Internal Revenue Service

memorandum

date: June 9, 2006

to: IRS Reports Clearance Office, Att'n: R. Joseph Durbala W:CAR:MP:FP:S:SP

from: /s/ Michael Rubin for
Martin L. Pippins, Manager, EP Technical Guidance and Quality Assurance
SE:T:EP:RA:G

subject: Additional hours for collection of information - OMB Control No. 1545-1673

This memo is to request an additional 19,950 hours to the existing 56,272 hours granted for the collection of information provisions of OMB Control No. 1545-1673 as a result of the publication of Rev. Proc. 2006-27, 2006-22 I.R.B. 945, on May 30, 2006. The subject OMB Control number was last published as Rev. Proc. 2003-44, 2003-1 C.B. 1051. While it is anticipated that this revenue procedure will be revised again before the current, valid OMB control number expires, it's unlikely any additional hours will be requested. Hence, it is felt that it is important to forward this document to your office now. The additions to the hours previously approved by the Office of Management and Budget are described below. A complete supporting statement also is attached. The items that may have to be revised by your office prior to the resubmission to OMB are highlighted in yellow. In addition, a draft OMB Form 83-I also is attached. The actual revenue procedure is 55 printed pages in length and the applicable issue of the IRB containing that revenue procedure is attached. Except for this paragraph, each increase in hours (both by section and overall) has been underlined.

Section 4.05 describes certain amendments that can be made in the Employee Plans Compliance Resolution System. We estimate that 600 employers will make such amendments annually. The estimated burden per respondent is from 4 hour to 8 hours, with the average burden of 6 hours, for a total estimated burden of 3,600 hours annually. This is an increase in 2,400 hours annually.

Section 6.05 requires employers to notify employees in the instance of the correction of excess amounts or a failure to meet the limits on contributions under section 415. We estimate that 1,300 employers will take such action annually. The estimated burden per respondent is from 1 hour to 5 hours, with the average burden of 3 hours, for a total estimated burden of 3,900 hours annually. This is an increase in 2,600 hours annually.

Sections 11.02-11.04 describe the requirements to submit a request for a voluntary compliance statement. We estimate that 2,550 employers will make such submissions annually. The estimated burden per respondent is from 8 hours to 16 hours, with an average burden of 12 hours, for a total estimated burden of 30,600 hours annually. This is an increase in 9,784 hours annually.

A new section 11.11 was inserted and an Appendix E was added. These two provisions pertain to the issuance of an acknowledgement letter by the Service and require the insertion of data in Appendix E (or a copy of Appendix E) by the plan sponsor or its representative in order for the Service to issue an acknowledgement of receipt. We estimate that 2,550 employers, etc., will

make such requests annually. The estimated burden per respondent is from 15 minutes to 45 minutes with an average burden of 30 minutes for a total estimated burden of 1,275 hours annually.

A new section 11.14 describes how the submission package for requesting a compliance statement should be assembled. We estimate that 2,550 employers, etc., will make submissions annually. The estimated burden per respondent is from 1 hour to 2 hours with an average burden of 1.5 hours for a total estimated burden of 3,825 hours annually.

In addition, what was section 11.11 and section 11.12 have been renumbered as section 11.12 and section 11.13.

Section 13.01 describes the audit requirements for the audit closing agreement program for 403(b) plans. Generally, the audit closing agreement program is available in the instance of an Operational Failure of a 403(b) plan. However, that section provides that the audit closing agreement program for 403(b) plans is not available for Operational Failures that relate to a misuse or diversion the assets of a 403(b) plan. We estimate that 19 employers will enter into closing agreements under the audit closing agreement program for 403(b) plans annually. The estimated burden per respondent is from 2 hours to 12 hours with an average burden of 9 hours for a total estimated burden of 171 hours annually. This is an increase of 66 hours annually.

The total burden for this submission is 19,434 responses (for a net decrease of 6,588 responses as a result of an extension of items that are eligible for self-correction), by 3,745 respondents (for a net decrease of 547 respondents/recordkeepers as a result of an extension of items that are eligible for self-correction) and an increase to 76,222 hours (for an overall increase of 19,950 hours) as a result of increased complexities of cases that are being submitted.

Of course, the number of hours in the revenue procedure is in addition to hours already requested in various forms, regulations, etc.

Attachments

TABLE OF CONTENTS

PART I. INTRODUCTION TO EMPLOYEE PLANS COMPLIANCE RESOLUTION SYSTEM

SECTION 1. PURPOSE AND OVERVIEW

.01 *Purpose*. This revenue procedure updates the comprehensive system of correction programs for sponsors of retirement plans that are intended to satisfy the requirements of § 401(a), 403(a), 403(b), 408(k), or 408(p) of the Internal Revenue Code (the "Code"), but that have not met these requirements for a period of time. This system, the Employee Plans Compliance Resolution System ("EPCRS"), permits plan sponsors to correct these failures and thereby continue to provide their employees with retirement benefits on a tax-favored basis. The components of EPCRS are the Self-Correction Program ("SCP"), the Voluntary Correction Program ("VCP"), and the Audit Closing Agreement Program ("Audit CAP").

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

- Sponsors and other administrators of eligible plans should be encouraged to establish administrative practices and procedures that ensure that these plans are operated properly in accordance with the applicable requirements of the Code.
- Sponsors and other administrators of eligible plans should satisfy the applicable plan document requirements of the Code.
- Sponsors and other administrators should make voluntary and timely correction of any plan failures, whether involving discrimination in favor of highly compensated employees, plan operations, the terms of the plan document, or adoption of a plan by an ineligible employer. 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 tax liability and participants' potential tax liability.
- Fees and sanctions should be graduated in a series of steps so that there is always an incentive to correct promptly.
- Sanctions for plan 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.
- Sponsors should be able to rely on the availability of EPCRS in taking corrective actions to maintain the tax-favored status of their plans.

.03 *Overview*. EPCRS includes the following basic elements:

- *Self-correction (SCP)*. A Plan Sponsor that has established compliance practices and procedures may, at any time without paying any fee or sanction, correct insignificant Operational Failures under a Qualified Plan or a 403(b) Plan, or a SEP or a SIMPLE IRA Plan, provided the SEP or SIMPLE IRA Plan is established and maintained on a document approved by the Service.

In addition, in the case of a Qualified Plan that is the subject of a favorable determination letter from the Service or in the case of a 403(b) Plan, the Plan Sponsor generally may correct even significant Operational Failures without payment of any fee or sanction.

- *Voluntary correction with Service approval (VCP).* A Plan Sponsor, at any time before audit, may pay a limited fee and receive the Service's approval for correction of a Qualified Plan, 403(b) Plan, SEP or SIMPLE IRA Plan. Under VCP, there are special procedures for anonymous submissions and group submissions.
- *Correction on audit (Audit CAP).* If a failure (other than a failure corrected through SCP or VCP) is identified on audit, the Plan Sponsor may correct the failure and pay a sanction. 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.

SECTION 2. EFFECT OF THIS REVENUE PROCEDURE ON PROGRAMS

.01 *Effect on programs.* This revenue procedure modifies and supersedes Rev. Proc. 2003–44, 2003–1 C.B. 1051, which was the prior consolidated statement of the correction programs under EPCRS. The modifications to Rev. Proc. 2003–44 that are reflected in this revenue procedure include:

- providing that if the Plan Sponsor corrects the failures in accordance with the requirements of this revenue procedure, the plan will be treated as satisfying § 401(a), § 403(b), § 408(k), or § 408(p), as applicable, for purposes of applying § 3121(a)(5) (FICA taxes) and § 3306(b)(5) (FUTA taxes) (section 3.01)
- revising the requirements for submitting a determination letter application when correcting certain Qualification Failures by plan amendment (sections 4.06, 10.08, and 11.03(3))
- clarifying that an egregious failure includes providing more favorable benefits to an owner based on a purported collective bargaining agreement where there has in fact been no good faith bargaining (section 4.11)
- providing rules relating to the availability of programs under EPCRS in cases where the plan or plan sponsor is a party to an abusive tax avoidance transaction (sections 4.13 and 11.02(11))
- updating the definition of Favorable Letter (section 5.01(4))
- revising provisions affecting 403(b) plans by revising the definition of Excess Amounts (section 5.02(3))
- updating the definition of Under Examination (section 5.03)
- expanding VC and Audit CAP to terminating Orphan Plans and, with respect to those plans, providing for a possible exception to the requirement for full correction and a waiver of the VCP fee in appropriate circumstances (sections 5.06, 6.02(5)(f), and 12.02(3))
- adding a correction method for certain plan loan failures (sections 6.02(6) and 6.07), including adding a correction method for a plan that permits plan loans operationally but does not have the appropriate plan loan language (Appendix B 2.07(2))
- revising the correction method for a failure to include an eligible employee in a cash or deferred arrangement under § 401(k) (section 6.02(7), Appendix A .05, and Appendix B 2.02)
- adding an alternative correction method for a failure to obtain spousal consent (section 6.04(2)(c))
- revising provisions affecting 403(b) plans by eliminating the term Total Sanction Amount and replacing it with the term "Maximum Payment Amount" and eliminating correction by retention of Excess Amounts (sections 5.02(4) and 6.06(2))
- providing that as part of both VCP and Audit CAP, if the failure involves the failure to satisfy the minimum required distribution requirements of § 401(a)(9), the Service will waive the excise tax requirements of § 4974 in appropriate cases (section 6.09(2))
- expanding excise taxes that the Service may not pursue (section 6.09(3) and (4))
- clarifying the scope of a compliance statement issued with respect to certain nonamender failures
- clarifying submission procedures for Anonymous Submissions (section 10.10), and Group Submissions (section 10.11)
- revising the acknowledgement procedures of receipt of a submission (section 11.11 and new Appendix E — Acknowledgement Letter)
- providing a submission assembly procedure (section 11.14)
- reducing the compliance fee for a plan where the sole failure is the failure to satisfy the minimum distribution rules for 50 or fewer employees (section 12.02(2))
- reducing the compliance fee for a plan where the sole failure is the failure to timely adopt certain plan amendments (section 12.03)
- reducing the general compliance fee for SEPs and SIMPLE IRAs (section 12.05)
- adding a fee schedule for plans in the determination letter process found to be nonamenders of tax law changes (section 14.04)
- providing that if a nonamender failure is discovered during an Employee Plans Examination, then it is expected that the applicable sanction will be greater than the applicable fee under section 14.04 (section 14.02)
- providing a streamlined submission procedure for certain nonamender failures (Appendix F)

.02 *Future enhancements.* (1) It is expected that the EPCRS revenue procedure will continue to be updated from time to time, including, as noted above, further improvements to EPCRS based on comments previously received. In addition, the Service and Treasury continue to invite further comments on how to improve EPCRS. Comments should be sent to:

Internal Revenue Service
Attention: SE:T:EP:RA:VC
1111 Constitution Avenue, NW
Washington, D.C. 20224

(2) Comments are requested for certain specific issues under EPCRS. First, comments are requested regarding methods to correct a failure to provide an eligible employee the opportunity to make a catch-up contribution that is permitted under the terms of the plan and § 414(v). (See 6.02(7) and Appendix B 2.02.) Sec-

ond, given that § 402A permits a § 401(a) or 403(b) plan to offer employees the opportunity to designate elective deferrals as Roth contributions for taxable years beginning after December 31, 2005, comments are requested regarding methods to correct a failure to provide an eligible employee with the opportunity to make elective deferrals for a plan that permits an eligible employee to designate elective deferrals as Roth contributions. Third, the correction mechanism in current §1.415–6(b)(6) of the Income Tax Regulations is not included in the regulations that were proposed under § 415 (70 FR 31214) and published on May 31, 2005. The preamble to the proposed regulations provides that the correction mechanism (for excess annual additions) will be included in EPCRS in the future. It is expected that correction mechanism will in any event continue to be available under EPCRS, including under SCP where correction of a significant operational failure is permitted. Accordingly, comments are requested regarding the applicable correction methods for this failure. Comments are also requested on whether the correction mechanisms provided for in current §1.415–6(b)(6), including the maintenance of suspense accounts, should be retained as options under EPCRS, or whether correction of excess annual additions should be treated as excess amounts under this revenue procedure (*i.e.*, distributed or forfeited, as appropriate). Fourth, comments are requested regarding whether additional correction methods are needed in order for plans to take advantage of the fiduciary safe harbor recently issued by the Department of Labor for Orphan Plans (71 FR 20820) where the plan is subject to the requirements of §§ 401(a)(11) and 417 in light of the ability to satisfy those requirements by purchase of a commercial annuity contract.

PART II. PROGRAM EFFECT AND ELIGIBILITY

SECTION 3. EFFECT OF EPCRS; RELIANCE

.01 *Effect of EPCRS on retirement plans.* For a Qualified Plan, a 403(b) Plan, a SEP, or a SIMPLE IRA Plan, if the eligibility requirements of section 4 are satisfied and the Plan Sponsor corrects a failure in accordance with the applicable requirements of SCP in section 7, VCP in sections 10 and 11, or Audit CAP in section 13, the Service will not treat the retirement plan as failing to meet § 401(a), § 403(b), § 408(k), or § 408(p), as applicable. Thus, for example, if the Plan Sponsor corrects the failures in accordance with the requirements of this revenue procedure, the plan will be treated as satisfying § 401(a), § 403(b), § 408(k), or § 408(p), as applicable, for purposes of applying § 3121(a)(5) (FICA taxes) and § 3306(b)(5) (FUTA taxes).

.02 *Compliance statement.* If a Plan Sponsor or Eligible Organization receives a compliance statement under VCP, the compliance statement is binding upon the Service and the Plan Sponsor or Eligible Organization as provided in section 10.09.

.03 *Other taxes and penalties.* See section 6.09 for rules relating to other taxes and penalties.

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

SECTION 4. PROGRAM ELIGIBILITY

.01 *EPCRS Programs.* (1) *SCP.* SCP is available only for Operational Failures. Qualified Plans and 403(b) Plans are eligible for SCP with respect to significant and insignificant Operational Failures. SEPs and SIMPLE IRA Plans are eligible for SCP with respect to insignificant Operational Failures only.

(2) *VCP.* Qualified Plans, 403(b) Plans, SEPs and SIMPLE IRA Plans are eligible for VCP. VCP provides general procedures for correction of all Qualification Failures: Operational, Plan Document, Demographic, and Employer Eligibility.

(3) *Audit CAP.* Audit CAP is available for Qualified Plans, 403(b) Plans, SEPs and SIMPLE IRA Plans for correction of all failures found on examination that have not been corrected in accordance with SCP or VCP.

(4) *Eligibility for other arrangements.* The Service may extend EPCRS to other arrangements.

.02 *Effect of examination.* If the plan or Plan Sponsor is Under Examination, VCP is not available and SCP is only available as follows: while the plan or Plan Sponsor is Under Examination, insignificant Operational Failures can be corrected under SCP; and, if correction has been completed or substantially completed before the plan or Plan Sponsor is Under Examination, correction of significant Operational Failures can be completed under SCP.

.03 *Favorable Letter requirement.* The provisions of SCP relating to significant Operational Failures (see section 9) are available for a Qualified Plan only if the plan is the subject of a Favorable Letter. The provisions of SCP relating to insignificant Operational Failures (see section 8) are available for a SEP but only if the plan document consists of either (i) a valid Model Form 5305–SEP or 5305A–SEP adopted by an employer in accordance with the instructions on the applicable form (see Rev. Proc. 2002–10, 2002–1 C.B. 401), or (ii) a prototype SEP that has a current favorable opinion letter which has been amended in accordance with the procedures set forth in Rev. Proc. 2002–10. The provisions of SCP relating to insignificant Operational Failures (see section 8) are available for a SIMPLE IRA Plan but only if the plan document consists of either (i) a valid Model Form 5305–SIMPLE or 5304–SIMPLE adopted by an employer in accordance with the instructions on the applicable form (see Rev. Proc. 2002–10), or (ii) a current favorable opinion letter for a Plan Sponsor that has adopted a prototype SIMPLE IRA Plan which has been amended in accordance with the procedures set forth in Rev. Proc. 2002–10.

.04 *Established practices and procedures.* In order to be eligible for SCP, 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 applicable Code requirements. For example, the plan administrator of a Qualified Plan that may be top-heavy under § 416 may include in its plan operating manual a specific annual step to determine whether the plan is top-heavy and, if so, to ensure that the minimum contribution requirements of the top-heavy rules are satisfied. A plan document alone does not constitute evidence of established procedures. In order for a Plan Sponsor or administrator to use SCP, these established procedures must have been in place and routinely followed, and an Operational Failure must have occurred through an oversight or mistake in applying them.

In addition, SCP may also be used in situations where the operational failure occurred because the procedures that were in place, while reasonable, were not sufficient to prevent the occurrence of the failure. In the case of a failure that relates to Transferred Assets or to a plan assumed in connection with a corporate merger, acquisition, or other similar employer transaction between the Plan Sponsor and sponsor of the transferor plan or the prior plan sponsor of an assumed plan, the plan is considered to have established practices and procedures for the Transferred Assets if such practices and procedures are in effect for the Transferred Assets by the end of the first plan year that begins after the corporate merger, acquisition, or other similar transaction.

.05 *Correction by plan amendment.* (1) *Availability of correction by plan amendment in VCP and Audit CAP.* A Plan Sponsor may use VCP and Audit CAP for a Qualified Plan to correct Plan Document, Demographic, and Operational Failures by a plan amendment, including correcting an Operational Failure by 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). In addition, a Plan Sponsor may correct an Operational Failure by plan amendment to amend the plan to the extent necessary to reflect the corrective action. For example, if the plan failed to satisfy the average deferral percentage ("ADP") test required under § 401(k)(3) and the Plan Sponsor must make qualified nonelective contributions not already provided for under the plan, the plan may be amended to provide for qualified nonelective contributions. Except as provided in section 4.06, 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.

(2) *Availability of correction by plan amendment in SCP.* A Plan Sponsor may use SCP for a Qualified Plan to correct an Operational Failure by a plan amendment in order to conform the terms of the plan to the plan's prior operations only to correct Operational Failures listed in section 2.07 of Appendix B. These failures must be corrected in accordance with the correction methods set forth in section 2.07 of Appendix B. SCP is not otherwise available for a Plan Sponsor to correct an Operational Failure by a plan amendment. Any plan amendment must comply with the requirements of § 401(a), including the requirements of §§ 401(a)(4), 410(b), and 411(d)(6).

.06 *Submission for a determination letter.* (1) Under VCP and Audit CAP, a determination letter will be issued to correct a nonamender failure. In addition, a determination letter may be issued (a) to correct a failure in a plan that is either submitted under VCP or that is being examined during the last 12 months of the plan's remedial amendment cycle, as defined in section 13 of Rev. Proc. 2005–66, 2005–37 I.R.B. 509 (an "on-cycle" filing), or (b) to correct a failure in either a VCP filing submitted for a terminating plan or a terminating plan under examination. For this purpose, the term "nonamender failure" means a failure to amend the plan to reflect a change in a qualification requirement within the plan's applicable remedial amendment period, as set forth in Rev. Proc. 2005–66. A change in a qualification requirement includes a change arising from a statutory change, or a change in the requirements provided in regulations or other guidance published in the Internal Revenue Bulletin. A determination letter issued under VCP with respect to a nonamender failure will include only a determination on all applicable laws with respect to which the remedial amendment period has expired. Notwithstanding the above, a determination letter will not be issued with respect to a failure to amend a plan timely for (a) good faith plan amendments for the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107–16 (EGTRRA), within the period described in Notice 2001–42, 2001–2 C.B. 70, including those changes listed in Notice 2005–5, 2005–3 I.R.B. 337, (b) plan amendments for the final and temporary regulations under §401(a)(9) as they appeared in the April 1, 2003, edition of 26 CFR Part 1 (the § 401(a)(9) final and temporary regulations) within the period described in Rev. Proc. 2002–29, 2002–1 C.B. 1176, as modified by Rev. Proc. 2003–10, 2003–1 C.B. 259, and (c) interim amendments as provided in section 5 of Rev. Proc. 2005–66. The preceding sentence is not applicable if (i) the failure is submitted in a VCP filing made during an on-cycle year, (ii) the plan is being examined during an on-cycle year, (iii) the failure is submitted in a VCP filing for a terminating plan, or (iv) the plan is a terminating plan Under Examination. Except as provided in section 10.08, in cases where a determination letter is not issued with respect to failures corrected through plan amendment, the issuance of a compliance statement or closing agreement will constitute a determination as to the effect of any plan amendment on the qualification of the plan. Notwithstanding any other provision of this section 4.06, the Service reserves the right to require the submission of a determination letter application with respect to any amendment proposed or adopted to correct any Qualification Failure under VCP or Audit CAP.

(2) In the case of any correction of an Operational Failure through plan amendment under SCP, as permitted under section 4.05(2), a Plan Sponsor must submit a determination letter application. The determination letter application must be submitted before the end of the plan's applicable remedial amendment period described in Rev. Proc. 2005–66. As part of the determination letter submission, the amendment under SCP must be identified as such in the cover letter.

.07 *Availability of correction of Employer Eligibility Failure.* SCP is not available for a Plan Sponsor to correct an Employer Eligibility Failure.

.08 *Availability of correction of a terminated plan.* Correction of Qualification Failures in a terminated plan may be made under VCP and Audit CAP, whether or not the plan trust is still in existence.

.09 *Availability of correction of an Orphan Plan.* An Orphan Plan that is terminating may be corrected under VCP and Audit CAP, provided that the party acting on behalf of the plan is an Eligible Party, as defined in section 5.06(2).

.10 *Availability of correction of § 457 plans.* Submissions relating to § 457(b) eligible governmental plans will be accepted by the Service on a provisional basis outside of EPCRS through standards that are similar to EPCRS.

.11 *Egregious failures.* SCP is not available to correct Operational Failures that are egregious. For example, any of the following would be considered egregious: (a) a plan has consistently and improperly covered only highly compensated em-

ployees; (b) a plan provides more favorable benefits for an owner of the employer based on a purported collective bargaining agreement where there has in fact been no good faith bargaining between *bona fide* employee representatives and the employer (see Notice 2003–24, 2003–1 C.B. 853, with respect to welfare benefit funds); or (c) a contribution to a defined contribution plan for a highly compensated employee is several times greater than the dollar limit set forth in § 415. VCP is available to correct egregious failures; however, these failures are subject to the fees described in section 12.06. Audit CAP also is available to correct egregious failures.

.12 *Diversion or misuse of plan assets.* SCP, VCP, and Audit CAP are not available to correct failures relating to the diversion or misuse of plan assets.

.13 *Abusive tax avoidance transactions.* (1) *Effect on Programs.* (a) *SCP.* With respect to SCP, in the event that the plan or the Plan Sponsor has been a party to an abusive tax avoidance transaction (as defined in section 4.13(2)), SCP is not available to correct any Operational Failure that is directly or indirectly related to the abusive tax avoidance transaction.

(b) *VCP.* With respect to VCP, if the Service determines that a plan or Plan Sponsor was, or may have been, a party to an abusive tax avoidance transaction (as defined in section 4.13(2)), then the matter will be referred to the Internal Revenue Service's Employee Plans' Tax Shelter Coordinator. Upon receiving a response from the Tax Shelter Coordinator, the Service may determine that the plan or the Plan Sponsor has been a party to an abusive tax avoidance transaction, and that the failures addressed in the VCP submission are related to that transaction. In those situations, the Service will conclude the review of the submission without issuing a compliance statement and will refer the case for examination. However, if the Tax Shelter Coordinator determines that the plan failures are unrelated to the abusive tax avoidance transaction or that no abusive tax avoidance transaction occurred, then the Service will continue to address the failures identified in the VCP submission, and may issue a compliance statement with respect to those failures. In no event may a compliance statement be relied on for the purpose of concluding that the plan or Plan Sponsor was not a party to an abusive tax avoidance transaction. In addition, even if it is concluded that the failures can be addressed pursuant to a VCP submission, the Service reserves the right to make a referral of the abusive tax avoidance transaction matter for examination.

(c) *Audit CAP and SCP (for plans Under Examination).* For plans Under Examination, if the Service determines that the plan or Plan Sponsor was, or may have been, a party to an abusive tax avoidance transaction, the matter may be referred to the Internal Revenue Service's Employee Plans' Tax Shelter Coordinator. With respect to plans Under Examination, an abusive tax avoidance transaction includes a transaction described in section 4.13(2) and any other transaction that the Service determines was designed to facilitate the impermissible avoidance of tax. Upon receiving a response from the Tax Shelter Coordinator, (i) if the Service determines that a failure is related to the abusive tax avoidance transaction, the Service reserves the right to conclude that neither Audit CAP nor SCP is available for that failure and (ii) if the Service determines that satisfactory corrective actions have not been taken with regard to the transaction, the Service reserves the right to conclude that neither Audit CAP nor SCP is available to the plan.

(2) *Definition.* For purposes of section 4.13(1) (except to the extent otherwise provided in section 4.13(1)(c)), an abusive tax avoidance transaction means any listed transaction under § 1.6011–4(b)(2) and any other transaction identified as an abusive transaction in the IRS website entitled "EP Abusive Tax Transactions."

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

SECTION 5. DEFINITIONS

The following definitions apply for purposes of this revenue procedure:

.01 *Definitions for Qualified Plans.* The definitions in this section 5.01 apply to Qualified Plans.

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

(2) *Qualification Failure.* The term "Qualification Failure" means any failure that adversely affects the qualification of a plan. There are four types of Qualification Failures: (a) Plan Document Failures; (b) Operational Failures; (c) Demographic Failures; and (d) Employer Eligibility Failures.

(a) *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. In addition, if a plan has not been timely or properly amended during an applicable remedial amendment period for adopting good faith or interim amendments with respect to disqualifying provisions, as described in §1.401(b)–1(b)(1), the plan is considered to have 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 not an Operational Failure, Demographic Failure, or Employer Eligibility Failure.

(b) *Operational Failure.* The term "Operational Failure" means a Qualification Failure (other than an Employer Eligibility 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 to reflect the plan's operations (*e.g.*, pursuant to § 401(b)). In the situation where a Plan Sponsor timely adopted a good faith or interim amendment which is not a disqualifying provision as described in § 1.401(b)–1(b)(1), and the plan was not operated in accordance with the terms of such amendment, the plan is considered to have an Operational Failure.

(c) *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 or an Employer Eligibility Failure. The correction of a Demographic

Failure generally requires a corrective amendment to the plan adding more benefits or increasing existing benefits (cf. § 1.401(a)(4)–11(g)).

(d) *Employer Eligibility Failure.* The term "Employer Eligibility Failure" means the adoption of a plan intended to include a qualified cash or deferred arrangement and satisfy the requirements of § 401(a) or §403(a) by an employer that fails to meet the employer eligibility requirements to establish a § 401(k) plan. An Employer Eligibility Failure is not a Plan Document, Operational, or Demographic Failure.

(3) *Excess Amount.* The term "Excess Amount" means (a) an Overpayment, (b) an elective deferral or employee after-tax contribution returned to satisfy § 415, (c) an elective deferral in excess of the limitation of § 402(g) that is distributed, (d) an excess contribution or excess aggregate contribution that is distributed to satisfy § 401(k) or § 401(m), (e) an elective deferral that is distributed to satisfy the limitation of § 401(a)(17), or (f) any similar amount that is required to be distributed in order to maintain plan qualification.

