

DEPARTMENT OF LABOR**Pension and Welfare Benefits Administration**

RIN 1210-AA76

Voluntary Fiduciary Correction Program**AGENCY:** Pension and Welfare Benefits Administration, Labor.**ACTION:** Voluntary Fiduciary Correction Program.

SUMMARY: The Department of Labor adopts a Voluntary Fiduciary Correction Program (VFC Program) by the Department of Labor's Pension and Welfare Benefits Administration (PWBA). The VFC Program allows certain persons to avoid potential Employee Retirement Income Security Act (ERISA) civil actions initiated by the Department of Labor, and the assessment of civil penalties under section 502(l) of ERISA in connection with investigation or civil action by the Department. The VFC Program is designed to benefit workers by encouraging the voluntary and timely correction of possible fiduciary breaches of Part 4 of Title I of ERISA. Although the VFC Program is being put into effect 30 days after publication in the **Federal Register**, the Department is seeking comments from the public on all aspects of the program.

DATES: Written comments must be received by the Department by May 15, 2000.

Effective Date: April 14, 2000.

ADDRESSES: Address questions regarding specific applications for relief under the VFC Program to the appropriate PWBA Regional Office listed in Appendix C.

Address comments on the VFC Program in writing to: VFC Program, Office of Enforcement, Pension and Welfare Benefits Administration, U.S. Department of Labor, Room N5702, 200 Constitution Ave., NW, Washington, DC 20210. Written comments may also be sent by Internet to: vfc-program@pwba.dol.gov.

Address comments that concern information collection requirements to the Office of Information and Regulatory Affairs, Office of Management and Budget, Room 10235, New Executive Office Building, Washington, DC 20503; Attention: Desk Officer for the Pension and Welfare Benefits Administration.

FOR FURTHER INFORMATION CONTACT:

For Specific Applications Under the VFC Program: Contact the appropriate PWBA Regional Office listed in Appendix C.

For General Questions Regarding the VFC Program: Contact the appropriate

PWBA Regional Office listed in Appendix C or Jeffrey A. Monhart, Investigator, Office of Enforcement, Pension and Welfare Benefits Administration, U.S. Department of Labor, Washington, DC (202) 219-8820.

For Comments on the VFC Program: Contact Elizabeth A. Goodman, Pension Law Specialist, Office of Regulations and Interpretations, Pension and Welfare Benefits Administration, U.S. Department of Labor, Washington, DC (202) 219-8671. (These are not toll-free numbers.)

SUPPLEMENTARY INFORMATION:**Background**

Title I of ERISA, 29 USC section 1001 *et seq.*, establishes certain standards with which officials of employee benefit plans covered by ERISA must comply. PWBA helps the public to understand the requirements of Title I of ERISA. In addition, PWBA conducts investigations to deter and correct violations of ERISA.

Based on PWBA's experience with the Pension Payback Program, 61 FR 9203 (March 7, 1996) (Pension Payback Program), and continued interest in such programs, PWBA has decided to establish the VFC Program. The project will be administered out of each of PWBA's ten regional offices. The VFC Program is designed to assist Plan Officials (as defined in Section 3) by specifying the steps necessary to correct certain potential violations of Title I of ERISA.

Section 409 of ERISA provides that a fiduciary who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by Part 4 of Title I of ERISA shall be personally liable to make good to a plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through the use of assets of the plan by the fiduciary. Where more than one fiduciary is liable for a breach, liability is joint and several. The Secretary of Labor has the authority, under sections 502(a)(2) and 502(a)(5), to bring civil actions to enforce the provisions of Title I of ERISA. Section 502(l) of ERISA requires the assessment of a civil penalty in an amount equal to 20 percent of the amount recovered under any settlement agreement with the Secretary or ordered by a court in an action initiated by the Secretary under section 502(a)(2) or 502(a)(5) with respect to any breach of fiduciary responsibility under (or other violation of) Part 4 by a fiduciary. Under ERISA section 502(l)(1)(B), this civil penalty may also be assessed against knowing participants in a breach.

PWBA believes that the possibility of investigation, commencement of a civil action, and imposition of a civil penalty under section 502(l) of ERISA may constrain persons who have engaged in a possible breach of fiduciary responsibility under Part 4 of Title I of ERISA from identifying themselves and working with PWBA to correct the breach fully and make the plan whole. To encourage the full correction of certain breaches of fiduciary responsibility and the restoration to participants and beneficiaries of losses resulting from those breaches, PWBA has decided to implement the VFC Program. Under this Program, persons who are potentially liable for a breach will be relieved of the possibility of civil investigation of that breach and/or civil action by the Secretary with respect to that breach, and imposition of civil penalties under ERISA section 502(l), if they satisfy the conditions for correcting the breach, as described in the VFC Program.

If a person files an application under the VFC Program, but the corrective action falls short of a complete and acceptable correction, PWBA may reject the application and pursue enforcement, including assessment of a section 502(l) penalty. However, no section 502(l) penalty would be imposed on the basis of any amounts restored to the plan prior to filing the VFC Program application. The penalty would only apply to the additional recovery amount, if any, paid to the plan pursuant to a court order or a settlement agreement with the Department.

Description of Voluntary Fiduciary Correction Program

The VFC Program is set forth in seven sections and three appendices. The VFC Program has been structured to maximize the ability of Plan Officials to identify and correct possible breaches that are within the scope of the Program without the need to consult with PWBA. As noted in Section 1, Purpose and Overview of the Voluntary Fiduciary Correction Program, PWBA believes that the VFC Program will assist Plan Officials in understanding the requirements of Part 4 of Title I of ERISA and will facilitate the correction of transactions and the restoration of losses to employee benefit plans resulting from fiduciary breaches.

Section 2, Effect of the VFC Program, makes clear that the applicant must be careful to ensure that the eligibility requirements are met and the corrections specified for individual transactions are performed before an application is filed under the VFC Program. Generally, if an applicant is in

full compliance with all of the terms and procedures set forth in the VFC Program, PWBA will issue a "no action letter" in the format shown in Appendix A with respect to the breach described in the application. We note, however, that relief under the VFC Program is limited to the transactions identified in the application and the persons who corrected those transactions. In certain cases, such as where PWBA becomes aware of possible criminal behavior, any material misrepresentations or omissions in the VFC application, or other abuse of the VFC Program, relief will not be available under the VFC Program and the Department may initiate an investigation which may lead to enforcement action. PWBA expects that such cases will be unusual. Full correction under the VFC Program does not preclude any other governmental agency, including the Internal Revenue Service (IRS), from exercising any rights it may have with respect to the transactions that are the subject of the application. The Department seeks comments on possible areas of coordination between PWBA and the IRS that would facilitate voluntary correction of breaches of Title I of ERISA. The Department notes that based on its preliminary review of the VFC Program, the IRS has indicated that except in those instances where the fiduciary breach or its correction result in a tax abuse situation or a plan qualification failure, a correction under this program generally will be acceptable under the Internal Revenue Code.

The VFC Program is designed to address a wide variety of situations where plans have been harmed as a result of possible breaches of fiduciary duty. Section 3, Definitions, makes clear that a transaction may be corrected without a determination that there is an actual breach; there need only be a possible breach. In addition, persons who may correct a fiduciary breach include not only the breaching fiduciary, but also plan sponsors, parties in interest or other persons who are in a position to correct a breach. However, the definition of Under Investigation, along with the criteria set forth in Section 4, Program Eligibility, provides that persons or plans who are the subject of pending investigations for violations of Title I of ERISA, or who appear to have engaged in criminal violations, may not take advantage of the VFC Program. Further, PWBA reserves the right to reject an application when warranted by the facts and circumstances of a particular case.

PWBA believes that it must assess a penalty under section 502(l) of ERISA to

the extent that it negotiates relief owed to the plan as a result of a transaction in exchange for a no action letter to the potentially liable persons. Accordingly, the VFC Program is structured so that applicants have the maximum information available to identify eligible transactions and make complete and fully acceptable corrections without discussion or negotiation with the Department.

Section 5, General Rules for Acceptable Correction, sets forth issues that are likely to be present with regard to any transaction described in Section 7. For example, Section 5 describes how fair market value determinations must be made, how correction amounts must be determined, and what documentation is required for all applications. Section 5 also makes clear that the cost of correction must be borne by the applicant and not the plan. In addition, Section 5 states when notice must be provided to participants and when former employees who have already been cashed out of a plan must also be included in any amount restored to a plan.

Section 6, Application Procedures, specifies the requirements for the application, including the required documentation and the penalty of perjury statement that must be signed by a plan fiduciary with knowledge of the transaction and the authorized representative, if any. Section 6 is supplemented by Appendix B, the VFC Program Checklist, that helps the applicant to determine whether he or she has met all of the application requirements, including all documentation, prior to submission to PWBA.

Section 7, Description of Eligible Transactions and Methods of Correction sets forth five types of transactions which may be corrected pursuant to the VFC Program. The first, "delinquent participant contributions to pension plans," is included in the Program based on PWBA's experience with the Pension Payback Program. PWBA notes that, unlike the Pension Payback Program, the VFC Program does not exempt from excise taxes any violations of section 4975 of the Internal Revenue Code (the Code). PWBA included the other types of transactions based on its enforcement experience. For the current stage of the VFC Program, PWBA has taken a conservative approach and has limited the eligible transactions to those where the nature of the transaction and the required correction could be described accurately without reference to a specific situation, and thus could be corrected satisfactorily without

consultation and negotiation with PWBA.

Request for Notice and Comments

Although the Department is not required to seek public comments on an enforcement policy, the Department solicits comments from the public on all aspects of this Program, including whether there are different ways in which the transactions included in the VFC Program could be corrected in accordance with the goals of the Program, as well as whether there are additional transactions involving fiduciary breaches that could be included in the VFC Program. At the same time, the Department has determined that the relief afforded by the VFC Program should be made available during and after the comment period. Delaying implementation of this Program until after the end of the comment period would serve no useful purpose and is unnecessary. Even without publication of this notice, the Department would have the authority to decline to investigate a potential breach of Title I of ERISA in a situation where it has received evidence of adequate correction. Delay in implementing the VFC Program would only deprive persons of the ability to use the clearly set forth procedural aspects of the Program during the comment period. The purpose of the VFC Program is to permit persons who may have violated certain provisions of Title I of ERISA to correct the violations and obtain assurance that the Department will take no further action with respect to the matter, including the assessment of a civil money penalty. Participation in the VFC Program is entirely voluntary and is favorable to those fiduciaries who meet the requirements. Implementation of the VFC Program does not foreclose resolution of fiduciary breaches by other means including entering into settlement agreements with the Department. Immediate implementation also favors participants of plans for which violations are corrected pursuant to the Program. Moreover, as explained above, the Department expects that the availability of the VFC Program will encourage fiduciaries, who otherwise might not do so, to correct violations and reimburse plan losses. As a result, the Department has determined that the VFC Program shall be implemented 30 days after publication in the **Federal Register**.

