IRS & DOL Update: What Has Changed Since Last Year & Why You Need to Know

April 2013
Monika Templeman, Esq.
Director, Employee Plans Examinations, IRS

Jalena Baumgardner
Manager, Employee Plans
With 118.7 Million U.S. Households

- Neither IRA or Retirement Plan 31%
- IRA 8%
- IRA & Retirement Plan 31%
- Retirement Plan 30%
• US Retirement Assets: $19.4 trillion
  • DC plans: $5.0 trillion
    • 401(k): $3.5 trillion
  • IRAs: $5.3 trillion
• Retirement savings = 36% of all financial household assets
2013 Priorities

• International
• 401(k) Plans
• 403(b) Plans
• Using a corporate approach
• Effective global tax administration
• Develop educational tools and guidance
• Partner with international stakeholders
• Address potential noncompliance and abuse
• Develop new global projects
• U.S. companies w/ increasing number of employees working
  • Abroad
  • In U.S. Territories
• Global economy has huge impact on retirement plans
  • Non-compliance
  • Information reporting on cross-border transactions
• Activity at all economic levels - from
  • Huge multinational corporations to
  • IRAs maintained by retirees
• Current exam focus
  • Large case (EPTA) examinations
    • Over 200 examined
  • Puerto Rico
  • U.S. Virgin Islands
• Large Case (EPTA)
  • Foreign pension expense deduction
  • Late deferral deposits
  • Improper reporting amounts (Form 1042-S)
International – Recurring Errors

• Puerto Rico
  • Inadequate/No fidelity bond
  • Non-amender/Late amender
  • No Hacienda determination letter
  • Incorrect plan characteristic code
  • Incorrect employer aggregation
    • Nondiscrimination testing
International – Recurring Errors

- U.S. Virgin Islands
  - Inadequate/No fidelity bond
  - Non-amender/Late amender
  - Late deferral deposits
  - Eligible employees excluded from plan
  - Incorrect vesting percentages
  - Defaulted plan loans
International – Projects

• EPCU
  • Completed – Reports Posted
    • Domestic trusts
    • Foreign distributions
  • Current
    • Hacienda Compliance Project
  • Future
    • Virgin Island Fidelity Bond Project
    • Coverage Project
Section 401(k) plans are the most popular plans in the United States

- More the 500,000 401(k) plans
- Cover over 60 million participants

401(k) Compliance is a key priority

- Most prevalent plan, so audits prevalent as well to ensure plan form and operation issues
• Report will be issued in 2013
• Final Report will enable us to
  • Design and improve case selection strategies
  • Develop follow-up compliance projects
  • Provide better outreach
• Brief Historical Recap
  • 2010 - EPCU contacts 1,200 401(k) plan sponsors
  • Questionnaire completed on-line
  • 98% response rate
  • 2012 – Interim report published
401(k) Plans – Internal Control

Operate and Maintain a 401(k) Plan

- Operating a 401(k) plan
- Reducing or suspending safe harbor nonelective contributions in cases of substantial business hardship
- Internal Control Tool for 401(k) Plans

401(k) Questionnaire Location on the New www.irs.gov/Retirement-Plans
401(k) Plans – Recurring Errors

- Non-amender/Late amender
- Failure to follow the terms of the plan
  - Definition of “Compensation”
  - Matching contributions
- Nondiscrimination testing (ADP/ACP)
- Omitting eligible employees
- IRC 402(g) limits
- Timely deposit of employee elective deferrals
401(k) Plans – EPCU Projects

- Completed projects with reports on website
  - 401(k) Excess Deferrals Project
    - Over 26,000 W-2Cs filed to correct errors
    - Corrected software/date transmission problems
  - 401(k) Money Purchase Plan Project
    - Only 1 of over 700 contacts had improper plan
- Completed – Report Coming Soon
  - 401(k) Questionnaire Final Report
  - 401(k) Untimely Deferral Deposit Project
401(k) Plans – Projects

• EPCU Upcoming Projects
  • Based on Final Report findings

• Learn/Educate/Self-Correct/Enforce (LESE)
  • Completed
    • IRC 402(g) Excesses (only a few issues found)
    • Top Heavy 401(k) Plans (many issues found)
  • In-Progress
    • Safe Harbor 401(k) Plans
      • Based on 401(k) Interim Report findings
    • Initial Year 401(k) Plans
403(b) Plans – Exam Activity

- A slight increase of audits from the past few years
  - Public schools
  - Colleges and universities
  - Hospitals
  - Tax-exempt organizations
- All five areas bringing in new agents to work 403(b) examinations
• Adds definitions of Plan Document Failure, Overpayment and Favorable Letter
• Revises definitions of Operational, Demographic and Employer Eligibility Failure
• Failure to adopt a written plan may be corrected under VCP and Audit CAP
• Temporarily reduced compliance fee for failure to timely adopt a written 403(b) plan
403(b) Plans – Recurring Errors

- Universal Availability
  - Public schools
  - Colleges and universities
- Excess Contributions (all market segments)
  - Age 50 catch-up
  - 402(g)
- Improper Hardship Distributions
  - Public Schools
  - Hospitals
403(b) Plans – EPCU Projects

• Completed – Report Coming Soon
  • Universal Availability
    • K-12 (with a follow up)
    • Higher education

• Future
  • 457 plans sponsored by tax-exempt organizations
Multiemployer Plans – Recurring Errors

- Minimum distribution requirements
- Deficient plan/amendment language
- Failure to properly calculate retirement benefits
- Failure to actuarially adjust benefits when commencement date is after normal retirement age
- Non-collectively bargained employees in plan without participation agreement
The EPCRS Menu

What’s Your Choice?

