



GALLOP, JOHNSON & NEUMAN, L.C.

Attorneys and Counselors at Law

BENEFITS ALERT

Failure To Update Benefit Plan Documents Can Be Costly

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The Internal Revenue Code (“Code”) contains numerous rules that a retirement plan must satisfy to constitute a qualified plan and enjoy the related tax benefits. The rules applicable to qualified plans such as 401(k) plans, profit sharing plans and pension plans, as well as the exceptions to the rules, create a complex structure for qualified plans.

In general, the governing plan document must meet all qualification requirements in written form and must be updated as required by changes in the law. For example, every 401(k) plan document must state the plan’s eligibility and vesting rules, which must comply with the Code’s current requirements regarding eligibility and vesting.

Any required provision that is not present in the plan document or any provision that fails to comply with the Code’s requirements is referred to as a disqualifying provision. A plan that is not timely amended to correct the provision may lose its qualified status. When a change in the law requires plans to be amended, the Internal Revenue Service (“IRS”) designates which plan provisions must be added or changed to reflect law changes.

The deadlines to implement required changes are not always clear. Since plans were last required to be restated in their entirety for a series of laws carrying the acronym of GUST, a number of amendments have been required to be incorporated into the plan document,

beginning in 2003. These include the following:

- Good Faith EGTRRA Amendment;
- Amendment to include Code Section 132(f) in the Definition of Compensation;
- Minimum Required Distribution Regulations Amendment;
- Automatic Rollover Amendment; and
- Amendment to Comply with Regulations Issued Under Code Section 415.

The deadlines for most of these amendments have passed

Despite the care taken by plan sponsors, errors often occur in the maintenance of plan documents. Such errors may result in disqualification of the plan, resulting in the potential forfeiture of tax benefits of the plan for the employer and the participants. Alternatively, the IRS may seek significant monetary sanctions rather than disqualification of the plan. Penalties range from \$2,500 to \$80,000 depending on the size of the plan and the extent of the deficiencies. It is to no one’s advantage to have such plan document failures disqualify a plan or for the plan sponsor to incur monetary penalties assessed so onerous that plan sponsors are discouraged from having plans altogether.

Fortunately, programs are available to correct plan document deficiencies and avoid plan disqualification or significant monetary sanctions. Most recently, under Revenue Procedure 2008-50, the IRS has offered additional relief and guidance on the correction of failures that are common among plans. The updated procedures are designed to be user-friendly and recognize some of the practical realities of plan administration.

In general, the IRS encourages plan sponsors to report plan document failures voluntarily. These failures may be corrected using an IRS program called the Voluntary Compliance Program or VCP. For example, plan sponsors who have failed to timely adopt plan amendments or restate their plans to comply with law changes may utilize VCP to correct the errors. Under the program the plan sponsor submits an application with a fee to the IRS identifying the plan document failures along with the proposed amendment to the plan document. The fee is sometimes as low as \$375. By doing this, the plan sponsor avoids the risk of plan disqualification or a more significant monetary sanction.

Plan sponsors should periodically review plan documents with counsel to ensure that plans have been properly updated with required amendments and are compliant with current law. If a plan has not been amended in a timely manner, legal counsel should be contacted immediately for assistance in updating the plan document and correcting errors through a VCP filing.

If you have any questions regarding plan document compliance or the IRS' Voluntary Compliance Program, please contact one of the attorneys referenced below in Gallop, Johnson & Neuman's Employee Benefits and Executive Compensation Practice Group.

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If you wish to obtain further information regarding the issues discussed above, please contact either the Gallop, Johnson & Neuman attorney who normally provides or manages your legal services or Tom Mug or Mitch Gibson of the Firm's Employee Benefits and Executive Compensation Practice Group.

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