(4) *Favorable Letter.* The term "Favorable Letter" means, in the case of a Qualified Plan, a current favorable determination letter for an individually designed plan (including a volume submitter plan that is not identical to an approved volume submitter plan), a current favorable opinion letter for a Plan Sponsor that has adopted a master or prototype plan, (standardized or nonstandardized), or a current favorable advisory letter and certification that the Plan Sponsor has adopted a plan that is identical to an approved volume submitter plan. A plan has a current favorable determination letter, opinion letter, or advisory letter if (a), (b), (c), or (d) below is satisfied:

(a) The plan has a favorable determination letter, opinion letter, or advisory letter/certification that considers GUST (GUST is an acronym for the Uruguay Round Agreements Act (GATT), the Uniformed Services Employment and Reemployment Rights Act of 1994 (USERRA), the Small Business Job Protection Act of 1996 (SBJPA), the Taxpayer Relief Act of 1997 (TRA '97), the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA '98), and the Community Renewal Tax Relief Act of 2000 (CRA).)

(b) The plan is initially adopted or effective after December 31, 2001, and the Plan Sponsor timely submits an application for a determination letter or adopts an approved master or prototype plan or volume submitter plan within the plan's remedial amendment period under § 401(b).

(c) The plan is terminated prior to the expiration of the applicable GUST remedial amendment period under § 401(b) and the plan was amended to reflect the provisions of GUST (including § 415, as provided in Rev. Rul. 2002–27, 2002–1 C.B. 925, in the case of defined contribution plans), the provisions of the 401(a)(9) final and temporary regulations, and in the case of defined benefit plans, the 1994 Group Annuity Reserving Table (94 GAR) (see Rev. Rul. 2001–62, 2001–2 C.B. 632).

(d) The plan is terminated prior to the expiration of the applicable Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) remedial amendment period under § 401(b) and the plan was amended to reflect the provisions of EGTRRA and any other legislation that was in effect when the plan was terminated.

(5) *Maximum Payment Amount.* The term "Maximum Payment Amount" means a monetary 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:

(a) tax on the trust (Form 1041) (and any interest or penalties applicable to the trust return),

(b) 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),

(c) additional income tax resulting from income inclusion for participants in the plan (Form 1040), including the tax on plan distributions that have been rolled over to other qualified trusts (as defined in § 402(c)(8)(A)) or eligible retirement plans (as defined in § 402(c)(8)(B)) (and any interest or penalties applicable to the participants' returns), and

(d) any other tax that results from a Qualification Failure that would apply but for the correction under this revenue procedure.

(6) *Overpayment.* The term "Overpayment" means a distribution to an employee or beneficiary that exceeds the employee's or beneficiary's benefit under the terms of the plan, including a distribution that results from a failure to comply with plan terms that implement § 401(a)(17), § 401(m) (but only with respect to the forfeiture of nonvested matching contributions that are excess aggregate contributions), § 411(a)(3)(G), or § 415. An Overpayment does not include a distribution of any Excess Amount described in section 5.01(3)(b) through (f).

(7) *Plan Sponsor.* The term "Plan Sponsor" means the employer that establishes or maintains a qualified retirement plan for its employees.

(8) *Transferred Assets.* The term "Transferred Assets" means plan assets that were received, in connection with a corporate merger, acquisition or other similar employer transaction, by the plan in a transfer (including a merger or consolidation of plan assets) under § 414(l) from a plan sponsored by an employer that was not a member of the same controlled group as the Plan Sponsor immediately prior to the corporate merger, acquisition, or other similar employer transaction. If a transfer of plan assets related to the same employer transaction is accomplished through several transfers, then the date of the transfer is the date of the first transfer.

.02 *Definitions for 403(b) Plans.* The definitions in this section 5.02 apply to 403(b) Plans.

(1) *403(b) Plan.* The term "403(b) Plan" means a plan or program intended to satisfy the requirements of § 403(b).

(2) *403(b) Failure.* A 403(b) Failure is any Operational, Demographic, or Employer Eligibility Failure as defined below.

(a) *Operational Failure.* The term "Operational Failure" means any of the following:

(i) A failure to satisfy the requirements of § 403(b)(12)(A)(ii) (relating to the availability of salary reduction contributions);

(ii) A failure to satisfy the requirements of § 401(m) (as applied to 403(b) Plans pursuant to § 403(b)(12)(A)(i));

(iii) A failure to satisfy the requirements of § 401(a)(17) (as applied to 403(b) Plans pursuant to § 403(b)(12)(A)(i));

(iv) A failure to satisfy the distribution restrictions of § 403(b)(7) or § 403(b)(11);

(v) A failure to satisfy the incidental death benefit rules of § 403(b)(10);

(vi) A failure to pay minimum required distributions under § 403(b)(10);

(vii) A failure to give employees the right to elect a direct rollover under § 403(b)(10), including the failure to give meaningful notice of such right;

(viii) A failure of the annuity contract or custodial agreement to provide participants with a right to elect a direct rollover under §§ 403(b)(10) and 401(a)(31);

(ix) A failure to satisfy the limit on elective deferrals under § 403(b)(1)(E);

(x) A failure of the annuity contract or custodial agreement to provide the limit on elective deferrals under §§ 403(b)(1)(E) and 401(a)(30);

(xi) A failure involving contributions or allocations of Excess Amounts; or

(xii) Any other failure to satisfy applicable requirements under § 403(b) that (A) results in the loss of § 403(b) status for the plan or the loss of § 403(b) status for one or more custodial account(s) or annuity contract(s) under the plan and (B) is not a Demographic Failure, an Employer Eligibility Failure, or a failure related to contributions on behalf of individuals who are not employees of the employer.

(b) *Demographic Failure.* The term "Demographic Failure" means a failure to satisfy the requirements of § 401(a)(4), § 401(a)(26), or § 410(b) (as applied to 403(b) Plans pursuant to § 403(b)(12)(A)(i)).

(c) *Employer Eligibility Failure.* The term "Employer Eligibility Failure" means any of the following:

(i) The adoption of a plan intended to satisfy the requirements of § 403(b) by a Plan Sponsor that is not a tax-exempt organization described in § 501(c)(3) or a public educational organization described in § 170(b)(1)(A)(ii);

(ii) A failure to satisfy the nontransferability requirement of § 401(g);

(iii) A failure to initially establish or maintain a custodial account as required by § 403(b)(7); or

(iv) A failure to purchase (initially or subsequently) either an annuity contract from an insurance company (unless grandfathered under Rev. Rul. 82–102, 1982–1 C.B. 62) or a custodial account from a regulated investment company utilizing a bank or an approved non-bank trustee/custodian.

(3) *Excess Amount.* The term "Excess Amount" means any amount returned to ensure that the plan satisfies the requirements of § 401(a)(30), 415, or 403(b)(2) (for plan years prior to January 1, 2002). In addition, the term "Excess Amount" includes (for all plan years) any distributions required to ensure that the plan complies with the applicable requirements of § 403(b).

(4) *Maximum Payment Amount.* The term "Maximum Payment Amount" means a monetary amount that is approximately equal to the tax the Service could collect as a result of the 403(b) Failure and is the sum for the open taxable years of the:

(a) additional income tax resulting from income inclusion for employees or other participants (Form 1040), including the tax on distributions that have been rolled over to other qualified trusts (as defined in § 402(c)(8)(A)) or eligible retirement plans (as defined in § 402(c)(8)(B)) (and any interest or penalties applicable to the participants' returns), and

(b) any other tax that results from a 403(b) Failure that would apply but for the correction under this revenue procedure.

(5) *Plan Sponsor.* The term "Plan Sponsor" means the employer that offers a 403(b) Plan to its employees.

.03 *Under Examination.* (1) The term "Under Examination" means: (a) a plan that is under an Employee Plans examination (that is, an examination of a Form 5500 series or other Employee Plans examination); (b) a Plan Sponsor that is under an Exempt Organizations examination (that is, an examination of a Form 990 series or other Exempt Organizations examination); or (c) a plan that is under investigation by the Criminal Investigation Division of the Internal Revenue Service.

(2) 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 Employee Plans 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), 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, § 401(a)(30), § 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 test set forth in § 410(b)(2).

(3) An Employee Plans examination also includes a case in which a Plan Sponsor has submitted any Form 5300 series form 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 a 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. In addition, if, during the review process, the agent requests additional information that indicates the existence of a Qualification Failure(s) not previously identified by the Plan Sponsor, the plan is considered to be under an Employee Plans examination. If, in such a case, the determination letter request under review is subsequently withdrawn, the plan is nevertheless considered to be under an Employee Plans examination for purposes of eligibility under SCP and VCP with respect to those issues raised by the agent reviewing the determination letter application. The fact that a Plan Sponsor voluntarily submits a determination letter application does not constitute a voluntary

identification of Qualification Failures to the Service. In order to be eligible to perfect a determination letter application into a VCP submission, the Plan Sponsor (or the authorized representative) must identify each Qualification Failure, in writing, to the reviewing agent before the agent recognizes the existence of the Qualification Failure(s) or addresses the Qualification Failure(s) in communications with the Plan Sponsor (or the authorized representative).

(4) A Plan Sponsor that is under an Exempt Organizations examination includes any Plan Sponsor that has received (or whose representative has received) verbal or written notification from Exempt Organizations 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.

.04 *SEP.* The term "SEP" means a plan intended to satisfy the requirements of § 408(k). For purposes of this revenue procedure, the term SEP also includes a salary reduction SEP ("SARSEP") described in § 408(k)(6), when applicable.

.05 *SIMPLE IRA Plan.* The term "SIMPLE IRA Plan" means a plan intended to satisfy the requirements of § 408(p).

.06 *Definitions for Orphan Plans.* (1) *Orphan Plan.* With respect to VCP and Audit CAP, the term "Orphan Plan" means any Qualified Plan with respect to which an "Eligible Party" (defined in section 5.06(2)) has determined that the Plan Sponsor (a) no longer exists, (b) cannot be located, (c) is unable to maintain the plan, or (d) has abandoned the plan pursuant to regulations issued by the Department of Labor. However, the term "Orphan Plan" does not include any plan terminated pursuant to Department of Labor regulations governing the termination of abandoned individual account plans.

(2) *Eligible Party.* For purposes of section 5.06(1), the term "Eligible Party" means:

(a) A court appointed representative with authority to terminate the plan and dispose of the plan's assets;

(b) In the case of an Orphan Plan under investigation by the Department of Labor, a person or entity who the Department of Labor determined has accepted responsibility for terminating the plan and distributing the plan's assets; or

(c) In the case of a Qualified Plan to which Title I of the Employee Retirement Income Security Act of 1974 ("ERISA") has never applied, a surviving spouse who is the sole beneficiary of a plan that provided benefits to a participant who was (i) the sole owner of the business that sponsored the plan and (ii) the only participant in the plan.

SECTION 6. CORRECTION PRINCIPLES AND RULES OF GENERAL APPLICABILITY

.01 *Correction principles; rules of general applicability.* The general correction principles in section 6.02 and rules of general applicability in sections 6.03 through 6.11 apply for purposes of this revenue procedure.

.02 *Correction principles.* Generally, a 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). Even if correction is made for a closed taxable year, the tax liability associated with that year will not be redetermined because of the correction. 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 failure not occurred, including restoration of current and former participants and beneficiaries to the benefits and rights they would have had if the failure had not occurred.

(2) *Reasonable and appropriate correction.* The correction should be reasonable and appropriate for the failure. Depending on the nature of the failure, there may be more than one reasonable and appropriate correction for the failure. For Qualified Plans, any correction method permitted under Appendix A or Appendix B is deemed to be a reasonable and appropriate method of correcting the related Qualification Failure. Any correction method permitted under Appendix A or Appendix B applicable to a 403(b) Plan, a SEP, or a SIMPLE IRA Plan is deemed to be a reasonable and appropriate method of correcting the related 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, regulations thereunder, or other guidance of general applicability. For example, for Qualified Plans and 403(b) plans, the correction method set forth in § 1.402(g)–1(e)(2) would be the typical means of correcting a failure under § 402(g).

(b) The correction method for failures relating to nondiscrimination should provide benefits for nonhighly compensated employees. For example, for Qualified Plans, 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) made under a Qualified Plan 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) or § 403(b) (for example, § 401(a)(4), § 411(d)(6), or § 403(b)(12), as applicable), § 408(k) for SEPs, or § 408(p) for SIMPLE IRA Plans, or a parallel requirement in Part 2 of Subtitle B of Title I of ERISA (for plans that are subject to Subtitle B of Part 2 of Title I of ERISA).

If an additional failure is created as a result of the use of a correction method in this revenue procedure, then that failure also must be corrected in conjunction with the use of that correction method and in accordance with the requirements of this revenue procedure.

(3) *Consistency requirement.* Generally, where more than one correction method is available to correct a type of Operational Failure for a plan year (or where there are alternative ways to apply a correction method), the correction method (or one of the alternative ways to apply the correction method) should be applied consistently in correcting all Operational Failures of that type for that plan year. Similarly, earnings adjustment methods generally should be applied consistently with respect to corrective contributions or allocations for a particular type of Operational Failure for a plan year. In the case of a Group Submission, the consistency requirement applies on a plan by plan basis.

(4) *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 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 (including losses) and forfeitures that would have been allocated to the participant's account if the failure had not occurred. However, the corrective allocation need not be adjusted for losses. See section 3 of Appendix B for additional information on calculation of earnings for corrective allocations.

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

(5) *Special exceptions to full correction.* In general, a 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 either, (i) it is possible to make a precise calculation but 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 or (ii) it is not possible to make a precise calculation (for example, where it is impossible to provide plan data), reasonable estimates may be used in calculating appropriate correction. If it is not feasible to make a reasonable estimate of what the actual investment results would have been, a reasonable interest rate may be used.

(b) *Delivery of small benefits.* If the total corrective distribution due a participant or beneficiary is $50 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. This section 6.02(5)(b) does not apply to corrective contributions.

(c) *Recovery of small Overpayments.* Generally, under VCP or Audit CAP, if the total amount of an Overpayment made to a participant or beneficiary is $100 or less, the Plan Sponsor is not required to seek the return of the Overpayment from the participant or beneficiary. The Plan Sponsor is not required to notify the participant or beneficiary that the Overpayment is not eligible for favorable tax treatment accorded to distributions from Qualified Plans (and, specifically, is not eligible for tax-free rollover).

(d) *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 Employer 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 are provided to the individual at that time. The Internal Revenue Service Letter Forwarding Program may not be used to locate participants in order to collect amounts owed to the plan.

(e) *Small Excess Amounts.* Generally, under VCP or Audit CAP, if the total amount of an Excess Amount with respect to the benefit of a participant or beneficiary is $100 or less, the Plan Sponsor is not required to distribute or forfeit such Excess Amount. However, if the Excess Amount exceeds a statutory limit, the participant or beneficiary must be notified that the Excess Amount, including earnings, is not eligible for favorable tax treatment accorded to distributions from Qualified Plans (and, specifically, is not eligible for tax-free rollover). See section 6.06(1) for such notice requirements.

(f) *Orphan Plans.* The Service retains the discretion to determine under VCP and Audit CAP whether full correction will be required in a terminating Orphan Plan.

(6) *Correction principle for loan failures.* In the case of a loan failure corrected in accordance with section 6.07(2)(b) or (c) and section 6.07(3), the participant is generally responsible for paying the corrective payment. However, with respect to the failure listed in section 6.07(3), the employer should pay a portion of the correction payment on behalf of the participant equal to the interest that accumulates as a result of such failure — generally de-

termined at a rate equal to the greater of the plan loan rate or the rate of return under the plan.

(7) *Correction for exclusion of employees for elective contributions or after-tax employee contributions.* If a Qualified Plan has an Operational Failure that consists of excluding an employee that should have been eligible to make an elective contribution under a cash or deferred arrangement or an after-tax employee contribution, the employer should contribute to the plan on behalf of the excluded employee an amount that makes up for the value of the lost opportunity to the employee to have a portion of his or her compensation contributed to the plan accumulated with earnings tax free in the future. This correction principle applies solely to this limited circumstance. It does not, for example, extend to the correction of a failure to satisfy a nondiscrimination test, *e.g.*, the ADP test pursuant to § 401(k)(3) and the ACP test pursuant to § 401(m)(2). Specific methods and examples to correct this failure are provided in Appendix A .05 and Appendix B 2.02. Similarly, the methods and examples provided for correcting this failure do not extend to other failures. Thus, the correction methods and the examples in Appendix A .05 and Appendix B 2.02 cannot, for example, be used to correct ADP/ACP failures. Finally, the methods and examples do not address situations where an employee was excluded from a plan that provided for the opportunity to make designated Roth contributions.

(8) *Reporting.* Any corrective distributions from the plan should be properly reported.

.03 *Correction of an Employer Eligibility Failure.* (1) The permitted correction of an Employer Eligibility Failure is the cessation of all contributions (including salary reduction and after-tax contributions) beginning no later than the date the application under VCP is filed. Pursuant to VCP correction, the assets in such a plan are to remain in the trust, annuity contract, or custodial account and are to be distributed no earlier than the occurrence of one of the applicable distribution events, *e.g.*, for 403(b) Plans, the events described in § 403(b)(7) (to the extent the assets are held in custodial accounts) or § 403(b)(11) (for those assets invested in annuity contracts that would be subject to § 403(b)(11) restrictions if the employer were eligible).

(2) Cessation of contributions is not required if continuation of contributions would not be an Employer Eligibility Failure (for example, with respect to a tax-exempt employer that may maintain a § 401(k) plan after 1996).

(3) A plan that is corrected through VCP is treated as subject to all of the requirements and provisions of § 401(a) for a Qualified Plan, § 403(b) for a 403(b) Plan, § 408(k) for a SEP, and § 408(p) for a SIMPLE IRA Plan (including Code provisions relating to rollovers). Therefore, the Plan Sponsor must also correct all other failures in accordance with this revenue procedure.

.04 *Correction of a failure to obtain spousal consent.* (1) Normally, the correction method under VCP for a failure to obtain spousal consent for a distribution that is subject to the spousal consent rules under §§ 401(a)(11) and 417 is similar to the correction method described in Appendix A .07. The Plan Sponsor must notify the affected participant and spouse (to whom the participant was married at the time of the distribution), so that the spouse can provide spousal consent to the distribution actually made or the participant may repay the distribution and receive a qualified joint and survivor annuity.

(2)(a) As alternatives to the correction method in section 6.04(1), correction for a failure to obtain spousal consent may be made under either section 6.04(2)(b) or section 6.04(2)(c).

(b) In the event that spousal consent to the prior distribution is not obtained (*e.g.*, because the spouse chooses not to consent, the spouse does not respond to the notice, or the spouse cannot be located), the spouse is entitled to a benefit under the plan equal to the portion of the qualified joint and survivor annuity that would have been payable to the spouse upon the death of the participant had a qualified joint and survivor annuity been provided to the participant under the plan at the annuity starting date for the prior distribution. Such spousal benefit must be provided if a claim is made by the spouse.

(c) In the event that spousal consent to the prior distribution is not obtained, the plan may offer the spouse the choice between (i) the survivor annuity benefit described in section 6.04(2)(b) or (ii) a single-sum payment equal to the actuarial present value of that survivor annuity benefit (calculated using the applicable interest rate and mortality table under § 417(e)(3)). Any such single-sum payment is treated in the same manner as a distribution under § 402(c)(9) for purposes of rolling over the payment to an IRA or other eligible retirement plan.

.05 *Correction by plan amendment.* In a case in which correction of a Qualification Failure includes correction of a Plan Document Failure, Demographic Failure, or Operational Failure by plan amendment, a determination letter application may be required. See section 4.06.

.06 *Special rules relating to Excess Amounts.* (1) *Treatment of Excess Amounts under Qualified Plans.* Except as otherwise provided in section 6.02(5)(c), a distribution of an Excess Amount is not eligible for the favorable tax treatment accorded to distributions from Qualified Plans (such as eligibility for rollover under § 402(c)). Thus, for example, if such a distribution was contributed to an individual retirement arrangement ("IRA"), the contribution is not a valid rollover contribution for purposes of determining the amount of excess contributions (within the meaning of § 4973) to the individual's IRA. A distribution of an Excess Amount is generally treated in the manner described in section 3 of Rev. Proc. 92–93, 1992–2 C.B. 505, relating to the corrective disbursement of elective deferrals. The distribution must be reported on Forms 1099–R for the year of distribution with respect to each participant or beneficiary receiving such a distribution. Except as otherwise provided in section 6.02(5)(c), where an Excess Amount has been or is being distributed, the Plan Sponsor must notify the recipient that (a) an Excess Amount has been or will be distributed and (b) an Excess Amount is not eligible for favorable tax treatment accorded to distributions from Qualified Plans (and, specifically, is not eligible for tax-free rollover).

(2) *Treatment of Excess Amounts under 403(b) Plans.* The distribution of Excess Amounts is not an eligible rollover distribution within the meaning of § 403(b)(8). A distribution of Excess Amounts is generally treated in the manner described in section 3 of Rev. Proc. 92–93 relating to the corrective disbursement of elec-

tive deferrals. The distribution must be reported on Forms 1099–R for the year of distribution with respect to each participant or beneficiary receiving such a distribution. Except as otherwise provided in section 6.02(5)(c), where an Excess Amount has been or is being distributed, the Plan Sponsor must notify the recipient that (a) an Excess Amount has been or will be distributed and (b) an Excess Amount is not eligible for favorable tax treatment accorded to distributions from Qualified Plans (and, specifically, is not eligible for tax-free rollover).

.07 *Rules relating to reporting plan loan failures.* (1) *General rule for loans.* Unless correction is made in accordance with this section 6.07(2) or (3), a deemed distribution under § 72(p)(1) in connection with a failure relating to a loan to a participant made from a Qualified Plan or a 403(b) Plan must be reported on Form 1099–R with respect to the affected participant and any applicable income tax withholding amount that was required to be paid in connection with the failure (see § 1.72(p)–1, Q&A–15) must be paid by the employer. As part of VCP, the deemed distribution may be reported on Form 1099–R with respect to the affected participant for the year of correction (instead of the year of the failure).

(2) *Special rules for loans.* (a) *In general.* The correction methods set forth in this section 6.07(2) (b) and (c) and section 6.07(3) are only available for plan loan failures that are corrected through VCP. The correction methods described in section 6.07(2) (b) and (c) and section 6.07(3) are not available if the maximum period for repayment of the loan pursuant to § 72(p)(2)(B) has expired. The Service reserves the right to limit the use of the correction methods listed in section 6.07(2) (b) and (c) and section 6.07(3) to situations that it considers appropriate; for example, where the loan failure is caused by employer action. A deemed distribution corrected under section 6.07(2) (b) or (c) or under section 6.07(3) is not required to be reported on Form 1099–R and repayments made by correction under sections 6.07(2) and 6.07(3) do not result in the affected participant having additional basis in the plan for purposes of determining the tax treatment of subsequent distributions from the plan to the affected participant.

(b) *Loans in excess of § 72(p)(2)(A).* A failure to comply with plan provisions requiring that loans comply with § 72(p)(2)(A) may be corrected by a corrective repayment to the plan based on the excess of the loan amount over the maximum loan amount under § 72(p)(2)(A). In the event that loan repayments were made in accordance with the amortization schedule for the loan before correction, such prior repayments may be applied (i) solely to reduce the portion of the loan that did not exceed the maximum loan amount under § 72(p)(2)(A) (so that the corrective repayment would equal the original loan excess plus interest thereon), (ii) to reduce the loan excess to the extent of the interest thereon, with the remainder of the repayments applied to reduce the portion of the loan that did not exceed the maximum loan amount under § 72(p)(2)(A) (so that the corrective repayment would equal the original loan excess), or (iii) *pro rata* against the loan excess and the maximum loan amount under § 72(p)(2)(A) (so that the corrective repayment would equal the outstanding balance remaining on the original loan excess on the date that corrective repayment is made). After the corrective payment is made, the loan may be reformed to amortize the remaining principal balance as of the date of repayment over the remaining period of the original loan. This is permissible as long as the recalculated payments over the remaining period would not cause the loan to violate the maximum duration permitted under § 72(p)(2)(B). The maximum duration is determined from the date the original loan was made. In addition, the amortization payments determined for the remaining period must comply with the level amortization requirements of § 72(p)(2)(C).

(c) *Loan terms that do not satisfy § 72(p)(2)(B) or (C).* For a failure of loan repayment terms to provide for a repayment schedule that complies with § 72(p)(2)(B) or (C), the failure may be corrected by a reamortization of the loan balance in accordance with § 72(p)(2)(C) over the remaining period that is the maximum period that complies with § 72(p)(2)(B) measured from the original date of the loan.

(3) *Defaulted loans.* A failure to repay the loan in accordance with the loan terms where the terms satisfy § 72(p)(2) may be corrected by (i) a lump sum repayment equal to the additional repayments that the affected participant would have made to the plan if there had been no failure to repay the plan, plus interest accrued on the missed repayments, (ii) reamortizing the outstanding balance of the loan, including accrued interest, over the remaining payment schedule of the original term of the loan, or (iii) any combination of (i) or (ii).

.08 *Correction under statute or regulations.* Generally, none of the correction programs are available 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.

.09 *Matters subject to excise taxes.* (1) Except as provided in this revenue procedure, 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.

(2) As part of VCP and Audit CAP, if the failure involves the failure to satisfy the minimum required distribution requirements of § 401(a)(9), in appropriate cases, the Service will waive the excise tax under § 4974 applicable to plan participants. The waiver will be included in the compliance statement or in the closing agreement in the case of Audit CAP. The Plan Sponsor, as part of the submission, must request the waiver and in cases where the participant subject to the excise tax is an owner-employee, as defined in § 401(c)(3), or a 10 percent owner of a corporation, the Plan Sponsor must also provide an explanation supporting the request. See section 12.02(2) relating to the applicable compliance fee for certain § 401(a)(9) failures.

(3) As part of VCP, if the failure involves a correction that requires the Plan Sponsor to make a plan contribution that is not deductible, in appropriate cases, the Service will not pursue the excise tax un-

der § 4972 on such nondeductible contributions. The Plan Sponsor, as part of the submission must request the relief and provide an explanation supporting the request.

(4) As part of VCP, if a failure results in excess contributions as defined in §4979(c) or excess aggregate contributions as defined in §4979(d) under a plan, the Service will not pursue the excise tax under § 4979 in appropriate cases, *e.g.*, where correction is made for any case in which the ADP test was timely performed but, due to reliance on inaccurate data, resulted in an insufficient amount of excess elective contributions having been distributed to HCEs. The Plan Sponsor, as part of the submission, must request the relief and provide an explanation supporting the request.

.10 *Correction for SEPs and SIMPLE IRA Plans.* (1) *Correction for SEPs and SIMPLE IRA Plans generally.* Generally, the correction for a SEP or a SIMPLE IRA Plan is expected to be similar to the correction required for a Qualified Plan with a similar Qualification Failure (*i.e.*, Plan Document Failure, Operational Failure, Demographic Failure and Employer Eligibility Failure).

