who could have been affected by the failure; (6) whether correction was made within a reasonable time after discovery of the failure; and (7) the reason for the

Employee Plans CPE Technical Topics for 1998

failure (for example, data errors such as errors in the transcription of data, the transposition of numbers, or minor arithmetic errors). No single factor is determinative.

.03 Multiple failures. In the case of a plan with more than one Operational Failure in a single year, or Operational Failures that occur in more than one year, the Operational Failures are eligible for correction under this section only if all of the Operational Failures (other than Operational Failures that are not treated as resulting in disqualification of the plan under section 9, the VCR program in section 10, or Walk-in CAP in section 11) are insignificant in the aggregate.

.04 Examples. The following examples illustrate the application of this section. It is assumed, in each example, that the eligibility requirements of section 4 relating to APRSC have been satisfied and that no Operational Failures occurred other than the Operational Failures identified below.

Example 1: In 1984, Employer X established Plan A, a profit-sharing plan that satisfies the requirements of § 401(a) in form. In 1999, the benefits of 50 of the 250 participants in Plan A were limited by § 415(c). However, when the Service examined Plan A in 2002, it discovered that, during the 1999 limitation year, the annual additions allocated to the accounts of 3 of these employees exceeded the maximum limitations under § 415(c). Employer X contributed \$3,500,000 to the plan for the plan year. The amount of the excesses totalled \$4,550. Based on data provided by Employer X, the Service did not find any evidence of other failures in the plan. Under these facts, because the number of participants affected by the failure relative to the total number of participants who could have been affected by the failure, and the monetary amount of the failure relative to the total employer contribution to the plan for the 1999 plan year, are insignificant, the § 415(c) failure in Plan A that occurred in 1999 would be eligible for correction under this section.

Example 2: The facts are the same as in Example 1, except that the failure to satisfy § 415 occurred during each of the 1998, 1999, and 2000 limitation years. In addition, the three participants affected by the § 415 failure were not identical each year. The fact that the § 415 failures occurred during more than one limitation year did not cause the failures to be significant; accordingly, the failures are still eligible for correction under this section.

Example 3: The facts are the same as in Example 1, except that the annual additions of 18 of the 50 employees whose benefits were limited by § 415(c) nevertheless exceeded the maximum limitations under § 415(c) during the 1999 limitation year, and the amount of the excesses ranged from \$1,000 to \$9,000, and totalled \$150,000. Under these facts, taking into account the number of participants affected by the failure relative to the total number of participants who could have been affected by the failure for the 1999 limitation year (and the monetary amount of the failure relative to the total employer contribution), the failure is significant. Accordingly, the § 415(c) failure in Plan A that occurred in 1999 is ineligible for correction under this section as an insignificant failure.

Example 4: Employer J maintains Plan C, a money purchase pension plan established in 1992. The plan document satisfies the requirements of § 401(a) of the Code. The formula under the plan provides for an employer contribution equal to 10% of compensation, as defined in the plan. During its examination of the plan for the 1999 plan year, the Service discovered that the employee responsible for entering data into the employer's computer made minor arithmetic errors in transcribing the

Employee Plans CPE Technical Topics for 1998

compensation data with respect to 6 of the plan's 40 participants, resulting in excess allocations to those 6 participants' accounts. Under these facts, the number of participants affected by the failure relative to the number of participants that could have been affected is insignificant, and the failure is due to minor data errors. Thus, the failure occurring in 1999 would be insignificant and therefore eligible for correction under this section.

Example 5: Public School maintains for its 200 employees a salary reduction 403(b) plan (the "Plan") which satisfies the requirements of § 403(b). The business manager has primary responsibility for administering the Plan, in addition to other administrative functions within Public School. During the 1998 plan year, a former employee should have received an additional minimum distribution of \$278 under § 403(b)(10). Another participant received an impermissible hardship withdrawal of \$2,500. Another participant made elective deferrals of \$11,000, \$1,000 of which was in excess of the § 402(g) limit. Under these facts, even though multiple failures occurred in a single plan year, the failures will be eligible for correction under this section because in the aggregate the failures are insignificant.

SECTION 9. SELF-CORRECTION OF SIGNIFICANT OPERATIONAL FAILURES

.01 Requirements. The requirements of this section are satisfied with respect to an Operational Failure (even if significant) if the Operational Failure is corrected and the correction is either completed or substantially completed (in accordance with section 9.03) by the last day of the correction period described in section 9.02.

.02 Correction period. The last day of the correction period for an Operational Failure is the last day of the second plan year following the plan year for which the failure occurred. However, in the case of a failure to satisfy the requirements of § 401(k)(3), 401(m)(2), or 401(m)(9), the plan year that includes the last day of the additional period for correction permitted under § 401(k)(8) or 401(m)(6) is treated, for this purpose, as the plan year for which the Operational Failure occurs. The correction period for an Operational Failure that occurs for any plan year ends, in any event, on the first date the plan or plan sponsor is Under Examination for that plan year (determined without regard to the exception in the preceding sentence). (But see section 9.03 for special rules permitting completion of correction after the end of the correction period.)

.03 Substantial completion of correction. Correction of an Operational Failure is substantially completed by the last day of the correction period only if the requirements of either paragraph (1) or (2) are satisfied.

(1) The requirements of this paragraph (1) are satisfied if:

(a) during the correction period, the plan sponsor is reasonably prompt in identifying the Operational Failure, formulating a correction method, and initiating correction in a manner that demonstrates a commitment to completing correction of the Operational Failure as expeditiously as practicable, and

(b) within 90 days after the last day of the correction period, the plan sponsor completes correction of the Operational Failure.

(2) The requirements of this paragraph (2) are satisfied if:

Employee Plans CPE Technical Topics for 1998

(a) during the correction period, correction is completed with respect to 85% of all participants affected by the Operational Failure, and

(b) thereafter, the plan sponsor completes correction of the Operational Failure with respect to the remaining affected participants in a diligent manner.

.04 Example. The following example illustrates the application of this section. Assume that the eligibility requirements of section 4 relating to APRSC have been met.

Employer Z established a qualified defined contribution plan in 1986 and received a favorable determination letter for TRA '86. During 1999, while doing a self-audit of the operation of the plan for the 1998 plan year, the plan administrator discovered that, despite the practices and procedures established by Employer Z with respect to the plan, several employees eligible to participate in the plan were excluded from participation. The administrator also found that for 1998 the elective deferrals of additional employees exceeded the § 402(g) limit and discovered Operational Failures in 1998 with respect to the top-heavy provisions of the plan. During the 1999 plan year, the plan sponsor made corrective contributions on behalf of the excluded employees, distributed the excess deferrals to the affected participants, and made a top-heavy minimum contribution to all participants entitled to that contribution for the 1999 plan year. Each corrective contribution and distribution was credited with earnings at a rate appropriate for the plan from the date the corrective contribution or distribution should have been made to the date of correction. The Service subsequently found, upon an examination of the plan, that the Operational Failures for the 1998 plan year were corrected by the plan administrator within the correction period and thus satisfied the requirements of this section.

