

DOL Updates Voluntary Fiduciary Correction Program

The U.S. Department of Labor (“DOL”) has finalized its 2005 revisions to the Voluntary Fiduciary Correction Program (“VFC Program”) with a number of changes. A summary of the 2005 revisions can be viewed in our April 12, 2005, *Management Alert* at www.seyfarth.com/MA041205. The updates (“2006 Update”) to the VFC Program include:

- ◆ a narrower definition of “under investigation” to permit more persons to qualify for the VFC Program;
- ◆ additional transactions eligible for correction;
- ◆ coordination with the Voluntary Correction Program of the IRS’ Employee Plans Compliance Resolution System (“EPCRS”);
- ◆ new correction methods for party in interest transactions; and
- ◆ expanded scope of relief.

The VFC Program is intended to encourage voluntary correction of fiduciary violations by permitting persons to avoid potential penalties — particularly the 20% Section 502(l) assessment on DOL settlements and Section 4975 prohibited transaction penalty taxes — by using the Program. The updated VFC Program becomes effective on May 19, 2006. Until May 19, 2006, reliance on the prior version of the VFC Program is permitted.

Definition of “Under Investigation” Narrowed

Prior to the 2006 Update, the VFC Program was not available to a plan or other person that is “under investigation” by the DOL or any other federal agency in connection with a plan transaction. The 2006 Update narrows the definition of “under investigation” to make it more plan specific. It will now apply to those situations when an investigation (either ongoing or for which notice has been given) involves the plan or an act or transaction involving the plan. For example, a plan would be considered to be “under examination” if it were undergoing an employee plan examination by the IRS. The VFC Program will continue to be available for

non-criminal investigations and examinations of a plan, or a person in connection with an act or transaction directly related to the plan, by the Pension Benefit Guaranty Corporation (PBGC) or certain state agency officials, subject to disclosure of the investigation in applying under the Program.

New Covered Transactions

The VFC Program is only available for the correction of certain listed transactions. The 2006 Update expands the previously listed transactions to include:

- ◆ **plan expense violations** involving the use of plan assets to pay expenses that should have been borne by the plan sponsor — either because a plan provision requires that such expenses be paid by the plan sponsor or such expenses are “settlor” expenses (*i.e.*, expenses not permitted to be paid with plan assets under applicable law);
- ◆ **plan loan violations** involving the level amortization requirement for plan loans; and
- ◆ **illiquid asset violations** involving the holding of an illiquid asset by a plan that was acquired from a “party in interest” (*i.e.*, plan fiduciary) pursuant to a statutory or administrative exemption.

Coordination with IRS’ Voluntary Correction Program

The 2006 Update changes the correction of participant loan violations involving a failure to comply with plan provisions for amount, duration or level amortization. Under the final VFC Program, correction only has to be made with IRS approval under the Voluntary Correction Program of the IRS’ EPCRS Program, when published. Once correction is completed, a copy of the resulting EPCRS compliance agreement, together with evidence of the payment of any required amounts, may be submitted to the DOL under the VFC Program.

Expanded Scope of Penalty Relief

The DOL adopted Prohibited Transaction Exemption 2002-51 (PTE 2002-51) to exempt certain transactions covered by the VFC Program from the excise taxes that would otherwise apply. PTE 2002-51 has been amended in connection with the 2006 Update to:

- ♦ cover the use of plan assets to pay expenses to a service provider for services that are properly characterized as “settlor” expenses, provided such payments were not expressly prohibited by the plan document; and
- ♦ eliminate the requirement to provide notice to “interested parties” of correction under the VFC Program for the failure to timely transmit participant contributions and/or loan repayments to a pension plan.

The elimination of the notice requirement is only available if specific requirements under PTE 2002-51 are satisfied (*e.g.*, the amount of the excise tax that would otherwise apply is \$100 or less).

ERISA Sections 502(l) and 502(i) permit the DOL to assess civil penalties for transactions covered by the VFC Program. However, “no action” letters issued under the VFC Program prior to the 2006 Update covered only penalties under ERISA Section 502(l). ERISA Section 502(i) provides civil penalties for “prohibited transactions” with respect to welfare plans and nonqualified pension plans. The 2006 Update provides relief from the imposition of potential civil penalties under both Section 501(l) and 502(i). This change was made to provide more complete relief for corrections completed under the VFC Program.

Correction of Party in Interest Transactions

Prior to the 2006 Update, the VFC Program provided that violations involving a plan’s purchase of an asset from a “party in interest” had to be corrected by selling the asset back to the party in interest or to a non-party in interest. The 2006 Update permits a plan to retain the asset purchased from a party in interest by settling the correction amount in cash, provided that an independent fiduciary determines that the plan will realize a greater benefit from this correction than it would from the resale of the asset. An independent fiduciary is not required if the plan sells the asset back to the party in interest.

The VFC Program permits a similar cash settlement or reversal of the transaction to correct a plan’s sale of an asset to a party in interest. The 2006 Update modifies this correction to require a determination by an independent fiduciary only in the situation where the plan settles the transaction in cash.

The VFC Program provides a valuable correction option for persons who are involved in the covered transactions. However, it is important to remember that the VFC Program does not apply to any transactions that are not specifically listed, and that it is generally not binding on any other governmental agencies (*i.e.*, IRS). Accordingly, careful analysis should be performed prior to electing to make an application under the VFC Program.

If you have any questions concerning the Voluntary Fiduciary Correction Program, please contact the Seyfarth Shaw Employee Benefits attorney with whom you work or any Employee Benefits attorney on the website at www.seyfarth.com.

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