(2) *Special correction for SEPs and SIMPLE IRA Plans.* In any case in which correction under section 6.10(1) is not feasible for a SEP or SIMPLE IRA Plan or in any other case determined by the Service in its discretion (including failures relating to §§ 402(g), 415, and 401(a)(17), failures relating to deferral percentages, discontinuance of contributions to a SARSEP or SIMPLE IRA Plan, and retention of Excess Amounts for cases in which there has been no violation of a statutory limitation with respect to a SEP or SIMPLE IRA Plan), the Service may provide for a different correction. See section 12.06(2) for a special fee that may apply in such a case.

(3) *Correction of failure to satisfy deferral percentage test.* If the failure involves a violation of the deferral percentage test under § 408(k)(6)(A)(iii) applicable to a SARSEP, the failure may be corrected in either one of the following ways:

(a) The Plan Sponsor may make contributions that are 100% vested to all eligible nonhighly compensated employees (to the extent permitted by § 415) necessary to raise the deferral percentage needed to pass the test. This amount may be calculated as the same percentage of compensation (regardless of the terms of the SEP).

(b) The Plan Sponsor may effect distribution of excess contributions, adjusted for earnings through the date of correction, to highly compensated employees to correct the failure. The Plan Sponsor must also contribute to the SEP an amount equal to the total amount distributed. This amount must be allocated to (i) current employees who were nonhighly compensated employees in the year of the failure, (ii) current nonhighly compensated employees who were nonhighly compensated employees in the year of the failure, or (iii) employees (both current and former) who were nonhighly compensated employees in the year of the failure.

(4) *Treatment of undercontributions to a SEP or a SIMPLE IRA Plan.* (a) *Make-up contributions; earnings.* The Plan Sponsor should correct undercontributions to a SEP or a SIMPLE IRA Plan by contributing make-up amounts that are fully vested, adjusted for earnings credited from the date of the failure to the date of correction.

(b) *Earnings adjustment methods.* Insofar as SEP and SIMPLE IRA Plan assets are held in IRAs, there is no earnings rate under the SEP or SIMPLE IRA Plan as a whole. If it is not feasible to make a reasonable estimate of what the actual investment results would have been, a reasonable interest rate may be used.

(5) *Treatment of Excess Amounts under a SEP or a SIMPLE IRA Plan.* (a) *Distribution of Excess Amounts.* For purposes of section 6.10, an Excess Amount is an amount contributed on behalf of an employee that is in excess of an employee's benefit under the plan, or an elective deferral in excess of the limitations of §§ 402(g) or 408(k)(6)(A)(iii). If an Excess Amount is attributable to elective deferrals, the Plan Sponsor may effect distribution of the Excess Amount, adjusted for earnings through the date of correction, to the affected participant. The amount distributed to the affected participant is includible in gross income in the year of distribution. The distribution is reported on Form 1099–R for the year of distribution with respect to each participant receiving the distribution. In addition, the Plan Sponsor must inform affected participants that the distribution of an Excess Amount is not eligible for favorable tax treatment accorded to distributions from a SEP or a SIMPLE IRA Plan (and, specifically, is not eligible for tax-free rollover). If the Excess Amount is attributable to employer contributions, the Plan Sponsor may effect distribution of the employer Excess Amount, adjusted for earnings through the date of correction, to the Plan Sponsor. The amount distributed to the Plan Sponsor is not includible in the gross income of the affected participant. The Plan Sponsor is not entitled to a deduction for such employer Excess Amount. The distribution is reported on Form 1099–R issued to the participant indicating the taxable amount as zero.

(b) *Retention of Excess Amounts.* If an Excess Amount is retained in the SEP or SIMPLE IRA Plan under section 6.10(5), a special fee, in addition to the VCP submission fee, will apply. See section 12.05(2) for the special fee. The Plan Sponsor is not entitled to a deduction for an Excess Amount retained in the SEP or SIMPLE IRA Plan. In the case of an Excess Amount retained in a SEP that is attributable to a § 415 failure, the Excess Amount, adjusted for earnings through the date of correction, must reduce affected participants' applicable § 415 limit for the year following the year of correction (or for the year of correction if the Plan Sponsor so chooses), and subsequent years, until the excess is eliminated.

(c) *De minimis Excess Amounts.* If the total Excess Amount in a SEP or SIMPLE IRA Plan, whether attributable to elective deferrals or employer contributions, is $100 or less, the Plan Sponsor is not required to distribute the Excess Amount and the special fee described in section 12.05(2) does not apply.

.11 *Confidentiality and disclosure.* Because each correction program relates directly to the enforcement of the Code 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.

.12 *No effect on other law.* Correction under these programs has no effect on the rights of any party under any other law, including Title I of ERISA. The Department of Labor maintains a Voluntary Fiduciary Correction Program under which certain ERISA fiduciary violations may be cor-

rected. The Department of Labor also maintains a Delinquent Filer Voluntary Compliance Program under which certain failures to comply with the annual reporting requirements (Form 5500 series) under ERISA may be corrected.

PART IV. SELF-CORRECTION (SCP)

SECTION 7. IN GENERAL

The requirements of this section 7 are satisfied with respect to an Operational Failure if the Plan Sponsor of a Qualified Plan, a 403(b) Plan, a SEP, or a SIMPLE IRA Plan satisfies the requirements of section 8 (relating to insignificant Operational Failures) or, in the case of a Qualified Plan or a 403(b) Plan, section 9 (relating to significant Operational Failures).

SECTION 8. SELF-CORRECTION OF INSIGNIFICANT OPERATIONAL FAILURES

.01 *Requirements.* The requirements of this section 8 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 8 is available for correcting an insignificant Operational Failure even if the plan or Plan Sponsor is Under Examination and even if the Operational Failure is discovered on 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 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. Additionally, factors (2), (4), and (5) should not be interpreted to exclude small businesses.

.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 8 only if all of the Operational Failures are insignificant in the aggregate. Operational Failures that have been corrected under SCP in section 9 and VCP in sections 10 and 11 are not taken into account for purposes of determining if Operational Failures are insignificant in the aggregate.

.04 *Examples.* The following examples illustrate the application of this section 8. It is assumed, in each example, that the eligibility requirements of section 4 relating to SCP have been satisfied and that no Operational Failures occurred other than the Operational Failures identified below.

Example 1: In 1991, Employer X established Plan A, a profit-sharing plan that satisfies the requirements of § 401(a) in form. In 2003, the benefits of 50 of the 250 participants in Plan A were limited by § 415(c). However, when the Service examined Plan A in 2006, it discovered that, during the 2003 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 totaled $4,550. 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 2003 plan year, are insignificant, the § 415(c) failure in Plan A that occurred in 2003 would be eligible for correction under this section 8.

Example 2: The facts are the same as in *Example 1*, except that the failure to satisfy § 415 occurred during each of the 2003, 2004, and 2005 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 8.

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 2003 limitation year, and the amount of the excesses ranged from $1,000 to $9,000, and totaled $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 2003 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 2003 is ineligible for correction under this section 8 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 2004 plan year, the Service discovered that the employee responsible for entering data into the employer's computer made minor arithmetic errors in transcribing the 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 2004 would be insignificant and therefore eligible for correction under this section 8.

Example 5: Public School maintains for its 200 employees a salary reduction 403(b) Plan (the "Plan") that 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 2004 plan year, a former employee should have received an additional minimum required distribution of $278 under § 403(b)(10). Another participant received an impermissible hardship withdrawal of $2,500. Another participant made elective deferrals of which $1,000 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 8 because in the aggregate the failures are insignificant.

SECTION 9. SELF-CORRECTION OF SIGNIFICANT OPERATIONAL FAILURES

.01 *Requirements.* The requirements of this section 9 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 9.04) by the last day of the correction period described in section 9.02.

.02 *Correction period.* (1) *End of 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 correction period does not end until the last day of

the second plan year following the plan year that includes the last day of the additional period for correction permitted under § 401(k)(8) or 401(m)(6). If a 403(b) Plan does not have a plan year, the plan year is deemed to be the calendar year for purposes of this subsection.

(2) *Extension of correction period for Transferred Assets.* In the case of an Operational Failure that relates only to Transferred Assets, or to a plan assumed in connection with a corporate merger, acquisition or other similar employer transaction, the correction period does not end until the last day of the first plan year that begins after the corporate merger, acquisition, or other similar employer transaction between the Plan Sponsor and the sponsor of the transferor plan or the prior sponsor of an assumed plan.

(3) *Effect of examination.* 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 second sentence of section 9.02). (But see section 9.04 for special rules permitting completion of correction after the end of the correction period.)

.03 *Correction by plan amendment.* In order to complete correction by plan amendment (as permitted under section 4.05), the appropriate determination letter application must be submitted before the end of the plan's applicable remedial amendment period described in Rev. Proc. 2005–66.

.04 *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:

(a) during the correction period, correction is completed with respect to 85 percent 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.

.05 *Examples.* The following examples illustrate the application of this section 9. Assume that the eligibility requirements of section 4 relating to SCP have been met.

Example 1: Employer Z established a qualified defined contribution plan in 2003 and received a favorable determination letter. During 2005, while doing a self-audit of the operation of the plan for the 2004 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 2004 Operational Failures occurred because the elective deferrals of additional employees exceeded the § 402(g) limit and Employer Z failed to make the required top-heavy minimum contribution. During the 2005 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 2004 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. Under these facts, the Plan Sponsor has corrected the Operational Failures for the 2004 plan year within the correction period and thus satisfied the requirements of this section 9.

Example 2: Employer A established a qualified defined contribution plan, Plan A, in 1990 and has received a favorable determination letter for the applicable law changes. In April 2003, Employer A purchased all of the stock of Employer B, a wholly-owned subsidiary of Employer C. Employees of Employer B participated in Plan C, a qualified defined contribution plan sponsored by Employer C. Following Employer A's review of Plan C, Employer A and Employer C agreed that Plan A would accept a transfer of plan assets attributable to the account balances of the employees of Employer B who had participated in Plan C. As part of this agreement, Employer C represented to Employer A that Plan C is tax qualified. Employers A and C also agreed that such transfer would be in accordance with § 414(l) and § 1.414(l)–1 and addressed issues related to costs associated with the transfer. Following the transaction, the employees of Employer B began participation in Plan A. Effective July 1, 2003, Plan A accepted the transfer of plan assets from Plan C. After the transfer, Employer A determined that all the participants in one division of Employer B had been incorrectly excluded from allocation of the profit sharing contributions for the 1998 and 1999 plan years. During 2004, Employer A made corrective contributions on behalf of the affected participants. The corrective contributions were credited with earnings at a rate appropriate for the plan from the date the corrective contribution should have been made to the date of correction and Employer A otherwise complied with the requirements of SCP. Under these facts, Employer A has, within the correction period, corrected the Operational Failures for the 1998 and 1999 plan years with respect to the assets transferred to Plan A, and thus satisfied the requirements of this section 9.

PART V. VOLUNTARY CORRECTION PROGRAM WITH SERVICE APPROVAL (VCP)

SECTION 10. VCP PROCEDURES

.01 *VCP requirements.* The requirements of this section 10 are satisfied with respect to failures submitted in accordance with the requirements of this section 10 if the Plan Sponsor pays the compliance fee required under section 12 and implements the corrective actions and satisfies any other conditions in the compliance statement described in section 10.08.

.02 *Identification of failures.* VCP is not based upon an examination of the plan by the Service. Only the failures raised by the Plan Sponsor or failures identified by the Service in processing the application are addressed under VCP, and only those failures will be covered by the VCP compliance statement. The Service will not make any investigation or finding under VCP concerning whether there are failures.

.03 *Effect of VCP submission on examination.* Because VCP does not arise out of an examination, consideration under VCP 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. However, a Plan Sponsor's statements describing failures are made only for purposes of VCP and will not be regarded by the Service as an admission of a failure for purposes of any subsequent examination. See section 5.03 for the definition of Under Examination.

.04 *No concurrent examination activity.* Except in unusual circumstances, a plan that has been properly submitted under VCP will not be examined while the submission is pending. Notwithstanding the above, a plan that is eligible for a Group

Submission under section 10.11 may be examined while the Group Submission is pending with respect to issues not identified in the Group Submission at the time such plan comes Under Examination. In addition, if it is determined that either the plan or the Plan Sponsor was, or may have been a party to an abusive tax avoidance transaction (as defined in section 4.13(2)), the Service may authorize the examination of the plan, even if a submission pursuant to VCP 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 VCP could be subject to examination.

.05 *Determination letter application for plan amendments related to a VCP submission.* In any case in which a determination letter is submitted pursuant to section 4.06, the Plan Sponsor must submit a copy of the amendment, the appropriate application form (*i.e.*, Form 5300 series), and the appropriate user fee concurrently and to the same address as the VCP submission. The user fee for the determination letter application and the fee for the VCP submission must be submitted on separate checks made payable to the U.S. Treasury. See section 11.12 for the VCP mailing address.

.06 *Determination letter applications not related to a VCP submission.* (1) The Service may process a determination letter application submitted under the determination letter program (including an application requested on Form 5310) concurrently with a VCP 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 VCP submission.

(2) A submission of a plan under the determination letter program does not constitute a submission under VCP. If the Plan Sponsor discovers a Qualification Failure, the Qualification Failure may not be corrected as part of the determination letter process. The Plan Sponsor may use SCP and VCP instead, as applicable. If the Service in connection with a determination letter application discovers a Qualification Failure, the Service may issue a closing agreement with respect to the failures identified or, if appropriate, refer the case to Employee Plans Examinations. In either case, the fee structure in section 12, relating to VCP will not apply. Except as provided in section 10.06(3), the fee structure in section 14 relating to Audit CAP will apply. See section 5.03(3) for a description of when a plan submitted for a determination letter is considered to be Under Examination.

(3) If the Service in connection with a determination letter application discovers the plan has not been amended timely for tax legislation changes, the fee structure in section 14.04 will apply.

.07 *Processing of submission.* (1) *Screening of submission.* Upon receipt of a submission under VCP, the Service will review whether the eligibility requirements of section 4 and the submission requirements of section 11 are satisfied.

(2) *Eligibility of submission.* If, at any stage of the review process, the Service determines that a VCP submission is seriously deficient or that the application of VCP would be inappropriate or impractical, the Service reserves the right to return the submission, including any compliance fee, without contacting the Plan Sponsor.

(3) *Review of submission.* Once the Service determines that the submission is complete under VCP, 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.

(4) *Additional information required.* 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 Employee Plans Examinations. 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 (by the applicable group manager).

(5) *Additional failures discovered after initial submission.* (a) A Plan Sponsor that discovers additional unrelated Qualification or 403(b) 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.

(b) If the Service discovers an unrelated Qualification or 403(b) 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 the Plan Sponsor did not voluntarily bring it forward. In this case, if the additional failure is significant, all aspects of the plan may be examined and the rules pertaining to Audit CAP will apply.

(6) *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 (generally through 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 (by the applicable group manager). Additional conferences may be held at the discretion of the Service.

(7) *Failure to reach resolution.* If the Service and the Plan Sponsor cannot reach agreement with respect to the submission, the matter will be closed, the compliance fee will not be returned, and the case may be referred to Employee Plans Examinations. In the case of an Anonymous Submission that fails to reach resolution under this revenue procedure, the Service will refund 50% of the applicable VCP fee. See section 12.01 for the VCP fee.

(8) *Issuance of compliance statement.* If agreement is reached, the Service will send to the Plan Sponsor a compliance statement specifying the corrective action required. If the original submission is subsequently materially modified, then, unless the Plan Sponsor has submitted a penalty of perjury statement with respect

to such subsequent modifications, the Plan Sponsor will be required to sign the compliance statement. In such case, the Service will send to the Plan Sponsor an unsigned compliance statement specifying the corrective action required. Within 30 calendar days of the date the compliance statement is sent, a Plan Sponsor must sign the compliance statement and return it and any compliance fee required to be paid at the time that the compliance statement is signed (see section 11.05). The Service will then issue a signed copy of the compliance statement to the Plan Sponsor. If the Plan Sponsor does not sign the compliance statement and send it to the Service (with a compliance fee, if applicable) within 30 calendar days, the plan may be referred to Employee Plans Examinations.

(9) *Timing of correction.* The Plan Sponsor must implement 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 prior to the expiration of the correction period and in writing and must be approved by the Service.

(10) *Modification of compliance statement.* 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 compliance fee for the modification will be the lesser of the original compliance fee or $3,000.

(11) *Verification.* Once the compliance statement has been issued, the Service may require verification that the correction methods have been complied with and that any plan administrative procedures required by the compliance 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 plan may be referred to Employee Plans Examinations.

.08 *Compliance statement.* (1) *General description of compliance statement.* The compliance statement issued for a VCP submission addresses the failures identified, the terms of correction, including any revision of administrative procedures, and the time period within which proposed corrections must be implemented, including any changes in administrative procedures. The compliance statement also provides that the Service will not treat the plan as failing to satisfy the applicable requirements of the Code on account of the failures described in the compliance statement if the conditions of the compliance statement are satisfied. Unless a determination letter application is included with a VCP submission for an on-cycle or terminating plan in accordance with section 4.06, with respect to a failure to amend a plan timely for (a) good faith plan amendments for the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. 107–16 (EGTRRA), within the period described in Notice 2001–42 including those changes listed in Notice 2005–5, (b) plan amendments for the final and temporary regulations under § 401(a)(9) as they appeared in the April 1, 2003, edition of 26 CFR Part 1 (the § 401(a)(9) final and temporary regulations) within the period described in Rev. Proc. 2002–29 as modified by Rev. Proc. 2003–10, and (c) interim amendments as provided in section 5 of Rev. Proc. 2005–66, the issuance of a compliance statement will result in the corrective amendments being treated as if they had been adopted timely for the purpose of determining the availability of the remedial amendment period currently described in Rev. Proc. 2005–66. However, the issuance of such a compliance statement will not constitute a determination as to whether the plan amendment as drafted complies with the change in qualification requirement. Where current procedures are inadequate for operating the plan in conformance with the applicable requirements of the Code, the compliance statement will be conditioned upon the implementation of stated administrative procedures. The Service may prescribe appropriate administrative procedures in the compliance statement.

(2) *Compliance statement conditioned upon timely correction.* The compliance statement is conditioned on (i) there being no misstatement or omission of material facts in connection with the submission and (ii) the implementation of the specific corrections and satisfaction of any other conditions in the compliance statement.

(3) *Authority delegated.* Compliance statements (including relief from any excise tax as provided under section 6.09) are authorized to be signed by Area Managers reporting to the Director, Employee Plans Examinations, and managers within Employee Plans Rulings and Agreements, under the Tax Exempt and Government Entities Operating Division of the Service.

.09 *Effect of compliance statement on examination.* The compliance statement is binding upon both the Service and the Plan Sponsor or Eligible Organization (as defined in section 10.11(2)) 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 compliance statement, even with respect to the same taxable year or years to which the compliance statement relates.

.10 *Special rules relating to Anonymous (John Doe) Submissions.* (1) The Anonymous Submission procedure in this section 10.10 permits submission of Qualified Plans, 403(b) Plans, SEPs and SIMPLE IRA Plans under VCP without initially identifying the applicable plan(s), the Plan Sponsor(s), or the Eligible Organization. The requirements of this revenue procedure relating to VCP, including sections 10, 11, and 12, apply to these submissions. However, information identifying the plan or the Plan Sponsor may be redacted (and the power of attorney statement and the penalty of perjury statement need not be included with the initial submission). In addition, if a determination letter application will be requested as part of the submission, the determination letter application should not be submitted until the time all identifying information is provided to the Service. For purposes of processing the submission, the State of the Plan Sponsor must be identified in the initial submission. All anonymous submissions must be numbered or labeled on the first page of the VCP submission by the plan sponsor or its representative to facilitate identification and tracking of the submission. The identification number should be unique to the submission and should not be used with respect to any other anonymous submission of the plan sponsor or representative. Once the Service and the plan representative reach

agreement with respect to the submission, the Service will contact the plan representative in writing indicating the terms of the agreement. The Plan Sponsor will have 21 calendar days from the date of the letter of agreement to identify the plan and Plan Sponsor. If the Plan Sponsor does not submit the identifying material (including the power of attorney statement and the penalty of perjury statement) within 21 calendar days of the letter of agreement, the matter will be closed and the compliance fee will not be returned.

(2) Notwithstanding section 10.04, until the plan(s) and Plan Sponsor(s) are identified to the Service, a submission under this subsection does not preclude or impede an examination of the Plan Sponsor or its plan(s). Thus, a plan submitted under the Anonymous Submission procedure that comes Under Examination prior to the date the plan(s) and Plan Sponsor(s) identifying materials are received by the Service will no longer be eligible under VCP.

.11 *Special rules relating to Group Submissions.* (1) *General rules.* An Eligible Organization may submit a VCP request for a Qualified Plan, a 403(b) Plan, a SEP, or a SIMPLE IRA Plan under a Group Submission for Plan Document, Operational and Employer Eligibility Failures. If a Sponsor of a master or prototype plan submits failures with respect to more than one master or prototype plan, each plan will be treated as a separate submission and a separate fee must be submitted for each prototype plan. Similarly, if a Volume Submitter practitioner submits failures with respect to more than one Volume Submitter plan, each plan will be treated as a separate submission and a separate fee must be submitted for each specimen plan.

(2) *Eligible Organizations.* For purposes of a Group Submission, the term "Eligible Organization" means either (a) a Sponsor (as that term is defined in section 4.07 of Rev. Proc. 2005–16, 2005–10 I.R.B. 674) of a master or prototype plan, (b) a Volume Submitter practitioner, as that term is defined in section 13.04 of Rev. Proc. 2005–16, (c) an insurance company or other entity that has issued annuity contracts or provides services with respect to assets for 403(b) Plans, or (d) an entity that provides its clients with administrative services with respect to Qualified Plans, 403(b) Plans, SEPs or SIMPLE IRA Plans. An Eligible Organization is not eligible to make a Group Submission unless the submission includes a failure resulting from a systemic error involving the Eligible Organization that affects at least 20 plans and that result in at least 20 plans implementing correction. If, at any time before the Service issues the compliance statement, the number of plans falls below 20, the Eligible Organization must notify the Service that it is no longer eligible to make a Group Submission (and the compliance fee may be retained).

(3) *Special Group Submission procedures.* (a) In general, a Group Submission is subject to the same procedures as any VCP submission in accordance with sections 10 and 11, except that the Eligible Organization is responsible for performing the procedural obligations imposed on the Plan Sponsor under sections 10 and 11. See section 11.02(15) for a special submission requirement with respect to Group Submissions.

(b) The Eligible Organization must provide notice to all Plan Sponsors of the plans included in the Group Submission. The notice must be provided at least 90 days before the Eligible Organization provides the Service with the information required in section 10.11(3)(c). The purpose of the notice is to provide each Plan Sponsor with information relating to the Group Submission request. The notice should explain the reason for the Group Submission and inform the Plan Sponsor that the Plan Sponsor's plan will be included in the Group Submission unless the Plan Sponsor responds within the 90-day period to exclude the Plan Sponsor's plan from the Group Submission.

(c) When an Eligible Organization receives an unsigned compliance statement on the proposed correction and agrees to the terms of the compliance statement, the Eligible Organization must return to the Service within 120 calendar days not only the signed compliance statement and any additional compliance fee under section 12.05, but also a list containing (i) the employers' tax identification numbers for the Plan Sponsors of the plans to which the compliance statement may be applicable, (ii) the plans by name, plan number, type of plan and number of plan participants, (iii) a certification that each Plan Sponsor received notice of the Group Submission, and (iv) a certification that each Plan Sponsor timely filed the Form 5500 return for each plan. This list can be submitted at any stage of the submission process provided that the requirements of section 10.11(3)(b) have been satisfied. Applicants are encouraged to submit the list on a computer disk in Microsoft Word. Only those plans for which correction is actually made within 240 calendar days of the date of the signed compliance statement (or within such longer period as may be agreed to by the Service at the request of the Eligible Organization) will be covered by the compliance statement.

(d) Notwithstanding section 4.02, if a Plan Sponsor of a plan that is eligible to be included in the Group Submission is notified of an impending Employee Plans examination after the Eligible Organization filed the Group Submission application, the Plan Sponsor's plan will be included in the Group Submission. However, with respect to such plan, the Group Submission will not preclude or impede an examination of the plan with respect to any failures not identified in the Group Submission application at the time the plan comes Under Examination.

.12 *Multiemployer and multiple employer plans.* (1) 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.

(2) If a VCP submission for a multiemployer or multiple employer plan has failures that apply to fewer than all of the employers under the plan, the plan administrator may choose to have the compliance fee (in section 12) or sanction (in section 14) calculated separately for each employer based on the assets attributable to that employer, rather than being attributable to the assets of the entire plan. Thus, the plan administrator may choose to apply the provisions of this paragraph where the failure is attributable in whole or in part to data, information, actions, or inactions that are within the control of the employers rather than the multiemployer or multiple employer plan (such as attribution in whole or in part to the failure of a employer to provide the plan administrator with full and complete information).

SECTION 11. APPLICATION PROCEDURES FOR VCP

.01 *General rules.* The requirements of this section 11 are satisfied if the request for a compliance statement from the Service under VCP satisfies the informational and other requirements of this section 11. In general, a request under VCP consists of a letter from the Plan Sponsor (which may be a letter from the Plan Sponsor's representative) or Eligible Organization (or 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. If the sole failure involves the failure by the Plan Sponsor to amend a plan timely for (a) good faith plan amendments for EGTRRA, (b) plan amendments for the final and temporary regulations under § 401(a)(9) or (c) interim amendments, then the Plan Sponsor may follow the streamlined submission procedure described in Appendix F. In such circumstance, a complete submission pursuant to Appendix F will satisfy the submission requirements provided below.

.02 *Submission requirements.* The letter from the Plan Sponsor or the Plan Sponsor's representative must contain the following:

(1) A statement identifying the type of plan submitted (*e.g.*, Qualified Plan, 403(b) Plan, SEP, or SIMPLE IRA Plan) and, if applicable, whether the submission is a Group Submission, an Anonymous Submission, a nonamender submission, a multiemployer or multiple employer plan submission, or an Orphan Plan submission. In addition, if the submission involves a Qualified Plan, the statement should also identify the type of Qualified Plan being submitted (*e.g.*, Defined Benefit, Money Purchase, Profit Sharing, or Stock Bonus, and 401(k) or ESOP).

(2) A complete description of the failures, the years in which the failures occurred, including closed years (that is, years for which the statutory period has expired), and the number of employees affected by each failure.

(3) A description of the administrative procedures in effect at the time the failures occurred.

(4) An explanation of how and why the failures arose.

(5) 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.

(6) 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(4)).

(7) 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 (whether matched or 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 ADP test in § 401(k)(3), the Plan Sponsor must submit the ADP test results both before the correction and after the correction.

(8) 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 or will be affected by the correction.

(9) A description of the measures that have been or will be implemented to ensure that the same failures will not recur.

(10) A statement that, to the best of the Plan Sponsor's knowledge, neither the plan nor the Plan Sponsor is Under Examination.

(11) A statement that neither the plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction (as defined in section 4.13(2)) or a brief identification of any abusive tax avoidance transaction to which the plan or the Plan Sponsor has been a party.

(12) If a submission includes a failure that relates to Transferred Assets and the failure occurred prior to the transfer, a description of the transaction (including the dates of the employer change and the plan transfer).

(13) A statement (if applicable) that the plan is currently being considered in a determination letter application that is not related to the VCP application. If the request for a determination letter is made while a request for consideration under VCP is pending, the Plan Sponsor must update the VCP request to add this information.