PART V. VOLUNTARY CORRECTION WITH SERVICE APPROVAL (VCR AND WALK-IN CAP)

SECTION 10. VCR PROGRAM

.01 VCR requirements. The requirements of this section are satisfied with respect to an Operational Failure if the submission requirements of section 12 below are satisfied and the plan sponsor corrects the failures identified in accordance with the compliance statement described in section 10.13.

.02 Identification of failures. VCR is not based upon an examination of the plan by the Service. The Service will not make any investigation or finding under the VCR program concerning whether there are Operational Failures. Only the Operational Failures raised by the plan sponsor or Operational Failures identified by the Service in processing the application will be addressed under the program, and only those failures will be covered by the program. However, because the VCR program does not arise out of an examination, consideration under the VCR program does not preclude or impede (under § 7605(b) or any administrative provisions adopted by the Service) a subsequent examination of the plan sponsor or the plan by the Service with respect to the taxable year (or years) involved with respect to matters that are outside the compliance statement. A plan sponsor's statements describing Operational Failures are made only for purposes of the VCR program and will not be regarded by the Service as an admission of a failure for purposes of any subsequent examination.

Employee Plans CPE Technical Topics for 1998

.03 No concurrent examination activity. Except in unusual circumstances, a plan that has been properly submitted under the VCR program will not be examined while the submission is pending. This practice regarding concurrent examinations does not extend to other plans of the plan sponsor. Thus, any plan of the plan sponsor that is not pending under the VCR program could be subject to examination by the appropriate Key District Office.

.04 Insufficient information. Where it is not possible to obtain sufficient information to properly determine the nature or extent of a failure or there is insufficient information to effect proper correction, or in other special circumstances where the application of the VCR program would be inappropriate or impractical, the failure cannot be corrected under the VCR program.

.05 Closing agreements with respect to the excise tax under § 4974. As a general rule, a plan sponsor is not required to enter into a closing agreement with the Service with respect to the excise tax due under § 4974 because of the failure to satisfy the minimum distribution requirements under § 401(a)(9). However, the Service retains the discretion to require a plan sponsor to enter into a closing agreement in rare or unusual cases. The Service will enter into a closing agreement at the request of the plan sponsor only in cases where 10 or more plan participants are subject to the excise tax under § 4974. In such cases, the closing agreement entered into will require the plan sponsor to pay 100 percent of the excise tax due under § 4974.

.06 Initial processing.

(1) The Service will review whether the eligibility requirements of section 4 and the submissions requirements of section 12 are satisfied.

(2) If the plan is not the subject of a Favorable Letter or the failure is not an Operational Failure, the compliance fee will be returned to the plan sponsor, and the plan sponsor will be informed of the option to voluntarily request consideration under Walk-in CAP in the appropriate Key District Office.

(3) If a plan sponsor requests a compliance statement under the VCR program for a plan with egregious failures described in section 4.06, the compliance fee will be returned and the plan sponsor will be given 60 days to voluntarily request consideration under Walk-in CAP in the appropriate Key District Office. If by the end of the 60-day period, a request for consideration under Walk-in CAP has not been received in the appropriate Key District Office, the VCR request will be forwarded to that office for examination consideration.

(4) If the Service determines that a submission is seriously deficient, the Service reserves the right to return the submission and the compliance fee without contacting the plan sponsor.

(5) If a request for consideration under the VCR program is not described in paragraph (2), (3), or (4) above, but nevertheless fails to comply with the provisions of this revenue procedure or if additional information is required, a Service representative will generally contact the plan sponsor or the plan sponsor's representative and explain what is needed to complete the submission. The plan sponsor will have 21 calendar days from the date of this contact to provide the requested information. If the information is not received within 21 days, the matter will be closed, the compliance fee will not be returned, and the case may be referred to the

Employee Plans CPE Technical Topics for 1998

appropriate Key District Office in accordance with section 10.06(5). Any request for an extension of the 21-day time period must be made in writing within the 21-day time period and must be approved by the Service.

.07 Processing of acceptable submission. Once the Service determines that a request for consideration under the VCR program is acceptable, the Service will consult with the plan sponsor or the plan sponsor's representative to discuss the proposed corrections and the plan's administrative procedures. If agreement is reached, the Service will issue a compliance statement with an enclosed acknowledgment letter for signature by the plan sponsor. The case will not be closed favorably until the Service has received the signed acknowledgement letter from the plan sponsor. The Service will discuss the appropriateness of the plan's existing administrative procedures with the plan sponsor. Where current procedures are inadequate for operating the plan in conformance with the qualification requirements of the Code, the compliance statement will be conditioned upon the implementation of stated procedures within the stated time period. The Service may prescribe appropriate administrative procedures in the compliance statement.

.08 Failures discovered after initial submission.

(1) A plan sponsor that discovers additional, unrelated Operational Failures after its initial submission may request that such failures be added to its submission. The Service retains the discretion to reject the inclusion of such failures if the request is not timely, for example, if the plan sponsor makes its request when processing of the VCR submission is substantially complete.

(2) If the Service discovers an unrelated Operational Failure while the request is pending under the VCR program, the failure generally will be added to the failures under consideration in the submission. The Service retains the discretion to determine that a failure is outside the scope of the voluntary request for consideration because it was not voluntarily brought forward by the plan sponsor. In this case, the plan may be forwarded to the appropriate Key District Office for consideration on examination, but forwarding to the Key District Office will occur only in rare or unusual circumstances.

.09 Conference right. If the Service initially determines that it cannot issue a compliance statement because the parties cannot agree upon correction or a change in administrative procedures, the plan sponsor or the plan sponsor's representative will be contacted by the Service representative and offered a conference with the Service. The conference can be held either in person or by telephone, and must be held within 21 calendar days of the date of contact. The plan sponsor will have 21 calendar days after the date of the conference to submit additional information in support of the submission. Any request for an extension of the 21-day time period must be made in writing within the 21-day time period and must be approved by the Service. Additional conferences may be held at the discretion of the Service.

.10 Failure to reach resolution. If resolution cannot be reached (for example, where information is not timely provided to the Service or because agreement cannot be reached on correction or a change in administrative procedures), the compliance fee will not be returned, and the case may be referred to the appropriate Key District Office for examination consideration.

