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## LEGAL UPDATE

### IRS Announces New Pre-Audit Compliance Pilot Program

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In early June, the IRS announced via newsletter a new pre-audit compliance opportunity for employer-sponsored retirement plans selected for audit beginning immediately (the Pilot Program). Under the Pilot Program, the IRS will send an initial letter to plan sponsors whose retirement plans have been selected for upcoming audits. This letter will explain that the plan has been identified for audit and that the sponsor has 90 days to identify and voluntarily correct any compliance issues with the plan and notify the IRS of the corrective actions taken. This is a welcome departure from the long-time voluntary correction principle that allowed voluntary correction only until the IRS had identified the plan for audit. The IRS will evaluate whether to continue the program and/or include it in its EPCRS program at the end of the pilot program (which was not disclosed).

The program as described in the announcement provides some powerful incentives to encourage plan sponsors to voluntarily comply in the 90 days following receipt of the initial letter. The first is a reduction in the sanctions involved in the audit process. Traditionally, sanctions for compliance issues discovered in a retirement plan audit were calculated under the IRS's Audit CAP program which considers the nature, extent, and severity of the failure, and are based on a percentage of plan assets, which can be extremely expensive even for a small plan covering a limited number of employees. Under the announcement, if a plan sponsor responds to the initial audit letter with compliance items it has identified and the fixes it has implemented, the IRS will not assess sanctions for failures eligible for self-correction and will assess sanctions for corrections made in accordance with its published Voluntary Correction Program based on the user fees applicable to that

program (which currently max out at \$3,500, a figure significantly lower than most Audit CAP sanction fees). The announcement also indicates that if a plan sponsor responds to the initial letter, the IRS will determine whether to issue a closing letter or to conduct a limited or full scope audit. How it will make that determination has not been disclosed, but it appears that plan sponsors may have some ability to limit an impending audit or avoid an audit completely by responding to the initial letter in a way that demonstrates full compliance.

Plan sponsors that receive an initial letter should immediately contact their retirement plan advisers to begin the

process of identifying compliance failures, taking any appropriate corrective actions, and preparing a summary of the compliance issues and corrections made for the IRS. In addition, operational and plan document errors discovered by a plan sponsor should receive priority for timely correction to ensure any compliance issue can be resolved within 90 days of the receipt of an initial letter.

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