Although the Department is implementing the VFC Program effective 30 days after publication in the **Federal Register**, it believes that rapid implementation of a final version of the VFC Program would benefit the public.

Accordingly, the Department plans to implement a final version of the VFC Program within 180 days following the close of the 60 day period for comments on the VFC Program.

Executive Order 12866

Under Executive Order 12866, the Department must determine whether a regulatory action is "significant" and therefore subject to the requirements of the Executive Order and subject to review by the Office of Management and Budget (OMB). Under section 3(f), the order defines a "significant regulatory action" as an action that is likely to result in a rule (1) having an annual effect on the economy of \$100 million or more, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local or tribal governments or communities (also referred to as "economically significant"); (2) creating serious inconsistency or otherwise interfering with an action taken or planned by another agency; (3) materially altering the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (4) raising novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order. Pursuant to the terms of the Executive Order, it has been determined that this action is "significant" and subject to OMB review under section 3(f)(4) of the Executive Order.

In the Department's view, the benefits of the VFC Program will substantially outweigh its costs, because participation is voluntary, the administrative cost of correcting a potential fiduciary breach through voluntary participation in the VFC Program will be lower than the cost of a correction resulting from investigation and litigation, and the value and security of the assets of plans participating in the VFC Program will be increased.

No costs will be imposed by the VFC Program unless Plan Officials choose to avail themselves of the opportunity to correct a potential fiduciary breach under the terms of the Program. Participation is expected to occur only when the projected benefit outweighs the anticipated cost for the Plan Official. The costs of electing to correct potential breaches of fiduciary responsibility under terms of the VFC Program are expected to arise from fair market value determinations; computations of losses or profits on the use of plan assets; the administrative costs of supplemental distributions, recomputation of account

balances and distribution of notices to participants concerning recomputation; transaction costs for disposal of assets; and the description and documentation of the correction for purposes of the application to the Department.

The value of assets or losses restored to employee benefit plans as a result of Plan Officials' participation in the VFC Program is not viewed as a cost to Plan Officials, but rather as a transfer from a fiduciary or other party in interest to the participants and beneficiaries of the plan. Plan Officials may not transfer the costs of compliance with the terms of the VFC Program to participants and beneficiaries.

The principal benefit of the VFC Program will accrue to participants and beneficiaries through restoration of losses to the plan or reversal of impermissible transactions involving the assets of the plan, resulting in greater security of their plan assets. Benefits will also accrue to plan fiduciaries through both risk reduction and the savings of civil penalties that would otherwise be payable on the amount of assets recovered by plans following a civil investigation or litigation. Where the Department determines that it will take no civil enforcement action and recommend no legal action in response to a complete application under the VFC Program, the fiduciary will be relieved of potential demands on its resources that might be represented by a civil investigation and any subsequent litigation.

The VFC Program will also allow the Department to encourage compliance with Part 4 of Title I of ERISA while making even more effective use of its limited enforcement resources. The Department believes that the correction of violations through the VFC Program will be less costly than correction through active intervention, and that VFC Program applicants have a high likelihood of accomplishing an appropriate correction of a potential violation. To the extent that Plan Officials who wish to correct potential violations do so voluntarily and appropriately, the Department may direct its resources toward other areas where active intervention is more likely to be necessary.

More generally, publication of the specific examples of transactions which may violate ERISA and the activities required to correct those violations will serve to better inform plan fiduciaries and assist them in satisfying their fiduciary obligations in future transactions involving plan assets.

The Department estimates the cost of the VFC Program for the number of Plan Officials estimated to choose to make

use of it will total \$1,877,400. The total benefit to participants and beneficiaries is estimated at approximately \$80 million, while the benefit to Plan Officials, to the extent it can be quantified, is estimated at \$5.4 million. These figures do not include an estimate of the potential benefit to Plan Officials of the reduced risk of investigation and litigation, or the benefit to the Department, to participants and beneficiaries, and to the public in general of realizing efficiencies in the use of enforcement resources, because these elements of the Program's benefit are not readily quantifiable. Because the VFC Program is voluntary, the Department assumes that Plan Officials will in no event make use of the Program unless the projected benefit outweighs the estimated cost of participation.

A discussion of the elements of the costs and benefits of the VFC Program and estimates of their magnitude where they can be specifically quantified follows. The Department projects that Plan Officials of approximately 700 plans will apply for and use the VFC Program. This estimate is based on the Department's previous experience with the Pension Payback Program in which approximately 0.1 percent of plans which permitted employee contributions elected to participate during the six month period in which the Pension Payback Program was in effect.

The Department expects a similar rate of participation among the approximately 200,000 plans which currently permit employee contributions. However, it assumes this participation by Plan Officials of 200 plans will occur over an annual period in the absence of the six-month time limitation included in the Pension Payback Program.

Because the VFC Program permits correction of several other types of transactions in addition to the repayment of delinquent employee contributions, the Department has assumed that the annual rate of participation in the VFC Program by Plan Officials of plans other than those which permit employee contributions will be comparable to the 0.1 percent assumed for those which permit employee contributions, resulting in participation by Plan Officials of about 500 additional plans, and total participation of 700 plans. The Department views this estimate as an upper bound; actual participation may be somewhat smaller depending on the cost effectiveness of correcting the actual transactions involved, the complexity of the legal and factual

issues involved in a given transaction, and the degree of similarity between an actual transaction and a transaction and correction described by the terms of the VFC Program. The Department recognizes that Plan Officials may not view the VFC Program as offering a cost effective means of correcting all potential violations.

The Department also estimates that \$79,870,000, or an average of \$114,300 per plan, will be recovered by plans annually as a result of participation in the VFC Program. Based on its enforcement experience, the Department estimates that about 70 percent of this total, or \$56 million, will consist of restored principal and earnings losses, and restored profits on the use of plan assets by fiduciaries or parties in interest. The total estimated recovery represents the midpoint between the average monetary recovery (excluding assets recovered through litigation) per plan that resulted from civil investigations completed by the Department in the year ended September 30, 1998, and the average per plan monetary recovery which arose from the Pension Payback Program, as applied to the 700 plans assumed to elect to participate in the VFC Program. The Department believes this estimate is reasonable in light of the range of transactions which may be corrected under the VFC Program. It is estimated that approximately 88,000 participants, or an average of 126 participants per plan, will be affected annually by corrections under the VFC Program.

Based on its recent experience with the collection of civil penalties under section 502(l), the Department estimates that Plan Officials will be relieved of approximately \$5.4 million in civil penalties as a result of correction of transactions through the VFC Program. This estimate is based on the 700 plans assumed to participate, and the average section 502(l) penalty actually collected per plan subject to the penalty in the last two fiscal years. Actual collections take into account the offset of any excise tax payable as a result of a violation of section 4975 of the Code, which is also consistent with the terms of the VFC Program.

The costs to Plan Officials to participate in the VFC Program will arise from a range of possible required activities depending on the nature of the transaction to be corrected, including evaluation by Plan Officials and their professionals of the need and usefulness of participation in the VFC Program, obtaining market value determinations, executing asset transactions, adjusting account balances and benefit distributions, documenting the

correction, and completing and mailing the application to participate in the Program. The Department anticipates that Plan Officials will in most cases seek the services of a professional (typically an attorney, accountant, or professional administrator) to conduct the applicable activities, although the resources of Plan Officials are expected to be needed as well to gather information, and prepare, sign, and photocopy the application. It is estimated that the entire correction will require approximately 40 hours to complete, including 8 hours of the Plan Official's time, and 32 hours of professional time.

At the assumed rate of participation, the total cost of these activities is estimated to amount to \$1,877,400 (or an average of \$2,700 per Plan Official), assuming an average cost of \$55 per hour for work performed in house by Plan Officials and their employees, and a rate of \$70 per hour for purchased services. This estimate also includes application materials and mailing costs.

Paperwork Reduction Act

The Department of Labor has submitted the information collection request (ICR) included in the Voluntary Fiduciary Correction Program to OMB using emergency review procedures for review and clearance in accordance with the Paperwork Reduction Act of 1995 (PRA 95) (44 U.S.C. Chapter 35). OMB approval has been requested by April 14, 2000. The Department and OMB are particularly interested in comments which:

- Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;
- Evaluate the accuracy of the agency's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used;
- Enhance the quality, utility, and clarity of the information to be collected; and
- Minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology, e.g., permitting electronic submission of responses.

Comments should be sent to the Office of Information and Regulatory Affairs, Office of Management and Budget, Room 10235, New Executive Office Building, Washington, DC 20503;

Attention: Desk Officer for the Pension and Welfare Benefits Administration. Although comments may be submitted through May 15, 2000, OMB requests that comments be received within 10 days of publication of this Voluntary Fiduciary Correction Program to ensure their consideration.

The Department, as part of its continuing effort to reduce paperwork and respondent burden, conducts a preclearance consultation program to provide the general public and Federal agencies with an opportunity to comment on proposed and continuing collections of information in accordance with PRA 95. This helps to ensure that requested data can be provided in the desired format, reporting burden (time and financial resources) is minimized, collection instruments are clearly understood, and the impact of collection requirements on respondents can be properly assessed. Currently, PWBA is soliciting comments concerning the ICR included in the Voluntary Fiduciary Correction Program.

Requests for copies of the ICR may be addressed to: Gerald B. Lindrew, Office of Policy and Research, U.S. Department of Labor, Pension and Welfare Benefits Administration, 200 Constitution Avenue, NW, Room N-5647, Washington, DC 20210. Telephone: (202) 219-4782; Fax: (202) 219-4745 (these are not toll-free numbers).

The VFC Program will permit Plan Officials to correct voluntarily certain potential violations of Part 4 of Title I of ERISA, and to avoid the possibility of civil action and the assessment of civil penalties, provided specific conditions are met. The ICR included in the VFC Program would require the Plan Official to describe the correction of the potential breach of fiduciary duty and provide supporting documentation with respect to the correction. The type of supporting documentation will vary with the nature of the transaction involved, but is described in the VFC Program in as specific a manner as deemed feasible. The Plan Official is also required to complete an application which includes identification of the employee benefit plan and the Plan Official or representative, relevant plan documents including a fidelity bond, a statement under penalty of perjury that must be signed by a plan fiduciary with knowledge of the transaction and the authorized representative, if any, and signature. Under certain circumstances a Plan Official may also be required to prepare and distribute notices informing participants and beneficiaries of changes in their account balances. The information submitted to the Department will permit the Department

to verify the correction of potential fiduciary breaches and restoration of losses, to evaluate the adequacy of actions taken by a Plan Official pursuant to the VFC Program, and to determine whether further action is necessary to protect the rights of participants and beneficiaries.