Employee Plans CPE Technical Topics for 1998

.11 Concurrent processing of determination letter applications. The Service may process a determination letter application (including an application requested on Form 5310, Application for Determination of Qualification Upon Termination) concurrently with a VCR submission for the same plan. However, issuance of the determination letter in response to an application made on a Form 5310 will be suspended pending the closure of the VCR submission.

.12 Special rules relating to SVP.

(1) Under the VCR program, certain Operational Failures may be corrected under the Standardized VCR Procedure ("SVP") rules in this section. SVP is available if the plan's only identified Operational Failure or Failures are ones that are listed in Appendix A of this revenue procedure and the failures are corrected in accordance with the applicable correction method set forth in Appendix A. The plan sponsor must request an SVP compliance statement and pay the reduced compliance fee set forth in section 13.04.

(2) The correction methods set forth in Appendix A are strictly construed and are the only acceptable correction methods for SVP failures. If the plan sponsor wishes to modify a correction method provided in Appendix A or to propose another method, the plan sponsor may not use SVP, but may request a compliance statement under the regular VCR procedures.

(3) SVP is not available if the plan sponsor has identified more than two SVP failures in a single SVP request. If there are one or two failures that can be corrected under SVP and other failures that cannot be corrected under SVP, SVP is not available. The Service reserves the right to shift a request for consideration under SVP into the regular VCR program if the plan sponsor submits a second SVP request with respect to the same plan while the first SVP request is being considered or during the 12 months after the first SVP compliance statement is issued.

(4) The Service will review an SVP request within 120 days of the date the submission is received and determined to be complete. If the Service determines that the request is acceptable, the Service will issue a compliance statement on the plan sponsor's proposed correction.

.13 General description of compliance statement. Under the VCR program, a plan sponsor receives a compliance statement from the Service. The compliance statement addresses the failures identified, the terms of correction, and any revision of administrative procedures, and provides that the Service will not treat the plan as disqualified on account of the Operational Failures described in the compliance statement. In addition, the time period within which proposed corrections and changes in administrative procedures must be implemented are set forth in the compliance statement. The compliance statement is conditioned on the accuracy or acceptability of any calculations or other material submitted in connection with the request.

.14 Compliance statement conditioned upon timely correction. The compliance statement is conditioned upon the implementation of the specific corrections and administrative changes set forth in the compliance statement within 150 days of the date of the compliance statement. Any request for an extension of this time period must be made in advance and in writing and must be approved by the Service.

Employee Plans CPE Technical Topics for 1998

.15 Compliance statement for new plans conditioned upon timely amendment. Reliance on any compliance statement issued for a plan initially adopted or effective after December 7, 1994, other than an adoption of a master or prototype or regional prototype plan, is conditioned upon the plan being timely submitted for a determination letter within the plan's remedial amendment period under § 401(b).

.16 Acknowledgement letter. Within 30 calendar days after the compliance statement is issued, a plan sponsor that wishes to agree to the terms of the compliance statement must send a signed acknowledgement letter to the Service, agreeing to the terms of the compliance statement. If the plan sponsor does not send the Service a signed acknowledgement letter within 30 calendar days, the plan may be referred to the appropriate Key District Office for examination consideration. Once the compliance statement has been issued (based on the information provided), the plan sponsor cannot request a modification of the compliance terms except by a new request for a compliance statement. However, if the requested modification is minor and is postmarked no later than 30 days after the compliance statement is issued, the VCR compliance fee for the modification will be the lesser of the original compliance fee or \$1,250.

.17 Verification. Once the compliance statement has been issued, the Service may require verification that the corrections have been made and that any plan administrative procedures required by the statement have been implemented. This verification does not constitute an examination of the books and records of the employer or the plan (within the meaning of § 7605(b)). If the Service determines that the plan sponsor did not implement the corrections and procedures within the stated time period, the Service may consider the issues in an examination.

SECTION 11. WALK-IN CAP

.01 Walk-in CAP requirements.

(1) The requirements of this section are satisfied with respect to a Plan Document, an eligible Operational (see section 4.01), or a Demographic Failure if the submission requirements of section 12 are satisfied, the plan sponsor pays the compliance correction fee, and the plan sponsor corrects the failures identified in accordance with a closing agreement entered into by the Service and the plan sponsor. Payment of the compliance correction fee is generally required at the time the closing agreement is signed.

(2) A determination letter application is not a submission under Walk-in CAP.

(3) Depending on the nature of the failure, the Service will discuss the appropriateness of the plan's existing administrative procedures with the plan sponsor. Where current administrative procedures are inadequate for operating the plan in conformance with the qualification requirements of the Code, the closing agreement may be conditioned upon the implementation of stated administrative procedures.

(4) In addition, the plan sponsor is required to obtain a Favorable Letter before the closing agreement is signed unless the Service determines that it is unnecessary based on the facts and

Employee Plans CPE Technical Topics for 1998

circumstances (for example, because the plan already has a Favorable Letter and no significant amendments are adopted). If a Favorable Letter is required, the plan sponsor would be required to pay the applicable user fee for obtaining the letter.

.02 Failures discovered after initial submission.

(1) A plan sponsor that discovers additional, unrelated failures after its initial submission may request that such failures be added to its submission. However, the Service retains the discretion to reject the inclusion of such failures if the request is not timely, for example, if the plan sponsor makes its request when processing of the submission is substantially complete.

(2) If the Service discovers an unrelated plan failure while the request is pending, the failure generally will be added to the failures under consideration. However, the Service retains the discretion to determine that a failure is outside the scope of the voluntary request for consideration because it was not voluntarily brought forward by the plan sponsor. In this case, if the additional failure is significant, all aspects of the plan will be examined, and the rules pertaining to Audit CAP will apply.

.03 Failure to reach resolution. If the Service and the plan sponsor cannot reach agreement with respect to the submission, all aspects of the plan may be examined, and the rules pertaining to Audit CAP will apply.

.04 Effect of closing agreement. The closing agreement is binding upon both the Service and the plan sponsor with respect to the specific tax matters identified therein for the periods specified, but does not preclude or impede an examination of the plan by the Service relating to matters outside the closing agreement, even with respect to the same taxable year or years to which the closing agreement relates.

SECTION 12. APPLICATION PROCEDURES FOR VCR AND WALK-IN CAP

.01 General rules. This section sets forth the procedures for requesting a compliance statement from the Service under the VCR program (including SVP) and for requesting a closing agreement under Walk-in CAP. In general, a request under the VCR program or Walk-in CAP consists of a letter from the plan sponsor or the plan sponsor's representative to the Service that contains a description of the failures, a description of the proposed methods of correction, and other procedural items, and includes supporting information and documentation as described below.