(14) In the case of a 403(b) Plan submission, a statement that the Plan Sponsor has contacted all other entities involved with the plan and has been assured of cooperation in implementing the applicable correction, to the extent necessary. For example, if the plan's failure is the failure to satisfy the requirements of § 403(b)(11)(E) on elective deferrals, the Plan Sponsor must, prior to making the VCP application, contact the insurance company or custodian with control over the plan's assets to assure cooperation in effecting a distribution of the excess deferrals and the earnings thereon. An application under VCP must also contain a statement as to the type of employer (*e.g.*, a tax-exempt organization described in § 501(c)(3)) submitting the VCP application.

(15) A Group Submission must be signed by the Eligible Organization or the Eligible Organization's authorized representative and accompanied by a copy of the relevant portions of the plan document(s). In addition, a Group Submission must include a separate page for each affected Plan Sponsor that provides the Plan Sponsor's name, EIN, plan name, and failure(s).

.03 *Required documents.* A VCP submission must be accompanied by the following documents:

(1) *Form 5500 or similar information.* (a) In the case of a plan required to file Form 5500, a copy of the first three pages

of the most recently filed Form 5500 series return and the applicable Financial Information Schedule. In the case of a terminated plan, the Form 5500 must be the one filed for the plan year prior to the plan year for which the Final Form 5500 return was filed.

(b) In the case of any plan not required to file Form 5500, *e.g.*, a governmental plan, nonelecting church plan, SEP, SIMPLE IRA Plan, or an applicable 403(b) plan, the information that generally would be included on the first three pages of Form 5500, including the name and number of the plan, the Plan Sponsor's EIN, and the amount of plan assets to the extent that the information is available to the Plan Sponsor.

(c) In the case of an Anonymous Submission, the employee census may be redacted and replaced by numbers that are rounded up.

(2) *Plan document.* A copy of the entire plan document or the relevant portions of the plan document. For example, in a case involving an 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. If the plan is a 403(b) Plan and a plan document is not available, a written description of the plan should be submitted, with sample salary reduction agreements if relevant. In the case of a SEP and a SIMPLE IRA Plan, the entire plan document should be submitted.

(3) *Determination letter application.* In any case in which correction of a Qualification Failure is made by plan amendment, as permitted under section 4.05, other than the adoption of an amendment designated by the Service as a model amendment or the adoption of a prototype or volume submitter plan for which the Plan Sponsor has reliance on the plan's opinion or advisory letter as provided in Rev. Proc. 2006–6, 2006–1 I.R.B. 204, and the Plan Sponsor is submitting a determination letter request as permitted under section 4.06, the Plan Sponsor must submit a copy of the amendment, the appropriate application form (*i.e.*, Form 5300 series) to the extent required by section 4.06, and the appropriate user fee concurrently and to the same address as the VCP submission. The user fee for the determination letter application and the fee for the VCP submission must be submitted on separate checks made payable to the U.S. Treasury. See section 11.12 for the VCP mailing address.

.04 *Date fee due generally.* Except as provided in sections 11.05 and 12.02(3), the VCP fee under section 12 and, if applicable, the determination letter user fee, must be included with the submission. The VCP fee and the determination letter user fee must be submitted on separate checks made payable to the U.S. Treasury. If the appropriate fees are not included in the submission, the submission will be returned.

.05 *Additional fee due for SEPs, SIMPLE IRA Plans, and Group Submissions.* In the case of a SEP, a SIMPLE IRA Plan, or a Group Submission, the initial fee described in section 12.02, 12.04, or 12.05 must be included in the submission and any additional fee is due at the time the compliance statement is signed by the Plan Sponsor and returned to the Service, or when agreement has been reached between the Service and the Plan Sponsor regarding correction of the failure(s).

.06 *Signed submission.* The submission must be signed by the Plan Sponsor or the sponsor's authorized 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 requirements of section 9.02(11) and (12) of Rev. Proc. 2006–4, 2006–1 I.R.B. 132, and submit Form 2848, *Power of Attorney and Declaration of Representative.* A Form 2848 that designates a representative not qualified to sign Part II of the Form 2848, *e.g.*, an unenrolled return preparer, will not be accepted. A Plan Sponsor may authorize an individual, such as an unenrolled return preparer, to inspect or receive confidential information using Form 8821, *Tax Information Authorization* (See Form 8821 and Instructions.)

.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 Plan Sponsor's representative.

.09 *Checklist.* The Service will be able to respond more quickly to a VCP request if the request is carefully prepared and complete. The checklist in Appendix C 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 C must be completed, signed, and dated by the Plan Sponsor or the Plan Sponsor's representative. A photocopy of this checklist may be used.

.10 *Designation.* The letter to the Service should indicate in the upper right hand corner of the letter the type of plan submitted under VCP, a Qualified Plan, 403(b) Plan, SEP, or SIMPLE IRA Plan. In addition, if the submission is a Group Submission, an Anonymous Submission, a nonamender submission, a multiemployer or multiple employer plan submission, or an Orphan Plan submission, the letter should so indicate.

.11 *Acknowledgement Letter.* The Service will acknowledge receipt of a VCP submission if the Plan Sponsor or the Plan Sponsor's representative completes the Acknowledgement Form in Appendix E and includes it in the submission. A photocopy of Appendix E may be used.

.12 *VCP mailing address.* All VCP submissions and accompanying determination applications, if applicable, should be mailed to:

Internal Revenue Service
Attention: SE:T:EP:RA:VC
P.O. Box 27063
McPherson Station
Washington, D.C. 20038

.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 VCP requests.

.14 *Assembling the submission.* The Service will be able to process a submission more quickly if the submission package contains all of the items required by the

Appendix C check list and is assembled in the following order:

(1) If applicable, Form 8717, *User Fee for Employee Plan Determination Letter Request*, and the check for the determination letter user fee made payable to the U.S. Treasury.

(2) Determination letter application (*i.e.*, Form 5300 series form), if applicable

(3) Submission signed by the Plan Sponsor or Plan Sponsor's authorized representative, with a check for the VCP fee made payable to the U.S. Treasury attached to the front of the submission letter. The submission should include the following:

- Type of plan (or group of plans) being submitted
- Description of the failures (if the failures relate to Transferred Assets, include a description of the related employer transaction)
- An explanation of how and why the failures arose
- Description of the method for correcting failures, including earnings methodology (if applicable) and supporting computations (if applicable)
- Description of the method used to locate or notify former employees affected by the failures or corrections. If no former employees are affected by the failures or corrections, then the letter should affirmatively state that position when addressing this issue.
- Description of the administrative procedures that have been or will be implemented to ensure that the failures do not recur
- Whether a request that participant loans corrected under this revenue procedure not be treated as distributions §72(p) is being made and supporting rationale for such request. Alternatively, whether a request that participant loans corrected under this revenue procedure should be treated as distributions in the year of correction is being made and supporting rationale for such request.
- Whether relief from imposition of the excise taxes under §§ 4972, 4974 or 4979 is being requested, and the supporting rationale for such relief
- If the plan is an Orphan Plan, whether relief from the VCP application fee is being requested, and the supporting rationale for such relief
- A statement on whether the plan is being considered in an unrelated determination letter application (if applicable)
- Statement that the plan is not Under Examination
- Statement that the Plan Sponsor is not under an Exempt Organizations examination
- A statement that neither the plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction (as defined in section 4.13(2)) or a brief identification of any abusive tax avoidance transaction to which the plan or the Plan Sponsor has been a party.
- Penalty of perjury statement

(4) Completed and signed Appendix C checklist

(5) Appendix E acknowledgement letter

(6) *Power of Attorney* (Form 2848) or *Tax Information Authorization* (Form 8821), if applicable

(7) Form 5500, (first three pages and the applicable Financial Information Schedule) or equivalent information

(8) Copy of opinion or determination letter (if applicable)

(9) Relevant plan document language or plan document (if applicable)

(10) Any other items that may be relevant to the submission

SECTION 12. VCP FEES

.01 *VCP fees.* The compliance fees for all submissions under VCP are determined under this section 12. All fees must be submitted by check made payable to the U.S. Treasury and, except for the special fees described in sections 12.04 and 12.05(2), must be included with the initial submission.

.02 *VCP fee for Qualified Plans and 403(b) Plans.* (1) Subject to section 12.02(2), the compliance fee for a submission under VCP for Qualified Plans and 403(b) Plans (including Anonymous Submissions) is determined in accordance with the following chart.

Number of Participants	Fee
20 or fewer	$ 750
21 to 50	$ 1,000
51 to 100	$ 2,500
101 to 500	$ 5,000
501 to 1,000	$ 8,000
1,001 to 5,000	$15,000
5,001 to 10,000	$20,000
Over 10,000	$25,000

(2) If (a) the VCP submission involves the failure to satisfy the minimum distribution requirements of § 401(a)(9) for 50 or fewer participants, (b) such failure is the only failure of the submission, and (c) the failure would result in the imposition of the excise tax under § 4974, the compliance fee is $500.

(3) At the discretion of the Service, the VCP fee may be waived in the case of a terminating Orphan Plan. In such cases,

the submission must include a request for a waiver of the VCP fee.

.03 *VCP fee for nonamender failures.* In general, the compliance fee for plans with a nonamender failure, as described in section 4.06, is determined in accordance with the chart in section 12.02. The applicable fee for a VCP submission that contains only nonamender failures is reduced by 50% if it is submitted within a one-year period following the expiration of the plan's remedial amendment period for complying with such changes. Notwithstanding the above, the compliance fee for a submission that contains only a failure to amend the plan timely with respect to (a) good faith plan amendments for EGTRRA within the period described in Notice 2001–42 including those changes listed in Notice 2005–5, (b) plan amendments for the § 401(a)(9) final and temporary regulations within the period described in Rev. Proc. 2002–29, as modified by Rev. Proc. 2003–10, or (c) interim amendments as provided in section 5 of Rev. Proc. 2005–66 is $375.00.

.04 *VCP fee for Group Submission.* The compliance fee for a Group Submission is based on the number of plans affected by the failure as described in the compliance statement. The initial fee for the first 20 plans is $10,000. An additional fee is due equal to the product of the number of plans in excess of 20 multiplied by $250. The maximum compliance fee for a Group Submission is $50,000. If more than one master or prototype plan is submitted as a Group Submission, each master or prototype plan is considered a separate Group Submission for purposes of the compliance fee.

.05 *VCP fee for SEPs and SIMPLE IRA Plans.* (1) In general, the compliance fee for a SEP or a SIMPLE IRA Plan submission (including an Anonymous Submission) is $250. Notwithstanding the preceding sentence, the Service reserves the right to impose the fee schedule under section 12.02 or section 12.06 in appropriate circumstances.

(2) In any case in which a SEP or SIMPLE IRA Plan correction is not similar to a correction for a similar Qualification Failure (as provided under section 6.10(1)), the Service may impose an additional fee. If the failure involves an Excess Amount to a SEP or a SIMPLE IRA Plan and the Plan Sponsor retains the Excess Amount in the SEP or SIMPLE IRA Plan, a fee equal to at least 10 percent of the Excess Amount excluding earnings will be imposed. This is in addition to the SEP or SIMPLE IRA Plan compliance fee set forth in section 12.05(1).

.06 *VCP fee for egregious failures.* Notwithstanding the preceding provisions of this section 12, in cases involving failures that are egregious (as described in section 4.08), the compliance fee for Qualified Plans, 403(b) Plans, SEPs and SIMPLE IRA Plans is the greater of (1) the fee that would be determined under the preceding provisions of this section 12, or (2) an amount equal to a negotiated percentage of the Maximum Payment Amount, such percentage not to exceed 40 percent.

.07 *Establishing the number of plan participants.* Compliance fees under this section 12 are determined based on the total number of plan participants. For a description of participant, see the Instructions for Form 5500, lines 6 and 7. For new plans and ongoing plans, the number of plan participants is determined from the most recently filed Form 5500 series. Thus, with respect to the 2004 Form 5500, the Plan Sponsor would use the number shown in item 7f (or the equivalent item on the Form 5500 C/R or EZ) to establish the total number of plan participants. In the case of a terminated plan, the Form 5500 used to determine the number of plan participants must be the one filed for the plan year prior to the plan year for which the Final Form 5500 return was filed. If the submission involves a plan with Transferred Assets and no new incidents of the failure occurred after the end of the second plan year that begins after the corporate merger, acquisition, or other similar employer transaction, the Plan Sponsor may calculate the number of plan participants based on the Form 5500 information that would have been filed by the Plan Sponsor for the plan year that includes the employer transaction if the Transferred Assets were maintained as a separate plan.

PART VI. CORRECTION ON AUDIT (AUDIT CAP)

SECTION 13. DESCRIPTION OF AUDIT CAP

.01 *Audit CAP requirements.* If the Service identifies a Qualification or 403(b) Failure (other than a failure that has been corrected in accordance with SCP or VCP) upon an Employee Plans or Exempt Organizations examination of a Qualified Plan, 403(b) Plan, SEP, or SIMPLE IRA Plan, the requirements of this section 13 are satisfied with respect to the failure if the Plan Sponsor corrects the failure, pays a sanction in accordance with section 14, satisfies any additional requirements of section 13.03, and enters into a closing agreement with the Service.

.02 *Payment of sanction.* Payment of the sanction under section 14 generally is required at the time the closing agreement is signed. All sanction amounts should be submitted by certified check or cashier's check made payable to the U.S. Treasury.

.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. If existing administrative procedures are inadequate for operating the plan in conformance with the applicable requirements of the Code, the closing agreement may be conditioned upon the implementation of stated procedures. In addition, for Qualified Plans, pursuant to section 4.06, the Plan Sponsor may be required to obtain a Favorable Letter before the closing agreement is signed. If a Favorable Letter is required, the Plan Sponsor is 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 or, in the case of a 403(b) Plan, SEP, or SIMPLE IRA Plan will not have reliance on this revenue procedure.

.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 Internal Revenue Manual ("IRM") 7.2.2, EPCRS.

SECTION 14. AUDIT CAP SANCTION

.01 *Determination of sanction.* Except as otherwise provided in section 14.04, 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, based on the factors below.

.02 *Factors considered.* Factors include: (1) the steps taken by the Plan Sponsor to ensure that the plan had no failures; (2) the steps taken to identify failures that may have occurred; (3) the extent to which correction had progressed before the examination was initiated, including full correction; (4) the number and type of employees affected by the failure; (5) the number of nonhighly compensated employees who would be adversely affected if the plan were not treated as qualified or as satisfying the requirements of § 403(b), § 408(k) or § 408(p); (6) whether the failure is a failure to satisfy the requirements of § 401(a)(4), § 401(a)(26), or § 410(b), either directly or through § 403(b)(12); (7) the period over which the failure(s) 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 (8) the reason for the failure(s) (for example, data errors such as errors in transcription of data, the transposition of numbers, or minor arithmetic errors). Factors relating only to Qualified Plans also include: (1) whether the plan is the subject of a Favorable Letter; (2) whether the plan has both Operational and other failures; (3) the extent to which the plan has accepted Transferred Assets, and the extent to which the failure(s) relate to Transferred Assets and occurred before the transfer; and (4) whether the failure(s) were discovered during the determination letter process. If one of the failures discovered during an Employee Plans examination includes the failure to amend the plan timely for relevant legislation, it is expected that the sanction will be greater than the applicable fee described in section 14.04. Additional factors relating only to 403(b) Plans include: (1) whether the plan has a combination of Operational, Demographic, or Employer Eligibility Failures; (2) the extent to which the failure relates to Excess Amounts; and (3) whether the failure is solely an Employer Eligibility Failure.

.03 *Transferred Assets.* If the examination involves a plan with Transferred Assets and the Service determines that no new incidents of the failures that relate to the Transferred Assets occur after the end of the second plan year that begins after the corporate merger, acquisition, or other similar employer transaction, the sanction under Audit CAP will not exceed the sanction that would apply if the Transferred Assets were maintained as a separate plan.

.04 *Fee for nonamenders discovered during the determination letter application process not related to a VCP submission.* (1) The compliance fee for nonamenders (as defined in section 4.06) not voluntarily identified by the Plan Sponsor, but instead discovered by the Service in connection with the determination letter application process as described in section 5.03(3) is determined in accordance with the chart below. This fee schedule applies if the only failure in the submission is the nonamender failure.

(2) The acronyms listed in the chart refer to the following laws:

(a) Employee Retirement Income Security Act of 1974 (ERISA),

(b) Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA); Deficit Reduction Act of 1984 (DEFRA); and Retirement Equity Act of 1984 (REA) together (T/D/R),

(c) Tax Reform Act of 1986 (TRA '86),

(d) Unemployment Compensation Act of 1992 (UCA); Omnibus Budget and Reconciliation Act of 1993 (OBRA '93),

(e) The Uruguay Round Agreements Act; the Uniformed Services Employment and Reemployment Rights Act of 1994; the Small Business Job Protection Act of 1996; the Taxpayer Relief Act of 1997; the Internal Revenue Service Restructuring and Reform Act of 1998; and the Community Renewal Tax Relief Act of 2000 (collectively known as "GUST"),

(f) Final and temporary regulations under § 401(a)(9), 74 FR 18987, published on April 17, 2002 ("401(a)(9) Regs"),

(g) The Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA").

Number of Participants	EGTRRA/ subsequent legislation	GUST/ 401(a)(9) Regs	UCA/ OBRA '93	TRA '86	T/D/R	ERISA
20 or less	$ 2,500	$ 3,000	$ 3,500	$ 4,000	$ 4,500	$ 5,000
21–50	$ 5,000	$ 6,000	$ 7,000	$ 8,000	$ 9,000	$10,000
51–100	$ 7,500	$ 9,000	$10,500	$12,000	$13,500	$15,000
101–500	$12,500	$15,000	$17,500	$20,000	$22,500	$25,000
501–1,000	$17,500	$21,000	$24,500	$28,000	$31,500	$35,000
1,001–5,000	$25,000	$30,000	$35,000	$40,000	$45,000	$50,000
5,001–10,000	$32,500	$39,000	$45,500	$52,000	$58,500	$65,000
Over 10,000	$40,000	$48,000	$56,000	$64,000	$72,000	$80,000

PART VII. EFFECT ON OTHER DOCUMENTS; EFFECTIVE DATE; PAPERWORK REDUCTION ACT

SECTION 15. EFFECT ON OTHER DOCUMENTS

.01 *Rev. Proc. 2003–44 modified and superseded.* Rev. Proc. 2003–44 is modified and superseded by this revenue procedure.

SECTION 16. EFFECTIVE DATE

This revenue procedure is generally effective September 1, 2006. However, (1) sections 11.11, 11.14, and 14.04 are effective on or after May 30, 2006, and (2) plan sponsors are permitted, at their option, to apply the provisions of this revenue procedure on or after May 30, 2006.

Specifically, except in the case of (1) above and unless a plan sponsor applies the provisions of this revenue procedure earlier, this revenue procedure is effective:

(a) with respect to SCP, for failures for which correction is not complete before September 1, 2006;

(b) with respect to VCP, for applications submitted on or after September 1, 2006; and

(c) with respect to Audit CAP, for examinations begun on or after September 1, 2006.

SECTION 17. 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 1545–1673.

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 OMB control number.

The collection of information in this revenue procedure is in sections 4.05, 6.02(5)(d), 6.05, 10.01, 10.02, 10.05–.07, 10.10–10.12, 11.02–11.04, 11.06–11.14, 13.01, section 2.01–2.07 of Appendix B, Appendix C, and Appendix E. This information is required to enable the Commissioner, Tax Exempt and Government Entities Division 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 and tax-deferred 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, businesses or other for-profit institutions, nonprofit institutions, and small businesses or organizations.

The estimated total annual reporting or recordkeeping burden is 76,222 hours.

The estimated annual burden per respondent/recordkeeper varies from .5 to 45.5 hours, depending on individual circumstances, with an estimated average of 20.4 hours. The estimated number of respondents or recordkeepers is 3,745.

The estimated frequency of responses is occasional.

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 authors of this revenue procedure are Avaneesh Bhagat and Louis Leslie of the Tax Exempt and Government Entities Division. For further information concerning this revenue procedure, please contact the Employee Plans' taxpayer assistance telephone service at 1–877–829–5500 between 8:30 a.m. and 6:30 p.m., Eastern Time, Monday through Friday (a toll-free number). Mr. Bhagat and Mr. Leslie may be reached at (202) 283–9888 (not a toll-free number).

APPENDIX A

OPERATIONAL FAILURES AND CORRECTION METHODS

.01 *General rule.* This appendix sets forth Operational Failures and Correction Methods relating to Qualified Plans. 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(4) of Rev. Proc. 2006–27. The correction methods in this appendix are acceptable under SCP and VCP. Additionally, the correction methods and the earnings adjustment methods in Appendix B are acceptable under SCP and VCP. To the extent a failure listed in this appendix could occur under a 403(b) Plan, a SEP or a SIMPLE IRA Plan, the correction method listed for such failure may be used to correct the failure.

.02 *Failure to properly provide the minimum top-heavy benefit under § 416 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, for plan years beginning on or before December 31, 2001, 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)–6 and formerly in § 1.401(k)–1(g)(13)(ii)) 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 be the same percentage of compensation. QNCs contributed to satisfy the ADP test need not be taken into account for determining additional contributions (*e.g.*, a matching contribution), if any. 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 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 correction method, the plan may not be restructured into component plans 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 in 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.* (1) For plans with employer provided contributions or benefits (which are neither elective contributions under a qualified cash or deferred arrangement under § 401(k) nor matching or after-tax employee contributions that are subject to § 401(m)), 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.

(2) For plans providing benefits subject to § 401(k) or § 401(m), the corrective contribution for an improperly excluded employee is described in the following paragraphs. (See examples 3 through 10 of Appendix B.)

(a) If the employee was not provided the opportunity to elect and make elective deferrals (other than designated Roth contributions) to a 401(k) plan that does not satisfy the safe harbor contribution requirements of section 401(k)(12), the employer must make a QNC to the plan on behalf of the employee that compensates for the "missed deferral opportunity." The missed deferral opportunity is equal to 50% of the employee's "missed deferral." The missed deferral is determined by multiplying the actual deferral percentage for the employee's group in the plan (either highly compensated or nonhighly compensated) for the year of exclusion by the employee's compensation for that year. The employee's missed deferral amount is reduced further to the extent necessary to ensure that the missed deferral does not exceed applicable plan limits, including the annual deferral limit under § 402(g) for the calendar year in which the failure occurred. Under this 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 applicable ADP, the corresponding missed deferral and the required QNC. Likewise, restructuring the plan into component plans is not permitted in order to reduce the applicable ADP, the corresponding missed deferral and the required QNC. The QNC required to compensate the employee for the missed deferral opportunity for the year of exclusion is adjusted for earnings until the corrective QNC is made on behalf of the affected employee.

(b) If the employee should have been eligible for but did not receive an allocation of employer matching contributions under a non-safe harbor plan because he or she was not given the opportunity to make elective deferrals, the employer should make a QNC on behalf of the affected employee. The QNC will be equal to the matching contribution the employee would have received had the employee made a deferral equal to the missed deferral determined under section .05(2)(a) of this Appendix A. The QNC must be adjusted for earnings until the corrective QNC is made on behalf of the affected employee.

(c) If the employee was not provided the opportunity to elect and make elective deferrals (other than designated Roth contributions) to a safe harbor 401(k) plan that uses a rate of matching contributions to satisfy the safe harbor requirements of § 401(k)(12), then the missed deferral is deemed equal to the greater of 3% of compensation or the maximum deferral percentage for which the employer provides a matching contribution rate that is at least as favorable as 100% of the elective deferral made by the employee. This estimate of the missed deferral replaces the estimate based on the ADP test in a traditional 401(k) plan. The required QNC on behalf of the excluded employee is equal to (i) the missed deferral opportunity, which is an amount equal to 50% of the missed deferral, plus (ii) the matching contribution that would apply based on the missed deferral. If an employee was not provided the opportunity to elect and make elective deferrals to a safe harbor 401(k) plan that uses nonelective contributions to satisfy the safe harbor requirements of § 401(k)(12), then the missed deferral is deemed equal to 3% of compensation. The required QNC on behalf of the excluded employee is equal to (i) 50% of the missed deferral, plus (ii) the nonelective contribution required to be made on behalf of the employee. The QNC required to compensate the employee for the missed deferral opportunity and the corresponding matching or nonelective contribution is adjusted for earnings until the corrective QNC is made on behalf of the affected employee.

(d) If the employee should have been eligible to elect and make after-tax employee contributions (other than designated Roth contributions), the employer must make a QNC to the plan on behalf of the employee that is equal to the "missed opportunity for making after-tax employee contributions." The missed opportunity for making after-tax employee contributions is equal to 40% of the employee's "missed after-tax contributions." The employee's missed after-tax contributions are equal to the actual contribution percentage (ACP) for the employee's group (either highly compensated or nonhighly compensated) times the employee's compensation, but with the resulting amount not to exceed applicable plan limits. If the ACP consists of both matching and after-tax employee contributions, then, in lieu of basing the employee's missed after-tax employee contributions on the ACP for the employee's group, the employer is permitted to determine separately the portion of the ACP that is attributable to after-tax employee contributions for the employee's group (either highly compensated or nonhighly compensated), multiplied by the employee's compensation for the year of exclusion. The QNC also must be adjusted for earnings until the corrective QNC is made on behalf of the affected employee.

(e) If the employee was improperly excluded from an allocation of employer matching contributions because he or she was not given the opportunity to make after-tax employee contributions (other than designated Roth contributions), the employer should make a QNC on behalf

of the affected employee. The QNC is equal to the matching contribution the employee would have received had the employee made an after-tax employee contribution equal to the missed after-tax employee contribution determined under section .05(2)(d).

(f) The methods for correcting the failures described in this section .05(2) do not apply until after the correction of other qualification failures. Thus, for example, if in addition to the failure of excluding an eligible employee, the plan also failed the ADP or ACP test, the correction methods described in section .05(2)(a) through (e) cannot be used until after correction of the ADP or ACP test failures.

.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 distribution period. For this purpose, adjusted account balance means the actual account balance, determined in accordance with § 1.401(a)(9)–5 Q&A–3 of the 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 or spousal consent for a distribution subject to the participant and spousal consent rules under §§ 401(a)(11), 411(a)(11), and 417.* (1) 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 the event that participant 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 for the spouse's life beginning 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.

(2) An alternative permitted correction method is to give each affected participant a choice between (i) providing informed consent for the distribution actually made, (ii) receiving a qualified joint and survivor annuity (both (i) and (ii) of this section .07(2) are as described in section .07(1) of this Appendix A), or (iii) a single-sum payment equal to the actuarial present value of that survivor annuity benefit (calculated using the applicable interest rate and mortality table under § 417(e)(3)). For example, if the actuarial present value of a $300 per month annuity payable to the spouse for the spouse's life beginning upon the participant's death is $7,837 (calculated using the applicable interest rate and mortality table under § 417(e)(3), and based on the assumptions that the participant is age 65, that the spouse is age 62, and that the applicable interest rate is 6%), then the single-sum payment under clause (iii) of this section .07(2) is equal to $7,837. If the spouse elects to receive the single-sum payment, then the payment is treated in the same manner as a distribution under § 402(c)(9) for purposes of rolling over the payment to an IRA or other eligible retirement plan.