It is estimated that Plan Officials of 700 employee benefit plans will avail themselves of the opportunity to correct potential violations pursuant to the VFC Program annually. The Department estimates that approximately 8 hours of Plan Officials' time will be required to assemble documents and complete and sign the application to participate in the VFC Program. It is further assumed that evaluation, correction and documentation of transactions under the VFC Program will require approximately 32 hours, and that Plan Officials will generally elect to hire service providers to complete this work. Only 6 hours of this total is expected to be associated with the information collection requirements of the VFC Program (including descriptions and documentation, copying relevant supporting statements, preparing notices, etc.). The assumed hourly rate for purchased services related to fulfilling information collection requirements is estimated to be \$70 per hour, for a total cost to the 700 Plan Officials of \$295,400. This includes an allowance of \$2 per application for materials and mailing costs.

Type of Review: New.

Agency: Pension and Welfare Benefits Administration, Department of Labor.

Title: Voluntary Fiduciary Correction Program.

OMB Number: 1210-NEW.

Affected Public: Individuals or households; business or other for-profit; not-for-profit institutions.

Frequency of Response: On occasion.

Total Respondents: 700.

Total Responses: 700.

Estimated Burden Hours: 5,600.

Estimated Annual Costs (Operating and Maintenance): \$295,400.

Persons are not required to respond to the collection of information unless it displays a currently valid OMB control number. Comments submitted in response to this notice will be summarized and/or included in the request for OMB approval of the information collection request; they will also become a matter of public record.

Regulatory Flexibility Act

This document reflects an enforcement policy of the Department and is not being issued as a general notice of proposed rulemaking. Therefore, the Regulatory Flexibility Act

(5 U.S.C. 601 *et seq.*) (RFA) does not apply. However, PWBA has considered the potential costs and benefits of this action for small plans and small Plan Officials in the development of the VFC Program. The Department is interested in comments which would suggest alternatives to the provisions of the VFC Program which would accomplish the stated purpose of the Program while minimizing the impact on small entities.

PWBA generally considers a small entity to be an employee benefit plan with fewer than 100 participants. The basis of this definition is found in section 104(a)(2) of ERISA, which permits the Secretary of Labor to prescribe simplified annual reports for pension plans which cover fewer than 100 participants. However, because the VFC Program specifically prohibits the cost of participation from being borne by the plan and participants, this program will impose no costs on the plans which realize the benefits of the correction of potential violations. Costs will be borne instead by the Plan Officials of an estimated 700 employee benefit plans each year. Plan Officials may include both individual fiduciaries, plan sponsors, or parties in interest, and businesses in their roles as fiduciaries, plan sponsors, or parties in interest.

Although the number of Plan Officials of small plans that will elect to avail themselves of the opportunity to correct potential breaches of fiduciary duty under the terms of the VFC Program is not known, the potential costs and benefits to each Plan Official is summarized below, on the basis of the assumption that each of the participating Plan Officials will itself be a small entity.

Participation in the VFC Program is entirely voluntary, and as such, it is assumed that Plan Officials will elect to participate only when the potential benefits to a Plan Official are expected to exceed the cost of participation. Benefits may include the reduction of exposure to the risk of investigation and subsequent litigation, the potential cost of which cannot be specifically quantified, and the savings of penalties under section 502(l) of ERISA which would otherwise be payable on amounts required to be restored to plans by fiduciaries pursuant to a settlement agreement with the Department or court order.

As described in detail above, to the extent that the per small Plan Official costs and benefits of participation in the VFC Program can be quantified, assuming all participating Plan Officials are small entities, administrative costs of participation are estimated to amount to an average of \$2,700 per Plan Official,

while savings of section 502(l) penalties are estimated at \$7,754 per Plan Official. While the average value of assets estimated to be restored to plans as a result of participation in the VFC Program, or \$114,300 per plan, may be viewed as an expense by Plan Officials, in the Department's view, this expense arises from a potential breach of fiduciary duty rather than from participation in the VFC Program. The fiduciary's potential liability for a breach of fiduciary duty and the cost of remedial relief are expected to be comparable, regardless of whether a violation is corrected under the terms of the VFC Program, or as a result of an investigation and any subsequent litigation.

On this basis, small Plan Officials electing to correct potential fiduciary breaches through participation in the VFC Program are expected to derive a net benefit, even without consideration of the potential savings associated with the reduction of risk and exposure to the use of its resources in connection with an investigation or litigation. Because penalties and additional resource demands are often relatively more burdensome for small entities than large, the Department views the VFC Program as offering a flexible and economically advantageous alternative to currently available methods of correcting potential breaches of fiduciary duty which recognizes the special circumstances of small entities. The Department invites comments on this analysis, and on alternatives which further reduce the potential burden of participation in the VFC Program for small Plan Officials.

Unfunded Mandates Reform Act

For purposes of the Unfunded Mandates Reform Act of 1995 (Pub. L. 104-4), as well as Executive Order 12875, this regulatory action does not include any Federal mandate that may result in expenditures by State, local, or tribal governments, and will not impose an annual burden of \$100 million or more on the private sector.

Voluntary Fiduciary Correction Program

Section 1. Purpose and Overview of the VFC Program

Section 2. Effect of the VFC Program

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Section 4. VFC Program Eligibility

Section 5. General Rules for Acceptable Corrections

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(b) Correction Amount

(c) Costs of Correction

(d) Distributions

(e) Notice

Section 6. Application Procedures

Section 7. Description of Eligible

Transactions and Methods of Correction

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(b) Loans

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2. Loan at Below-Market Interest Rate to a Party in Interest with Respect to the Plan
3. Loan at Below-Market Interest Rate to a Person Who is Not a Party in Interest with Respect to the Plan
4. Loan at Below-Market Interest Rate Solely Due to a Delay in Perfecting the Plan's Security Interest

(c) Purchases, Sales and Exchanges

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2. Sale of an Asset (Including Real Property) by a Plan to a Party in Interest
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4. Purchase of an Asset (Including Real Property) By a Plan from a Person Who is Not a Party in Interest with Respect to the Plan at a Price Other Than Fair Market Value
5. Sale of an Asset (Including Real Property) By a Plan to a Person Who is Not a Party in Interest with Respect to the Plan at a Price Other Than Fair Market Value

(d) Benefits

1. Payment of Benefits Without Properly Valuing Plan Assets on Which Payment is Based

(e) Plan Expenses

1. Duplicative, Excessive, or Unnecessary Compensation Paid by a Plan
2. Payment of Dual Compensation to a Plan Fiduciary

Appendix A. Sample VFC Program No Action Letter

Appendix B. VFC Program Checklist

Appendix C. List of PWBA Regional Offices

Section 1. Purpose and Overview of the VFC Program

The purpose of the VFC Program is to protect the financial security of workers by encouraging identification and correction of transactions that violate Part 4 of Title I of ERISA. Part 4 of Title I of ERISA sets out the responsibilities of employee benefit plan fiduciaries. Section 409 of ERISA provides that a fiduciary who breaches any of these responsibilities shall be personally liable to make good to the plan any losses to the plan resulting from each breach and to restore to the plan any profits the fiduciary made through the use of the plan's assets. Section 405 of ERISA provides that a fiduciary may, under certain circumstances, be liable for a co-fiduciary's breach of his or her fiduciary responsibilities. In addition, under certain circumstances, there may be liability for knowing participation in a fiduciary breach. In order to assist all affected persons in understanding the

requirements of ERISA and meeting their legal responsibilities, PWBA is providing guidance on what constitutes adequate correction under Title I of ERISA for the breaches described in this Program.

Section 2. Effect of the VFC Program

(a) *In general.* PWBA generally will issue to the applicant a no action letter¹ with respect to a breach identified in the application if the eligibility requirements of section 4 are satisfied and a Plan Official corrects a breach, as defined in section 3, in accordance with the requirements of sections 5, 6 and 7. Pursuant to the no action letter it issues, PWBA will not initiate a civil investigation under Title I of ERISA regarding the applicant's responsibility for any transaction described in the no action letter, or assess a civil penalty under section 502(l) of ERISA on the correction amount paid to the plan or its participants.

(b) *Verification.* PWBA reserves the right to conduct an investigation at any time to determine (1) the truthfulness and completeness of the factual statements set forth in the application and (2) that the corrective action was, in fact, taken.

(c) *Limits on the effect of the VFC Program.* (1) *In general.* Any no action letter issued under the VFC Program is limited to the breach and persons identified therein. Moreover, the method of calculating the correction amount described in this Program is only intended to correct the specific breach described in the application. Other methods of calculating losses may be more appropriate, depending on the facts and circumstances. This Program assumes that the transaction is otherwise an appropriate investment decision for the plan. If a transaction gave rise to violations not addressed in the Program, such as imprudence not addressed in the Program or a failure to diversify plan assets, the relief afforded by the Program would not extend to such additional violations.

(2) *No implied approval of other matters.* A no action letter does not imply Departmental approval of matters not included therein, including steps that the fiduciaries take to prevent recurrence of the breach described in the application and to ensure the plan's future compliance with Title I of ERISA.

(3) *Material misrepresentation.* Any no action letter issued under the VFC Program is conditioned on the truthfulness, completeness and accuracy of the statements made in the application and of any subsequent oral

and written statements or submissions. Any material misrepresentations or omissions will void the no action letter, retroactive to the date that the letter was issued by PWBA, with respect to the transaction that was materially misrepresented.

(4) *Applicant fails to satisfy terms of the VFC Program.* If an application fails to satisfy the terms of the VFC Program, as determined by PWBA, PWBA reserves the right to investigate and take any other action with respect to the transaction and/or plan that is the subject of the application, including refusing to issue a no action letter.

(5) *Criminal investigations not precluded.* Compliance with the terms of the VFC Program will not preclude:

(i) PWBA or any other governmental agency from conducting a criminal investigation of the transaction identified in the application;

(ii) PWBA's assistance to such other agency; or

(iii) PWBA making the appropriate referrals of criminal violations as required by section 506(b) of ERISA.²

(6) *Other actions not precluded.*

Compliance with the terms of the VFC Program will not preclude PWBA from taking any of the following actions:

(i) Seeking removal from positions of responsibility with respect to a plan or other non-monetary injunctive relief against any person responsible for the transaction at issue;

(ii) referring information regarding the transaction to the IRS as required by section 3003(c) of ERISA;³ or

(iii) imposing civil penalties under section 502(c)(2) of ERISA based on the failure or refusal to file a timely, complete and accurate annual report Form 5500. Applicants should be aware that amended annual report filings may be required if possible breaches of ERISA have been identified, or if action is taken to correct possible breaches in accordance with the VFC Program.

(7) *Not binding on others.* The issuance of a no action letter does not affect the ability of any other government agency, or any other person, to enforce any rights or carry out any authority they may have, with respect to matters described in the no action letter.

² Section 506(b) provides that the Secretary of Labor shall have the responsibility and authority to detect and investigate and refer, where appropriate, civil and criminal violations related to the provisions of Title I of ERISA and other related Federal laws, including the detection, investigation, and appropriate referrals of related violations of Title 18 of the United States Code.

³ Section 3003(c) provides that, whenever the Secretary of Labor obtains information indicating that a party in interest or disqualified person is violating section 406 of ERISA, she shall transmit such information to the Secretary of the Treasury.