.02 Multiemployer and multiple employer plans. In the case of a multiemployer or multiple employer plan, the plan administrator (rather than any contributing or adopting employer) must request consideration of the plan under the programs. The request must be with respect to the plan, rather than a portion of the plan affecting any particular employer.

.03 Submission requirements. The letter from the plan sponsor or the plan sponsor's representative must contain the following:

Employee Plans CPE Technical Topics for 1998

- (1) A complete description of the failures and the years in which the failures occurred, including closed years (that is, years for which the statutory period has expired).
- (2) A description of the administrative procedures in effect at the time the failures occurred.
- (3) An explanation of how and why the failures arose.
- (4) A detailed description of the method for correcting the failures that the plan sponsor has implemented or proposes to implement. Each step of the correction method must be described in narrative form. The description must include the specific information needed to support the suggested correction method. This information includes, for example, the number of employees affected and the expected cost of correction (both of which may be approximated if the exact number cannot be determined at the time of the request), the years involved, and calculations or assumptions the plan sponsor used to determine the amounts needed for correction. See section 10.12 for special procedures regarding SVP.
- (5) A description of the methodology that will be used to calculate earnings or actuarial adjustments on any corrective contributions or distributions (indicating the computation periods and the basis for determining earnings or actuarial adjustments, in accordance with section 6.02(3)).
- (6) Specific calculations for each affected employee or a representative sample of affected employees. The sample calculations must be sufficient to demonstrate each aspect of the correction method proposed. For example, if a plan sponsor requests a compliance statement with respect to a failure to satisfy the contribution limits of § 415(c) and proposes a correction method that involves elective contributions (both matched and unmatched) and matching contributions, the plan sponsor must submit calculations illustrating the correction method proposed with respect to each type of contribution. As another example, with respect to a failure to satisfy the actual deferral percentage ("ADP") test in § 401(k)(3), the plan sponsor must submit the ADP test results both before the correction and after the correction.
- (7) The method that will be used to locate and notify former employees and beneficiaries, or an affirmative statement that no former employees or beneficiaries were affected by the failures.
- (8) A description of the measures that have been or will be implemented to ensure that the same failures will not recur.
- (9) A statement that, to the best of the plan sponsor's knowledge, neither the plan nor the plan sponsor is Under Examination.
- (10) In the case of a VCR submission, a statement (if applicable) that the plan is currently being considered in a determination letter application. If the request for a determination letter is made while a request for consideration under VCR is pending, the plan sponsor must update the VCR request to add this information.
- (11) In the case of an SVP submission, a statement that it is an SVP request, a description of the applicable correction in accordance with Appendix A, and a statement that the plan sponsor

Employee Plans CPE Technical Topics for 1998

proposes to implement (or has implemented) the correction(s).

.04 Required documents. The submission must be accompanied by the following documents:

(1) In the case of a VCR submission, a copy of the first page and a copy of the page containing employee census information (currently, line 7f of the 1997 Form 5500) and a copy of the page containing the total amount of plan assets (currently, line 31f of the 1997 Form 5500) of the most recently filed Form 5500 series return, or in the case of a Walk-in CAP submission, a copy of the most recently filed Form 5500 series return.

(2) A copy of the relevant portions of the plan document. For example, in a case involving improper exclusion of eligible employees from a profit-sharing plan with a cash or deferred arrangement, relevant portions of the plan document include the eligibility, allocation, and cash or deferred arrangement provisions of the basic plan document (and the adoption agreement, if applicable), along with applicable definitions in the plan.

(3) In the case of a VCR submission, a copy of the determination letter, opinion letter, or notification letter that considered TRA '86, except:

(a) individually designed plans (including volume submitter plans) for which the TRA '86 remedial amendment period under § 401(b) would have expired but for the fact that an application for a determination or notification letter that considers TRA '86 was timely submitted to the Service and is pending at the time of the application to the VCR program should submit a copy of the determination letter that considered TEFRA, DEFRA, and REA and a copy of the letter from the Service acknowledging receipt of the TRA '86 determination letter application (Form 2693),

(b) plans for which the TRA '86 remedial amendment period has not yet expired should submit a copy of the determination, opinion, or notification letter that considered TEFRA, DEFRA, and REA and a statement that explains the reason why the period has not yet expired (for example, because the plan is a governmental plan, or because it is an adopter of a master or prototype plan that is still entitled to continued or interim reliance under Rev. Proc. 89-9, 1989-1 C.B. 780), and

(c) plans initially adopted or effective after December 7, 1994, should submit a statement indicating that the plan will be submitted timely for a determination, opinion, or notification letter within the plan's remedial amendment period under § 401(b).

.05 Fee. The VCR submission must include the appropriate fee described in section 13.02 or 13.04 below. (The Walk-in CAP compliance correction fee is due at the time the closing agreement is signed.)

.06 Signed submission. The submission must be signed by the plan sponsor or the sponsor's representative.

.07 Power of attorney requirements. To sign the submission or to appear before the Service in connection with the submission, the plan sponsor's representative must comply with the

Employee Plans CPE Technical Topics for 1998

requirements of section 9.02(11) and (12) of Rev. Proc. 98-4, 1998-1 I.R.B. 113.

.08 Penalty of perjury statement. The following declaration must accompany a request and any factual information or change in the submission at a later time: "**Under penalties of perjury, I declare that I have examined this submission, including accompanying documents, and, to the best of my knowledge and belief, the facts presented in support of this submission are true, correct, and complete.**" The declaration must be signed by the plan sponsor, not the sponsor's representative.

.09 Checklist. The Service will be able to respond more quickly to a VCR or Walk-in CAP request if the request is carefully prepared and complete. The checklist in Appendix B is designed to assist plan sponsors and their representatives in preparing a submission that contains the information and documents required under this revenue procedure. The checklist in Appendix B must be completed, signed, and dated by the plan sponsor or the plan sponsor's representative, and should be placed on top of the submission. A photocopy of this checklist may be used.

.10 Designation. The letter to the Service should be designated "VCR PROGRAM," "SVP/VCR PROGRAM," or "WALK-IN CAP PROGRAM," as appropriate, in the upper right hand corner of the letter.