.08 *Failure to satisfy the § 415 limits in a defined contribution plan.* The permitted correction for failure to limit annual additions (other than elective deferrals and after-tax employee contributions) allocated to participants in a defined contribution plan as required in § 415 (even if the excess 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 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 after-tax employee contributions that could be made with respect to an individual under the § 415 limits) is to distribute the elective deferrals or after-tax employee contributions using a method similar to that described under § 1.415–6(b)(6)(iv). Elective deferrals and after-tax 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.

APPENDIX B

CORRECTION METHODS AND EXAMPLES; EARNINGS ADJUSTMENT METHODS AND EXAMPLES

SECTION 1. PURPOSE, ASSUMPTIONS FOR EXAMPLES AND SECTION REFERENCES

.01 *Purpose.* (1) This appendix sets forth correction methods relating to Operational Failures under Qualified Plans. This appendix also sets forth earnings adjustment methods. The correction methods and earnings adjustment methods described in this appendix are acceptable under SCP and VCP.

(2) To the extent a failure listed in this appendix could occur under a 403(b) Plan, SEP, or a SIMPLE IRA Plan, the correction method listed for such failure may be used to correct the failure.

.02 *Assumptions for Examples.* Unless otherwise specified, for ease of presentation, the examples assume that:

(1) the plan year and the § 415 limitation year are the calendar year;

(2) the employer maintains a single plan intended to satisfy § 401(a) and has never maintained any other plan;

(3) in a defined contribution plan, the plan provides that forfeitures are used to reduce future employer contributions;

(4) the Qualification Failures are Operational Failures and the eligibility and other requirements for SCP, VCP or Audit CAP, whichever applies, are satisfied; and

(5) there are no Qualification Failures other than the described Operational Failures, and if a corrective action would result in any additional Qualification Failure, appropriate corrective action is taken for that additional Qualification Failure in accordance with EPCRS.

.03 *Section references.* References to section 2 and section 3 are references to the section 2 and 3 in this appendix.

SECTION 2. CORRECTION METHODS AND EXAMPLES

.01 *ADP/ACP Failures.*

(1) Correction Methods. (a) Appendix A Correction Method. Appendix A, section .03 sets forth a correction method for a failure to satisfy the actual deferral percentage ("ADP"), actual contribution percentage ("ACP"), or, for plan years beginning on or before December 31, 2001, multiple use test set forth in §§ 401(k)(3), 401(m)(2), and 401(m)(9), respectively.

(b) One-to-One Correction Method. (i) General. In addition to the correction method in Appendix A, a failure to satisfy the ADP test, ACP test, or, for plan years beginning on or before December 31, 2001, the multiple use test may be corrected by using the one-to-one correction method set forth in this section 2.01(1)(b). Under the one-to-one correction method, an excess contribution amount is determined and assigned to highly compensated employees as provided in paragraph (1)(b)(ii) below. That excess contribution amount (adjusted for earnings) is either distributed to the highly compensated employees or forfeited from the highly compensated employees' accounts as provided in paragraph (1)(b)(iii) below. That same dollar amount (*i.e.*, the excess contribution amount, adjusted for earnings) is contributed to the plan and allocated to nonhighly compensated employees as provided in paragraph (1)(b)(iv) below. Under this 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)). Likewise, restructuring the plan into component plans is not permitted.

(ii) Determination of the Excess Contribution Amount. The excess contribution amount for the year is equal to the excess of (A) the sum of the excess contributions (as defined in § 401(k)(8)(B)), the excess aggregate contributions (as defined in § 401(m)(6)(B)), and for plan years beginning on or before December 31, 2001 the amount treated as excess contributions or excess aggregate contributions under the multiple use test for the year, as assigned to each highly compensated employee in accordance with § 401(k)(8)(C) and (m)(6)(C), over (B) previous corrections that complied with § 401(k)(8), (m)(6), and, for plan years beginning on or before December 31, 2001, the multiple use test.

(iii) Distributions and Forfeitures of the Excess Contribution Amount. (A) The portion of the excess contribution amount assigned to a particular highly compensated employee under paragraph (1)(b)(ii) is adjusted for earnings through the date of correction. The amount assigned to a particular highly compensated employee, as adjusted, is distributed or, to the extent the amount was forfeitable as of the close of the plan year of the failure, is forfeited. If the amount is forfeited, it is used in accordance with the plan provisions relating to forfeitures that were in effect for the year of the failure. If the amount so assigned to a particular highly compensated employee has been previously distributed, the amount is an Excess Amount within the meaning of section 5.01(3) of this revenue procedure. Thus, pursuant to section 6.05 of this revenue procedure, the employer must notify the employee that the Excess Amount was not eligible for favorable tax treatment accorded to distributions from qualified plans (and, specifically, was not eligible for tax-free rollover).

(B) If any matching contributions (adjusted for earnings) are forfeited in accordance with § 411(a)(3)(G), the forfeited amount is used in accordance with the plan provisions relating to forfeitures that were in effect for the year of the failure.

(C) If a payment was made to an employee and that payment is a forfeitable match described in either paragraph (1)(b)(iii)(A) or (B), then it is an Overpayment defined in section 5.01(6) of this revenue procedure that must be corrected (see sections 2.04 and 2.05 below).

(iv) Contribution and Allocation of Equivalent Amount. (A) The employer makes a contribution to the plan that is equal to the aggregate amounts distributed and forfeited under paragraph (1)(b)(iii)(A) (*i.e.*, the excess contribution amount adjusted for earnings, as provided in paragraph (1)(b)(iii)(A), which does not include any matching contributions forfeited in accordance with § 411(a)(3)(G) as provided in paragraph (1)(b)(iii)(B)). The contribution must satisfy the vesting requirements and distribution limitations of § 401(k)(2)(B) and (C).

(B)(1) This paragraph (1)(b)(iv)(B)(*1*) applies to a plan that uses the current year testing method described in § 1.401(k)–2(a)(2), § 1.401(m)–2(a)(2) and, for periods prior to the effective date of those regulations, Notice 98–1, 1998–1 C.B. 327. The contribution made under paragraph (1)(b)(iv)(A) is allocated to the account balances of those individuals who were either (I) the eligible employees for the year of the failure who were not highly compensated employees for that year or (II) the eligible employees for the year of the failure who were not highly compensated employees for that year and who also are not highly compensated employees for the year of correction. Alternatively, the contribution is allocated to account balances of eligible employees described in (I) or (II) of the preceding sentence, except that the allocation is made only to the account balances of those employees who are employees on a date during the year of the correction that is no later than the date of correction. Regardless of which of these four options (described in the two preceding sentences) the employer selects, eligible employees must receive a uniform allocation (as a percentage of compensation) of the contribution. (See Examples 1 and 2.) Under the one-to-one correction method, the amount allocated to the account balance of an employee (*i.e.*, the employee's share of the total amount contributed under paragraph (1)(b)(iv)(A)) is

not further adjusted for earnings and is treated as an annual addition under § 415 for the year of the failure for the employee for whom it is allocated.

(2) This paragraph (1)(b)(iv)(B)(2) applies to a plan that uses the prior year testing method described in § 1.401(k)–2(a)(2), § 1.401(m)–2(a)(2) and, for periods prior to the effective date of those regulations, Notice 98–1. Paragraph (1)(b)(iv)(B)(*1*) is applied by substituting "the year prior to the year of the failure" for "the year of the failure".

(2) Examples.

Example 1:

Employer A maintains a profit-sharing plan with a cash or deferred arrangement that is intended to satisfy § 401(k) using the current year testing method The plan does not provide for matching contributions or employee after-tax contributions. In 2005, it was discovered that the ADP test for 2003 was not performed correctly. When the ADP test was performed correctly, the test was not satisfied for 2003 For 2003, the ADP for highly compensated employees was 9% and the ADP for nonhighly compensated employees was 4%.

Accordingly, the ADP for highly compensated employees exceeded the ADP for nonhighly compensated employees by more than two percentage points (in violation of § 401(k)(3)). There were two highly compensated employees eligible under the 401(k) plan during 2003, Employee P and Employee Q. Employee P made elective deferrals of $10,000, which is equal to 10% of Employee P's compensation of $100,000 for 2003. Employee Q made elective deferrals of $9,500, which is equal to 8% of Employee Q's compensation of $118,750 for 2003.

Correction:

On June 30, 2005, Employer A uses the one-to-one correction method to correct the failure to satisfy the ADP test for 2003. Accordingly, Employer A calculates the dollar amount of the excess contributions for the two highly compensated employees in the manner described in § 401(k)(8)(B). The amount of the excess contribution for Employee P is $4,000 (4% of $100,000) and the amount of the excess contribution for Employee Q is $2,375 (2% of $118,750), or a total of $6,375. In accordance with § 401(k)(8)(C), $6,375, the excess contribution amount, is assigned $3,437.50 to Employee P and $2,937.50 to Employee Q. It is determined that the earnings on the assigned amounts through June 30, 2005 are $687 and $587 for Employees P and Q, respectively. The assigned amounts and the earnings are distributed to Employees P and Q Therefore, Employee P receives $4,124.50 ($3,437.50 + $687) and Employee Q receives $3,524.50 ($2,937 50 + $587). In addition, on the same date, Employer A makes a corrective contribution to the 401(k) plan equal to $7,649 (the sum of the $4,124.50 distributed to Employee P and the $3,524.50 distributed to Employee Q). The corrective contribution is allocated to the account balances of eligible nonhighly compensated employees for 2003, *pro rata* based on their compensation for 2003 (subject to § 415 for 2003)

Example 2:

The facts are the same as in *Example 1*, except that for 2003 the plan also provides for (1) after-tax employee contributions and (2) matching contributions equal to 50% of the sum of an employee's elective deferrals and after-tax employee contributions that do not exceed 10% of the employee's compensation. The plan provides that matching contributions are subject to the plan's 20% per year of service vesting schedule and that matching contributions are forfeited and used to reduce employer contributions if associated elective deferrals or employee after-tax contributions are distributed to correct an ADP or ACP test failure. For 2003, nonhighly compensated employees made after-tax employee contributions and no highly compensated employee made any after-tax employee contributions. Employee P received a matching contribution of $5,000 (50% of $10,000) and Employee Q received a matching contribution of $4,750 (50% of $9,500). Employees P and Q were 100% vested in 2003. It was determined that the plan satisfied the requirements of the ACP test for 2003.

Correction

The same corrective actions are taken as in *Example 1*. In addition, in accordance with the plan's terms, corrective action is taken to forfeit Employee P's and Employee Q's matching contributions associated with their distributed excess contributions. Employee P's distributed excess contributions and associated matching contributions are $3,437.50 and $1,718 75, respectively Employee Q's distributed excess contributions and associated matching contributions are $2,937.50 and $1,468.75, respectively. Thus, $1,718 75 is forfeited from Employee P's account and $1,468.75 is forfeited from Employee Q's account. In addition, the earnings on the forfeited amounts are also forfeited. It is determined that the respective earnings on the forfeited amount for Employee P is $250 and for Employee Q is $220. The total amount of the forfeitures of $3,657 50 (Employee P's $1,718.75 + $250 and Employee Q's $1,468.75 + $220) is used to reduce contributions for 2005 and subsequent years.

.02 *Exclusion of Otherwise Eligible Employees.*

(1) Exclusion of Eligible Employees in a 401(k) or (m) Plan. (a) Correction Method. (i) Appendix A Correction Method for Full Year Exclusion. Appendix A, section .05 sets forth the correction method for the exclusion of an eligible employee from electing and making elective deferrals (other than designated Roth contributions) and after-tax employee contributions (other than designated Roth contributions) to a plan that provides benefits that are subject to the requirements of § 401(k) or (m) for one or more full plan years. (See Example 3.) Appendix A section .05 also specifies the method for determining missed deferrals and the corrective contributions for employees who were improperly excluded from electing and making elective deferrals to a safe harbor 401(k) plan for one or more full plan years. (See Examples 8, 9 and 10.) In section 2.02(1)(a)(ii) below, the correction method for the exclusion of an eligible employee from all contributions (other than designated Roth contributions) under a 401(k) or (m) plan for a full year is expanded to include correction for the exclusion of an eligible employee from all contributions (other than designated Roth contributions) under a 401(k) or (m) plan for a partial plan year. This correction for a partial year exclusion may be used in conjunction with the correction for a full year exclusion.

(ii) Expansion of Correction Method to Partial Year Exclusion. (A) In General. The correction method in Appendix A, section .05 is expanded to cover an employee who was improperly excluded from electing and making elective deferrals (other than designated Roth contributions) or after-tax employee contributions (other than designated Roth contributions) for a portion of a plan year or from receiving matching contributions (on either elective deferrals or after-tax employee contributions) for a portion of a plan year. In such case, a permitted correction method for the failure is for the employer to satisfy this section 2.02(1)(a)(ii). The employer makes a corrective contribution on behalf of the excluded employee that satisfies the vesting requirements and distribution limitations of § 401(k)(2)(B) and (C). The method and examples described to correct the failure to include otherwise eligible employees do not apply until after correction of other qualification failures. Thus, for example, the corrections described in the narrative and examples in this section cannot be used until after correction of ADP or ACP test failures.

(B) Elective Deferral Failures. The appropriate corrective contribution for the failure to allow an employee to elect and make elective deferrals (other than designated Roth contributions) for a portion of the plan year is equal to the missed deferral opportunity which is an amount equal to 50% of the employee's missed deferral. The employee's missed deferral is determined by multiplying the ADP of the employee's group (either highly or nonhighly compensated), determined prior to correction under this section 2.02(1)(a)(ii), by the employee's plan compensation for the

portion of the year during which the employee was improperly excluded. In a safe harbor 401(k) plan, the employee's missed deferral is determined by multiplying 3% (or, if greater, whatever percentage of the participant's compensation which, if contributed as an elective deferral, would have been matched at a rate of 100% or more) by the employee's plan compensation for the portion of the year during which the employee was improperly excluded. The corrective contribution for the portion of the plan year during which the employee was improperly excluded from being eligible to make elective deferrals is reduced to the extent that (*1*) the sum of the missed deferral and any elective deferrals actually made by the employee for that year would exceed (2) the maximum elective deferrals permitted under the plan for the employee for that plan year (including the § 402(g) limit). The corrective contribution is adjusted for earnings. For purposes of correcting other failures under this revenue procedure (including determination of any required matching contribution) after correction has occurred under this section 2.02(1)(ii)(B), the employee is treated as having made pre-tax elective deferrals equal to the employee's missed deferral for the portion of the year during which the employee was improperly excluded. (See Examples 4 and 5.)

(C) After-tax Employee Contribution Failures. The appropriate corrective contribution for the failure to allow employees to elect and make after-tax employee contributions for a portion of the plan year is equal to the missed after-tax employee contributions opportunity, which is an amount equal to 40% of the employee's missed after-tax employee contributions. The employee's missed after-tax employee contributions is determined by multiplying the ACP of the employee's group (either highly or nonhighly compensated), determined prior to correction under this section 2.02(1)(a)(ii)(C), by the employee's plan compensation for the portion of the year during which the employee was improperly excluded. If the ACP consists of both matching and after-tax employee contributions, then for purposes of the preceding sentence, in lieu of basing the missed after-tax employee contributions on the ACP for the employee's group (either highly compensated or nonhighly compensated), the employer is permitted to determine separately the portions of the ACP that are attributable to matching contributions and after-tax employee contributions and base the missed after-tax employee contributions on the portion of the ACP that is attributable to after-tax employee contributions. The missed after-tax employee contribution is reduced to the extent that (*1*) the sum of that contribution and the actual total after-tax employee contributions made by the employee for the plan year would exceed (2) the sum of the maximum after-tax employee contributions permitted under the plan for the employee for the plan year. The corrective contribution is adjusted for earnings.

(D) Matching Contribution Failures. The appropriate corrective contribution for the failure to make matching contributions for an employee because the employee was precluded from making elective deferrals (other than designated Roth contributions) or after-tax employee contributions for a portion of the plan year is equal to the matching contribution that would have been made for the employee if (1) the employee's elective deferrals for that portion of the plan year had equaled the employee's missed deferrals (determined under section 2.02(1)(a)(i)(B)) or (2) the employee's after-tax contribution for that portion of the plan year had equaled the employee's missed after-tax employee contribution (determined under section 2.02(1)(a)(ii)(C). This matching contribution is reduced to the extent that (1) the sum of this contribution and other matching contributions actually made on behalf of the employee for the plan year would exceed (2) the maximum matching contribution permitted if the employee had made the maximum matchable contributions permitted under the plan for the plan year. The corrective contribution is adjusted for earnings.

(E) Use of Prorated Compensation. For purposes of this paragraph (1)(a)(ii), for administrative convenience, in lieu of using the employee's actual plan compensation for the portion of the year during which the employee was improperly excluded, a *pro rata* portion of the employee's plan compensation that would have been taken into account for the plan year, if the employee had not been improperly excluded, may be used.

(F) Special Rule for Brief Exclusion from Elective Deferrals and After-Tax Employee Contributions. An employer is not required to make a corrective contribution with respect to elective deferrals or after-tax employee contributions, as provided in sections 2.02(1)(a)(ii)(B) and (C), (but is required to make a corrective contribution with respect to any matching contributions, as provided in section 2.02(1)(a)(ii)(D)) for an employee for a plan year if the employee has been provided the opportunity to make elective deferrals or after-tax employee contributions under the plan for a period of at least the last 9 months in that plan year and during that period the employee had the opportunity to make elective deferrals or after-tax employee contributions in an amount not less than the maximum amount that would have been permitted if no failure had occurred. (See Examples 6 and 7.)

(b) Examples.

Example 3.

Employer B maintains a 401(k) plan. The plan provides for matching contributions for eligible employees equal to 100% of elective deferrals that do not exceed 3% of an employee's compensation. The plan allows employees to make after-tax employee contributions up to a maximum of the lesser of 2% of compensation or $1,000. The after-tax employee contributions are not matched. The plan provides that employees who complete one year of service are eligible to participate in the plan on the next designated entry date. The entry dates are January 1, and July 1. In 2005, it is discovered that Employee V, a NHCE with compensation of $30,000, was excluded from the plan for the 2003 plan year even though she satisfied the plan's eligibility requirements as of January 1, 2003.

For the 2003 plan year, the relevant employee and contribution information is as follows

	Compensation	*Elective deferral*	*Match*	*After-Tax Employee Contribution*
Highly Compensated Employees (HCEs):				
R	$200,000	$ 6,000	$6,000	0
S	$150,000	$12,000	$4,500	$1,000
Nonhighly Compensated Employees (NHCEs):				
T	$80,000	$12,000	$2,400	$1,000
U	$50,000	$ 500	$ 500	0

HCEs:

ADP - 5.5%
ACP - 3.33%
ACP attributable to matching contributions - 3%
ACP attributable to after-tax employee contributions - 0.33%

NHCEs:

ADP - 8%
ACP - 2.63%
ACP attributable to matching contributions - 2%
ACP attributable to after-tax employee contributions - 0.63%

Correction:

Employer B uses the correction method for a full year exclusion, described in Appendix A section 05, to correct the failure to include Employee V in the plan for the full plan year beginning January 1, 2003. Employer B calculates the corrective QNC to be made on behalf of Employee V as follows:

Elective deferrals. Employee V was eligible to, but was not provided with the opportunity to, elect and make elective deferrals in 2003. Thus, Employer B must make a QNC to the plan on behalf of Employee V equal to the missed deferral opportunity for Employee V - 50% of Employee V's missed deferral. The QNC is adjusted for earnings. The missed deferral for Employee V is estimated by using the ADP for NHCEs for 2003 and multiplying that percentage by Employee V's compensation for 2003. Accordingly, the missed deferral for Employee V, on account of the employee's improper exclusion from the plan is $2,400 (8% x $30,000). The missed deferral opportunity is $1,200 (*i.e.*, 50% x $2,400). Thus, the required corrective contribution for the failure to provide Employee V with the opportunity to make elective deferrals to the plan is $1,200 (plus earnings).

Matching contributions. Employee V should have been eligible for, but did not receive an allocation of, employer matching contributions because Employee V was not provided the opportunity to make elective deferrals in 2003. Thus, Employer B must make a QNC to the plan on behalf of Employee V that is equal to the matching contribution Employee V would have received had the missed deferral been made. The QNC is adjusted for earnings. Under the terms of the plan, if Employee V had made an elective deferral of $2,400 or 8% of compensation ($30,000), the employee would have been entitled to a matching contribution equal to 100% of first 3% of Employee V's compensation ($30,000) or $900. Accordingly, the contribution required to replace the missed employer matching contribution is $900 (plus earnings).

After-tax employee contributions: Employee V was eligible to, but was not provided with the opportunity to, elect and make after-tax employee contributions in 2003. Employer B must make a QNC to the plan equal to the missed opportunity for making after-tax employee contributions for Employee V - 40% of Employee V's missed after-tax employee contribution. The QNC is adjusted for earnings. The missed after-tax employee contribution for Employee V is estimated by using the ACP for NHCEs (to the extent that the ACP is attributable to after-tax employee contributions) for 2003 and multiplying that percentage by Employee V's compensation for 2003. Accordingly, the missed after-tax employee contribution for Employee V, on account of the employee's improper exclusion from the plan is $189 (0.63% x $30,000). The missed opportunity to make after-tax employee contributions to the plan is $76 (40% x $189). Thus, the required corrective contribution for the failure to provide Employee V with the opportunity to make the $189 after-tax employee contribution to the plan is $76 (plus earnings).

The total required corrective QNC, before adjustments for earnings, on behalf of Employee V is $2,176 ($1,200 for the missed deferral opportunity plus $900 for the missed matching contribution plus $76 for the missed opportunity to make after-tax employee contributions). The required corrective QNC is further adjusted for earnings.

Example 4

Employer C maintains a 401(k) plan. The plan provides for matching contributions for each payroll period that are equal to 100% of an employee's elective deferrals that do not exceed 2% of the eligible employee's plan compensation during the payroll period. The plan provides for after-tax employee contributions. The after-tax employee contribution cannot exceed $1,000 for the plan year. The plan provides that employees who complete one year of service are eligible to participate in the plan on the next January 1 or July 1 entry date. Employee X, a nonhighly compensated employee, who met the eligibility requirements and should have entered the plan on January 1, 2003 was not offered the opportunity to participate in the plan. In August of 2003, the error was discovered and Employer C offered Employee X the opportunity to make elective deferrals and after-tax employee contributions as of September 1, 2003. Employee X made elective deferrals equal to 4% of the employee's plan compensation for each payroll period from September 1, 2003 through December 31, 2003 (resulting in elective deferrals of $400). Employee X's plan compensation for 2003 was $36,000 ($26,000 for the first eight months and $10,000 for the last four months). Employer C made matching contributions equal to $200 on behalf of Employee X, which is 2% of Employee X's plan compensation for each payroll period from September 1, 2003 through December 31, 2003 ($10,000). After being allowed to participate in the plan, Employee X made $250 of after-tax employee contributions for the 2003 plan year. The ADP for nonhighly compensated employees for 2003 was 3% and the ACP for nonhighly compensated employees for 2003 was 2.3%. The ACP attributable to matching contributions for nonhighly compensated employees for 2003 was 1.8%. The ACP attributable to employee contributions for nonhighly compensated employees for 2003 was 0.5%.

Correction:

In accordance with section 2.02(1)(a)(ii), Employer C uses the correction method described in Appendix A section 05 to correct for the failure to provide Employee X the opportunity to elect and make elective deferrals and after-tax employee contributions, and as a result, not receiving matching contributions for a portion of the plan year (January 1, 2003 through August 31, 2003). Thus, Employer C makes a corrective contribution on behalf of Employee X that satisfies the requirements of section 2.02(1)(a)(ii). Employer C elects to utilize the provisions of section 2.02(1)(a)(ii)(E) to determine Employee X's compensation for the portion of the year in which Employee X was not provided the opportunity to make elective deferrals and after-tax employee contributions. Thus, for administrative convenience, in lieu of using actual plan compensation of $26,000 for the period Employee X was excluded, Employee X's annual plan compensation

is prorated for the eight-month period that the employee was excluded from participating in the plan. The corrective contribution is determined as follows.

(1) Corrective contribution for missed deferral Employee X was eligible to, but was not provided with the opportunity to, elect and make elective deferrals from January 1 through August 31 of 2003. Employer C must make a corrective contribution to the plan on behalf of Employee X equal to Employee X's missed deferral opportunity for that period - 50% of Employee X's missed deferral. From January 1 through August 31, 2003. The corrective contribution is adjusted for earnings. Employee X's missed deferral is determined by multiplying the 3% ADP for nonhighly compensated employees by $24,000 (8/12ths of the employee's 2003 compensation of $36,000). Accordingly, the missed deferral is $720. The missed deferral is not reduced because when this amount is added to the amount already deferred, no plan limit (including § 402(g)) was exceeded. Accordingly, the required corrective contribution is $360 (*i.e.*, 50% multiplied by the missed deferral amount of $720) The required corrective contribution is adjusted for earnings.

(2) Corrective contribution for missed matching contribution. Under the terms of the plan, if Employee X had made an elective deferral of $720 or 3% of compensation for the period of exclusion ($24,000), the employee would have been entitled to a matching contribution equal to 2% of $24,000 or $480 The missed matching contribution is not reduced because no plan limit is exceeded when this amount is added to the matching contribution already contributed for the 2003 plan year Accordingly, the required corrective contribution is $480. The required corrective contribution is adjusted for earnings

(3) Corrective contribution for missed after-tax employee contribution: Employee X was eligible to, but was not provided with the opportunity to elect and make after-tax employee contributions from January 1 through August 31 of 2003 Employer C must make a corrective contribution to the plan on behalf of Employee X equal to the missed opportunity to make after-tax employee contributions. The missed opportunity to make after-tax employee contributions is equal to 40% of Employee X's missed after-tax employee contributions. The corrective contribution is adjusted for earnings. The missed after-tax employee contribution amount is equal to the 0.5% ACP attributable to employee contributions for nonhighly compensated employees multiplied by $24,000 (8/12ths of the employee's 2003 plan compensation of $36,000). Accordingly, the missed after-tax employee contribution amount is $120 The missed after-tax employee contribution is not reduced because the sum of $120 and the previously made after-tax employee contribution of $250 is less than the overall plan limit of $1,000. Therefore, the required corrective contribution is $48 (*i.e* , 40% multiplied by the missed after-tax employee contribution of $120). The corrective contribution is adjusted for earnings.

The total required QNC on behalf of the employee is $888 ($360 for the missed deferral opportunity plus $480 for the missed matching contribution plus $48 for the missed opportunity to make after-tax employee contributions).

Example 5:

The facts (including the ADP and ACP data) are the same as in *Example 5*, except that it is now determined that Employee X, after being included in the plan in 2003, made after-tax employee contributions of $950.

Correction:

The correction is the same as in *Example 4*, except that the corrective contribution required to replace the missed after-tax employee contribution will be re-calculated to take into account applicable plan limits in accordance with the provisions of section 2 02(1)(a)(ii)(C). The required corrective contribution is determined as follows.