¹ See Appendix A.

(8) *Example.* A plan fiduciary causes the plan to purchase real estate from the plan sponsor under circumstances to which no prohibited transaction exemption applies. In connection with this transaction, the purchase causes the plan assets to be no longer diversified, in violation of ERISA section 404(a)(1)(C). If the application reflects full compliance with the requirements of the Program, the Department's no action letter would apply to the violation of ERISA section 406(a)(1)(A), but would not apply to the violation of section 404(a)(1)(C).

(d) *Correction.* The correction criteria listed in the VFC Program represent PWBA enforcement policy and are provided for informational purposes to the public, but are not intended to confer enforceable rights on any person who purports to correct a violation. Applicants are advised that the term "correction" as used in the VFC Program is not necessarily the same as "correction" pursuant to section 4975 of the Code.⁴ Correction may not be achieved under the Program by engaging in a new prohibited transaction.

(e) *PWBA's authority to investigate.* PWBA reserves the right to conduct an investigation and take any other enforcement action relating to the transaction identified in a VFC Program application in certain circumstances, such as prejudice to the Department that may be caused by the expiration of the statute of limitations period, material misrepresentations, or significant harm to the plan or its participants that is not cured by the correction provided under the VFC Program. PWBA may also conduct a civil investigation and take any other enforcement action relating to matters not covered by the VFC Program application, or relating to other plans sponsored by the same plan sponsor, while a VFC Program application involving the plan or the plan sponsor is pending.

(f) *Confidentiality.* PWBA will maintain the confidentiality of any documents submitted under the VFC Program, to the extent permitted by law. However, as noted in (c)(5) and (6) of this section, PWBA has an obligation to make referrals to the IRS and to refer to other agencies evidence of criminality and other information for law enforcement purposes.

Section 3. Definitions

(a) The terms used in this document have the same meaning as provided in section 3 of ERISA, 29 USC section 1002, unless separately defined herein.

(b) The following definitions apply for purposes of the VFC Program:

(1) *Breach.* The term "Breach" means any transaction which is or may be a breach of the fiduciary responsibilities contained in Part 4 of Title I of ERISA.

(2) *Plan Official.* The term "Plan Official" means a plan fiduciary, plan sponsor, party in interest with respect to a plan, or other person who is in a position to correct a Breach.

(3) *Under Investigation.* The term "Under Investigation" means a plan or person that is being investigated pursuant to ERISA section 504(a) or any criminal statute affecting a transaction which involves an employee benefit plan. A plan that is Under Investigation by PWBA includes any plan for which a Plan Official, or a representative, has received oral or written notification from PWBA of an investigation of the plan. A plan is not considered to be Under Investigation by PWBA merely because PWBA staff have contacted a Plan Official or representative in connection with a complaint, unless the complaint concerns the transaction described in the application.

Section 4. VFC Program Eligibility

Eligibility for the VFC Program is conditioned on the following:

(a) Neither the plan nor the applicant is Under Investigation.

(b) The application contains no evidence of potential criminal violations as determined by PWBA.

Section 5. General Rules for Acceptable Corrections

(a) *Fair Market Value Determinations.* Many corrections require that the current or fair market value of an asset be determined as of a particular date, usually either the date the plan originally acquired the asset or the date of the correction, or both. In order to be acceptable as part of a VFC Program correction, the valuation must meet the following conditions:

(1) If there is a generally recognized market for the property (e.g., the New York Stock Exchange), the fair market value of the asset is the average value of the asset on such market on the applicable date, unless the plan document specifies another objectively determined value (e.g., the closing price).

(2) If there is no generally recognized market for the asset, the fair market value of that asset must be determined

in accordance with generally accepted appraisal standards by a qualified, independent appraiser and reflected in a written appraisal report signed by the appraiser.

(3) An appraiser is "qualified" if he or she has met the education, experience, and licensing requirements that are generally recognized for appraisal of the type of asset being appraised.

(4) An appraiser is "independent" if he or she is not one of the following, does not own or control any of the following, and is not owned or controlled by, or affiliated with, any of the following:

(i) The prior owner of the asset, if the asset was purchased by the plan;

(ii) The purchaser of the asset, if the asset was or is now being sold by the plan;

(iii) Any other owner of the asset, if the plan is not the sole owner;

(iv) A fiduciary of the plan;

(v) A party in interest with respect to the plan (except to the extent the appraiser becomes a party in interest when retained to perform this appraisal for the plan); or

(vi) The VFC Program applicant.

(b) *Correction Amount.* (1) *In general.* Many of the transactions described in the VFC Program result in a loss to the plan or a profit to some party to the transaction. Determining the amount of the loss to the plan requires calculating how much money the plan would have now if a particular transaction had not occurred. In general, the VFC Program requires the fiduciary or other Plan Official to restore to the employee benefit plan the Principal Amount, plus the greater of (i) Lost Earnings from the Loss Date to the Recovery Date or (ii) Restoration of Profits resulting from the use of the Principal Amount for the same period.

(2) *Principal Amount.* "Principal Amount" is the amount that would have been available to the plan for investment or distribution on the date of the Breach, had the Breach not occurred. What constitutes the Principal Amount is identified for each transaction set forth in section 7 of the VFC Program. The generic term "Principal Amount" is the base on which Lost Earnings are calculated.

(3) *Loss Date.* "Loss Date" is the date that the plan lost the use of the Principal Amount.

(4) *Recovery Date.* "Recovery Date" is the date that the Principal Amount is restored to the plan.

(5) *Lost Earnings.* For purposes of the VFC Program, Lost Earnings to be restored to a plan is the greater of (i) the amount that otherwise would have been earned on the Principal Amount from

⁴ See section 4975(f)(5) of the Internal Revenue Code (IRC); section 141.4975-13 of the temporary Treasury Regulations and section 53.4941(e)-1(c) of the Treasury Regulations. The Internal Revenue Service has indicated that except in those instances where the fiduciary breach or its correction result in a tax abuse situation or a plan qualification failure, a correction under this program generally will be acceptable under the Internal Revenue Code.

the Loss Date to the Recovery Date had the Principal Amount been invested during such period in accordance with applicable plan provisions and Title I of ERISA, less actual net earnings or realized net appreciation (or, if applicable, plus any net loss to the plan as a result of the transaction), or (ii) the amount that would have been earned on the Principal Amount at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code, less actual net earnings or realized net appreciation (or, if applicable, plus any net loss to the plan as a result of the transaction). In addition, if the date on which the Lost Earnings is paid to the plan is a date after the Recovery Date, payment must include an additional amount that is the greater of (i) the amount that would have been earned by the plan on the Lost Earnings if it had been paid on the Recovery Date, or (ii) the amount that would have been earned on the Lost Earnings at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code. For a participant-directed defined contribution plan, the Lost Earnings to be restored to the plan is the amount that each participant would have earned on the Principal Amount from the Loss Date to the Recovery Date. However, for administrative convenience, the Lost Earnings amount for a participant-directed defined contribution plan may be calculated using the rate of return of the investment alternative that earned the highest rate of return among the designated broad range of investment alternatives available under the plan during the applicable period.

(6) *Restoration of Profits.* "Restoration of Profits" is the amount of profit made on the use of the Principal Amount, or the property purchased with the Principal Amount, by the fiduciary or party in interest who engaged in the Breach, or by a knowing participant in the Breach. If the Principal Amount was used for a specific purpose such that the actual profit can be determined, that actual profit must be calculated from the Loss Date to the Recovery Date and returned to the plan. If the Principal Amount was commingled with other funds so that the actual profit cannot be determined, the Restoration of Profits will be calculated as interest on the Principal Amount at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code. In addition, if the date on which the Restoration of Profits is paid to the plan is a date after the Recovery Date, payment must include an additional amount that is the greater of (i) the amount that would have been earned by

the plan on the Restoration of Profits if it had been paid on the Recovery Date, or (ii) the amount that would have been earned on the Restoration of Profits at an interest rate equal to the underpayment rate defined in section 6621(a)(2) of the Code.

(7) The principles of this paragraph (b) are illustrated by the following examples:

Example 1. An employer who sponsors a plan with a qualified cash or deferred arrangement within the meaning of section 401(k)(2) of the Code ("401(k) plan") normally deposits participant contributions in the plan's trust account within two business days of each pay day. For this employer, the second business day after pay day is the date on which the participant contributions become plan assets, because it is the earliest date on which this employer can reasonably segregate the participant contributions from the employer's general assets.⁵ However, for the pay period ending January 31, a Monday, participant contributions totaling \$10,000 were not deposited until March 2.

The Principal Amount is \$10,000. The Loss Date is February 2, the date on which the participant contributions became plan assets and should have been deposited in the plan's trust account. The Recovery Date is March 2, the date that the participant contributions were deposited in the plan's trust account.

The 401(k) plan offers five investment alternatives. During the month of February, one of the plan's mutual funds had a 12% annualized yield, including all reinvestment earnings. This was the highest return earned by any of the five investment alternatives in this period. The employer elects to use this rate of return for the loss calculations. Accordingly, the Lost Earnings amount is \$100 (\$10,000 times 12% annual yield times one-twelfth of a year).

The employer had the use of \$10,000 of the 401(k) plan's assets between February 2 and March 2, while the participant contributions remained commingled with the employer's general assets. The employer's cost of funds (the actual profit from the use of the participant contributions) cannot readily be determined; therefore, the Restoration of Profits amount is calculated using the underpayment rate defined in Code section 6621(a)(2). Assuming the section 6621 rate was 9%, the Restoration of Profits amount is \$75 (\$10,000 times 9% per annum times one-twelfth of a year).

In this example, the Lost Earnings amount (\$100) is greater than the Restoration of Profits amount (\$75). Since the Principal Amount of \$10,000 was paid to the plan on March 2, the total correction amount to be paid to the plan is the Lost Earnings of \$100.

Assume further, in this example, that although the Principal Amount of \$10,000 was paid to the plan on March 2, the Lost Earnings of \$100 were not paid to the plan until a year later. Accordingly, an additional \$12 (\$100 times 12 percent—the plan's annual yield), must be paid to the Plan along with the \$100 Lost Earnings amount.

⁵ See 29 CFR 2510.3-102.

Example 2. On March 15, a plan's trustees authorized the purchase of 1,000 shares of stock. The plan paid \$75 per share when the fair market value was \$70 per share.⁶ The Principal Amount is \$5,000 (1,000 shares times the \$5 per share overpayment). The Loss Date is March 15, the date of the overpayment. The Recovery Date will be the date on which the fiduciary or other person repays to the plan the correction amount.

Assume that the plan recoups the \$5,000 overpayment a year after the original purchase. During this year, the plan's other investments earned 9%, including all reinvestment earnings. The Lost Earnings amount is \$450 (\$5,000 times 9% annual yield times one year). If the Restoration of Profit amount is less than \$450, the total amount to be paid to the plan is \$5,450 (the Principal Amount of \$5,000 plus Lost Earnings of \$450).