.11 VCR/SVP mailing address. VCR/SVP submissions should be mailed to:

Internal Revenue Service
Attention: CP:E:EP:VCR
P.O. Box 14073
Ben Franklin Station
Washington, D.C. 20044

.12 Walk-in CAP mailing address. Walk-in CAP submissions should be mailed to the Closing Agreement Coordinator in the appropriate Key District Office:

NORTHEAST REGION EP/EO Division Review Staff
Internal Revenue Service
10 Metro Tech Center
625 Fulton Street
Brooklyn, NY 11201
Office (718) 488-2372
FAX (718) 488-2405

Employee Plans CPE Technical Topics for 1998

Revenue Service	SOUTHEAST REGION Room 1520 P.O. Box 13163 Baltimore, MD 21203 Office (410) 962-3499 FAX (410) 962-0882	EP/EO Division Technical Branch	Internal
	MIDSTATES REGION Internal Revenue Service 230 S. Dearborn Chicago, IL 60604 Office (312) 886-4700 FAX (312) 886-3275	EP/EO Division Branch Office	
	WESTERN REGION Internal Revenue Service Attention: EP Walk-in CAP Coordinator McCaslin Industrial Park 2 Cupania Circle Monterey Park, CA 91755-7431 Office (213) 725-1852 FAX (213) 725-7065	EP/EO Division	

.13 Maintenance of copies of submissions. Plan sponsors and their representatives should maintain copies of all correspondence submitted to the Service with respect to their VCR and Walk-in CAP requests.

SECTION 13. FEES

.01 Rev. Proc. 98-8 modified. The VCR compliance fee is processed under the user fee program described in Rev. Proc. 98-8, 1998-1 I.R.B. 225, as modified by this revenue procedure.

.02 VCR fee. Unless SVP is applicable, the VCR compliance fee depends on the assets of the plan and the number of plan participants.

(1) The fee for a plan with assets of less than \$500,000, and no more than 1,000 plan participants, is \$500.

(2) The fee for a plan with assets of at least \$500,000, and no more than 1,000 plan participants, is \$1,250.

(3) The fee for a plan with more than 1,000 plan participants but less than 10,000 plan participants is \$5,000.

(4) The fee for a plan with 10,000 or more plan participants is \$10,000.

Employee Plans CPE Technical Topics for 1998

.03 Establishing number of plan participants. The compliance fee is calculated by the plan sponsor using the numbers from the most recently filed Form 5500 series to establish the fee. Thus, with respect to the 1997 Form 5500, the plan sponsor would use the number shown on line 7(f) (or the equivalent line on the Form 5500 C/R or EZ) to establish the number of plan participants and would use line 31(f) (or the equivalent line on the Form 5500 C/R or EZ) to establish the amount of plan assets.

.04 SVP fee. The SVP compliance fee is \$350.

.05 Walk-in CAP compliance correction fee. (1) Compliance correction fee chart. The compliance correction fee for a Walk-in CAP application is determined in accordance with the chart below. The chart contains a graduated range of fees based on the size of the plan (with the number of participants determined as provided in section 13.03). Each range includes a minimum amount, a maximum amount, and a presumptive amount. In each case, the minimum amount is the applicable VCR fee in section 13.02. It is expected that in most instances the compliance correction fee imposed will be at or near the presumptive amount in each range; however, the fee may be a higher or lower amount within the range, depending on the factors in paragraph (2) below.

Employee Plans CPE Technical Topics for 1998

# of participants	Fee range	Presumptive Amount
10 or fewer	VCR fee* to \$4,000	\$2,000
11 to 50	VCR fee* to \$8,000	\$4,000
51 to 100	VCR fee* to \$12,000	\$6,000
101 to 300	VCR fee* to \$16,000	\$8,000
301 to 1000	VCR fee* to \$30,000	\$15,000
over 1,000	VCR fee* to \$70,000	\$35,000

* Items marked by asterisk refer to the VCR compliance fee that would apply under section 13.02 if the plan had been submitted under the VCR program.

(2) Factors considered. Consideration of whether the compliance correction fee should be equal to, greater than, or less than the presumptive amount will depend on factors relating to the nature, extent, and severity of the failure. These factors include: (a) whether the failure is a failure to satisfy the requirements of § 401(a)(4), § 401(a)(26), or § 410(b), (b) whether the plan has both Operational and Plan Document Failures, (c) the period over which the violation occurred (for example, the time that has elapsed since the end of the applicable remedial amendment period under § 401(b) for a Plan Document Failure), and (d) whether the plan has a Favorable Letter.

(3) Egregious failures. In cases involving failures that are egregious (as described in section 4.06), (a) the maximum compliance correction fee applicable to the plan under the chart in 13.05(1) is increased to 40 percent of the Maximum Payment Amount, and (b) no presumptive amount applies.

PART VI. CORRECTION ON AUDIT (AUDIT CAP)

SECTION 14. DESCRIPTION OF AUDIT CAP

.01 Audit CAP requirements. In the event the Service identifies a Qualification Failure (other than a failure that is not treated as resulting in disqualification of the plan under APRSC, VCR, or Walk-in CAP) upon an Employee Plans or Exempt Organizations examination of a Qualified Plan, the requirements of this section are satisfied with respect to the failure if the plan sponsor corrects the failure, pays a sanction in accordance with section 14.02, satisfies any additional requirements of section 14.03, and enters into a closing agreement with the Service.

.02 Payment of sanction. Under Audit CAP, the plan sponsor is subject to a sanction determined in accordance with section 15. Payment of the sanction generally will be required at the time the closing agreement is signed.

Employee Plans CPE Technical Topics for 1998

.03 Additional requirements. Depending on the nature of the failure, the Service will discuss the appropriateness of the plan's existing administrative procedures with the plan sponsor. Where existing administrative procedures are inadequate for operating the plan in conformance with the qualification requirements of the Code, the closing agreement may be conditioned upon the implementation of stated procedures. In addition, the plan sponsor may be required to obtain a Favorable Letter before the closing agreement is signed unless the Service determines that it is unnecessary based on the facts and circumstances (for example, because the plan already has a Favorable Letter and no significant amendments are adopted). If a Favorable Letter is required, the plan sponsor would be required to pay the applicable user fee for obtaining the letter.

.04 Failure to reach resolution. If the Service and the plan sponsor cannot reach an agreement with respect to the correction of the failure(s) or the amount of the sanction, the plan will be disqualified.

.05 Effect of closing agreement. A closing agreement constitutes an agreement between the Service and the plan sponsor that is binding with respect to the tax matters identified therein for the periods specified.

.06 Other procedural rules. The procedural rules for Audit CAP are set forth in chapter 11 of Internal Revenue Manual ("IRM") 7(10)54. This revenue procedure modifies and replaces the portions of IRM 7(10)54 that relate to eligibility (section 4.2 and section 4.3.1) and sanctions (section 4.3.3) under Audit CAP. The other provisions of IRM 7(10)54, relating mostly to matters of internal procedure, remain unchanged.

SECTION 15. AUDIT CAP SANCTION

.01 Determination of sanction. The sanction under Audit CAP is a negotiated percentage of the Maximum Payment Amount. Sanctions will not be excessive and will bear a reasonable relationship to the nature, extent, and severity of the failures.

