

MEMO# 35930

November 20, 2024

IRS Provides Guidance on Inadvertent Benefit Overpayments from Retirement Plans

[35930]

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TO: ICI Members

Pension Committee

Pension Operations Advisory Committee SUBJECTS: Pension

Tax RE: IRS Provides Guidance on Inadvertent Benefit Overpayments from Retirement Plans

The IRS recently released Notice 2024-77, providing guidance on retirement plans' treatment of inadvertent benefit overpayments.[\[1\]](#)

Background

Section 301 of the SECURE 2.0 Act provided new rules regarding plans' recovery of retirement plan overpayments, effective as of December 29, 2022.[\[2\]](#) Section 301(b) adds two new sections to the Internal Revenue Code ("Code").[\[3\]](#)

New Code section 414(aa) addresses the qualification requirements under section 401(a) with respect to inadvertent benefit overpayments (as well as under Code section 403). It provides that a plan will not fail to be treated as qualified merely because (1) it has not obtained repayment of an overpayment made by the plan or (2) the plan sponsor amends the plan to adjust for prior inadvertent benefit overpayments. It also provides that, in the case of an overpayment, a plan is still required to observe the limitations of Code sections 401(a)(17) (the annual compensation limit) and 415 (the annual DB and DC plan limits).

New Code section 402(c)(12) addresses the treatment of certain inadvertent benefit overpayments as eligible rollover distributions, providing that if a plan does not seek recoupment of such an overpayment, and the payment otherwise would have been an eligible rollover distribution, then the overpayment may be treated as an eligible rollover distribution. Further, if the plan does seek recoupment of a portion of the overpayment, that portion that is returned to the plan will be treated as an eligible rollover distribution that has been transferred to the plan.[\[4\]](#)

In a separate provision of the SECURE 2.0 Act (section 305), Congress expanded the IRS Employee Plans Compliance Resolution System (EPCRS)[\[5\]](#) to allow plans to self-correct

inadvertent plan violations.[\[6\]](#) The Act directs Treasury to update EPCRS within two years of enactment. In 2023, IRS issued Notice 2023-43, which provides guidance with respect to the expansion of EPCRS as required under Section 305.[\[7\]](#)

Notice 2024-77

The Notice provides guidance regarding the two new Code sections on inadvertent benefit overpayments and addresses their impact on the current version of EPCRS. The Notice applies with respect to new Code sections 414(aa) and 402(c)(12) as of October 15, 2024 (the date the Notice was issued). For periods before October 15, taxpayers may rely on a good faith, reasonable interpretation of the statute. Section 301 of the SECURE 2.0 Act is effective as of December 29, 2022, and the Notice confirms that Code section 402(c)(12) applies as of December 29, 2022, regardless of when an inadvertent benefit overpayment was made.

Defines Inadvertent Benefit Overpayment (Q-1). The SECURE 2.0 Act did not define "inadvertent benefit overpayment." The Notice defines it as an "eligible inadvertent failure" (as defined in section 305 of the SECURE 2.0 Act) that occurs due to a payment from a plan that exceeds the amount payable under the terms of the plan or a limitation in the Code or regulations. It includes a payment made before a distribution is permitted. It does not include a payment made to a disqualified person or an owner-employee[\[8\]](#) or a payment made under EPCRS to correct a different qualification failure.

Addresses EPCRS requirement that overpayment be corrected (Q-2). Under the current version of EPCRS, an overpayment generally must be corrected, and EPCRS provides various correction methods. The Notice provides that any requirement in EPCRS that a corrective payment be made to a plan with respect to an inadvertent benefit overpayment no longer applies (the requirement continues to apply in the case of failures to meet the 415 and 401(a)(17) limits, and certain failures related to the DB plan funding requirements in Code section 436). The Notice acknowledges that other failures that result from an inadvertent benefit overpayment could require a corrective payment,[\[9\]](#) and an employer may need to make a corrective payment to restore an impermissible forfeiture.

Confirms that recoupment of overpayment is still permitted (Q-3). EPCRS currently provides that a plan's recoupment from overpayment recipients is permitted but not required. New Code section 414(aa)(1) does not change this rule. The Notice highlights the fact that it does not address the new ERISA provision regarding inadvertent benefit overpayments, added by Section 301(a) of SECURE 2.0, which imposes conditions on a plan's recoupment from a participant or beneficiary.

Explains when rollover of overpayment is permitted (Q-4). The Notice provides guidance regarding rollover treatment in three circumstances: where recoupment is not sought, where recoupment is sought and the overpayment is repaid, and where recoupment is sought but the amount is not repaid.

1. An individual who receives an inadvertent benefit overpayment and rolls over that overpayment retains the tax-favored status of the overpayment for the portion of the overpayment for which recoupment is not sought. This treatment does not apply where the limits of Code section 415 or 401(a)(17) are exceeded.
2. If an individual receives an inadvertent benefit overpayment and rolls it over to another plan and the plan that made the overpayment then seeks recoupment, then the amount transferred back to that plan as a recoupment is treated as an eligible rollover distribution. The Notice confirms that regardless of the plan terms, the

originating plan is treated as permitting the transfer back of the inadvertent benefit overpayment as an eligible rollover distribution, and the transfer from the second plan is treated as an eligible rollover distribution.

3. If recoupment is sought, and the individual does not repay the amount, then the amount is not treated as an eligible rollover distribution. The plan must notify the individual that any unreturned portion of the inadvertent benefit overpayment is not eligible for treatment as a tax-free rollover.

Requires corrective payments in the case of DB plan funding-based benefit restriction failures (Q-5). The Notice provides that for Code section 436 failures occurring as a result of an inadvertent benefit overpayment, if not recouped from the individual, a corrective payment is required to be made to the plan under the same circumstances (under EPCRS) as other overpayments that are not inadvertent benefit overpayments.