Example 3. Assume the same facts as in Example 2, except that the proceeds of the sale were used to make another investment which yielded a 15% annual rate of return, the Restoration of Profits amount is \$750 (\$5,000 times 15% per annum times one year). In this example, the Restoration of Profits amount (\$750) is greater than the Lost Earnings amount (\$450). The total amount to be paid to the plan is \$5,750 (the Principal Amount of \$5,000 plus Restoration of Profits of \$750).

Example 4. On April 20, a plan paid \$6,000 in legal fees for legal services that the plan sponsor, not the plan, was obligated to pay. The Principal Amount is \$6,000. The Loss Date is April 20, the date the plan improperly paid the plan sponsor's legal expenses. The Recovery Date will be the date on which the plan sponsor reimburses the plan \$6,000. Assume that the plan sponsor reimburses the plan on October 20, six months after the Loss Date. During this period, the plan's investments earned 10% per annum, including all reinvestment earnings. The Lost Earnings amount is \$300 (\$6,000 times 10% annual yield multiplied by one-half).

The plan sponsor had constructive use of \$6,000 from April 20 until October 20. The plan sponsor's cost of funds (the actual profit from the use of the money) cannot readily be determined; therefore, the Restoration of Profits amount is calculated using the underpayment rate defined in Code section 6621(a)(2). Assuming the section 6621 rate was 8% during the whole period, the Restoration of Profits amount is \$240 (\$6,000 times 8% per annum multiplied by one-half).

In this example, the Lost Earnings amount (\$300) is greater than the Restoration of Profits amount (\$240). The total amount to be paid to the plan is \$6,300 (the Principal Amount of \$6,000 plus Lost Earnings of \$300).

(c) *Costs of Correction.* (1) The fiduciary, plan sponsor or other Plan

⁶ If a plan's fiduciaries authorized the purchase of a specific dollar amount of stock rather than the purchase of a specific number of shares, and the plan acquired fewer shares than it should have as a result of paying too much per share, the amount lost equals the number of additional shares that the plan should have acquired, plus any appreciation, dividends, or stock splits associated with those additional shares.

Official, not the plan, shall pay the costs of correction.

(2) The principle of paragraph (c)(1) is illustrated in the following example and in (d) below:

Example: The plan fiduciaries did not obtain a required independent appraisal in connection with a transaction described in Section 7. In connection with correcting the transaction, the plan fiduciaries now propose to have the appraisal performed as of the date of purchase. The plan document permits the plan to pay reasonable and necessary expenses; the fiduciaries have objectively determined that the cost of the proposed appraisal is reasonable and is not more expensive than the cost of an appraisal contemporaneous with the purchase. The plan may therefore pay for this appraisal. However, the plan may not pay any costs associated with recalculating participant account balances to take into account the new valuation. There would be no need for these additional calculations or any increased appraisal cost if the plan's assets had been valued properly at the time of the purchase. Therefore, the cost of recalculating the plan participants' account balances is not a reasonable plan expense, but is part of the Costs of Correction.

(d) *Distributions.* Some plans will have to make supplemental distributions to former employees, beneficiaries receiving benefits, or alternate payees, if the original distributions were too low because of the Breach. In these situations, the Plan Official or plan administrator must determine who received distributions from the plan during the time period affected by the Breach, recalculate the account balances, and determine the amount of the underpayment to each affected individual. The applicant must demonstrate in writing to PWBA that the plan has used best efforts to locate and pay any former employee, beneficiary, or alternate payee who has received a lump sum distribution but is due an additional distribution as a result of the correction of the transaction. The costs of such efforts would be part of the Costs of Correction.

(e) *Notice.* (1) *In general.* The applicant or the plan administrator must provide written notice of the correction to all plan participants. The notice shall state that the correction was made pursuant to the applicant's participation in the VFC Program, and that the individuals receiving notice may obtain a copy of the application, including all supporting documentation, from the plan administrator upon written request. The notification must also state that the application has been submitted to the VFC Program Coordinator at the appropriate Regional Office of the United States Department of Labor, Pension and Welfare Benefits

Administration and include the address and phone number of such Regional Office. Generally, notice must be provided no later than the date required for distribution of the Summary Annual Report. Notice may be accomplished by posting, regular mail, or electronic mail. The notice must be distributed or posted in a manner reasonably calculated to inform participants in the affected plan of the applicant's participation in the VFC Program.

(2) *Special Notice Requirements.* (i) *Supplemental distributions.* When the correction involves a supplemental distribution, a notice explaining the distribution must also be sent to each individual entitled to the supplemental distribution at the same time as the supplemental distribution.

(ii) *Adjustment of plan account balances.* When the correction involves an adjustment to the account balance of a participant, beneficiary receiving benefits, or alternate payee, a notice explaining the adjustment must be provided at the same time that the individual is furnished with the benefit statement that includes the adjustment. This provision does not require the creation of additional benefit statements. The notice is provided whenever the benefit statement is ordinarily provided.

Section 6. Application Procedures

(a) *In general.* Each application must adhere to the requirements set forth below. Failure to do so may render the application invalid.

(b) *Preparer.* The application must be prepared by a Plan Official or his or her authorized representative (e.g., attorney, accountant, or other service provider). If a representative of the Plan Official is submitting the application, the application must include a statement signed by the Plan Official that the representative is authorized to represent the Plan Official.

(c) *Contact person.* Each application must include the name, address and telephone number of a contact person. The contact person must be familiar with the contents of the application, and have authority to respond to inquiries from PWBA.

(d) *Detailed narrative.* The applicant must provide to PWBA a detailed narrative describing the Breach and the corrective action. The narrative must include:

- (i) a list of all persons materially involved in the Breach and its correction (e.g., fiduciaries, service providers, borrowers);
- (ii) the EIN number and address of the plan sponsor and administrator;

(iii) the date the plan's most recent Form 5500 was filed;

(iv) an explanation of the Breach, including the date it occurred;

(v) an explanation of how the Breach was corrected, by whom and when; and (vi) specific calculations demonstrating how Principal Amount and Lost Earnings or Restoration of Profits were computed and an explanation of why payment of Lost Earnings or Restoration of Profits was chosen to correct the Breach.

(e) *Supporting documentation.* The applicant must also include:

(i) the current fidelity bond for the plan;

(ii) a copy of the plan document, and any other pertinent documents (such as the adoption agreement, trust agreement, or insurance contract) with the relevant sections identified;

(iii) documentation that supports the narrative description of the transaction and correction;

(iv) documentation establishing the Lost Earnings amount, including documentation of the return on the plan's other investments during the time period on which the Lost Earnings is calculated with respect to the transaction described in the VFC Program application;

(v) documentation establishing the amount of Restoration of Profits;

(vi) all documents described in Section 7 with respect to the transaction involved;

(vii) proof of payment of Principal Amount and Lost Earnings or Restoration of Profits; and

(viii) a copy of the sample notification to all affected participants.

(5) *Examples of supporting documentation.* (i) Examples of documentation supporting the description of the transaction and correction are leases, appraisals, notes and loan documents, service provider contracts, invoices, settlement documents, deeds, perfected security interests, and amended annual reports.

(ii) Examples of acceptable proof of payment include copies of canceled checks, executed wire transfers, a signed, dated receipt from the recipient of funds transferred to the plan (such as a financial institution), and bank statements for the plan's account.

(g) *Penalty of Perjury Statement.* Each application must also include a Penalty of Perjury statement. The statement shall be signed and dated by a plan fiduciary with knowledge of the transaction that is the subject of the application and the authorized representative, if any. The statement must accompany the application and any subsequent additions to the

application. The statement shall read as follows:

I certify under penalty of perjury that I have reviewed this application and all supporting documents and that to the best of my belief the contents are true and complete and comply with all terms and conditions of the VFC Program. I further certify under penalty of perjury that at the date of this certification neither the Department nor any other Federal agency has informed me of an intention to investigate or examine the plan or otherwise made inquiry with respect to the transaction described in this application. I further certify under penalty of perjury that neither I nor any person acting under my supervision or control with respect to the operation of an ERISA-covered employee benefit plan:

(1) is the subject of any criminal investigation or prosecution involving any offense against the United States;⁷

(2) has been convicted of a criminal offense involving employee benefit plans at any time or any other offense involving financial misconduct which was punishable by imprisonment exceeding one year for which sentence was imposed during the preceding thirteen years or which resulted in actual imprisonment ending within the last thirteen years, nor has such person entered into a consent decree with the Department or been found by a court of competent jurisdiction to have violated any fiduciary responsibility provisions of ERISA during such period; or

(3) has sought to assist or conceal the transaction described in this application by means of bribery, graft payments to persons with fiduciary responsibility for this plan or with the knowing assistance of persons engaged in ongoing criminal activity.

(h) *Checklist.* The checklist in Appendix B must be completed, signed, and submitted with the application.

(i) *Where to apply.* The application shall be mailed to the appropriate Regional PWBA office listed in Appendix C.

(j) *Record keeping.* The applicant must maintain copies of the application and any subsequent correspondence with PWBA for the period required by section 107 of ERISA.

Section 7. Description of Eligible Transactions and Corrections Under the VFC Program

PWBA has identified certain Breaches and methods of correction that are suitable for the VFC Program. Any Plan Official may correct a Breach listed in this Section in accordance with the applicable correction method. The correction methods set forth are strictly construed and are the only acceptable correction methods under the VFC Program for the transactions described in this Section. PWBA will not accept applications concerning correction of breaches not described in this Section.

A. Contributions

1. Delinquent Participant Contributions to Pension Plans

(a) *Description of Transaction.* An employer receives directly from participants, or withholds from employees' paychecks, certain amounts for contribution to a pension plan. Instead of forwarding the contributions for investment in accordance with the provisions of the plan and within the time frames described in the Department's regulation at 29 CFR 2510.3-102, the employer retains the contributions for a longer period of time.

(b) *Correction of Transaction.* (1) *Unpaid contributions.* For participant contributions not yet paid to the plan, pay to the plan the Principal Amount, plus the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the employer's use of the Principal Amount, as described in Section 5(b). The Principal Amount is the amount of the unpaid participant contributions. The Loss Date for each participant contribution is the earliest date on which it could reasonably have been segregated from the employer's general assets. In no event shall the Loss Date be later than the applicable maximum time period described in the Department's regulation at 29 CFR 2510.3-102.

(2) *Late contributions.* If the participant contributions were remitted to the plan outside the time period required by the regulation, the only correction required is to pay to the plan the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the employer's use of the Principal Amount, as described in Section 5(b).

(3) *Examples.* The principles of this paragraph (b) are illustrated in the following examples:

Example 1. See Example 1 under Section 5(b).

Example 2. Employer X is a large national corporation which sponsors a section 401(k)

plan. X is able to segregate participant contributions no later than 10 business days after the end of the month in which participant contributions were withheld from employees' paychecks. For the pay period ending June 15, participant contributions totaling \$900,000 were not deposited until August 14.