.02 Factors considered. The amount of the sanction will depend on factors relating to the nature, extent, and severity of the failures, including the extent to which correction had progressed before the examination was initiated. Other factors relating to the nature, extent, and severity of the failures include: (1) the number and type of employees affected by the failure, (2) the number of nonhighly compensated employees who would be adversely affected if the plan was not treated as qualified, (3) whether the failure is a failure to satisfy the requirements of § 401(a)(4), § 401(a)(26), or § 410(b), (4) whether the plan has both Operational and Plan Document Failures, (5) the period over which the failure occurred (for example, the time that has elapsed since the end of the applicable remedial amendment period under § 401(b) for a Plan Document Failure), (6) the reason for the failure (for example, data errors such as errors in transcription of data, the transposition of numbers, or minor arithmetic errors), and (7) whether the plan is the subject of a Favorable Letter.

PART VII. CHRONOLOGY, EFFECT ON OTHER DOCUMENTS, AND EFFECTIVE DATE

Employee Plans CPE Technical Topics for 1998

SECTION 16. CHRONOLOGY

.01 APRSC. (1) On March 26, 1991, the Service established the Administrative Policy Regarding Sanctions (APRS), under which, at the discretion of the applicable Key District Office, certain minor Operational Failures of the qualification requirements for pension, profit-sharing and stock bonus plans could be treated as not resulting in either plan disqualification or the related adverse tax consequences. To be eligible for relief under APRS, Operational Failures had to satisfy six narrowly drawn criteria.

(2) On December 23, 1996, the Service replaced APRS with APRSC, an administrative policy that broadened the scope of APRS in three significant ways: (a) it expanded the original criteria for eligibility, (b) it established a self-correction procedure whereby plan sponsors may correct their plans for Operational Failures within a specified time period, and (c) it extended relief to § 403(b) plans.

(3) Announcement 97-121 extended the period for correcting Operational Failures under Part IV of APRSC from the end of the first plan year following the plan year in which the Operational Failure occurred, to the end of the second plan year following the plan year in which the Operational Failure occurred.

.02 VCR program. (1) On November 16, 1992, the Service established the VCR program as a temporary, experimental program ending on December 31, 1993. On September 20, 1993, Rev. Proc. 93-36, 1993-2 C.B. 474, extended the expiration date of the VCR program to December 31, 1994, and added SVP, a simplified correction procedure for certain listed failures.

(2) On September 26, 1994, Rev. Proc. 94-62, 1994-2 C.B. 778, extended the VCR program indefinitely and provided that the VCR program would continue to be administered in the Headquarters Office. In addition, Rev. Proc. 94-62 expanded the types of failures that could be corrected under SVP, modified the VCR eligibility standards, and made other administrative and technical changes.

(3) On April 15, 1996, Rev. Proc. 96-29, 1996-1 C.B. 693, modified Rev. Proc. 94-62 to change the eligibility standards of the VCR program relating to whether or not a plan is Under Examination and whether a plan is considered to have a favorable letter.

.03 Walk-in CAP.

(1) The Service established the Walk-in CAP program under Rev. Proc. 94-16, 1994-1 C.B. 455, in response to requests by sponsors of plans that were not eligible for the VCR program, but were not under Employee Plans examination, to be given an opportunity, similar to the VCR program, to voluntarily correct their plan failures. Rev. Proc. 94-16 enabled sponsors of plans with Plan Document or certain Operational Failures to correct failures in their plans and pay a limited monetary sanction.

(2) On April 15, 1996, Rev. Proc. 96-29 modified Rev. Proc. 94-16 to change the definition of when a plan is ineligible for Walk-in CAP because the plan is under an Employee Plans or Exempt Organizations examination.

Employee Plans CPE Technical Topics for 1998

.04 Audit CAP. Audit CAP, established as a pilot program in 1990, permitted a sponsor of a Qualified Plan to avoid disqualification of its plan by entering into a closing agreement with the Service conditioned upon correction of plan failure(s) discovered upon an Employee Plans or Exempt Organizations examination and the payment of a monetary sanction. Audit CAP was expanded and made permanent in 1991.

SECTION 17. EFFECT ON OTHER DOCUMENTS

.01 Revenue procedures modified and superseded. Rev. Procs. 94-16, 94-62, and 96-29 are modified and superseded by this revenue procedure.

.02 Revenue procedure 98-8 modified. Rev. Proc. 98-8 is modified as provided in section 13.

.03 APRSC modified. APRSC is modified and restated in this revenue procedure.

.04 Audit CAP modified. Audit CAP is modified and restated, in part, in this revenue procedure.

SECTION 18. EFFECTIVE DATE

To provide a full opportunity for public comment and for the Service to consider comments, this revenue procedure is generally effective September 1, 1998; however, plan sponsors are permitted, at their option, to apply the provisions of this revenue procedure on or after March 9, 1998.

Specifically, unless a plan sponsor applies the provisions of this revenue procedure earlier, this revenue procedure is effective:

- (1) with respect to VCR and Walk-in CAP, for applications submitted on or after September 1, 1998;
- (2) with respect to Audit CAP, for examinations begun on or after September 1, 1998; and
- (3) with respect to APRSC, for failures for which correction is not complete before January 1, 1999.

SECTION 19. PAPERWORK REDUCTION ACT

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1598.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

The collection of information in this revenue procedure is in sections 4.05, 6.02(4)(c), 10.01, 10.02,

Employee Plans CPE Technical Topics for 1998

10.05-10.09, 10.12, 10.16, 11.01-11.03, 12.01-12.04, and 12.06-12.13, and Appendix B. This information is required to enable the Office of Assistant Commissioner (Employee Plans and Exempt Organizations) of the Internal Revenue Service to make determinations regarding the issuance of various types of closing agreements and compliance statements. This information will be used to issue closing agreements and compliance statements to allow individual plans to continue to maintain their tax qualified status. As a result, favorable tax treatment of the benefits of the eligible employees is retained. The likely respondents are individuals, state or local governments, business or other for-profit institutions, nonprofit institutions, and small businesses or organizations.

The estimated total annual reporting and/or recordkeeping burden is 43,000 hours.

The estimated annual burden per respondent/recordkeeper varies from .5 to 42.5 hours, depending on individual circumstances, with an estimated average of 21.5 hours. The estimated number of respondents and/or recordkeepers is 2,000.