Confirms that Code limits under 401(a)(17) and 415 must be observed (Q-6/Q-7). In contrast to the general rule described in Q-2 that corrective payment is no longer required in the case of an inadvertent benefit overpayment, failures related to Code section 401(a)(17) (the annual compensation limit) and Code section 415 (the annual plan limit) are exceptions to the general rule and must be corrected. Therefore, where an inadvertent benefit overpayment results in a section 401(a)(17) or 415 failure, to the extent the inadvertent benefit overpayment is not recouped on behalf of the plan from the individual, the plan sponsor or another person must make a corrective payment (as described in EPCRS for overpayment corrections). An inadvertent benefit overpayment that results from a 401(a)(17) or 415 failure, if not recouped, will not be treated as an eligible rollover distribution, and the plan must notify the individual that the amount is not eligible for tax-free rollover treatment. Similarly, a plan may not correct the failure by amending the plan to increase past benefit payments, in a manner that that results in a violation of section 401(a)(17) or 415 for a past year.

Lists provisions of EPCRS that are affected (Q-8). The Notice lists the following provisions of EPCRS that are modified or no longer applicable with respect to an inadvertent benefit overpayment:

- The definition of an overpayment in sections 5.01(3)(c) and 5.02(4) of Rev. Proc. 2021-30 is modified by Q&A-1 of the Notice for an overpayment that is an inadvertent benefit overpayment.
- Any requirement in section 6.06(3)(b)(ii) and (4)(b)(ii) of Rev. Proc. 2021-30 that a plan sponsor must notify an individual that an overpayment is not an eligible rollover distribution no longer applies to the portion of an inadvertent benefit overpayment not sought for recoupment (other than as specified in Q&A-4, Q&A-5, and Q&A-6 of the Notice with respect to the portion of an inadvertent benefit overpayment for which recoupment is sought but is not returned to the originating plan).
- Any requirement of a corrective payment in section 6.06 of Rev. Proc. 2021-30 no longer applies to an inadvertent benefit overpayment (other than as specified in Q&A-5 of the Notice with respect to a section 436 failure and in Q&A-6 of the Notice with respect to a section 401(a)(17) or 415 failure).
- Section 6.09(5) of Rev. Proc. 2021-30, which provides relief from the excise tax under section 4973, is no longer necessary for any inadvertent benefit overpayment that is treated as an eligible rollover distribution under section 402(c)(12). Accordingly, under those circumstances, section 6.09(5) of Rev. Proc. 2021-30 no longer applies.
- Section 6.09(6) of Rev. Proc. 2021-30, which provides relief from the 10 percent additional income tax under section 72(t), is no longer necessary for any inadvertent

benefit overpayment that is treated as an eligible rollover distribution under section 402(c)(12). Accordingly, under those circumstances, section 6.09(6) of Rev. Proc. 2021-30 no longer applies.

Comments Requested

The IRS requests comments on the Notice and all aspects of section 301(b) of the SECURE 2.0 Act and also how the new Code sections are affected by the effective date of the statute and the statute's reference to actions taken before the effective date (i.e., sections 301(c) and (d) of the SECURE 2.0 Act). Comments are due by December 16, 2024.

Shannon Salinas
Associate General Counsel - Retirement Policy

Notes

[1] Notice 2024-77, released on October 15, 2024, is available at <https://www.irs.gov/pub/irs-drop/n-24-77.pdf>.

[2] For a summary of the SECURE 2.0 Act, see ICI Memorandum No. 34795, dated January 12, 2023, available at <https://www.ici.org/memo34795>.

[3] Section 301(a) of the SECURE 2.0 Act provides special rules under ERISA for plan fiduciaries' decisions regarding whether and how to recoup benefit overpayments (including limitations and protections that apply when plan fiduciaries choose to recoup overpayments). The Notice does not address the ERISA provisions.

[4] New Code section 402(c)(12) provides as follows:

(12) In the case of an inadvertent benefit overpayment from a plan to which section 414(aa)(1) applies that is transferred to an eligible retirement plan by or on behalf of a participant or beneficiary—

(A) the portion of such overpayment with respect to which recoupment is not sought on behalf of the plan shall be treated as having been paid in an eligible rollover distribution if the payment would have been an eligible rollover distribution but for being an overpayment, and

(B) the portion of such overpayment with respect to which recoupment is sought on behalf of the plan shall be permitted to be returned to such plan and in such case shall be treated as an eligible rollover distribution transferred to such plan by the participant or beneficiary who received such overpayment (and the plans making and receiving such transfer shall be treated as permitting such transfer).

[5] EPCRS permits retirement plan sponsors to correct certain failures to meet applicable tax qualification requirements and thereby continue to provide employees with retirement benefits on a tax-favored basis. For a description of the current EPCRS program as reflected in Rev. Proc. 2021-30, see ICI Memorandum No. 33711, dated August 2, 2021, available at www.ici.org/memo33711.

[6] Section 305(e) of the Act defines an "eligible inadvertent failure." Self correction is not permitted where the error is identified by IRS prior to the plan initiating self-correction or

the self-correction is not completed within a reasonable period after such failure is identified. The Act directs IRS to expand EPCRS to allow IRA custodians to address certain inadvertent failures.

[7] For a summary of Notice 2023-43, see ICI Memorandum No. 35377, dated July 18, 2023, available at www.ici.org/memo35377.

[8] Disqualified person is defined in Code section 4975(e)(2) and owner-employee is defined in Code section 401(c).

[9] The Notice gives an example of an overpayment due to an incorrect allocation of a profit-sharing contribution, which causes another participant to receive an underpayment.

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