The Principal Amount is \$900,000. The Loss Date is July 14 (the tenth business day in July), the date on which the participant contributions became plan assets and should have been deposited in the plan's trust account. The Recovery Date is August 14, the date that the participant contributions were deposited in the plan's trust account.

The 401(k) plan offers eight investment alternatives with daily asset valuation. From July 14 through August 14, most of the plan participants experienced a decline in their account balances due to a decline in the stock market; however, some participants had a net investment gain. The Code section 6621(a)(2) rate during this period was 8% and was greater than the profit to the employer from the use of the funds during the pertinent time period.

For the participants whose account balances declined, the employer pays the Principal Amount plus the Restoration of Profits amount, calculated at 8%. For the other participants, the employer pays the Principal Amount plus the higher of each participant's actual investment earnings between July 14 and August 14 or the Restoration of Profits amount calculated at 8%. Since the Principal Amount of \$900,000 has already been paid to the plan, the correction amount to be paid to the plan is no less than the Restoration of Profits of \$6,000 (\$900,000 times 8% per annum times one-twelfth of a year).

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) for participant contributions received from participants, a copy of the accounting records which identify the date and amount of each contribution received;

(2) for participant contributions withheld from employees' paychecks, a copy of the payroll documents showing the date and amount of each withholding;

(3) a statement from a Plan Official identifying the earliest date on which the participant contributions reasonably could have been segregated from the employer's general assets, along with the supporting documentation on which the Plan Official relied in reaching this conclusion; and

(4) a sample notice to participants, including any former employee, beneficiary receiving benefits, or alternate payee who is entitled to a supplemental distribution.

⁷ For purposes of this paragraph, an "offense" includes criminal activity for which the Department of Justice may seek civil injunctive relief under the Racketeer Influenced and Corrupt Organizations statute (18 U.S.C. 1964(b)). A "subject" is any individual or entity whose conduct is within the scope of any ongoing inquiry being conducted by a Federal investigator(s) who is authorized to investigate criminal offenses against the United States.

B. Loans**1. Loan at Fair Market Interest Rate to a Party in Interest with Respect to the Plan**

(a) *Description of Transaction.* A plan made a loan to a party in interest at an interest rate no less than that for loans with similar terms (for example, the amount of the loan, amount and type of security, repayment schedule, and duration of loan) to a borrower of similar creditworthiness. The loan was not exempt from the prohibited transaction provisions of Title I of ERISA.

(b) *Correction of Transaction.* Pay off the loan in full, including any prepayment penalties. An independent commercial lender must also confirm in writing that the loan was made at a fair market interest rate for a loan with similar terms to a borrower of similar creditworthiness.

(c) *Documentation.* In addition to the documentation required by Section 6, submit a narrative describing the process used to determine the fair market interest rate at the time the loan was made, validated in writing by an independent commercial lender.

2. Loan at Below-Market Interest Rate to a Party in Interest with Respect to the Plan

(a) *Description of Transaction.* A plan made a loan to a party in interest with respect to the plan at an interest rate which, at the time the loan was made, was less than the fair market interest rate for loans with similar terms (for example, the amount of loan, amount and type of security, repayment schedule, and duration of the loan) to a borrower of similar creditworthiness. The loan was not exempt from the prohibited transaction provisions of Title I of ERISA.

(b) *Correction of Transaction.* Pay off the loan in full, including any prepayment penalties. (1) Pay to the plan the Principal Amount, plus the greater of (i) the Lost Earnings as described in Section 5(b), or (ii) the Restoration of Profits, if any, as described in Section 5(b).

(2) For purposes of this transaction, the Principal Amount is equal to the excess of the interest payments that would have been received if the loan had been made at the fair market interest rate (from the beginning of the loan until the Recovery Date) over interest payments actually received under the loan terms during such period. For purposes of the VFC Program, the fair market interest rate must be determined by an independent commercial lender.

(3) Pay any supplemental distributions that are due, as described in Section 5(d).

Example: The plan made to a party in interest a \$150,000 mortgage loan, secured by a first Deed of Trust, at a fixed interest rate of 4% per annum. The loan was to be fully amortized over 30 years. The fair market interest rate for comparable loans, at the time this loan was made, was 7% per annum. The party in interest or Plan Official must repay the loan in full plus any applicable prepayment penalties. The party in interest or Plan Official also must pay the difference between what the plan would have received through the Recovery Date had the loan been made at 7% and what, in fact, the plan did receive from the commencement of the loan to the Recovery Date, plus lost earnings on that amount as described in Section 5(b).

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) a narrative describing the process used to determine the fair market interest rate at the time the loan was made;

(2) a copy of the independent commercial lender's fair market interest rate determination(s);

(3) a copy of the independent fiduciary's dated, written approval of the fair market interest rate determination(s); and

(4) a sample notice to participants, including any former employee, beneficiary receiving benefits, or alternate payee who is entitled to a supplemental distribution.

3. Loan at Below-Market Interest Rate to a Person Who is Not a Party in Interest with Respect to the Plan

(a) *Description of Transaction.* A plan made a loan to a person who is not a party in interest with respect to the plan at an interest rate which, at the time the loan was made, was less than the fair market interest rate for loans with similar terms (for example, the amount of loan, amount and type of security, repayment schedule, and duration of the loan) to a borrower of similar creditworthiness.

(b) *Correction of Transaction.* (1) Pay to the plan the Principal Amount, plus Lost Earnings through the Recovery Date, as described in Section 5(b).

(2) Each loan payment has a Principal Amount equal to the excess of (a) interest payments that would have been received until the Recovery Date if the loan had been made at the fair market interest rate over (b) the interest actually received under the loan terms. The fair market interest rate must be determined by an independent commercial lender.

(3) From the inception of the loan to the Recovery Date, the amount to be paid to the plan is the Lost Earnings on

the series of Principal Amounts, calculated in accordance with Section 5(b).

(4) From the Recovery Date to the maturity date of the loan, the amount to be paid to the plan is the present value of the remaining Principal Amounts, as determined by an independent commercial lender. Instead of calculating the present value, it is acceptable for administrative convenience to pay the sum of the remaining Principal Amounts.

(5) The principles of this paragraph (b) are illustrated in the following example:

Example: The plan made a \$150,000 mortgage loan, secured by a first Deed of Trust, at a fixed interest rate of 4% per annum. The loan was to be fully amortized over 30 years. The fair market interest rate for comparable loans, at the time this loan was made, was 7% per annum. The borrower or the Plan Official must pay the excess of what the Plan would have received through the Recovery Date had the loan been made at 7% over what, in fact, the plan did receive from the commencement of the loan to the Recovery Date, plus Lost Earnings on that amount as calculated in Section 5(b). The Plan Official must also pay on the Recovery Date the difference in the value of the remaining payments on the loan between the 7% and the 4% for the duration of the time the plan is owed repayments on the loan.

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) a narrative describing the process used to determine the fair market interest rate at the time the loan was made;

(2) a copy of the independent commercial lender's fair market interest rate determination(s); and

(3) a copy of the supplemental distribution notice, if applicable.

4. Loan at Below-Market Interest Rate Solely Due to a Delay in Perfecting the Plan's Security Interest

(a) *Description of Transaction.* For purposes of the VFC Program, if a plan made a purportedly secured loan to a person who is not a party in interest with respect to the plan, but there was a delay in recording or otherwise perfecting the plan's interest in the loan collateral, the loan will be treated as an unsecured loan until the plan's security interest was perfected.

(b) *Correction of Transaction.* (1) Pay to the plan the Principal Amount, plus Lost Earnings as described in Section 5(b), through the date the loan is fully secured.

(2) The Principal Amount is equal to the difference between (a) interest payments actually received under the loan terms and (b) the interest payments

that would have been received if the loan had been made at the fair market interest rate for an unsecured loan. The fair market interest rate must be determined by an independent commercial lender.

(3) In addition, if the delay in perfecting the loan's security caused a permanent change in the risk characteristics of the loan, the fair market interest rate for the remaining term of the loan must be determined by an independent commercial lender. In that case, the correction amount includes an additional payment to the plan. The amount to be paid to the plan is the present value of the remaining Principal Amounts from the date the loan is fully secured to the maturity date of the loan. Instead of calculating the present value, it is acceptable for administrative convenience to pay the sum of the remaining Principal Amounts.

(4) The principles of this paragraph (b) are illustrated in the following examples:

Example 1: The plan made a mortgage loan, which was supposed to be secured by a Deed of Trust. The plan's Deed was not recorded for six months, but, when it was recorded, the Deed was in first position. The interest rate on the loan was the fair market interest rate for a mortgage loan secured by a first-position Deed of Trust. The loan is treated as an unsecured, below-market loan for the six months prior to the recording of the Deed of Trust.

Example 2: Assume the same facts as in Example 1, except that, as a result of the delay in recording the Deed, the plan ended up in second position behind another lender. The risk to the plan is higher and the interest rate on the note is no longer commensurate with that risk. The loan is treated as a below-market loan (based on the lack of security) for the six months prior to the recording of the Deed of Trust and as a below-market loan (based on secondary status security) from the time the Deed is recorded until the end of the loan.

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) a narrative describing the process used to determine the fair market interest rate for the period that the loan was unsecured and, if applicable, for the remaining term of the loan;

(2) a copy of the independent commercial lender's fair market interest rate determination(s); and

(3) a copy of the supplemental distribution notice, if applicable.

C. Purchases, Sales and Exchanges

1. Purchase of an Asset (Including Real Property) by a Plan From a Party in Interest

(a) *Description of Transaction.* A plan purchased an asset with cash from a party in interest with respect to the plan, and under the circumstances, no prohibited transaction exemption applies.

(b) *Correction of Transaction.* (1) The transaction must be corrected by the sale of the property back to the party in interest who originally sold the asset to the plan or to a person who is not a party in interest. Whether the asset is sold to a person who is not a party in interest with respect to the plan or is sold back to the original seller, the plan must receive the higher of (i) the fair market value (FMV) of the asset at the time of resale, without a reduction for the costs of sale; or (ii) the Principal Amount, plus the greater of (A) Lost Earnings on the Principal Amount as described in Section 5(b), or (B) the Restoration of Profits, if any, as described in Section 5(b).

(2) For this transaction, the Principal Amount is the plan's original purchase price.

(3) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan purchased from the plan sponsor a parcel of real property. The plan does not lease the property to any person. Instead, the plan uses the property as an office. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property at the time of purchase. The appraiser values the property at \$100,000, although the plan paid the plan sponsor \$120,000 for the property. As of the Recovery Date the property is valued at \$110,000. To correct the transaction, the plan sponsor repurchases the property for \$120,000 with no reduction for the costs of sale and reimburses the plan for the initial costs of sale. The plan sponsor also must pay the plan the greater of the plan's Lost Earnings and the price the plan paid the plan sponsor or the sponsor's profits on this amount. This example assumes that the plan sponsor did not make a profit on the \$120,000 proceeds from the original sale of the property to the plan.