The estimated frequency of responses is occasionally.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

DRAFTING INFORMATION

The principal author of this revenue procedure is Joyce Kahn of the Employee Plans Division. For further information concerning this revenue procedure, please contact the Employee Plans Division's taxpayer assistance telephone service between 1:30 and 3:30 p.m., Eastern Time, Monday through Thursday at (202) 622-6074/6075. (These telephone numbers are not toll-free numbers). Ms. Kahn may be reached at (202) 622-6214 (also not a toll-free number). For specific information regarding Walk-in CAP and APRSC, you may call Carlton Watkins, also at (202) 622-6214.

Employee Plans CPE Technical Topics for 1998

APPENDIX A OPERATIONAL FAILURES AND CORRECTIONS UNDER SVP

.01 General rule. This appendix sets forth Operational Failures and corrections under SVP in accordance with section 10.12. In each case, the method described corrects the Operational Failure identified in the headings below. Corrective allocations and distributions should reflect earnings and actuarial adjustments in accordance with section 6.02(3)(a).

.02 Failure to properly provide the minimum top-heavy benefit under § 416 of the Code to non-key employees. In a defined contribution plan, the permitted correction method is to properly contribute and allocate the required top-heavy minimums to the plan in the manner provided for in the plan on behalf of the non-key employees (and any other employees required to receive top-heavy allocations under the plan). In a defined benefit plan, the minimum required benefit must be accrued in the manner provided in the plan.

.03 Failure to satisfy the ADP test set forth in § 401(k)(3), the ACP test set forth in § 401(m)(2), or the multiple use test of § 401(m)(9). The permitted correction method is to make qualified nonelective contributions (QNCs) (as defined in § 1.401(k)-1(g)(13)) on behalf of the nonhighly compensated employees to the extent necessary to raise the actual deferral percentage or actual contribution percentage of the nonhighly compensated employees to the percentage needed to pass the test or tests. The contributions must be made on behalf of all eligible nonhighly compensated employees (to the extent permitted under § 415) and must either be the same flat dollar amount or the same percentage of compensation. QNCs contributed to satisfy the ADP test need not be matched. Employees who would have been eligible for a matching contribution had they made elective contributions must be counted as eligible employees for the ACP test, and the plan must satisfy the ACP test. Under this SVP correction method, a plan may not be treated as two separate plans, one covering otherwise excludable employees and the other covering all other employees (as permitted in § 1.410(b)-6(b)(3)) in order to reduce the number of employees eligible to receive QNCs. Likewise, under this SVP correction method, the plan may not be restructured into component plans (as permitted in § 1.401(k)-1(h)(3)(iii) for plan years before January 1, 1992) in order to reduce the number of employees eligible to receive QNCs.

.04 Failure to distribute elective deferrals in excess of the § 402(g) limit (in contravention of § 401(a)(30)). The permitted correction method is to distribute the excess deferral to the employee and to report the amount as taxable in the year of deferral and the year distributed. In accordance with § 1.402(g)-1(e)(1)(ii), a distribution to a highly compensated employee is included in the ADP test; a distribution to a nonhighly compensated employee is not included in the ADP test.

.05 Exclusion of an eligible employee from all contributions or accruals under the plan for one or more plan years. The permitted correction method is to make a contribution to the plan on behalf of the employees excluded from a defined contribution plan or to provide benefit accruals for the employees excluded from a defined benefit plan. If the employee should have been eligible to make an elective contribution under a cash or deferred arrangement, the employer must make a QNC to the plan on behalf of the employee that is equal to the actual deferral percentage for the employee's group (either highly compensated or nonhighly compensated). If

Employee Plans CPE Technical Topics for 1998

the employee should have been eligible to make employee contributions or for matching contributions (on either elective contributions or employee contributions), the employer must make a QNC to the plan on behalf of the employee that is equal to the actual contribution percentage for the employee's group (either highly compensated or nonhighly compensated). Contributing the actual deferral or contribution percentage for such employees eliminates the need to rerun the ADP or ACP test to account for the previously excluded employees. Under this SVP correction method, a plan may not be treated as two separate plans, one covering otherwise excludable employees and the other covering all other employees (as permitted in § 1.410(b)-6(b)(3)) in order to reduce the number of employees eligible to receive QNCs. Likewise, restructuring the plan into component plans under § 1.401(k)-1(h)(3)(iii) is not permitted in order to reduce the number of employees eligible to receive QNCs.

.06 Failure to timely pay the minimum distribution required under § 401(a)(9). In a defined contribution plan, the permitted correction method is to distribute the required minimum distributions. The amount to be distributed for each year in which the failure occurred should be determined by dividing the adjusted account balance on the applicable valuation date by the applicable divisor. For this purpose, adjusted account balance means the actual account balance, determined in accordance with § 1.401(a)(9)-1 Q&A F-5 of the proposed regulations, reduced by the amount of the total missed minimum distributions for prior years. In a defined benefit plan, the permitted correction method is to distribute the required minimum distributions, plus an interest payment representing the loss of use of such amounts.

.07 Failure to obtain participant and/or spousal consent for a distribution subject to the participant and spousal consent rules under §§ 401(a)(11), 411(a)(11) and 417. The permitted correction method is to give each affected participant a choice between providing informed consent for the distribution actually made or receiving a qualified joint and survivor annuity. In order to use this SVP correction method, the plan sponsor must have contacted each affected participant and spouse (to whom the participant was married at the annuity starting date) and received responses from each such individual before requesting consideration under SVP. In the event that participant and/or spousal consent is required but cannot be obtained, the participant must receive a qualified joint and survivor annuity based on the monthly amount that would have been provided under the plan at his or her retirement date. This annuity may be actuarially reduced to take into account distributions already received by the participant. However, the portion of the qualified joint and survivor annuity payable to the spouse upon the death of the participant may not be actuarially reduced to take into account prior distributions to the participant. Thus, for example, if in accordance with the automatic qualified joint and survivor annuity option under a plan, a married participant who retired would have received a qualified joint and survivor annuity of \$600 per month payable for life with \$300 per month payable to the spouse upon the participant's death but instead received a single-sum distribution equal to the actuarial present value of the participant's accrued benefit under the plan, then the \$600 monthly annuity payable during the participant's lifetime may be actuarially reduced to take the single-sum distribution into account. However, the spouse must be entitled to receive an annuity of \$300 per month payable for life beginning at the participant's death.