Corrective contribution for missed after-tax employee contribution: The missed after-tax employee contribution amount is equal to the 0.5% ACP attributable to after-tax employee contributions for nonhighly compensated employees multiplied by $24,000 (8/12ths of the employee's 2003 plan compensation of $36,000). The missed after-tax employee contribution amount, based on this calculation, is $120. However, the sum of this amount ($120) and the previously made after-tax employee contribution ($950) is $1,070. Because the plan limit for after-tax employee contributions is $1,000, the missed after-tax employee contribution needs to be reduced by $70, to ensure that the total after-tax employee contributions comply with the plan limit. Accordingly, the missed after-tax employee contribution is $50. ($120-$70), and, the required corrective contribution is $20 (*i.e.*, 40% multiplied by the missed after-tax employee contribution of $50). The corrective contribution is adjusted for earnings.

Example 6:

Employer D sponsors a 401(k) plan. The plan has a one year of service eligibility requirement and provides for January 1 and July 1 entry dates. Employee Y, who should have been provided the opportunity to elect and make elective deferrals on January 1, 2003 was not provided the opportunity to elect and make elective deferrals until July 1, 2003. The employee made $5,000 in elective deferrals to the plan in 2003. The employee was a highly compensated employee with compensation for 2003 of $200,000. Employee Y's compensation from January 1 through June 30, 2003 was $100,000. The ADP for highly compensated employees for 2003 was 10% The ADP for nonhighly compensated employees for 2003 was 8%. The § 402(g) limit for deferrals made in 2003 was $12,000.

Correction:

Corrective contribution for missed deferral Employee W's missed deferral is equal to the 10% ADP for highly compensated employees multiplied by $100,000 (compensation earned for the portion of the year in which Employee W was erroneously excluded, *i.e.*, January 1 through June 30, 2003). The missed deferral amount, based on this calculation is $10,000. However, the sum of this amount ($10,000) and the previously made elective contribution ($5,000) is $15,000. The 2003 § 402(g) limit for elective deferrals is $12,000 In accordance with the provisions of section 2 02(1)(a)(ii)(B), the missed deferral needs to be reduced by $3,000, to ensure that the total elective contribution complies with the applicable § 402(g) limit. Accordingly, the missed deferral is $7,000 ($10,000 -$3,000), and the required corrective contribution is $3,500 (*i.e.*, 50% multiplied by the missed deferral of $7,000). The corrective contribution is adjusted for earnings

Example 7:

Employer E maintains a 401(k) plan. The plan provides for matching contributions for each payroll period that are equal to 100% of an employee's elective deferrals that do not exceed 2% of the eligible employee's plan compensation during the payroll period. The plan also provides that the annual limit on matching contributions is $750. The plan provides for after-tax employee contributions. The after-tax employee contribution cannot exceed $1,000 during a plan year. The plan provides that employees who complete one year of service are eligible to participate in the plan on the next January 1 or July 1 entry date. Employee Z, a nonhighly compensated employee who met the eligibility requirements and should have entered the plan on January 1, 2003 was not offered the opportunity to participate in the plan In March of 2003, the error was discovered and Employer E offered the employee an election opportunity as of April 1, 2003. Employee Z had the opportunity to make the maximum elective deferrals and/or after-tax employee contributions that could have been made under the terms of the plan for the entire 2003 plan year. The employee made elective deferrals equal to 3% of the employee's plan compensation for each payroll period from April 1, 2003 through December 31, 2003 (resulting in elective deferrals of $960). The employee's plan compensation for 2003 was $40,000 ($8,000 for the first three months and $32,000 for the last nine months) Employer E made matching contributions equal to $640 for the excluded employee, which is 2% of the employee's plan compensation for each payroll period from April 1, 2003 through December 31, 2003 ($32,000). After being allowed to participate in the plan, the employee made $500 in after-tax employee contributions. The ADP for nonhighly compensated employees for 2003 was 3% and the ACP for nonhighly compensated employees for 2003 was 2.3%. The portion of the ACP attributable to matching contributions for nonhighly compensated employees for 2003 was 1.8%. The portion of the ACP attributable to after-tax employee contributions for nonhighly compensated employees for 2003 was 0.5%.

Correction:

Employer E uses the correction method for partial year exclusions, pursuant to section 2.02(1)(a)(ii), to correct the failure to include an eligible employee in the plan. Because Employee Z was given an opportunity to make elective deferrals and after-tax employee contributions to the plan for at least the last 9 months of the plan year (and the amount of the elective deferrals or after-tax employee contributions that the employee had the opportunity to make was not less than the maximum elective deferrals or after-tax employee contributions that the employee could have made if the employee had been given the opportunity to make elective deferrals and after-tax employee contributions on January 1, 2003), under the special rule set forth in section 2.02(1)(a)(ii)(F), Employer E is not

required to make a corrective contribution for the failure to provide the employee with the opportunity to make either elective deferrals or after-tax employee contributions. The employer only needs to make a corrective contribution for the failure to provide the employee with the opportunity to receive matching contributions on deferrals that could have been made during the first 3 months of the plan year. The calculation of the corrective contribution required to correct this failure is shown as follows:

The missed matching contribution is determined by calculating the matching contribution that the employee would have received had the employee been provided the opportunity to make elective deferrals during the period of exclusion, *i.e.*, January 1, 2003 through March 31, 2003. Assuming that the employee elected to defer an amount equal to 3% of compensation (which is the ADP for the nonhighly compensated employees for the plan year), then, under the terms of the plan, the employee would have been entitled to a matching contribution of 2% of compensation. Pursuant to the provisions of section 2.02(1)(a)(ii)(E), Employer E determines compensation by prorating Employee Z's annual compensation for the portion of the year that Employee Z was not given the opportunity to make elective deferrals or after-tax employee contributions. Accordingly, the required matching contribution for the period of exclusion is obtained by multiplying 2% by Employee Z's compensation of $10,000 (3/12ths of the employee's 2003 plan compensation of $40,000). Based on this calculation, the missed matching contribution is $200. However, when this amount is added to the matching contribution already received ($640), the total ($840) exceeds the $750 plan limit on matching contributions by $90. Accordingly, pursuant to section 2.02(1)(a)(ii)(D), the missed matching contribution figure is reduced to $110 ($200 minus $90). The required corrective contribution is $110. The corrective contribution is adjusted for earnings.

Example 8:

Employer G maintains a safe harbor 401(k) plan that uses a rate of matching contributions to satisfy the requirements of §401(k)(12). Employee M, a nonhighly compensated employee who met the eligibility requirements and should have entered the plan on January 1, 2003, was not offered the opportunity to defer under the plan and was erroneously excluded for all of 2003. Employee M's compensation for 2003 was $20,000.

The plan provides for matching contributions equal to 100% of elective deferrals that do not exceed 3% of an employee's compensation and 50% of elective deferrals that exceed 3% but do not exceed 5% of an employee's compensation.

Correction:

In accordance with the provisions of section 2.02(1)(a)(ii)(B), Employee M's missed deferral on account of exclusion from the safe harbor 401(k) plan is 3% of compensation. Thus, the missed deferral is equal to 3% multiplied by $20,000, or $600. Accordingly, the required corrective contribution for Employee M's missed deferral opportunity in 2003 is $300, *i.e.*, 50% of $600. The required matching contribution, based on the missed deferral of $600, is $600. The required corrective contribution for Employee M's missed matching contribution is $600. The total required corrective contribution, before adjustments for earnings, on behalf of Employee M is $900 (*i.e.*, $300 for the missed deferral opportunity, plus $600 for the missed matching contribution). The corrective contribution is adjusted for earnings.

Example 9:

Same facts as *Example 8*, except that the plan provides for matching contributions equal to 100% of elective deferrals that do not exceed 4% of an employee's compensation.

Correction:

In accordance with the provisions of section 2.02(1)(a)(ii)(B), Employee M's missed deferral on account of exclusion from the safe harbor 401(k) plan is 4% of compensation. The missed deferral is 4% of compensation because the plan provides for a 100% match for deferrals up to that level of compensation. (See Appendix A .05(2)(c).) Therefore, in this case, Employee M's missed deferral is equal to 4% multiplied by $20,000, or $800. The required corrective contribution for Employee M's missed deferral opportunity in 2003 is $400, *i.e.*, 50% multiplied by $800. The required matching contribution, based on the missed deferral of $800, is $800. Thus, the required corrective contribution for Employee M's missed matching contribution is $800. The total required corrective contribution, before adjustments for earnings, on behalf of Employee M is $1,200 (*i.e.*, $400 for the missed deferral opportunity plus $800 for the missed matching contribution). The corrective contribution is adjusted for earnings.

Example 10:

Same facts as *Example 8*, except that the plan uses a rate of nonelective contributions to satisfy the requirements of §401(k)(12) and provides for a nonelective contribution equal to 3% of compensation.

Correction:

In accordance with the provisions of section 2.02(1)(a)(ii)(B), Employee M's missed deferral on account of exclusion from the safe harbor 401(k) plan is 3% of compensation. Thus, the missed deferral is equal to 3% multiplied by $20,000, or $600. Thus, the required corrective contribution for Employee M's missed deferral opportunity in 2003 is $300 (50% of $600). The required nonelective contribution, based on the plan's formula of 3% of compensation for nonelective contributions, is $600. The total required corrective contribution, before adjustments for earnings, on behalf of Employee M is $900 (*i.e.*, $300 for the missed deferral opportunity, plus $600 for the missed nonelective contribution). The corrective contribution is adjusted for earnings.

(2) Exclusion of Eligible Employees In a Profit-Sharing Plan.

(a) Correction Methods. (i) Appendix A Correction Method. Appendix A, section .05 sets forth the correction method for correcting the failure to make a contribution on behalf of the employees improperly excluded from a defined contribution plan or to provide benefit accruals for the employees improperly excluded from a defined benefit plan. In the case of a defined contribution plan, the correction method is to make a contribution on behalf of the excluded employee. Section 2.02(2)(a)(ii) below clarifies the correction method in the case of a profit-sharing or stock bonus plan that provides for nonelective contributions (within the meaning of §1.401(k)–6 and formerly 1.401(k)–1(g)(10)).

(ii) Additional Requirements for Appendix A Correction Method as applied to Profit-Sharing Plans. To correct for the exclusion of an eligible employee from nonelective contributions in a profit-sharing or stock bonus plan under the Appendix A correction method, an allocation amount is determined for each excluded employee on the same basis as the allocation amounts were determined for the other employees under the plan's allocation formula (*e.g.*, the same ratio of allocation to compensation), taking into account all of the employee's relevant factors (*e.g.*, compensation) under that formula for that year. The employer makes a corrective contribution on behalf of the excluded employee that is equal to the allocation amount for the excluded employee. The corrective contribution is adjusted for earnings. If, as a result of excluding an employee, an amount was improperly allocated to the account balance of an eligible employee who shared in the original allocation of the nonelective contribution, no reduction is made to the account balance of the employee who shared in the original allocation on account of the improper allocation. (See Example 11.)

(iii) Reallocation Correction Method. (A) In General. Subject to the limitations set forth in section 2.02(2)(a)(iii)(F) below, in addition to the Appendix A correction method, the exclusion of an eligible employee for a plan year from a profit-sharing or stock bonus plan that provides for nonelective contributions may be corrected using the reallocation correction method set forth in this section 2.02(2)(a)(iii). Under the reallocation correction method, the account balance of the excluded employee is increased as provided in paragraph (2)(a)(iii)(B) below, the account balances of other employees are reduced as provided in paragraph (2)(a)(iii)(C) below, and the increases and reductions are reconciled, as necessary, as provided in paragraph (2)(a)(iii)(D) below. (See Examples 12 and 13.)

(B) Increase in Account Balance of Excluded Employee. The account balance of the excluded employee is increased by an amount that is equal to the allocation the employee would have received had the employee shared in the allocation of the nonelective contribution. The amount is adjusted for earnings.

(C) Reduction in Account Balances of Other Employees. (*1*) The account balance of each employee who was an eligible employee who shared in the original allocation of the nonelective contribution is reduced by the excess, if any, of (I) the employee's allocation of that contribution over (II) the amount that would have been allocated to that employee had the failure not occurred. This amount is adjusted for earnings taking into account the rules set forth in section 2.02(2)(a)(iii)(C)(*2*) and (*3*) below. The amount after adjustment for earnings is limited in accordance with section 2.02(2)(a)(iii)(C)(*4*) below.

(2) This paragraph (2)(a)(iii)(C)(2) applies if most of the employees with account balances that are being reduced are nonhighly compensated employees. If there has been an overall gain for the period from the date of the original allocation of the contribution through the date of correction, no adjustment for earnings is required to the amount determined under section 2.02(2)(a)(iii)(C)(*1*) for the employee. If the amount for the employee is being adjusted for earnings and the plan permits investment of account balances in more than one investment fund, for administrative convenience, the reduction to the employee's account balance may be adjusted by the lowest earnings rate of any fund for the period from the date of the original allocation of the contribution through the date of correction.

(3) If an employee's account balance is reduced and the original allocation was made to more than one investment fund or there was a subsequent distribution or transfer from the fund receiving the original allocation, then reasonable, consistent assumptions are used to determine the earnings adjustment.

(4) The amount determined in section 2.02(2)(a)(iii)(C)(*1*) for an employee after the application of section 2.02(2)(a)(iii)(C)(*2*) and (*3*) may not exceed the account balance of the employee on the date of correction, and the employee is permitted to retain any distribution made prior to the date of correction.

(D) Reconciliation of Increases and Reductions. If the aggregate amount of the increases under section 2.02(2)(a)(iii)(B) exceeds the aggregate amount of the reductions under section 2.02(2)(a)(iii)(C), the employer makes a corrective contribution to the plan for the amount of the excess. If the aggregate amount of the reductions under section 2.02(2)(a)(iii)(C) exceeds the aggregate amount of the increases under section 2.02(2)(a)(iii)(B), then the amount by which each employee's account balance is reduced under section 2.02(2)(a)(iii)(C) is decreased on a *pro rata* basis.

(E) Reductions Among Multiple Investment Funds. If an employee's account balance is reduced and the employee's account balance is invested in more than one investment fund, then the reduction may be made from the investment funds selected in any reasonable manner.

(F) Limitations on Use of Reallocation Correction Method. If any employee would be permitted to retain any distribution pursuant to section 2.02(2)(a)(ii)(C)(*4*), then the reallocation correction method may not be used unless most of the employees who would be permitted to retain a distribution are nonhighly compensated employees.

(b) Examples.

Example 11:

Employer D maintains a profit-sharing plan that provides for discretionary nonelective employer contributions. The plan provides that the employer's contributions are allocated to account balances in the ratio that each eligible employee's compensation for the plan year bears to the compensation of all eligible employees for the plan year and, therefore, the only relevant factor for determining an allocation is the employee's compensation. The plan provides for self-directed investments among four investment funds and daily valuations of account balances. For the 2003 plan year, Employer D made a contribution to the plan of a fixed dollar amount. However, five employees who met the eligibility requirements were inadvertently excluded from participating in the plan. The contribution resulted in an allocation on behalf of each of the eligible employees, other than the excluded employees, equal to 10% of compensation. Most of the employees who received allocations under the plan for the year of the failure were nonhighly compensated employees. No distributions have been made from the plan since 2003. If the five excluded employees had shared in the original allocation, the allocation made on behalf of each employee would have equaled 9% of compensation. The excluded employees began participating in the plan in the 2004 plan year.

Correction.

Employer D uses the Appendix A correction method to correct the failure to include the five eligible employees. Thus, Employer D makes a corrective contribution to the plan. The amount of the corrective contribution on behalf of the five excluded employees for the 2003 plan year is equal to 10% of compensation of each excluded employee, the same allocation that was made for other eligible employees, adjusted for earnings. The excluded employees receive an allocation equal to 10% of compensation (adjusted for earnings) even though, had the excluded employees originally shared in the allocation for the 2003 contribution, their account balances, as well as those of the other eligible employees, would have received an allocation equal to only 9% of compensation.

Example 12:

The facts are the same as in *Example 11*.

Correction

Employer D uses the reallocation correction method to correct the failure to include the five eligible employees. Thus, the account balances are adjusted to reflect what would have resulted from the correct allocation of the employer contribution for the 2003 plan year among all eligible employees, including the five excluded employees. The inclusion of the excluded employees in the allocation of that contribution would have resulted in each eligible employee, including each excluded employee, receiving an allocation equal to 9% of compensation. Accordingly, the account balance of each excluded employee is increased by 9% of the employee's 2003 compensation, adjusted for earnings. The account balance of each of the eligible employees other than the excluded employees is reduced by 1% of the employee's 2003 compensation, adjusted for earnings. Employer D determines the adjustment for earnings using the earnings rate of each eligible employee's excess allocation (using reasonable, consistent assumptions). Accordingly, for an employee who shared in the original allocation and directed the investment of the allocation into more than one investment fund or who subsequently transferred a portion of a fund that had been credited with a portion of the 2003 allocation to another fund, reasonable, consistent assumptions are followed to determine the adjustment for earnings. It is determined that the total of the initially determined reductions in account balances exceeds the total of the required increases in account balances. Accordingly, these initially determined reductions are decreased *pro rata* so that the total of the actual reductions in account balances equals the total of the increases in the account balances, and Employer D does not make any corrective contribution. The reductions from the account balances are made on a *pro rata* basis among all of the funds in which each employee's account balance is invested

Example 13.

The facts are the same as in *Example 11*.

Correction:

The correction is the same as in *Example 12*, except that, because most of the employees whose account balances are being reduced are nonhighly compensated employees, for administrative convenience, Employer D uses the earnings rate of the fund with the lowest earnings rate for the period of the failure to adjust the reduction to each account balance. It is determined that the aggregate amount (adjusted for earnings) by which the account balances of the excluded employees is increased exceeds the aggregate amount (adjusted for earnings) by which the other employees' account balances are reduced. Accordingly, Employer D makes a contribution to the plan in an amount equal to the excess. The reduction from account balances is made on a *pro rata* basis among all of the funds in which each employee's account balance is invested.

.03 *Vesting Failures.*

(1) Correction Methods. (a) Contribution Correction Method. A failure in a defined contribution plan to apply the proper vesting percentage to an employee's account balance that results in forfeiture of too large a portion of the employee's account balance may be corrected using the contribution correction method set forth in this paragraph. The employer makes a corrective contribution on behalf of the employee whose account balance was improperly forfeited in an amount equal to the improper forfeiture. The corrective contribution is adjusted for earnings. If, as a result of the improper forfeiture, an amount was improperly allocated to the account balance of another employee, no reduction is made to the account balance of that employee. (See Example 14.)

(b) Reallocation Correction Method. In lieu of the contribution correction method, in a defined contribution plan under which forfeitures of account balances are reallocated among the account balances of the other eligible employees in the plan, a failure to apply the proper vesting percentage to an employee's account balance which results in forfeiture of too large a portion of the employee's account balance may be corrected under the reallocation correction method set forth in this paragraph. A corrective reallocation is made in accordance with the reallocation correction method set forth in section 2.02(2)(a)(iii), subject to the limitations set forth in section 2.02(2)(a)(iii)(F). In applying section 2.02(2)(a)(iii)(B), the account balance of the employee who incurred the improper forfeiture is increased by an amount equal to the amount of the improper forfeiture and the amount is adjusted for earnings. In applying section 2.02(2)(a)(iii)(C)(*1*), the account balance of each employee who shared in the allocation of the improper forfeiture is reduced by the amount of the improper forfeiture that was allocated to that employee's account. The earnings adjustments for the account balances that are being reduced are determined in accordance with sections 2.02(2)(a)(iii)(C)(*2*) and (*3*) and the reductions after adjustments for earnings are limited in accordance with section 2.02(2)(a)(iii)(C)(*4*). In accordance with section 2.02(2)(a)(iii)(D), if the aggregate amount of the increases exceeds the aggregate amount of the reductions, the employer makes a corrective contribution to the plan for the amount of the excess. In accordance with section 2.02(2)(a)(iii)(D), if the aggregate amount of the reductions exceeds the aggregate amount of the increases, then the amount by which each employee's account balance is reduced is decreased on a *pro rata* basis. (See Example 15.)

(2) Examples.

Example 14:

Employer E maintains a profit-sharing plan that provides for nonelective contributions. The plan provides for self-directed investments among four investment funds and daily valuation of account balances. The plan provides that forfeitures of account balances are reallocated among the account balances of other eligible employees on the basis of compensation. During the 2003 plan year, Employee R terminated employment with Employer E and elected and received a single-sum distribution of the vested portion of his account balance. No other distributions have been made since 2003. However, an incorrect determination of Employee R's vested percentage was made resulting in Employee R receiving a distribution of less than the amount to which he was entitled under the plan. The remaining portion of Employee R's account balance was forfeited and reallocated (and these reallocations were not affected by the limitations of § 415). Most of the employees who received allocations of the improper forfeiture were nonhighly compensated employees.

Correction:

Employer E uses the contribution correction method to correct the improper forfeiture. Thus, Employer E makes a contribution on behalf of Employee R equal to the incorrectly forfeited amount (adjusted for earnings) and Employee R's account balance is increased accordingly. No reduction is made from the account balances of the employees who received an allocation of the improper forfeiture.

Example 15:

The facts are the same as in *Example 14*.

Correction:

Employer E uses the reallocation correction method to correct the improper forfeiture. Thus, Employee R's account balance is increased by the amount that was improperly forfeited (adjusted for earnings). The account of each employee who shared in the allocation of the improper forfeiture is reduced by the amount of the improper forfeiture that was allocated to that employee's account (adjusted for earnings). Because most of the employees whose account balances are being reduced are nonhighly compensated employees, for administrative convenience, Employer E uses the earnings rate of the fund with the lowest earnings rate for the period of the failure to adjust the reduction to each account balance. It is determined that the amount (adjusted for earnings) by which the account balance of Employee R is increased exceeds the aggregate amount (adjusted for earnings) by which the other employees' account balances are reduced. Accordingly, Employer E makes a contribution to the plan in an amount equal to the excess. The reduction from the account balances is made on a *pro rata* basis among all of the funds in which each employee's account balance is invested.

.04 *§ 415 Failures.*

(1) Failures Relating to a § 415(b) Excess.

(a) Correction Methods. (i) Return of Overpayment Correction Method. Overpayments as a result of amounts being paid in excess of the limits of § 415(b) may be corrected using the return of Overpayment correction method set forth in this paragraph (1)(a)(i). The employer takes reasonable steps to have the Overpayment (with appropriate interest) returned by the recipient to the plan and reduces future benefit payments (if any) due to the employee to reflect § 415(b). To the extent the amount returned by the recipient is less than the Overpayment, adjusted for earnings at the plan's earnings rate, then the employer or another person contributes the difference to the plan. In addition, in accordance with section 6.05 of this revenue procedure, the employer must notify the recipient that the Overpayment was not eligible for favorable tax treatment accorded to distributions from qualified plans (and, specifically, was not eligible for tax-free rollover). (See Examples 18 and 19.)

(ii) Adjustment of Future Payments Correction Method. (A) In General. In addition to the return of overpayment correction method, in the case of plan benefits that are being distributed in the form of periodic payments, Overpayments as a result of amounts being paid in excess of the limits in § 415(b) may be corrected by using the adjustment of future payments correction method set forth in this paragraph (1)(a)(ii). Future payments to the recipient are reduced so that they do not exceed the § 415(b) maximum limit

and an additional reduction is made to recoup the Overpayment (over a period not longer than the remaining payment period) so that the actuarial present value of the additional reduction is equal to the Overpayment plus interest at the interest rate used by the plan to determine actuarial equivalence. (See Examples 16 and 17.)

(B) Joint and Survivor Annuity Payments. If the employee is receiving payments in the form of a joint and survivor annuity, with the employee's spouse to receive a life annuity upon the employee's death equal to a percentage (*e.g.*, 75%) of the amount being paid to the employee, the reduction of future annuity payments to reflect § 415(b) reduces the amount of benefits payable during the lives of both the employee and spouse, but any reduction to recoup Overpayments made to the employee does not reduce the amount of the spouse's survivor benefit. Thus, the spouse's benefit will be based on the previous specified percentage (*e.g.*, 75%) of the maximum permitted under § 415(b), instead of the reduced annual periodic amount payable to the employee.

(C) Overpayment Not Treated as an Excess Amount. An Overpayment corrected under this adjustment of future payment correction method is not treated as an Excess Amount as defined in section 5.01(3) of this revenue procedure.

(b) Examples.

Example 16:

Employer F maintains a defined benefit plan funded solely through employer contributions. The plan provides that the benefits of employees are limited to the maximum amount permitted under § 415(b), disregarding cost-of-living adjustments under § 415(d) after benefit payments have commenced. At the beginning of the 1998 plan year, Employee S retired and started receiving an annual straight life annuity of $140,000 from the plan. Due to an administrative error, the annual amount received by Employee S for 1998 included an Overpayment of $10,000 (because the § 415(b)(1)(A) limit for 1998 was $130,000). This error was discovered at the beginning of 1999.

Correction:

Employer F uses the adjustment of future payments correction method to correct the failure to satisfy the limit in § 415(b). Future annuity benefit payments to Employee S are reduced so that they do not exceed the § 415(b) maximum limit, and, in addition, Employee S's future benefit payments from the plan are actuarially reduced to recoup the Overpayment. Accordingly, Employee S's future benefit payments from the plan are reduced to $130,000 and further reduced by $1,000 annually for life, beginning in 1999. The annual benefit amount is reduced by $1,000 annually for life because, for Employee S, the actuarial present value of a benefit of $1,000 annually for life commencing in 1999 is equal to the sum of $10,000 and interest at the rate used by the plan to determine actuarial equivalence beginning with the date of the first Overpayment and ending with the date the reduced annuity payment begins. Thus, Employee S's remaining benefit payments are reduced so that Employee S receives $129,000 for 1999, and for each year thereafter.

Example 17

The facts are the same as in *Example 16*.

Correction:

Employer F uses the adjustments of future payments correction method to correct the § 415(b) failure, by recouping the entire excess payment made in 1998 from Employee S's remaining benefit payments for 1999. Thus, Employee S's annual annuity benefit for 1999 is reduced to $119,400 to reflect the excess benefit amounts (increased by interest) that were paid from the plan to Employee S during the 1998 plan year. Beginning in 2000, Employee S begins to receive annual benefit payments of $130,000.

Example 18

The facts are the same as in *Example 16*, except that the benefit was paid to Employee S in the form of a single-sum distribution in 1998, which exceeded the maximum § 415(b) limits by $110,000.

Correction

Employer F uses the return of overpayment correction method to correct the § 415(b) failure. Thus, Employer F notifies Employee S of the $110,000 Overpayment and that the Overpayment was not eligible for favorable tax treatment accorded to distributions from qualified plans (and, specifically, was not eligible for tax-free rollover). The notice also informs Employee S that the Overpayment (with interest at the rate used by the plan to calculate the single-sum payment) is owed to the plan. Employer F takes reasonable steps to have the Overpayment (with interest at the rate used by the plan to calculate the single-sum payment) paid to the plan. Employee S pays the $110,000 (plus the requested interest) to the plan. It is determined that the plan's earnings rate for the relevant period was 2 percentage points more than the rate used by the plan to calculate the single-sum payment. Accordingly, Employer F contributes the difference to the plan.

Example 19:

The facts are the same as in *Example 18*.

