IRS Questionnaire Sent to College, University Plans Does Not Put Plans "Under Examination" but EPCRS Availability Remains Unclear

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The IRS Employee Plans Compliance Unit ("EPCU") is in the process of sending over 300 written questionnaires to a random sample of small, medium, and large institutes of higher education, including private and public colleges, universities, and trade and vocational schools. The questionnaire – on IRS Form 886-A – contains 18 separate questions but mainly focuses on one issue: whether the organization's Section 403(b) plan satisfies the "universal availability" requirement. Under that rule, if one employee has the opportunity to defer a portion of salary under the plan, then generally all employees must be offered the same opportunity. (Very limited exceptions apply.) The questionnaire seeks to identify plans that are not making the deferral opportunity universally available, either because the limited exceptions are misapplied, or the employer imposes additional conditions on deferring that are not permitted under law. A number of the questions refer specifically to exclusion of groups of employees unique to educational organizations, such as medical residents, and different categories of instructors, professors or lecturers. An IRS announcement on the project as well as links to the questionnaire, instructions for filling out same, and a glossary of terms, can be found here.

Organizations have 25 days to complete and return the questionnaire by fax, mail or e-mail. Upon review of the questionnaire, the IRS will either deem a plan to be compliant and issue a "closing letter," or will request additional information from the organization. If a problem is found the IRS will work with the organization to correct it, for instance by making fully vested employer contributions to restore the lost opportunity to make tax deferrals in prior plan years. (Generally the employer contribution requirement is equal to half of the deferral the employee would have made (the "lost opportunity" cost), but specific correction methods are not set forth in the questionnaire or in the IRS announcement of the program. Correction methods will be specified in a follow-up letter sent to organizations whose initial responses require follow-up.

Receipt of the questionnaire will not mean that a plan sponsor is "Under Examination" and thus barred from using the Voluntary Correction Program under the Employee Plans Compliance Resolution System ("EPCRS") to correct 403(b) operational errors currently identified in EPCRS (for instance, failure timely to implement an employee's salary deferral election). This was confirmed by the IRS, with regard to a similar 401(k) questionnaire project, in a recent issue of Employee Plans News. That said, the current version of EPCRS, set forth in Revenue Procedure 2008-50, does not provide as many corrections for Section 403(b) plans as are available to other types of qualified plans, largely because Rev. Proc. 2008-50 was drafted before Section 403(b) plans were required to be set forth in writing. For instance, VCP is not available for sponsors that lack a written Section 403(b) plan document or that have failed to operate the plan in accordance with its written terms, nor is it available for employer eligibility failures. The IRS is expected later this year to release an updated version of EPCRS that covers Section 403(b) corrections in greater detail. However, it is not known whether or not the new Revenue Procedure will contain relief for sponsors that failed to timely put a plan document in place or failed to operate a plan in accordance with its written terms.

Tax-exempt employers who receive a questionnaire strongly are advised to consult with their professional tax advisors before submitting a response to the IRS. An incorrect response – or an accurate response – could trigger potential contribution and tax liability on a significant scale, and the availability of EPCRS is uncertain. Such discoveries are better made – and resolutions discussed – with private advisors before the IRS is part of the conversation. If additional time to complete the questionnaire is necessary, employers should request it of the IRS before reaching the 25-day deadline.

http://www.irs.gov/retirement/article/0,,id=238459,00.html
http://www.irs.gov/pub/irs-tege/epn_2011_4.pdf
http://www.irs.gov/pub/irs-drop/rp-08-50.pdf