.08 Failure to satisfy the § 415(c) limits in a defined contribution plan. The permitted correction for failure to limit annual additions (other than elective deferrals and employee contributions) allocated to participants in a defined contribution plan as required in § 415(c) (even if the excess

Employee Plans CPE Technical Topics for 1998

did not result from the allocation of forfeitures or from a reasonable error in estimating compensation) is to place the excess annual additions into an unallocated account, similar to the suspense account described in § 1.415-6(b)(6)(iii), to be used as an employer contribution in the succeeding year(s). While such amounts remain in the unallocated account, the employer is not permitted to make additional contributions to the plan. The permitted SVP correction for failure to limit annual additions that are elective deferrals or employee contributions (even if the excess did not result from a reasonable error in determining the amount of elective deferrals or employee contributions that could be made with respect to an individual under the § 415 limits) is to distribute the elective deferrals or employee contributions using a method similar to that described under § 1.415-6(b)(6)(iv). Elective deferrals and employee contributions that are matched may be returned, provided that the matching contributions relating to such contributions are forfeited (which will also reduce excess annual additions for the affected individuals). The forfeited matching contributions are to be placed into an unallocated account to be used as an employer contribution in succeeding periods.

Employee Plans CPE Technical Topics for 1998

APPENDIX B

VCR/SVP/WALK-IN CAP CHECKLIST IS YOUR SUBMISSION COMPLETE?

INSTRUCTIONS

The Service will be able to respond more quickly to your VCR, SVP, or Walk-in CAP request if it is carefully prepared and complete. To ensure that your request is in order, use this checklist. Answer each question in the checklist by inserting yes, no, or N/A, if appropriate, in the blank next to the item. **Sign and date the checklist (as taxpayer or authorized representative) and place it on top of your request.**

You must submit a completed copy of this checklist with your request. If a completed checklist is not submitted with your request, substantive consideration of your submission will be deferred until a completed checklist is received.

TAXPAYER'S NAME _____

TAXPAYER'S I.D. NO. _____

PLAN NAME & NO. _____

ATTORNEY/P.O.A. _____

The following items relate to all submissions:

- _____ 1. Have you included a complete description of the failure(s) and the years in which the failure(s) occurred (including the years for which the statutory period has expired)? **(See section 12.03(1) of Rev. Proc. 98-22.) (Hereafter, all section references are to Rev. Proc. 98-22.)**
- _____ 2. Have you included an explanation of how and why the failure(s) arose, including a description of the administrative procedures for the plan in effect at the time the failure(s) occurred? **(See section 12.03(2) and (3).)**
- _____ 3. Have you included a detailed description of the method for correcting the failure(s) identified in your submission? This description must include, for example, the number of employees affected and the expected cost of correction (both of which may be approximated if the exact number cannot be determined at the time of the request), the years involved, and calculations or assumptions the plan sponsor used to determine the amounts needed for correction. In lieu of providing correction calculations with respect to each employee affected by a failure, you may submit calculations with respect to a representative sample of affected employees. However, the representative sample calculations must be

Employee Plans CPE Technical Topics for 1998

sufficient to demonstrate each aspect of the correction method proposed. Note that each step of the correction method must be described in narrative form. **(See section 12.03(4).)**

_____ 4. Have you described the earnings or interest methodology (indicating computation period and basis for determining earnings or interest rates) that will be used to calculate earnings or interest on any corrective contributions or distributions? (As a general rule, the interest rate (or rates) earned by the plan during the applicable period(s) should be used in determining the earnings for corrective contributions or distributions.) **(See section 12.03(5).)**

If you inserted "N/A" for item 4, enter explanation:

_____ 5. Have you submitted specific calculations for each affected employee or a representative sample of affected employees? **(See section 12.03(6).)**

_____ 6. Have you described the method that will be used to locate and notify former employees or, if there are no former employees affected by the failure(s), provided an affirmative statement to that effect? **(See section 12.03(7).)**

_____ 7. Have you provided a description of the administrative measures that have been or will be implemented to ensure that the same failure(s) do not recur? **(See section 12.03(8).)**

_____ 8. Have you included a statement that, to the best of the plan sponsor's knowledge, the plan is not currently under an Employee Plans examination? **(See section 12.03(8).)**

_____ 9. Have you included a statement that, to the best of the plan sponsor's knowledge, the plan sponsor is not under an Exempt Organizations examination? **(See section 12.03(8).)**

_____ 10. If the plan is currently being considered in a determination letter application on a Form 5310, have you included a statement to that effect? **(See section 12.03(10).)**

_____ 11. Have you included a copy of the portions of the plan document (and adoption agreement, if applicable) relevant to the failure(s) and method(s) of correction? **(See section 12.04(2).)**

_____ 12. Have you included a copy of the plan's most recent Favorable Letter and/or the required applicable document(s)? **(See section 12.04(3).)**

_____ 13. Have you included the appropriate voluntary compliance fee? **(See section 12.05.)**

Employee Plans CPE Technical Topics for 1998

- _____ 14. Have you included the original signature of the sponsor or the sponsor's representative? **(See section 12.06.)**
- _____ 15. Have you included a Power of Attorney (Form 2848)? Note: (representation under the VCR/SVP and Walk-in CAP is limited to attorneys, certified public accountants, enrolled agents, and enrolled actuaries; unenrolled return preparers are not eligible to act as representatives under the VCR program). **(See section 12.07.)**
- _____ 16. Have you included a Penalty of Perjury Statement signed (original signature only) and dated by the plan sponsor? **(See section 12.08.)**
- _____ 17. Have you designated your submission as a VCR, SVP, or Walk-in CAP submission, as appropriate? **(See section 12.10.)**

The following items relate only to submissions under VCR (including SVP):

- _____ 18. Have you included a copy of the first page, the page containing employee census information (currently line 7f of the 1997 Form 5500), and the information relating to plan assets (currently line 31f of the 1997 Form 5500) of the most recently filed Form 5500 series return? Note: If a Form 5500 is not applicable, insert N/A and furnish the name of the plan, and the census information required of Form 5500 series filers. **(See section 12.04(1).)**
- _____ 19. Have you proposed a time period of correction that is limited to 150 days from the date the compliance statement is issued? **(See section 12.14.)**

The following items relate only to submissions under SVP:

- _____ 20. Have you included a statement identifying your request as an SVP request? **(See section 12.03(11).)**
- _____ 21. Are each of the failures you have identified eligible for correction under SVP? **(See Appendix A.)**
- _____ 22. Have you identified no more than two SVP failures? (If more than two failures were identified, SVP is not available, but you may make a submission under VCR.) **(See section 10.12(3).)**
- _____ 23. Have you proposed to correct the failure(s) identified in your request using the permitted correction method(s) set forth in Appendix A? **(See Appendix A.)**

Employee Plans CPE Technical Topics for 1998

The following item relates only to submissions under Walk-in CAP:

- _____ 24. Have you included a copy of the most recently filed Form 5500? **(See section 12.04(1).)**

- _____ 25. Have you submitted an application for a determination letter? **(See section 11.01(4).)**

_____ **Signature**
_____ **Date**

_____ **Title or Authority**

_____ **Typed or printed**
name of person signing checklist