

Benefits

A Littler Mendelson **Time Sensitive** Newsletter

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Compliance Update: The Voluntary Fiduciary Compliance Program

By J. René Toadvine

The Department of Labor recently revised its Voluntary Fiduciary Correction Program (VFCP). Adopted by the U.S. Department of Labor (DOL) to encourage plan fiduciaries to comply with the provisions of ERISA by providing relief from certain penalties and enforcement actions, VFCP permits employers to proactively remedy fiduciary violations under ERISA by taking prescribed remedial actions. If a plan fiduciary complies with the requirements under VFCP, the plan fiduciary may correct certain specified fiduciary breach transactions and receive a "no action" letter from the DOL. Common fiduciary breaches that may be remedied under VFCP include delinquent participant contributions, prohibited purchases, sales and exchanges of assets and improper payments by the plan of certain expenses. In response to comments made by practitioners who requested that VFCP be broadened and made simpler, the DOL revised VFCP to provide more simplified procedures and add several transactions to the list of transactions eligible for relief under VFCP.

Simplified Procedures

The revised VFCP provides a model VFCP application form and reduces the amount of documentation required to be submitted with the application. The model form, while not mandatory, gives the plan fiduciary an outline of the information and documentation that must be included with the request for relief from DOL enforcement actions and

penalties. The form is available at www.dol.gov/ebsa.

In addition, the calculation of the VFCP correction amount (i.e., the calculation of lost earnings and restoration of profits) has been simplified. The DOL has added an online calculator to its website www.dol.gov/ebsa to perform the required calculations.

Added Eligible Transactions

The DOL expanded the list of transactions eligible for correction under VFCP by adding the following transactions:

- *Correction of the Purchase of Illiquid Assets.* It may be a fiduciary violation for a plan to hold illiquid assets such as restricted and thinly traded stock, limited partnership interests, real estate and collectibles. Under the revised VFCP, a plan may divest, rather than continue to hold, an illiquid asset previously purchased by the plan provided the plan fiduciary determines that the continued holding of such asset is not in the best interest of the plan or plan participants. To correct under VFCP, the plan fiduciary must determine: (a) that the asset has failed to appreciate, failed to provide a reasonable rate of return or has caused a loss to the plan; (b) that the sale of the asset is in the best interest of the plan and (c) following reasonable efforts to sell the asset to a non-party in interest, that the asset cannot immediately be sold for its original purchase price or its current fair

market value, if greater. Once such determination is made, VFCP permits the sale of the illiquid asset to a party in interest, provided the plan is returned to a financial position that is no worse than if the acquisition of the illiquid asset had never taken place. If the illiquid asset is a parcel of real estate, the plan fiduciary must certify that no party in interest owns real estate that is contiguous to the plan's parcel of real estate.

- *Correction of Certain Participant Loans.* If a plan loan is made to a party in interest that exceeds the maximum loan amount permitted by Section 72(p) of the Internal Revenue Code ("the Code"), it is a prohibited transaction. Instead of having to reverse the loan transaction as previously required, VFCP now permits correction by requiring the participant to pay back to the plan the excess amount of the loan. The remaining loan balance must be reamortized over the remaining duration of the original note.

If the plan loan is a prohibited transaction because the duration of the loan exceeds the maximum time period for repayment permitted by Section 72(p) of the Code, VFCP now permits correction if the plan reamortizes the loan and the loan is repaid over a period not to exceed the maximum time period permitted by the Code.

- *Correction of Delinquent Remittance of Participant Loan Repayments.* When a plan participant makes a plan loan repayment, the plan fiduciary is required to remit the loan repayment to the plan within a reasonable time after it is paid. If a plan fiduciary fails to meet this requirement, it is a fiduciary breach. VFCP now permits correction of the breach, provided such loan payment and the greater of (i) the lost earnings on the payment or (ii) the restoration of profits based on the employer's use of the payment, are remitted to the plan.

Effect of VFCP on Actions by Parties Other than the DOL

Full correction under VFCP does not preclude a plan participant or another governmental agency from bringing an action to enforce rights with respect to a transaction that is corrected under VFCP. However, the IRS has indicated that correction of a prohibited transaction under VFCP generally will constitute a correction for purposes of Section 4975 of the Code. Likewise, correction of an operational plan qualification failure under VFCP generally will constitute correction for purposes of the IRS' EPCRS program.

Prohibited Transaction Exemption

In connection with the revised VFCP, the DOL also recently issued a proposed amendment to PTCE 2002-51. PTCE 2002-51 provides relief from the Code's prohibited transaction excise taxes for certain transactions corrected under VFCP. The proposed amendment expands the list of transactions eligible for relief from the Code's prohibited transaction excise taxes.

Final Thoughts

Employers may wish to review their ERISA compliance procedures to ensure that they continue to satisfy the fiduciary obligations set forth in ERISA. To the extent fiduciary compliance issues exist, the revised VFCP may provide a vehicle for compliance resolution.

For further assistance, please consult one of our attorneys in the Employee Benefits Practice Group.