The impact of non-compliance left unchecked can be costly.

Preventive Maintenance – Fix Mistakes Immediately!!

<table>
<thead>
<tr>
<th></th>
<th>Audit CAP</th>
<th>Voluntary Correction</th>
<th>Self-Correction</th>
</tr>
</thead>
</table>
| Cost of Correction | ![
|
| IRS Fees        | ![
| Time Involved   | ![
| Result          | ![

ATTENTION: PLAN SPONSORS!
• Before, agents began with certain issues to examine
• With pilot, focus on the internal controls of plan and plan sponsor
  • If internal controls adequate, no need to expand audit
• Results in improved audit efficiency and less burden for compliant plan sponsors
Abusive Transactions/Emerging Issues

• Still examine/analyze/review potential abuse in retirement plans
• Emerging issues (patterns of non-compliance)
  • Hard to value assets
  • Defined benefit & PPA funding
  • Aggressive cash balance plans
  • Invalid collectively bargained plans
Promoter Investigations

• Actively working on issues in this area

• Examples
  • Sales of reportable transactions – goal to avoid taxation by exploiting
    • Tax exempt status
    • Tax deferral attributes of retirement plans
  • Springing cash value insurance contracts
  • Management Company S Corp ESOPs
Other EPCU Projects

• Current
  • Frozen plan amendments
  • Missing pension feature codes
  • Partial termination

• Coming Soon…
  • International and 401(k) projects discussed earlier
  • Form 5500EZ & record retention requirements
  • Form 5310-A
Three Agency Strategic Collaboration IRS/DOL/PBGC

- Form development
- Data sharing
- Project partnering
- Update
  - Internal documents
  - Disclosure requirements
  - Business needs
How Can I Find The Retirement Information?

1. Type "retirement" in search box
2. Information For:
   - Individuals
   - Businesses
   - Charities & Non-Profits
   - Government Entities
   - Tax Professionals
   - Retirement Plans
   - Tax Exempt Bonds
## Fix-It Guides - Common Problems, Real Solutions

Find, fix, and avoid common mistakes in plans.

### Video Explanations

#### SEP Plan Fix-It Guide

### Common Problems, Real Solutions

<table>
<thead>
<tr>
<th>Potential Mistake</th>
<th>Find the Mistake</th>
<th>Fix the Mistake</th>
<th>Avoid the Mistake</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) You have not updated your SEP plan document for current law</td>
<td>Determine if your Form 5305-SEP is the current revision (December 2004)</td>
<td>Adopt revised Form 5305-SEP</td>
<td>Maintain regular contact with the company that sold you the plan</td>
</tr>
<tr>
<td>(More) Video)</td>
<td>(More)</td>
<td>(More)</td>
<td>(More)</td>
</tr>
<tr>
<td>2) The plan excluded employees of related businesses from participating</td>
<td>Identify any companies that you own or with which you have a financial relationship</td>
<td>Apply reasonable correction method that would place affected employees in the position they would have been in if there were no operational plan mistakes</td>
<td>Determine if you own any other businesses</td>
</tr>
<tr>
<td>(More)</td>
<td>(More)</td>
<td>(More)</td>
<td>(More)</td>
</tr>
</tbody>
</table>
This Checklist is not a complete description of all plan requirements, and should not be used as a substitute for a complete plan review.

It is important to review the requirements for operating your 403(b) retirement plan annually. This checklist is a “quick tool” to help you keep your plan in compliance with many important tax rules. See IRS Publication 571, Tax Sheltered Annuity Plans (403(b) Plans) for Employees of Public Schools and Certain Tax-Exempt Organizations at www.irs.gov/ep. Underlined text below shows a link to expanded explanations and resources, also at www.irs.gov/ep.

1. Does your organization qualify as a public educational institution or as a charitable organization exempt from tax under IRC 501(c)(3)?
   Yes  No

   Only public educational institutions described in IRC 170(b)(1)(A)(ii), or 501(c)(3) organizations may establish a 403(b) plan.

6. If your program permits age 50+
catch-up contributions, were each of your employees age 50 and over informed of their rights to make catch-up deferrals?
   Yes  No

   If your plan permits, participants age 50+ may defer an additional $5,000 to the 403(b) plan for 2006.

7. Does the 403(b) annuity contract offer a Y/N
Other EP Internal Control Tools

- 401(k) Questionnaire
- Trends and Tips
- EPTA
  - Trends and Tips
  - Internal Controls Questionnaire
- EP Exam Guidelines
- Plan Maintenance Reminders
Department of the Treasury
Internal Revenue Service
www.irs.gov