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) documentation of the plan's purchase of the real property, including the date of the purchase, the plan's purchase price, and the identity of the seller;

(2) a narrative describing the relationship between the original seller of the asset and the plan; and

(3) the qualified, independent appraiser's report addressing the FMV of the asset purchased by the plan, both at the time of the original purchase and at the recovery date.

2. Sale of an Asset (Including Real Property) by a Plan to a Party in Interest

(a) *Description of Transaction.* A plan sold an asset for cash to a party in interest with respect to the plan, in a transaction that is not exempt from the prohibited transaction provisions of Title I of ERISA.

(b) *Correction of Transaction.* (1) The plan must receive the Principal Amount plus the greater of (i) Lost Earnings as described in Section 5(b), or (ii) the Restoration of Profits, if any, as described in Section 5(b). As an alternative to repayment of the Principal Amount, if it is determined that the plan will realize a greater benefit by repurchasing the property, the plan may repurchase the asset from the party in interest⁸ at the lower of the price for which it sold the property or the FMV of the property as of the Recovery Date plus restoration of the party in interest's net profits from owning the property, to the extent they exceed the plan's investment return from the proceeds of the sale. The determination as to which correction alternative the plan chooses must be made by an independent fiduciary.

(2) For this transaction, the Principal Amount is the amount by which the FMV of the asset (at the time of the original sale) exceeds the sale price.

(3) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan sold a parcel of unimproved real property to the plan sponsor. The sponsor did not make any profit on the use of the property. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property as of the date of sale. The appraiser valued the property at \$130,000, although the plan sold the property to the plan sponsor for \$120,000. However, the plan fiduciaries have reason to believe that the property will substantially increase in the near future based on the anticipated building of a shopping mall adjacent to the property in question and, as of the Recovery Date, the appraiser values the property at \$140,000. An independent fiduciary determines that the property is a prudent investment for the plan, and will not result in any liquidity or diversification problems. The plan corrects by repurchasing the property at the original

⁸ The repurchase of the same property from the party in interest to whom the asset was sold is a reversal of the original prohibited transaction. The sale is not a new prohibited transaction and therefore does not require an exemption.

sale price, with the party in interest assuming the costs of the reversal of the sale transaction.

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) documentation of the plan's sale of the asset, including the date of the sale, the sales price, and the identity of the original purchaser;

(2) a narrative describing the relationship of the purchaser to the asset and the relationship of the purchaser to the plan;

(3) the qualified, independent appraiser's report addressing the FMV of the property at the time of the sale from the plan and as of the Recovery Date; and

(4) the independent fiduciary's report that the property is a prudent investment for the plan.

3. Sale and Leaseback of Real Property to Employer

(a) *Description of Transaction.* The plan sponsor sold a parcel of real property to the plan, which then was leased back to the sponsor, in a transaction that is not otherwise exempt.

(b) *Correction of Transaction.* (1) The transaction must be corrected by the sale of the parcel of real property back to the plan sponsor or to a person who is not a party in interest with respect to the plan.⁹ The plan must receive the higher of (i) FMV of the asset at the time of resale, without a reduction for the costs of sale; or (ii) the Principal Amount, plus the greater of (A) Lost Earnings on the Principal Amount as described in Section 5(b), or (B) the Restoration of Profits, if any, as described in Section 5(b).

(2) If the plan has not been receiving rent at FMV, as determined by a qualified, independent appraisal, the sale price of the real property should not be based on the historic below-market rent that was paid to the plan.

(3) In addition to the correction amount in subparagraph (1), if the plan was not receiving rent at FMV, as determined by a qualified, independent appraiser, the Principal Amount also includes the difference between the rent actually paid and the rent that should have been paid at FMV. The plan sponsor must pay to the plan this additional Principal Amount, plus the

greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the plan sponsor's use of the Principal Amount, as described in Section 5(b).

(4) The principles of this paragraph (b) are illustrated in the following example:

Example: The plan purchased at FMV from the plan sponsor an office building that served as the sponsor's primary business site. Simultaneously, the plan sponsor leased the building from the plan at below the market rental rate. The Plan Official obtains from a qualified, independent appraiser an appraisal of the property reflecting the FMV of the property and rent. To correct the transaction, the plan sponsor purchases the property from the plan at the higher of the appraised value at the time of the resale or the original sales price and also pays the Lost Earnings. Because the rent paid to the plan was below the market rate, the sponsor must also make up the difference between the rent paid under the terms of the lease and the amount that should have been paid, plus Lost Earnings on this amount, as described in Section 5(b).

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) documentation of the plan's purchase of the real property, including the date of the purchase, the plan's purchase price, and the identity of the original seller;

(2) documentation of the plan's sale of the asset, including the date of sale, the sales price, and the identity of the purchaser;

(3) a narrative describing the relationship of the original seller to the plan and the relationship of the purchaser to the plan;

(4) a copy of the lease;

(5) documentation of the date and amount of each lease payment received by the plan; and

(6) the qualified, independent appraiser's report addressing both the FMV of the property at the time of the original sale and at the Recovery Date, and the FMV of the lease payments.

4. Purchase of an Asset (Including Real Property) By a Plan From a Person Who Is Not a Party in Interest With Respect to the Plan at a Price Other Than Fair Market Value

(a) *Description of Transaction.* A plan acquired an asset from a person who is not a party in interest with respect to the plan, without determining the asset's FMV. As a result, the plan paid more than it should have for the asset.

(b) *Correction of Transaction.* The Principal Amount is the difference between the actual purchase price and the asset's FMV at the time of purchase. The plan must receive the Principal Amount plus the Lost Earnings, as described in Section 5(b).

(1) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan bought unimproved land without obtaining a qualified, independent appraisal. Upon discovering that the purchase price was \$10,000 more than the appraised FMV, the Plan Official pays the plan the Principal Amount of \$10,000, plus Lost Earnings as described in Section 5(b).

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) Documentation of the plan's original purchase of the asset, including the date of the purchase, the purchase price, and the identity of the seller;

(2) A narrative describing the relationship of the seller to the plan; and

(3) A copy of the qualified, independent appraiser's report addressing the FMV at the time of the plan's purchase.

5. Sale of an Asset (Including Real Property) By a Plan to a Person who is not a Party in Interest with Respect to the Plan at a Price Less Than Fair Market Value

(a) *Description of Transaction.* A plan sold an asset to a person who is not a party in interest with respect to the plan, without determining the asset's FMV. As a result, the plan received less than it should have from the sale.

(b) *Correction of Transaction.* The Principal Amount is the amount by which the FMV of the asset as of the Recovery Date exceeds the price at which the plan sold the property. The plan must receive the Principal Amount plus Lost Earnings as described in Section 5(b).

(1) The principles of this paragraph (b) are illustrated in the following example:

Example: A plan sold unimproved land without taking steps to ensure that the plan received FMV. Upon discovering that the sale price was \$10,000 less than the FMV, the Plan Official pays the plan the Principal Amount of \$10,000 plus Lost Earnings as described in Section 5(b).

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) Documentation of the plan's original sale of the asset, including the date of the sale, the sale price, and the identity of the buyer;

(2) A narrative describing the relationship of the buyer to the plan; and

(3) A copy of the qualified, independent appraiser's report addressing the FMV at the time of the plan's sale.

⁹ If the plan purchased the property from the plan sponsor, the sale of the same property back to the plan sponsor is a reversal of the prohibited transaction. The sale is not a new prohibited transaction and therefore does not require an individual prohibited transaction exemption, as long as the plan did not make improvements while it owned the property.

D. Benefits

1. Payment of Benefits Without Properly Valuing Plan Assets on Which Payment is Based

(a) *Description of Transaction.* A defined contribution pension plan pays benefits based on the value of the plan's assets. If one or more of the plan's assets are not valued at current value, the benefit payments are not correct. If the plan's assets are overvalued, the current benefit payments will be too high. If the plan's assets are undervalued, the current benefit payments will be too low.

(b) *Correction of Transaction.* (1) Establish the correct value of the improperly valued asset for each plan year, starting with the first plan year in which the asset was improperly valued. Restore to the plan for distribution to the affected plan participants, or restore directly to the plan participants, the amount by which all affected participants were underpaid distributions to which they were entitled under the terms of the plan, plus the higher of Lost Earnings or the underpayment rate defined in section 6621(a)(2) of the Code on the underpaid distributions. File amended Annual Report Forms 5500, as detailed below.

(2) To correct the valuation defect, a Plan Official must determine the FMV of the improperly valued asset per Section 5(a), for each year in which the asset was valued improperly.

(3) Once the FMV has been determined, the participant account balances for each year must be adjusted accordingly.

(4) The annual report Forms 5500 must be amended and refiled for (i) the last three plan years or (ii) all plan years in which the value of the asset was reported improperly, whichever is less.

(5) The Plan Official or plan administrator must determine who received distributions from the plan during the time the asset was valued improperly. For distributions that were too low, the amount of the underpayment is treated as a Principal Amount for each individual who received a distribution. The Principal Amount and Lost Earnings must be paid to the affected individuals. For distributions that were too high, the total of the overpayments constitutes the Principal Amount for the plan. The Principal Amount plus the Lost Earnings, as described in Section 5(b), must be restored to the plan or to the participants.

(6) The principles of this paragraph (b) are illustrated in the following examples:

Example 1. On December 31, 1995, a profit sharing plan purchased a 20-acre parcel of real property for \$500,000, which represented a portion of the plan's assets. The plan has carried the property on its books at cost, rather than at FMV. One participant left the company on January 1, 1997, and received a distribution, which included her portion of the value of the property. The separated participant's account balance represented 2% of the plan's assets. As part of correction for the VFC Program, a qualified, independent appraiser has determined the FMV of the property for 1996, 1997, and 1998. The FMV as of December 31, 1996, was \$400,000. Therefore, this participant was overpaid by \$2,000 ((\$500,000-\$400,000) times 2%). The Plan Officials corrected the transaction by paying to the plan \$2,500, consisting of \$2,000 Principal Amount and \$500 Lost Earnings. The Lost Earnings were based on a return of 25%, which represents the total return on the plan's investments from the date of the distribution to the participant until the date of correction.

The plan administrator also filed an amended Form 5500 for plan years 1996 and 1997, to reflect the proper values. The plan administrator will include the correct asset valuation in the 1998 Form 5500 when that form is filed.

Example 2. Assume the same facts as in Example 1, except that the property had appreciated in value to \$600,000 as of December 31, 1996. The separated participant would have been underpaid by \$2,000. The correction consists of locating the participant and distributing \$2,500 to her (\$2,000 Principal Amount and \$500 Lost Earnings), as well as filing the amended Forms 5500 C/R.

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) A copy of the qualified, independent appraiser's report for each plan year in which the asset was revalued;

(2) A written statement confirming the date that amended Annual Report Forms 5500 with correct valuation data were filed;

(3) If losses are restored to the plan, proof of payment to the plan and copies of the adjusted participant account balances;

(4) if supplemental distributions are made, proof of payment to the individuals entitled to receive the supplemental distributions; and

(5) a sample notice to participants.