Correction:

Employer F uses the return of overpayment correction method to correct the § 415(b) failure. Thus, Employer F notifies Employee S of the $110,000 Overpayment and that the Overpayment was not eligible for favorable tax treatment accorded to distributions from qualified plans (and, specifically, was not eligible for tax-free rollover). The notice also informs Employee S that the Overpayment (with interest at the rate used by the plan to calculate the single-sum payment) is owed to the plan. Employer F takes reasonable steps to have the Overpayment (with interest at the rate used by the plan to calculate the single-sum payment) paid to the plan. As a result of Employer F's recovery efforts, some, but not all, of the Overpayment (with interest) is recovered from Employee S. It is determined that the amount returned by Employee S to the plan is less than the Overpayment adjusted for earnings at the plan's earnings rate. Accordingly, Employer F contributes the difference to the plan.

(2) Failures Relating to a § 415(c) Excess.

(a) Correction Methods. (i) Appendix A Correction Method. Appendix A, section .08 sets forth the correction method for correcting the failure to satisfy the § 415(c) limits on annual additions.

(ii) Forfeiture Correction Method. In addition to the Appendix A correction method, the failure to satisfy § 415(c) with respect to a nonhighly compensated employee (A) who in the limitation year of the failure had annual additions consisting of both (I) either elective deferrals or employee after-tax contributions or both and (II) either matching or nonelective contributions or both, (B) for whom the matching and nonelective contributions equal or exceed the portion of the employee's annual addition that exceeds the limits under § 415(c) ("§ 415(c) excess") for the limitation year, and (C) who has terminated with no vested interest in the matching and nonelective contributions (and has not been reemployed at the time of the correction), may be corrected by using the forfeiture correction method set forth in this paragraph. The § 415(c) excess is deemed to consist solely of the matching and nonelective contributions. If the employee's § 415(c) excess (adjusted for earnings) has previously been forfeited, the § 415(c) failure is deemed to be corrected. If the § 415(c) excess (adjusted for earnings) has not been forfeited, that amount is placed in an unallocated account, similar to the suspense account described in § 1.415–6(b)(6)(iii), to be used to reduce employer contributions in succeeding year(s) (or if the amount would have been allocated to other employees who were in the plan for the year of the failure if the failure had not occurred, then that amount is reallocated to the other employees in accordance with the plan's allocation formula). Note that while this correction method will permit more favorable tax treatment of elective deferrals for the employee than the Appendix A correction method, this correction method

could be less favorable to the employee in certain cases, for example, if the employee is subsequently reemployed and becomes vested. (See Examples 20 and 21.)

(iii) Return of Overpayment Correction Method. A failure to satisfy § 415(c) that includes a distribution of the § 415(c) excess attributable to nonelective contributions and matching contributions may be corrected using the return of Overpayment correction method set forth in this paragraph. The employer takes reasonable steps to have the Overpayment (*i.e.*, the distribution of the § 415(c) excess adjusted for earnings to the date of the distribution), plus appropriate interest from the date of the distribution to the date of the repayment, returned by the employee to the plan. To the extent the amount returned by the employee is less than the Overpayment adjusted for earnings at the plan's earnings rate, then the employer or another person contributes the difference to the plan. The Overpayment, adjusted for earnings at the plan's earnings rate to the date of the repayment, is to be placed in an unallocated account, similar to the suspense account described in § 1.415–6(b)(6)(iii), to be used to reduce employer contributions in succeeding year(s) (or if the amount would have been allocated to other eligible employees who were in the plan for the year of the failure if the failure had not occurred, then that amount is reallocated to the other eligible employees in accordance with the plan's allocation formula). In addition, the employer must notify the employee that the Overpayment was not eligible for favorable tax treatment accorded to distributions from qualified plans (and, specifically, was not eligible for tax-free rollover).

(b) Examples.

Example 20:

Employer G maintains a 401(k) plan. The plan provides for nonelective employer contributions, elective deferrals, and employee after-tax contributions. The plan provides that the nonelective contributions vest under a 5-year cliff vesting schedule. The plan provides that when an employee terminates employment, the employee's nonvested account balance is forfeited five years after a distribution of the employee's vested account balance and that forfeitures are used to reduce employer contributions. For the 1998 limitation year, the annual additions made on behalf of two nonhighly compensated employees in the plan, Employees T and U, exceeded the limit in § 415(c). For the 1998 limitation year, Employee T had § 415 compensation of $60,000, and, accordingly, a § 415(c)(1)(B) limit of $15,000. Employee T made elective deferrals and employee after-tax contributions. For the 1998 limitation year, Employee U had § 415 compensation of $40,000, and, accordingly, a § 415(c)(1)(B) limit of $10,000. Employee U made elective deferrals. Also, on January 1, 1999, Employee U, who had three years of service with Employer G, terminated his employment and received his entire vested account balance (which consisted of his elective deferrals). The annual additions for Employees T and U consisted of:

	T	U
Nonelective Contributions	$ 7,500	$ 4,500
Elective Deferrals	10,000	5,800
After-tax Contributions	500	0
Total Contributions	$18,000	$10,300
§ 415(c) Limit	$15,000	$10,000
§ 415(c) Excess	$ 3,000	$ 300

Correction:

Employer G uses the Appendix A correction method to correct the § 415(c) excess with respect to Employee T (*i.e.*, $3,000). Thus, a distribution of plan assets (and corresponding reduction of the account balance) consisting of $500 (adjusted for earnings) of employee after-tax contributions and $2,500 (adjusted for earnings) of elective deferrals is made to Employee T. Employer G uses the forfeiture correction method to correct the § 415(c) excess with respect to Employee U. Thus, the § 415(c) excess is deemed to consist solely of the nonelective contributions. Accordingly, Employee U's nonvested account balance is reduced by $300 (adjusted for earnings) which is placed in an unallocated account, similar to the suspense account described in § 1.415–6(b)(6)(iii), to be used to reduce employer contributions in succeeding year(s). After correction, it is determined that the ADP and ACP tests for 1998 were satisfied.

Example 21:

Employer H maintains a 401(k) plan. The plan provides for nonelective employer contributions, matching contributions and elective deferrals. The plan provides for matching contributions that are equal to 100% of an employee's elective deferrals that do not exceed 8% of the employee's plan compensation for the plan year. For the 1998 limitation year, Employee V had § 415 compensation of $50,000, and, accordingly, a § 415(c)(1)(B) limit of $12,500. During that limitation year, the annual additions for Employee V totaled $15,000, consisting of $5,000 in elective deferrals, a $4,000 matching contribution (8% of $50,000), and a $6,000 nonelective employer contribution. Thus, the annual additions for Employee V exceeded the § 415(c) limit by $2,500.

Correction:

Employer H uses the Appendix A correction method to correct the § 415(c) excess with respect to Employee V (*i.e.*, $2,500). Accordingly, $1,000 of the unmatched elective deferrals (adjusted for earnings) are distributed to Employee V. The remaining $1,500 excess is apportioned equally between the elective deferrals and the associated matching employer contributions, so Employee V's account balance is further reduced by distributing to Employee V $750 (adjusted for earnings) of the elective deferrals and forfeiting $750 (adjusted for earnings) of the associated employer matching contributions. The forfeited matching contributions are placed in an unallocated account; similar to the suspense account described in § 1.415–6(b)(6)(iii), to be used to reduce employer contributions in succeeding year(s). After correction, it is determined that the ADP and ACP tests for 1998 were satisfied.

.05 *Correction of Other Overpayment Failures.*

An Overpayment, other than one described in section 2.04(1) (relating to a § 415(b) excess) or section 2.04(2) (relating to a § 415(c) excess), may be corrected in accordance with this section 2.05. An Overpayment from a defined benefit plan is corrected in accordance with the rules in section 2.04(1). An Overpayment from a defined contribution plan is corrected in accordance with the rules in section 2.04(2)(a)(iii).

.06 *§ 401(a)(17) Failures.*

(1) Reduction of Account Balance Correction Method. The allocation of contributions or forfeitures under a defined contribution plan for a plan year on the basis of compensation in excess of the limit under § 401(a)(17) for the plan year may be corrected using the reduction of account balance correction method set forth in this paragraph. The account balance of an employee who received an allocation on the basis of compensation in

excess of the § 401(a)(17) limit is reduced by this improperly allocated amount (adjusted for earnings). If the improperly allocated amount would have been allocated to other employees in the year of the failure if the failure had not occurred, then that amount (adjusted for earnings) is reallocated to those employees in accordance with the plan's allocation formula. If the improperly allocated amount would not have been allocated to other employees absent the failure, that amount (adjusted for earnings) is placed in an unallocated account, similar to the suspense account described in § 1.415–6(b)(6)(iii), to be used to reduce employer contributions in succeeding year(s). For example, if a plan provides for a fixed level of employer contributions for each eligible employee, and the plan provides that forfeitures are used to reduce future employer contributions, the improperly allocated amount (adjusted for earnings) would be used to reduce future employer contributions. (See Example 20.) If a payment was made to an employee and that payment was attributable to an improperly allocated amount, then it is an Overpayment defined in section 5.01(6) of this revenue procedure that must be corrected (see sections 2.04 and 2.05).

(2) Example.

Example 22:

Employer J maintains a money purchase pension plan. Under the plan, an eligible employee is entitled to an employer contribution of 8% of the employee's compensation up to the § 401(a)(17) limit ($200,000 for 2003). During the 2003 plan year, an eligible employee, Employee W, inadvertently was credited with a contribution based on compensation above the § 401(a)(17) limit. Employee W's compensation for 2003 was $220,000. Employee W received a contribution of $17,600 for 2003 (8% of $220,000), rather than the contribution of $16,000 (8% of $200,000) provided by the plan for that year, resulting in an improper allocation of $1,600.

Correction:

The § 401(a)(17) failure is corrected using the reduction of account balance method by reducing Employee W's account balance by $1,600 (adjusted for earnings) and crediting that amount to an unallocated account, similar to the suspense account described in § 1.415–6(b)(6)(iii), to be used to reduce employer contributions in succeeding year(s).

.07 *Correction by Amendment.*

(1) § 401(a)(17) Failures. (a) Contribution Correction Method. In addition to the reduction of account balance correction method under section 2.06 of this Appendix B, an employer may correct a § 401(a)(17) failure for a plan year under a defined contribution plan by using the contribution correction method set forth in this paragraph. The employer contributes an additional amount on behalf of each of the other employees (excluding each employee for whom there was a § 401(a)(17) failure) who received an allocation for the year of the failure, amending the plan (as necessary) to provide for the additional allocation. The amount contributed for an employee is equal to the employee's plan compensation for the year of the failure multiplied by a fraction, the numerator of which is the improperly allocated amount made on behalf of the employee with the largest improperly allocated amount, and the denominator of which is the limit under § 401(a)(17) applicable to the year of the failure. The resulting additional amount for each of the other employees is adjusted for earnings. (See Example 21.)

(b) Examples.

Example 23:

The facts are the same as in *Example 22*.

Correction:

Employer J corrects the failure under VCP using the contribution correction method by (1) amending the plan to increase the contribution percentage for all eligible employees (other than Employee W) for the 2003 plan year and (2) contributing an additional amount (adjusted for earnings) for those employees for that plan year. To determine the increase in the plan's contribution percentage (and the additional amount contributed on behalf of each eligible employee), the improperly allocated amount ($1,600) is divided by the § 401(a)(17) limit for 2003 ($200,000). Accordingly, the plan is amended to increase the contribution percentage by 0.8 percentage points ($1,600/$200,000) from 8% to 8.8%. In addition, each eligible employee for the 2003 plan year (other than Employee W) receives an additional contribution of 0.8% multiplied by that employee's plan compensation for 2003. This additional contribution is adjusted for earnings.

(2) Hardship Distribution Failures and Plan Loan Failures. (a) Plan Amendment Correction Method. The Operational Failure of making hardship distributions to employees under a plan that does not provide for hardship distributions may be corrected using the plan amendment correction method set forth in this paragraph. The plan is amended retroactively to provide for the hardship distributions that were made available. This paragraph does not apply unless (i) the amendment satisfies § 401(a), and (ii) the plan as amended would have satisfied the qualification requirements of § 401(a) (including the requirements applicable to hardship distributions under § 401(k), if applicable) had the amendment been adopted when hardship distributions were first made available. (See Example 24.) The Plan Amendment Correction Method is also available for the Operational Failure of permitting plan loans to employees under a plan that does not provide for plan loans. The plan is amended retroactively to provide for the plan loans that were made available. This paragraph does not apply unless (i) the amendment satisfies § 401(a), and (ii) the plan as amended would have satisfied the qualification requirements of § 401(a) (and the requirements applicable to plan loans under § 72(p)) had the amendment been adopted when plan loans were first made available.

(b) Example.

Example 24:

Employer K, a for-profit corporation, maintains a 401(k) plan. Although plan provisions in 2002 did not provide for hardship distributions, beginning in 2002 hardship distributions of amounts allowed to be distributed under § 401(k) were made currently and effectively available to all employees (within the meaning of § 1.401(a)(4)–4). The standard used to determine hardship satisfied the deemed hardship distribution standards in § 1.401(k)–1(d)(2). Hardship distributions were made to a number of employees during the 2002 and 2003 plan years, creating an Operational Failure. The failure was discovered in 2004.

Correction:

Employer K corrects the failure under VCP by adopting a plan amendment, effective January 1, 2002, to provide a hardship distribution option that satisfies the rules applicable to hardship distributions in § 1.401(k)–1(d)(2). The amendment provides that the hardship distribution option is available to all employees. Thus, the amendment satisfies § 401(a), and the plan as amended in 2004 would have satisfied § 401(a) (including § 1.401(a)(4)–4 and the requirements applicable to hardship distributions under § 401(k)) if the amendment had been adopted in 2002.

(3) Early Inclusion of Otherwise Eligible Employee Failure. (a) Plan Amendment Correction Method. The Operational Failure of including an otherwise eligible employee in the plan who either (i) has not completed the plan's minimum age or service requirements, or (ii) has completed the plan's minimum age or service requirements but became a participant in the plan on a date earlier than the applicable plan entry date, may be corrected by using the plan amendment correction method set forth in this paragraph. The plan is amended retroactively to change

the eligibility or entry date provisions to provide for the inclusion of the ineligible employee to reflect the plan's actual operations. The amendment may change the eligibility or entry date provisions with respect to only those ineligible employees that were wrongly included, and only to those ineligible employees, provided (i) the amendment satisfies § 401(a) at the time it is adopted, (ii) the amendment would have satisfied § 401(a) had the amendment been adopted at the earlier time when it is effective, and (iii) the employees affected by the amendment are predominantly nonhighly compensated employees.

(b) Example

Example 25.

Employer L maintains a 401(k) plan applicable to all of its employees who have at least six months of service. The plan is a calendar year plan. The plan provides that Employer L will make matching contributions based upon an employee's salary reduction contributions. In 2001, it is discovered that all four employees who were hired by Employer L in 2000 were permitted to make salary reduction contributions to the plan effective with the first weekly paycheck after they were employed. Three of the four employees are nonhighly compensated. Employer L matched these employees' salary reduction contributions in accordance with the plan's matching contribution formula. Employer L calculates the ADP and ACP tests for 2000 (taking into account the salary reduction and matching contributions that were made for these employees) and determines that the tests were satisfied.

Correction:

Employer L corrects the failure under SCP by adopting a plan amendment, effective for employees hired on or after January 1, 2000, to provide that there is no service eligibility requirement under the plan and submitting the amendment to the Service for a determination letter.

SECTION 3. EARNINGS ADJUSTMENT METHODS AND EXAMPLES

.01 *Earnings Adjustment Methods.* (1) In general. (a) Under section 6.02(4)(a) of this revenue procedure, whenever the appropriate correction method for an Operational Failure in a defined contribution plan includes a corrective contribution or allocation that increases one or more employees' account balances (now or in the future), the contribution or allocation is adjusted for earnings and forfeitures. This section 3 provides earnings adjustment methods (but not forfeiture adjustment methods) that may be used by an employer to adjust a corrective contribution or allocation for earnings in a defined contribution plan. Consequently, these earnings adjustment methods may be used to determine the earnings adjustments for corrective contributions or allocations made under the correction methods in section 2 and under the correction methods in Appendix A. If an earnings adjustment method in this section 3 is used to adjust a corrective contribution or allocation, that adjustment is treated as satisfying the earnings adjustment requirement of section 6.02(4)(a) of this revenue procedure. Other earnings adjustment methods, different from those illustrated in this section 3, may also be appropriate for adjusting corrective contributions or allocations to reflect earnings.

(b) Under the earnings adjustment methods of this section 3, a corrective contribution or allocation that increases an employee's account balance is adjusted to reflect an "earnings amount" that is based on the earnings rate(s) (determined under section 3.01(3)) for the period of the failure (determined under section 3.01(2)). The earnings amount is allocated in accordance with section 3.01(4).

(c) The rule in section 6.02(5)(a) of this revenue procedure permitting reasonable estimates in certain circumstances applies for purposes of this section 3. For this purpose, a determination of earnings made in accordance with the rules of administrative convenience set forth in this section 3 is treated as a precise determination of earnings. Thus, if the probable difference between an approximate determination of earnings and a determination of earnings under this section 3 is insignificant and the administrative cost of a precise determination would significantly exceed the probable difference, reasonable estimates may be used in calculating the appropriate earnings.

(d) This section 3 does not apply to corrective distributions or corrective reductions in account balances. Thus, for example, while this section 3 applies in increasing the account balance of an improperly excluded employee to correct the exclusion of the employee under the reallocation correction method described in section 2.02(2)(a)(iii)(B), this section 3 does not apply in reducing the account balances of other employees under the reallocation correction method. (See section 2.02(2)(a)(iii)(C) for rules that apply to the earnings adjustments for such reductions.) In addition, this section 3 does not apply in determining earnings adjustments under the one-to-one correction method described in section 2.01(1)(b)(iii).

(2) Period of the Failure. (a) General Rule. For purposes of this section 3, the "period of the failure" is the period from the date that the failure began through the date of correction. For example, in the case of an improper forfeiture of an employee's account balance, the beginning of the period of the failure is the date as of which the account balance was improperly reduced.

(b) Rules for Beginning Date for Exclusion of Eligible Employees from Plan. (i) General Rule. In the case of an exclusion of an eligible employee from a plan contribution, the beginning of the period of the failure is the date on which contributions of the same type (*e.g.*, elective deferrals, matching contributions, or discretionary nonelective employer contributions) were made for other employees for the year of the failure. In the case of an exclusion of an eligible employee from an allocation of a forfeiture, the beginning of the period of the failure is the date on which forfeitures were allocated to other employees for the year of the failure.

(ii) Exclusion from a 401(k) or (m) Plan. For administrative convenience, for purposes of calculating the earnings rate for corrective contributions for a plan year (or the portion of the plan year) during which an employee was improperly excluded from making periodic elective deferrals or employee after-tax contributions, or from receiving periodic matching contributions, the employer may treat the date on which the contributions would have been made as the midpoint of the plan year (or the midpoint of the portion of the plan year) for which the failure occurred. Alternatively, in this case, the employer may treat the date on which the contributions would have been made as the first date of the plan year (or the portion of the plan year) during which an employee was excluded, provided that the earnings rate used is one half of the earnings rate applicable under section 3.01(3) for the plan year (or the portion of the plan year) for which the failure occurred.

(3) Earnings Rate. (a) General Rule. For purposes of this section 3, the earnings rate generally is based on the invest-

ment results that would have applied to the corrective contribution or allocation if the failure had not occurred.

(b) Multiple Investment Funds. If a plan permits employees to direct the investment of account balances into more than one investment fund, the earnings rate is based on the rate applicable to the employee's investment choices for the period of the failure. For administrative convenience, if most of the employees for whom the corrective contribution or allocation is made are nonhighly compensated employees, the rate of return of the fund with the highest earnings rate under the plan for the period of the failure may be used to determine the earnings rate for all corrective contributions or allocations. If the employee had not made any applicable investment choices, the earnings rate may be based on the earnings rate under the plan as a whole (*i.e.*, the average of the rates earned by all of the funds in the valuation periods during the period of the failure weighted by the portion of the plan assets invested in the various funds during the period of the failure).

(c) Other Simplifying Assumptions. For administrative convenience, the earnings rate applicable to the corrective contribution or allocation for a valuation period with respect to any investment fund may be assumed to be the actual earnings rate for the plan's investments in that fund during that valuation period. For example, the earnings rate may be determined without regard to any special investment provisions that vary according to the size of the fund. Further, the earnings rate applicable to the corrective contribution or allocation for a portion of a valuation period may be a *pro rata* portion of the earnings rate for the entire valuation period, unless the application of this rule would result in either a significant understatement or overstatement of the actual earnings during that portion of the valuation period.

(4) Allocation Methods. (a) In General. For purposes of this section 3, the earnings amount generally may be allocated in accordance with any of the methods set forth in this paragraph (4). The methods under paragraph (4)(c), (d), and (e) are intended to be particularly helpful where corrective contributions are made at dates between the plan's valuation dates.

(b) Plan Allocation Method. Under the plan allocation method, the earnings amount is allocated to account balances under the plan in accordance with the plan's method for allocating earnings as if the failure had not occurred. (See Example 26.)

(c) Specific Employee Allocation Method. Under the specific employee allocation method, the entire earnings amount is allocated solely to the account balance of the employee on whose behalf the corrective contribution or allocation is made (regardless of whether the plan's allocation method would have allocated the earnings solely to that employee). In determining the allocation of plan earnings for the valuation period during which the corrective contribution or allocation is made, the corrective contribution or allocation (including the earnings amount) is treated in the same manner as any other contribution under the plan on behalf of the employee during that valuation period. Alternatively, where the plan's allocation method does not allocate plan earnings for a valuation period to a contribution made during that valuation period, plan earnings for the valuation period during which the corrective contribution or allocation is made may be allocated as if that employee's account balance had been increased as of the last day of the prior valuation period by the corrective contribution or allocation, including only that portion of the earnings amount attributable to earnings through the last day of the prior valuation period. The employee's account balance is then further increased as of the last day of the valuation period during which the corrective contribution or allocation is made by that portion of the earnings amount attributable to earnings after the last day of the prior valuation period. (See Example 27.)

(d) Bifurcated Allocation Method. Under the bifurcated allocation method, the entire earnings amount for the valuation periods ending before the date the corrective contribution or allocation is made is allocated solely to the account balance of the employee on whose behalf the corrective contribution or allocation is made. The earnings amount for the valuation period during which the corrective contribution or allocation is made is allocated in accordance with the plan's method for allocating other earnings for that valuation period in accordance with section 3.01(4)(b). (See Example 28.)

(e) Current Period Allocation Method. Under the current period allocation method, the portion of the earnings amount attributable to the valuation period during which the period of the failure begins ("first partial valuation period") is allocated in the same manner as earnings for the valuation period during which the corrective contribution or allocation is made in accordance section 3.01(4)(b). The earnings for the subsequent full valuation periods ending before the beginning of the valuation period during which the corrective contribution or allocation is made are allocated solely to the employee for whom the required contribution should have been made. The earnings amount for the valuation period during which the corrective contribution or allocation is made ("second partial valuation period") is allocated in accordance with the plan's method for allocating other earnings for that valuation period in accordance with section 3.01(4)(b). (See Example 29.)

.02 *Examples.*

Example 26.

Employer L maintains a profit-sharing plan that provides only for nonelective contributions. The plan has a single investment fund. Under the plan, assets are valued annually (the last day of the plan year) and earnings for the year are allocated in proportion to account balances as of the last day of the prior year, after reduction for distributions during the current year but without regard to contributions received during the current year (the "prior year account balance"). Plan contributions for 1997 were made on March 31, 1998. On April 20, 2000, Employer L determines that an operational failure occurred for 1997 because Employee X was improperly excluded from the plan. Employer L decides to correct the failure by using the Appendix A correction method for the exclusion of an eligible employee from nonelective contributions in a profit-sharing plan. Under this method, Employer L determines that this failure is corrected by making a contribution on behalf of Employee X of $5,000 (adjusted for earnings). The earnings rate under the plan for 1998 was +20%. The earnings rate under the plan for 1999 was +10%. On May 15, 2000, when Employer L determines that a contribution to correct for the failure will be made on June 1, 2000, a reasonable estimate of the earnings rate under the plan from January 1, 2000 to June 1, 2000 is +12%.

Earnings Adjustment on the Corrective Contribution

The $5,000 corrective contribution on behalf of Employee X is adjusted to reflect an earnings amount based on the earnings rates for the period of the failure (March 31, 1998 through June 1, 2000) and the earnings amount is allocated using the plan allocation method. Employer L determines that a *pro rata* simplifying assumption may be used to determine the

earnings rate for the period from March 31, 1998 to December 31, 1998, because that rate does not significantly understate or overstate the actual earnings for that period. Accordingly, Employer L determines that the earnings rate for that period is 15% (9/12 of the plan's 20% earnings rate for the year). Thus, applicable earnings rates under the plan during the period of the failure are:

Time Periods	Earnings Rate
3/31/98 - 12/31/98 (First Partial Valuation Period)	+15%
1/1/99 - 12/31/99	+10%
1/1/00 - 6/1/00 (Second Partial Valuation Period)	+12%

If the $5,000 corrective contribution had been contributed for Employee X on March 31, 1998, (1) earnings for 1998 would have been increased by the amount of the earnings on the additional $5,000 contribution from March 31, 1998 through December 31, 1998, and would have been allocated as 1998 earnings in proportion to the prior year (December 31, 1997) account balances, (2) Employee X's account balance as of December 31, 1998, would have been increased by the additional $5,000 contribution, (3) earnings for 1999 would have been increased by the 1999 earnings on the additional $5,000 contribution (including 1998 earnings thereon) allocated in proportion to the prior year (December 31, 1998) account balances along with other 1999 earnings, and (4) earnings for 2000 would have been increased by the earnings on the additional $5,000 (including 1998 and 1999 earnings thereon) from January 1 to June 1, 2000, and would be allocated in proportion to the prior year (December 31, 1999) account balances along with other 2000 earnings. Accordingly, the $5,000 corrective contribution is adjusted to reflect an earnings amount of $2,084 ($5,000[(1.15)(1.10)(1.12)-1]) and the earnings amount is allocated to the account balances under the plan allocation method as follows.

(a) Each account balance that shared in the allocation of earnings for 1998 is increased, as of December 31, 1998, by its appropriate share of the earnings amount for 1998, $750 ($5,000(.15)).

(b) Employee X's account balance is increased, as of December 31, 1998, by $5,000.

(c) The resulting December 31, 1998 account balances will share in the 1999 earnings, including the $575 for 1999 earnings included in the corrective contribution ($5,750(.10)), to determine the account balances as of December 31, 1999. However, each account balance other than Employee X's account balance has already shared in the 1999 earnings, excluding the $575. Accordingly, Employee X's account balance as of December 31, 1999 will include $500 of the 1999 portion of the earnings amount based on the $5,000 corrective contribution allocated to Employee X's account balance as of December 31, 1998 ($5,000(.10)). Then each account balance that originally shared in the allocation of earnings for 1999 (*i.e.*, excluding the $5,500 additions to Employee X's account balance) is increased by its appropriate share of the remaining 1999 portion of the earnings amount, $75.

(d) The resulting December 31, 1999 account balances (including the $5,500 additions to Employee X's account balance) will share in the 2000 portion of the earnings amount based on the estimated January 1, 2000 to June 1, 2000 earnings included in the corrective contribution equal to $759 ($6,325(.12)). (See Table 1.)