E. Plan Expenses

1. Duplicative, Excessive, or Unnecessary Compensation Paid by a Plan

(a) *Description of Transaction.* A plan paid excessive compensation, including commissions or fees, to a service provider (such as an attorney, accountant, actuary, financial advisor,

or insurance agent); a plan paid two or more persons to provide the same services to the plan; or a plan paid a service provider for services that were not necessary for the operation of the plan.

(b) *Correction of Transaction.* (1) Restore to the plan the Principal Amount, plus the greater of (i) Lost Earnings or (ii) Restoration of Profits resulting from the use of the Principal Amount, as described in Section 5(b).

(2) The Principal Amount is the difference between (a) the amount actually paid by the plan to the service provider during the six years prior to the discontinuation of the payment of the excessive, duplicative, or unnecessary compensation and (b) the reasonable market value of the non-duplicative services.

(3) The principles of this paragraph (b) are illustrated in the following example:

Example. Excessive compensation. A plan hired an investment advisor who advised the plan's trustees about how to invest the plan's entire portfolio. In accordance with the plan document, the trustees instructed the advisor to limit the plan's investments to equities and bonds. In exchange for his services, the plan paid the investment advisor 3% of the value of the portfolio's assets. If the trustees had inquired they would have learned that comparable investment advisors charged 1% of the value of the assets for the type of portfolio that the plan maintained. To correct the transaction, the plan must be paid the Principal Amount of 2% of the value of the plan's assets, plus Lost Earnings, as described in Section 5(b).

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) a written estimate of the reasonable market value of the services;

(2) the estimator's qualifications; and

(3) the cost of the services at issue during the period that such services were provided to the plan.

2. Payment of Dual Compensation to a Plan Fiduciary

(a) *Description of Transaction.* A plan pays a fiduciary for services rendered to the plan when the fiduciary already receives full-time pay from an employer or an association of employers, whose employees are participants in the plan, or from an employee organization whose members are participants in the plan. The plan's payments to the plan fiduciary are not mere reimbursements of expenses properly and actually incurred by the fiduciary.

(b) *Correction of Transaction.* (1) Restore to the plan the Principal Amount, plus the greater of (i) Lost Earnings or (ii) Restoration of Profits

resulting from the fiduciary's use of the Principal Amount for the same period.

(2) The Principal Amount is the difference between (a) the amount actually paid by the plan during the six years prior to the discontinuation of the payments to the fiduciary and (b) the amount that represents reimbursements of expenses properly and actually incurred by the fiduciary.

(3) The principles of this paragraph (b) are illustrated in the following example:

Example. A union sponsored a health plan funded through contributions by employers. The union president receives \$50,000 per year from the union in compensation for his services as union president. He is appointed as a trustee of the health plan while retaining his position as union president. In exchange for acting as plan trustee, the union president is paid a salary of \$200 per week by the plan while still receiving the \$50,000 salary from the union. Since \$50,000 is full-time pay, the plan's weekly salary payments are improper. To correct the transaction, the plan must be paid the Principal Amount, which is the \$200 weekly salary amount for each week that the salary was paid, plus the higher of Lost Earnings or Restoration of Profits, as described in Section 5(b).

(c) *Documentation.* In addition to the documentation required by Section 6, submit the following documents:

(1) copies of the plan's accounting records which show the date and amount of compensation paid by the plan to the identified fiduciary; and

(2) if any of the amounts paid by the plan to the fiduciary represent reimbursements of expenses properly and actually incurred by the fiduciary, include copies of the plan records which indicate the date, amount, and character of these payments.

Signed at Washington, DC this 9th day of March, 2000.

Leslie Kramerich,

Acting Assistant Secretary for Pension and Welfare Benefits Administration, Department of Labor.

Appendix A—Sample VFC Program No Action Letter

Applicant (Plan Official)

Address

Dear Applicant (Plan Official):

Re: VFC Program Application No. xx-xxxxxx

The Department of Labor, Pension and Welfare Benefits Administration (PWBA), has responsibility for administration and enforcement of Title I of the Employee Retirement Income Security Act of 1974, as amended (ERISA). PWBA has established a Voluntary Fiduciary Correction Program to encourage the correction of breaches of fiduciary responsibility and the

restoration of losses to the plan participants and beneficiaries.

In accordance with the requirements of the VFC Program, you have identified the following transactions as breaches, or potential breaches, of Part 4 of Title I of ERISA, and you have submitted documentation to PWBA that demonstrates that you have taken the corrective action indicated.

[Briefly recap the violation and correction. *Example:* Failure to deposit participant contributions to the XYZ Corp. 401(k) plan within the time frames required by ERISA, from *date* to *date*. All participant contributions were deposited by *date* and lost earnings on the delinquent contributions were deposited and allocated to participants' plan accounts on *date*.]

Because you have taken the above-described corrective action, which is consistent with the requirements of the VFC Program, PWBA will take no civil enforcement action against you with respect to this breach. Specifically, PWBA will not recommend that the Solicitor of Labor initiate legal action against you, and PWBA will not impose the penalty in section 502(l) of ERISA on the amount you have repaid to the plan.

PWBA's decision to take no further action is conditioned on the completeness and accuracy of the representations made in your application. You should note that this decision will not preclude PWBA from conducting an investigation of any potential violations of criminal law in connection with the transaction identified in the application or investigating the transaction identified in the application with a view toward seeking appropriate relief from any other person. *[If the transaction is a prohibited transaction, add the following language: Please also be advised that pursuant to section 3003(c) of ERISA, 29 U.S.C. section 1203(c), the Secretary of Labor is required to transmit to the Secretary of the Treasury information indicating that a prohibited transaction has occurred. Accordingly, this matter will be referred to the Internal Revenue Service.]*

In addition, you are cautioned that PWBA's decision to take no further action is binding on PWBA only. Any other governmental agency, and participants and beneficiaries, remain free to take whatever action they deem necessary.

If you have any questions about this letter, you may contact the Regional VFC Program Coordinator at *applicable address and telephone number*.

Appendix B—VFC Program Checklist

Use this checklist to ensure that you are submitting a complete application. The applicant must sign and date the checklist and include it with the application. Indicate "Yes", "No" or "N/A" next to each item. A "No" answer or the failure to include a completed checklist will delay review of the application until all required items are received.

- _____ 1. Have you reviewed the eligibility, definitions, transaction and correction, and documentation sections of the VFC Program?
- _____ 2. Have you included the name, address and telephone number of a contact person familiar with the contents of the application?
- _____ 3. Have you provided the EIN # and address of the plan sponsor and plan administrator?
- _____ 4. Have you provided the date that the most recent Form 5500 was filed by the plan?
- _____ 5. Have you enclosed a signed and dated certification under penalty of perjury?
- _____ 6. Have you enclosed a copy of the plan document, and any other pertinent documents (such as the adoption agreement, trust agreement, or insurance contract) with the relevant sections identified?
- _____ 7. Have you enclosed a copy of the current fidelity bond for the plan?
- _____ 8. Where applicable, have you enclosed a copy of an appraiser's report?
- _____ 9. Have you enclosed other documents as specified by the individual transactions and corrections?
 - _____ a. a detailed narrative of the Breach, including the date it occurred;
 - _____ b. documentation that supports the narrative description of the transaction;
 - _____ c. an explanation of how the Breach was corrected, by whom and when, with supporting documentation;
 - _____ d. a list of all persons materially involved in the Breach and its correction (e.g., fiduciaries, service providers, borrowers);
 - _____ e. documentation establishing the return on the plan's other investments during the time period the plan engaged in the transaction described in the VFC Program application;
 - _____ f. specific calculations demonstrating how Principal Amount and Lost Earnings or Restoration of Profits were computed; and
 - _____ g. proof of payment of Principal Amount and Lost Earnings or Restoration of Profits.
- _____ 10. Have you made proper arrangements to provide notice to the plan participants?

_____ 11. Where applicable, have you enclosed a description of how the plan has used its best efforts to locate and pay former employees who have received lump sum distributions or rollovers but are due an additional distribution as a result of the correction of the transaction?

_____ 12. Has the plan implemented measures to ensure that the transactions specified in the application do not recur? (Do not include this with the application. The Department will not opine on the adequacy of these measures.)

Signature of Applicant and Date Signed

Name of Applicant (Typed):

Title/Relationship to the Plan (Typed):

Name of Plan, EIN and Plan Number (Typed):

Appendix C—List of PWBA Regional Offices

Atlanta Regional Office, 61 Forsyth Street, SW, Suite 7B54, Atlanta, GA 30303, telephone (404) 562-2156, fax (404) 562-2168; jurisdiction: Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, Tennessee, Puerto Rico.

Boston Regional Office, J.F.K. Building, Room 575, Boston, MA 02203,

telephone: (617) 565-9600, fax: (617) 565-9666; jurisdiction: Connecticut, Maine, Massachusetts, New Hampshire, central and western New York, Rhode Island, Vermont.

Chicago Regional Office, 200 West Adams Street, Suite 1600, Chicago, IL 60606, telephone (312) 353-0900, fax (312) 353-1023; jurisdiction: northern Illinois, northern Indiana, Wisconsin.

Cincinnati Regional Office, 1885 Dixie Highway, Suite 210, Ft. Wright, KY 41011-2664, telephone (606) 578-4680, fax (606) 578-4688; jurisdiction: southern Indiana, Kentucky, Michigan, Ohio.

Dallas Regional Office, 525 Griffin Street, Rm. 707, Dallas, TX 75202-5025, telephone (214) 767-6831, fax (214) 767-1055; jurisdiction: Arkansas, Louisiana, New Mexico, Oklahoma, Texas.

Kansas City Regional Office, 1100 Main Street, Suite 1200, Kansas City, MO 64105-2112, telephone (816) 426-5131, fax (816) 426-5511; jurisdiction: Colorado, southern Illinois, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, North Dakota, South Dakota, Wyoming.

Los Angeles Regional Office, 790 E. Colorado Boulevard, Suite 514, Pasadena, CA 91101, telephone (626) 583-7862, fax (626) 583-7845; jurisdiction: 10 southern counties of California, Arizona, Hawaii, American Samoa, Guam, Wake Island.

New York Regional Office, 6 World Trade Center, Room 625, New York, NY 10048, telephone (212) 637-0600, fax (212) 637-0512; jurisdiction: southeastern New York, northern New Jersey.

Philadelphia Regional Office, 3535 Market St., Room 12400, Philadelphia, PA 19104, telephone (215) 596-1134, fax (215) 596-4475; jurisdiction: Delaware, Maryland, southern New Jersey, Pennsylvania, Virginia, Washington, D.C., West Virginia.

San Francisco Regional Office, 71 Stevenson St., Suite 915, San Francisco, CA 94105, telephone (415) 975-4600, fax (415) 975-4589; jurisdiction: Alaska, 48 northern counties of California, Idaho, Nevada, Oregon, Utah, Washington.

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