TABLE 1
CALCULATION AND ALLOCATION OF THE
CORRECTIVE AMOUNT ADJUSTED FOR EARNINGS

	Earnings Rate	Amount	Allocated to:
Corrective Contribution		$5,000	Employee X
First Partial Valuation Period Earnings	15%	750[1]	All 12/31/1997 Account Balances[4]
1999 Earnings	10%	575[2]	Employee X ($500)/All 12/31/1998 Account Balances ($75)[4]
Second Partial Valuation Period Earnings	12%	759[3]	All 12/31/1999 Account Balances (including Employee X's $5,500)[4]
Total Amount Contributed		$7,084	

[1] $5,000 x 15%
[2] $5,750($5,000 +750) x 10%
[3] $6,325($5,000 +750 +575) x 12%
[4] After reduction for distributions during the year for which earning are being determined but without regard to contributions received during the year for which earnings are being determined.

Example 27:

The facts are the same as in *Example 26*.

Earnings Adjustment on the Corrective Contribution:

The earnings amount on the corrective contribution is the same as in *Example 23*, but the earnings amount is allocated using the specific employee allocation method. Thus, the entire earnings amount for all periods through June 1, 2000 (*i.e.*, $750 for March 31, 1998 to December 31, 1998, $575 for 1999, and $759 for January 1, 2000 to June 1, 2000) is allocated to Employee X. Accordingly, Employer L makes a contribution on June 1, 2000 to the plan of $7,084 ($5,000(1.15)(1.10)(1.12)). Employee X's account balance as of December 31, 2000 is increased by $7,084. Alternatively, Employee X's account balance as of December 31, 1999 is increased by $6,325 ($5,000(1.15)(1.10)), which shares in the allocation of earnings for 2000, and Employee X's account balance as of December 31, 2000 is increased by the remaining $759. (See Table 2.)

TABLE 2 CALCULATION AND ALLOCATION OF THE CORRECTIVE AMOUNT ADJUSTED FOR EARNINGS			
	Earnings Rate	Amount	Allocated to:
Corrective Contribution		$5,000	Employee X
First Partial Valuation Period Earnings	15%	750[1]	Employee X
1999 Earnings	10%	575[2]	Employee X
Second Partial Valuation Period Earnings	12%	759[3]	Employee X
Total Amount Contributed		$7,084	

[1]$5,000 x 15%
[2]$5,750($5,000 +750) x 10%
[3]$6,325($5,000 +750 +575) x 12%

Example 28:

The facts are the same as in *Example 26*.

Earnings Adjustment on the Corrective Contribution.

The earnings amount on the corrective contribution is the same as in *Example 23*, but the earnings amount is allocated using the bifurcated allocation method. Thus, the earnings for the first partial valuation period (March 31, 1998 to December 31, 1998) and the earnings for 1999 are allocated to Employee X. Accordingly, Employer L makes a contribution on June 1, 2000 to the plan of $7,084 ($5,000(1.15)(1.10)(1.12)). Employee X's account balance as of December 31, 1999 is increased by $6,325 ($5,000(1.15)(1.10)); and the December 31, 1999 account balances of employees (including Employee X's increased account balance) will share in estimated January 1, 2000 to June 1, 2000 earnings on the corrective contribution equal to $759 ($6,325(.12)). (See Table 3.)

TABLE 3 CALCULATION AND ALLOCATION OF THE CORRECTIVE AMOUNT ADJUSTED FOR EARNINGS			
	Earnings Rate	Amount	Allocated to:
Corrective Contribution		$5,000	Employee X
First Partial Valuation Period Earnings	15%	750[1]	Employee X
1999 Earnings	10%	575[2]	Employee X
Second Partial Valuation Period Earnings	12%	759[3]	12/31/99 Account Balances (including Employee X's $6,325)[4]
Total Amount Contributed		$7,084	

[1]$5,000 x 15%
[2]$5,750($5,000 +750) x 10%
[3]$6,325($5,000 +750 +575) x 12%
[4]After reduction for distributions during the 2000 year but without regard to contributions received during the 2000 year.

Example 29:

The facts are the same as in *Example 26*.

Earnings Adjustment on the Corrective Contribution

The earnings amount on the corrective contribution is the same as in *Example 23*, but the earnings amount is allocated using the current period allocation method. Thus, the earnings for the first partial valuation period (March 31, 1998 to December 31, 1998) are allocated as 2000 earnings. Accordingly, Employer L makes a contribution on June 1, 2000 to the plan of $7,084 ($5,000 (1.15)(1.10)(1.12)). Employee X's account balance as of December 31, 1999 is increased by the sum of $5,500 ($5,000(1.10)) and the remaining 1999 earnings on the corrective contribution equal to $75 ($5,000(.15)(.10)). Further, both (1) the estimated March 31, 1998 to December 31, 1998 earnings on the corrective contribution equal to $750 ($5,000(.15)) and (2) the estimated January 1, 2000 to June 1, 2000 earnings on the corrective contribution equal to $759 ($6,325(.12)) are treated in the same manner as 2000 earnings by allocating these amounts to the December 31, 2000 account balances of employees in proportion to account balances as of December 31, 1999 (including Employee X's increased account balance). (See, Table 4.) Thus, Employee X is allocated the earnings for the full valuation period during the period of the failure

TABLE 4
CALCULATION AND ALLOCATION OF THE
CORRECTIVE AMOUNT ADJUSTED FOR EARNINGS

	Earnings Rate	Amount	Allocated to:
Corrective Contribution		$5,000	Employee X
First Partial Valuation Period Earnings	15%	750[1]	12/31/99 Account Balances (including Employee X's $5,575)[4]
1999 Earnings	10%	575[2]	Employee X
Second Partial Valuation Period Earnings	12%	759[3]	12/31/99 Account Balances (including Employee X's $5,575)[4]
Total Amount Contributed		$7,084	

[1]$5,000 x 15%

[2]$5,750($5,000 +750) x 10%

[3]$6,325($5,000 +750 +575) x 12%

[4]After reduction for distributions during the year for which earnings are being determined but without regard to contributions received during the year for which earnings are being determined.

APPENDIX C
VCP CHECKLIST
IS YOUR SUBMISSION COMPLETE?

INSTRUCTIONS

The Service will be able to respond more quickly to your VCP 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, as appropriate, in the blank next to the item. *Sign and date the checklist (as taxpayer or authorized representative) and include it in the submission as provided in section 11.09 of Rev. Proc. 2006–27 (Hereafter, all section references are to Rev. Proc. 2006–27.)*

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. Does the submission consist solely of a failure to amend a plan timely for (a) good faith plan amendments for EGTRRA, (b) plan amendments for the final and temporary regulations under § 401(a)(9) or (c) interim amendments? If yes, please proceed to Appendix F. (See section 11.01 and sections 4.06 and 10.08.)

_____ 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 11.02(3) and (4).)

_____ 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 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 11.02(5).)

_____ 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 11.02(6).)

_____ 5. Have you submitted specific calculations for either affected employees or a representative sample of affected employees? (See section 11.02(7).)

_____ 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) or the correction(s), provided an affirmative statement to that effect? (See section 11.02(8).)

_____ 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 11.02(9).)

_____ 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 11.02(10).)

_____ 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 11.02(10).)

_____ 10. Have you included a statement that neither the plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction? Alternatively, have you provided a statement identifying the abusive tax avoidance transaction(s) to which the plan or the Plan Sponsor has been a party? (See section 11.02(11).)

_____ 11. If the submission includes a failure related to Transferred Assets, have you included a description of the related employer transaction, including the date of the employer transaction and the date the assets were transferred to the plan? (See section 11.02(12).)

_____ 12. 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 11.03(2).)

_____ 13. Have you included the original signature of the sponsor or the sponsor's authorized representative? (See section 11.06.)

_____ 14. Have you included a Power of Attorney (Form 2848) or Tax Information Authorization (Form 8821)? Note: Authorization to represent a plan sponsor before the Service using Form 2848 is limited to attorneys, certified public accountants, enrolled agents, and enrolled actuaries. (See section 11.07.)

_____ 15. Have you included a Penalty of Perjury Statement signed (original signature only) and dated by the Plan Sponsor? (See section 11.08.)

_____ 16. Have you designated your submission for a Qualified Plan, 403(b) Plan, SEP, SIMPLE IRA Plan, or Orphan Plan? In addition, the submission should indicate if the submission is a Group Submission, an Anonymous Submission, a nonamender submission, a multiemployer or multiple employer plan submission. (See section 11.10.)

_____ 17. Have you submitted the Appendix E acknowledgement letter? (See section 11.11.)

_____ 18. If you are requesting a waiver of the excise tax under § 4974 of the Code, have you included the request, and, if applicable, an explanation supporting the request for any affected owner-employee or 10 percent owner? (See section 6.09(2).)

_____ 19. If you are requesting relief of the excise tax under §§ 4972 or 4979, have you included the request and a detailed description of the failure? (See sections 6.09 (3) & (4).)

_____ 20. If you are you requesting that participant loans being corrected under this revenue procedure not be treated as distributions pursuant to § 72(p), have you included the request and a detailed description of the failure? Alternatively, if you are requesting that participant loans being corrected under this revenue procedure be recognized as distributions in the year of correction, instead of the year that the deemed distribution occurred under § 72(p), have you included the request and a detailed description of the failure? (See sections 6.02(6) and 6.07.)

_____ 21. Where applicable, have you submitted an application for a determination letter and Form 8717 together with a check for the user fee made payable to the U.S. Treasury? (See sections 10.06 and 11.03(3).)

_____ 22. If the plan is currently being considered in an unrelated determination letter application, have you included a statement to that effect? (See section 11.02(12).)

_____ 23. Have you included a copy of the first three pages of the Form 5500 (which includes employee census information) and the applicable Financial Information Schedule 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 11.03(1).)

_____ 24. Where applicable have you included a check for the VCP compliance fee, and, if applicable, a separate check for the determination letter fee each made payable to the U.S. Treasury? (See sections 10.06 and 12.01).)

_____ 25. If your submission is for a terminating Orphan Plan, have you included a request for a waiver of the VCP fee? (See section 12.02(3).)

_____ 26. Have you assembled your submission as described in section 11.14?

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

Signature

Date

Title or Authority

Typed or printed name of person signing checklist

APPENDIX D

SAMPLE FORMATS FOR VCP SUBMISSIONS

The following sample submission formats may be photocopied and used as part of a VCP submission.

I. SAMPLE FORMAT FOR VCP SUBMISSION FOR QUALIFIED PLAN

Indicate Plan Type, and whether submission is a Group or Anonymous Submission

Identification of Failures

A complete description, for each failure, which includes (but is not limited to):

1) A description of the failure
2) Years in which the failure occurred (including closed years)
3) Number of participants affected (may be estimated)
4) A description of the administrative procedures in effect at the time the failures occurred
5) Explanation of how and why the failures occurred

Description of Proposed Method of Correction

A complete description of the correction proposed, for each failure, which includes (but is not limited to):

1) a complete description of the method of correction proposed for correcting the failure and if multiple steps are involved, a narrative of the steps involved in implementing the proposed correction
2) the number of employees affected (may be estimated)
3) the expected cost of correction (may be estimated)
4) the years involved
5) calculations or assumptions used to determine the amounts needed for correction
6) 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(4) of Rev. Proc. 2006–27)
7) specific calculations, sufficient to demonstrate each aspect of the correction method proposed, for each affected employee or a representative sample of affected employees
8) 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 or will be affected by the correction
9) if a submission includes a failure that refers to Transferred Assets and the failure occurred prior to the transfer, a description of the transaction (including the dates of the employer change and the plan transfer)
10) any request (with supporting rationale) for either not treating participant loans as distributions pursuant to § 72(p) or that deemed distributions under § 72(p) be recognized in the year of correction
11) any specific request (with supporting rationale) for relief from excise taxes under §§ 4972, 4974 or 4979
12) for Orphan Plans only, any specific request for relief (with supporting rationale) from imposition of the Voluntary Compliance fee

Description of Administrative Procedures

A description of the administrative measures that have been or will be implemented to ensure that the failure(s) will not recur

Sample Statement regarding status of examination:

To the best of the Plan Sponsor's knowledge (1) the subject Plan is not currently under examination of either an Employee Plans Form 5500 series return or other Employee Plans examination, (2) the Plan Sponsor is not under an Exempt Organizations examination (that is, an examination of a Form 990 series return or other Exempt Organizations examination, (3) neither the Employer nor any of its representatives have received verbal or written notification from the TEGE Division of an impending examination or of any impending referral for such examination, nor is the Plan in Appeals or litigation for any issues raised in such an examination, and (4) the subject Plan is not currently under investigation by the Criminal Investigation Division of the Internal Revenue Service.

Sample Statement (if applicable) regarding status of any determination letter application not related to the VCP submission

The Plan Sponsor applied for and has currently pending an application for a favorable determination letter with the Service filed on ***(insert date)***.

Sample Statement regarding abusive tax avoidance transactions if neither the Plan nor the Plan Sponsor was a party to such a transaction (note - if either the plan or plan sponsor was a party to such a transaction, a statement describing the transaction will be required)

Neither the Plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction as defined in section 4.13(2) of Rev. Proc. 2006–27.

Sample Penalty of Perjury:

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 and information presented in support of this submission are true, correct and complete.

Name and Title (Executed by Plan Sponsor)

Required Documentation:

____ Copy of plan document (or relevant plan provisions, i.e., those provisions relating to the failure(s) described in the submission)

____ Copy of the first three pages of the most recently filed Form 5500 series return and the applicable Financial Information Schedule. (In the case of a terminated plan, the Form 5500 must be the one filed for the plan year prior to the plan year for which the Final Form 5500 return was filed.)

____ *Power of Attorney* (Form 2848) or *Tax Information Authorization* (Form 8821), if applicable

____ A statement that neither the plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction (as defined in section 4.13(2)) or a brief identification of any abusive tax avoidance transaction to which the plan or the Plan Sponsor has been a party

Determination letter application

Your submission must include a determination letter application on the appropriate Form 5300 series application form if you are correcting a nonamender failure. A nonamender failure is a failure to amend the plan to reflect a change in a qualification requirement within the plan's applicable remedial amendment period. A change in a qualification requirement includes a change arising from a statutory change, issuance of regulations or other guidance published in the Internal Revenue Bulletin. If you are correcting the nonamender failure through the adoption of an amendment designated by the Service as a model amendment or the adoption of a prototype or volume submitter plan for which you have reliance on the plan's opinion or advisory letter as provided in Rev. Proc. 2006–6, 2006–1 I.R.B. 204, no determination letter application is necessary. If your plan is terminating, or if you are correcting a failure other than a nonamender failure through a plan amendment and you are submitting your VCP submission during the same year the plan's remedial amendment period is expiring, you may request a determination letter on the plan. When submitting for a determination letter with a VCP submission, please submit the following documents:

____ a copy of the amendment (or entire plan, in the case of a nonamender failure)

____ the appropriate Form 5300 series application form, and

____ Form 8717 and the appropriate determination letter user fee

Assembling your submission

Please assemble your submission package in the order provided in section 11.14 of this revenue procedure (and partially reproduced below). The sample format above may be used as a tool for preparing the information required for your submission.

1. If applicable, Form 8717, *User Fee for Employee Plan Determination Letter Request*, and the check for the determination letter user fee made payable to the U.S. Treasury
2. Determination letter application (Form 5300 series), if applicable

3. Submission signed by the Plan Sponsor or Plan Sponsor's authorized representative, with a check for the VCP fee made payable to the U.S. Treasury attached to the front of the submission letter. The submission should include the following:

   - Type of plan (or group of plans) being submitted
   - Description of the failures (if the failures relate to Transferred Assets, include a description of the related employer transaction)
   - An explanation of how and why the failures arose
   - Description of the method for correcting failures, including earnings methodology (if applicable) and supporting computations (if applicable)
   - Description of the method used to locate or notify former employees affected by the failures or corrections and if no former employees are affected by the failures or corrections, then the letter should affirmatively state that position when addressing this issue
   - Description of the administrative procedures that have been or will be implemented to ensure that the failures do not recur
   - Whether a request that participant loans corrected under this revenue procedure not be treated as distributions §72(p) is being made and supporting rationale for such request. Alternatively, whether a request that participant loans corrected under this revenue procedure should be treated as distributions in the year of correction is being made and supporting rationale for such request.
   - Whether relief from imposition of the excise taxes under §§ 4972, 4974 or 4979 is being requested, and the supporting rationale for such relief
   - If the plan is an Orphan Plan, whether relief from the VCP application fee is being requested, and the supporting rationale for such relief
   - A statement on whether the plan is being considered in an unrelated determination letter application (if applicable)
   - Statement that the plan is not Under Examination
   - Statement that the Plan Sponsor is not under an Exempt Organizations examination
   - A statement that neither the plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction (as defined in section 4.13(2)) or a brief identification of any abusive tax avoidance transaction to which the plan or the Plan Sponsor has been a party
   - Penalty of perjury statement

4. Completed and signed checklist (see Appendix C of Rev. Proc. 2006–27)

5. Acknowledgement Letter, if desired (see Appendix E of Rev. Proc. 2006–27)

6. *Power of Attorney* (Form 2848) or *Tax Information Authorization* (Form 8821), if applicable

7. Form 5500, (first three pages and the applicable Financial Information Schedule) or equivalent information

8. Copy of opinion or determination letter (if applicable)

9. Relevant plan document language or plan document (if applicable)

10. Any other items that may be relevant to the submission

II. SAMPLE FORMAT FOR VCP SUBMISSION FOR QUALIFIED PLAN WHERE THE ONLY ISSUE IS A NONAMENDER FAILURE

Indicate Plan Type, and whether submission is a Group or Anonymous Submission

Identification of Failures

1) Indicate which tax legislation is the subject of the submission: (check all that apply)

____ The Employee Retirement Security Act of 1974 (ERISA)

____ The Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA)

____ The Deficit Reduction Act of 1984 (DEFRA)

____ The Retirement Equity Act of 1984 (REA)

____ The Tax Reform Act of 1986 (TRA '86)

____ The Unemployment Compensation Act of 1992 (UCA)

____ The Omnibus Budget Reconciliation Act of 1993 (OBRA '93)

____ The Uruguay Round Agreements Act; the Uniformed Services Employment and Reemployment Rights Act of 1994; the Small Business Job Protection Act of 1996; the Taxpayer Relief Act of 1997; the Internal Revenue Service Restructuring and Reform Act of 1998; and the Community Renewal Tax Relief Act of 2000 (collectively known as "GUST")

____ The good faith plan amendments for the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"), within the period described in Notice 2001–42 including those changes listed in Notice 2005–5

____ The final and temporary regulations under § 401(a)(9) of the Internal Revenue Code

____ interim amendments pursuant to section 5 of Rev. Proc. 2005–66

Please List:

_____

_____

_____

_____

____ EGTRRA

____ Other:

Please list: _____

2) Years in which the failure(s) occurred (including closed years)

3) A description of the administrative procedures in effect at the time the failures occurred

4) Explanation of how and why the failures occurred

Description of Proposed Method of Correction

Include appropriate determination letter application (see "Required Documentation," below).

Description of Administrative Procedures

A description of the administrative measures that have been or will be implemented to ensure that the failure(s) will not recur

Sample Statement regarding status of examination:

To the best of the Plan Sponsor's knowledge (1) the subject Plan is not currently under examination of either an Employee Plans Form 5500 series return or other Employee Plans examination, (2) the Plan Sponsor is not under an Exempt Organizations examination (that is, an examination of a Form 990 series return or other Exempt Organizations examination, (3) neither the Employer nor any of its representatives have received verbal or written notification from the TEGE Division of an impending examination or of any impending referral for such examination, nor is the Plan in Appeals or litigation for any issues raised in such an examination, and (4) the subject Plan is not currently under investigation by the Criminal Investigation Division of the Internal Revenue Service.

Sample Statement regarding abusive tax avoidance transactions if neither the Plan nor the Plan Sponsor was a party to such a transaction (note - if either the plan or plan sponsor was a party to such a transaction, a statement describing the transaction will be required)

Neither the Plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction as defined in section 4.13(2) of Rev. Proc. 2006–27.

Sample Statement (if applicable) regarding status of any determination letter application not related to the VCP submission

The Plan Sponsor applied for and has currently pending an application for a favorable determination letter with the Service filed on ***(insert date)***.

Sample Penalty of Perjury:

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 and information presented in support of this submission are true, correct, and complete.

_____

Name and Title (Executed by Plan Sponsor)

Required Documentation:

____ Appropriate determination letter application form (*i.e.*, Form 5300 series)

____ Copy of plan document in effect prior to proposed amendment

____ Copy of the proposed plan amendment

____ Form 8717 and determination user fee

____ Any other materials required to be submitted with determination letter application (see Forms 5300, 5310 & Schedule Q, and 5303)

____ Copy of the first three pages of the most recently filed Form 5500 series return and the applicable Financial Information Schedule (In the case of a terminated plan, include the Form 5500 filed for the plan year prior to the plan year for which the Final Form 5500 return was filed.)

____ *Power of Attorney* (Form 2848) or *Tax Information Authorization* (Form 8821), if applicable

____ A statement that neither the plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction (as defined in section 4.13(2)) or a brief identification of any abusive tax avoidance transaction to which the plan or the Plan Sponsor has been a party

____ Copy of determination letter most recently issued with respect to the plan

Your submission must include a determination letter application on the appropriate Form 5300 series application form if you are correcting a nonamender failure. A nonamender failure is a failure to amend the plan to reflect a change in a qualification requirement within the plan's applicable remedial amendment period. A change in a qualification requirement includes a change arising from a statutory change, issuance of regulations or other guidance published in the Internal Revenue Bulletin. If you are correcting the nonamender failure through the adoption of an amendment designated by the Service as a model amendment or the adoption of a prototype or volume submitter plan for which you have reliance on the plan's opinion or advisory letter as provided in Rev. Proc. 2006–6, 2006–1 I.R.B. 204, no determination letter application is necessary. If your plan is terminating, or if you are correcting a failure other than a nonamender failure through a plan amendment and you are submitting your VCP submission during the same year the plan's remedial amendment period is expiring, you may request a determination letter on the plan.

Assembling your submission

If you are preparing your submission using the sample format provided above, please assemble your submission package in the following order:

1. If applicable, Form 8717, *User Fee for Employee Plan Determination Letter Request*, and the check for the determination letter user fee made payable to the U.S. Treasury
2. Determination letter application (Form 5300 series), if applicable
3. Submission, with a check for the VC fee made payable to the U.S. Treasury attached to the front of the submission letter, and including:
   - Identification of Failures
   - Description of Proposed Method of Correction
   - Description of Administrative Procedures
   - Statement regarding status of examination
   - Statement regarding abusive tax avoidance transactions
   - Statement regarding unrelated determination letter application (if applicable)
   - Penalty of Perjury statement
4. Completed and signed Checklist (see Appendix C of Rev. Proc. 2006–27)
5. Acknowledgement Letter, if desired (see Appendix E of Rev. Proc. 2006–27)
6. *Power of Attorney* (Form 2848) or *Tax Information Authorization* (Form 8821), if applicable
7. Form 5500 (first three pages and the applicable Financial Information Schedule) or equivalent information including: number of participants in the plan and total amount of plan assets
8. Copy of opinion or determination letter
9. Copy of plan document in effect prior to the proposed plan amendment(s)
10. Copy of the proposed plan amendments

APPENDIX E
Acknowledgement Letter

[	]	INSERT NAME AND ADDRESS OF PLAN SPONSOR OR POWER OF ATTORNEY AT LEFT
[	]	
[	]	
[	]	

Plan Name: [Insert plan name and plan number]

Control #: _____ [To be completed by the Internal Revenue Service]

Received Date: _____ [To be completed by the Internal Revenue Service]

The Internal Revenue Service, Employee Plans Voluntary Compliance, has received your VCP Submission for the above-captioned plan. Your request has been assigned the control number listed above. This number should be referred to in any communication to us concerning your submission.

You will be contacted when the case is assigned to an agent. If you are not contacted within 120 days from the date of this letter, and need to inquire about the status of your case, please call (202) 283–9888 (not a toll-free number). Please leave a message with the name of the Plan, the Control Number, your name and a phone number where you can be reached.

Thank you for your cooperation.

APPENDIX F
VCP SAMPLE SUBMISSION FOR INTERIM NONAMENDERS

PLAN SPONSOR'S NAME _____

PLAN SPONSOR'S I.D. NO. _____

PLAN SPONSOR'S ADDRESS:

_____

_____

_____

PLAN NAME & NO. _____

PLAN SPONSOR REPRESENTATIVE NAME _____

PLAN SPONSOR REPRESENTATIVE ADDRESS:

_____

_____

_____

Identification of Failures:

The Plan identified above was not amended timely for: (check failure(s) that apply):

__ the good faith plan amendments for the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"), within the period described in Notice 2001–42 including those changes listed in Notice 2005–5

__ the final and temporary regulations under § 401(a)(9) of the Internal Revenue Code

__ interim amendments pursuant to section 5 of Rev. Proc. 2005–66

Please List:

_____

_____

Description of Proposed Method of Correction

The Plan Sponsor adopted amendments required to correct the failure(s) identified above. The signed and dated amendments are attached to this submission.

Description of steps taken to ensure that the failure does not recur [INSERT below]

Plan Sponsor's representations:

To the best of my knowledge (1) the subject Plan is not currently under examination of either an Employee Plans Form 5500 series return or other Employee Plans examination, (2) the Plan Sponsor is not under an Exempt Organizations examination (that is, an examination of a Form 990 series return or other Exempt Organizations examination, (3) neither the Employer nor any of its representatives have received verbal or written notification from the TEGE Division of an impending examination or of any impending referral for such examination, nor is the Plan in Appeals or litigation for any issues raised in such an examination, and (4) the subject Plan is not currently under investigation by the Criminal Investigation Division of the Internal Revenue Service.

Neither the Plan nor the Plan Sponsor has been a party to an abusive tax avoidance transaction as defined in section 4.13(2) of Rev. Proc. 2006–27.

The Plan Sponsor will neither attempt to amortize, deduct, or recover from the Internal Revenue Service any compliance fee paid in connection with this compliance statement, nor receive any Federal tax benefit on account of payment of such compliance fee.

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 and information presented in support of this submission are true, correct and complete.

Signed: _____

Name (printed): _____

Title: _____

Plan Sponsor's documents:

In addition to the corrective plan amendments described in the "Proposed Method of Correction," the Plan Sponsor encloses the following documents with this submission:

- VC fee of $375 made payable to the U.S. Treasury
- Copy of the first three pages of the most recently filed Form 5500 series return and the applicable Financial Information Schedule. (In the case of a terminated plan, the Form 5500 must be the one filed for the plan year prior to the plan year for which the Final Form 5500 return was filed)
- *Power of Attorney* (Form 2848) or *Tax Information Authorization* (Form 8821), if applicable

Enforcement Resolution:

The Internal Revenue Service will not pursue the sanction of plan disqualification on account of the qualification failures described in this VCP submission.

The Internal Revenue Service will treat the adoption of the amendments as making available the remedial amendment period, currently described in Rev. Proc. 2005–66.

Approved: _____

Joyce Kahn, Manager
Employee Plans Voluntary Compliance
Tax Exempt and Government Entities Division
Internal Revenue Service

Date: _____