

Washington Pulse



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IRS Releases Interim Guidance on Inadvertent Benefit Overpayments

The Internal Revenue Service (IRS) recently issued [Notice 2024-77](#), providing interim guidance on the treatment of “inadvertent benefit overpayments” from defined benefit and defined contribution plans as provided by Section 301 of the SECURE 2.0 Act of 2022 ([SECURE 2.0](#)). This interim guidance specifically refers to the application of the plan qualification and rollover distribution rules provided by Internal Revenue Code Sections ([IRC Secs.](#)) [414\(aa\)](#) and [402\(c\)\(12\)](#) to the correction methods available for inadvertent benefit overpayments under the Employee Plans Compliance Resolution System (EPCRS) as outlined in Revenue Procedure ([Rev. Proc.](#)) [2021-30](#).

Background

In September 2021, the IRS issued Rev. Proc. 2021-30, which updated previous guidance regarding the methods available under EPCRS to correct operational failures caused by “overpayments” from defined benefit and defined contribution plans. Rev. Proc. 2021-30 provides the following methods to correct operational failures caused by “overpayments”.

Methods to Correct Failures Caused by “Overpayments”	Defined Contribution	Defined Benefit
Corrective repayment options		
• lump sum	X	X
• installment		
• reductions in future periodic payments		
If plan sponsor chooses not to pursue full or partial repayment		
• plan sponsor must make corrective payment up to the full amount of the overpayment	X	X
If recoupment is required and not made by a participant		
• plan sponsor must notify the participant that the overpayment is considered an ineligible rollover distribution	X	X
Funding Exception Correction Method		
• no corrective payments required		X
• available to plans subject to IRC Sec. 436 that are sufficiently funded and satisfy other eligibility requirements		
Contribution Credit Correction Method		
• required corrective payments reduced by certain additional contributions in excess of minimum funding requirements		X

In December 2022, SECURE 2.0 added IRC Sections 414(aa) and 402(c)(12) to clarify that responsible plan fiduciaries have discretion as to whether to recoup inadvertent benefit payments from certain recipients and provide the criteria that must be met in order to properly execute the correction method. In October 2024, the IRS released Notice 2024-77, confirming the application of the new Internal Revenue Code Sections and providing details as to their impact on the correction methods provided under EPCRS as described in Rev. Proc. 2021-30.

Definition of “Inadvertent Benefit Overpayment”

“Eligible Inadvertent Failure”. SECURE 2.0 expanded EPCRS to include the definition of an “eligible inadvertent failure.” An “eligible inadvertent failure” is defined as a failure that occurs despite the existence of established practices

and procedures that satisfy standards as described in Rev. Proc. 2021-30. An eligible inadvertent failure does *not* include any failure that is considered egregious, related to the diversion or misuse of plan assets, or is directly or indirectly related to an abusive tax avoidance transaction.

“Inadvertent Benefit Payment”. Notice 2024-77 defines an “inadvertent benefit overpayment” as an “eligible inadvertent failure” that occurs due to a payment made from a defined benefit or defined contribution plan that exceeded the amount payable under the terms of the plan or a limitation provided in the Internal Revenue Code or Treasury Regulations. An inadvertent benefit overpayment also includes a payment made before a participant incurs a distributable event permitted under the terms of a qualified plan. An inadvertent benefit overpayment does *not* include an overpayment made

- to a disqualified person under the prohibited transaction rules,
- to an “owner-employee” as defined in [IRC Sec. 401\(c\)\(3\)](#), or
- pursuant to a correction method under EPCRS for a different qualification failure.

Retaining Status as a Qualified Plan

A plan sponsor may risk plan disqualification if an inadvertent benefit overpayment is not properly corrected. SECURE 2.0 added IRC Sec. 414(aa), which clarified that defined benefit and defined contribution plans under [IRC Secs. 401\(a\)](#) and [403](#) will *not* be disqualified if the plan

- fails to obtain payment from a participant, beneficiary, employer, plan sponsor, fiduciary, or other party because of an inadvertent benefit overpayment; or
- amends the plan document to either increase past or decrease future benefit payments to adjust for the inadvertent benefit overpayment.

The plan sponsor remains responsible for making contributions to meet minimum funding standards as provided by [IRC Secs. 412](#) and [430](#) and must apply the compensation limit and annual additions contribution limits as described in [IRC Secs. 401\(a\)\(17\)](#) and [415](#). The Secretary of the Treasury has also indicated the possibility of issuing additional guidance or regulations regarding the application of IRC Sec. 414(aa) to inadvertent benefit overpayment failures in the future.

Notice 2024-77 clarifies that a corrective payment is generally *not* required for an inadvertent benefit overpayment failure, unless another disqualifying event (failure) is created if recoupment of an inadvertent benefit overpayment is not made (e.g., if the amount of the inadvertent benefit overpayment is owed to another participant or to a forfeiture account). The guidance confirms that a plan sponsor retains the right to recoup the amount of an inadvertent benefit overpayment using permissible methods.

Single Employer Defined Benefit Plans. If a plan incurs an operational failure under [IRC Sec. 436](#) (funding-based limits on benefits) that results from an inadvertent benefit overpayment to a recipient, the plan sponsor or another person must make corrective payments under the procedures as described in Section 6 of Rev. Proc. 2021-30, to the extent the overpayment is not recouped from the recipient.

Treatment of Inadvertent Benefit Overpayments as Eligible or Ineligible Rollover Distributions

Notice 2024-77 aligns with the EPCRS correction method that states that an inadvertent benefit overpayment is treated as an ineligible rollover distribution (also referred to as a noneligible rollover distribution or NERD) if recoupment of the overpayment is required and is *not* recovered from a participant (see chart above). The Notice also provides clarity regarding if an overpayment is considered an eligible rollover distribution (ERD) or a NERD when an inadvertent benefit overpayment is transferred to another plan. According to this guidance, the portion of the overpayment that

- is *not* sought through recoupment will be treated as an ERD (if it would have otherwise been an ERD but for the overpayment);
- is sought through recoupment can be returned to the plan by a participant or beneficiary; and if so, will be treated as a rollover back into the plan (even if the plan does not permit rollover contributions).

Notice 2024-77 also confirms that if recoupment *is* sought from the recipient, the portion of the overpayment that is not returned, if any, is considered a NERD. The plan sponsor must notify the individual that the overpayment amount that was not returned to the plan is considered a NERD. This notification can be included in the same communication as the recoupment request.

Treatment of Inadvertent Benefit Overpayments Caused by Limit Failures

While corrective payments are generally *not* required for an inadvertent benefit overpayment, Notice 2024-77 states that this general rule does not apply for an inadvertent benefit overpayment that exceeds the compensation cap limit

as defined in IRC Sec. 401(a)(17) or the IRC Sec. 415 annual additions limit. If these limits are exceeded, the resulting inadvertent benefit overpayment requires obtaining a corrective payment. If recoupment of the inadvertent benefit overpayment is not obtained, the distribution is considered a NERD. Therefore, the plan sponsor must notify the individual that any portion not returned to the plan is not eligible for rollover. This notice can be combined with the recoupment request.

Amendment as a Corrective Method

A plan sponsor can self-correct an eligible inadvertent failure (which includes an inadvertent benefit overpayment) by amending the plan document to increase past benefit payments. But the amendment cannot cause any other failure, including a limit failure of IRC Secs. 401(a)(17), 415 or 436—unless, in the case of an IRC 436 limit failure, a contribution is made as allowed under IRC Sec. 436(c)(2) and Section 6.02(4)(e) of Rev. Proc. 2021-30.

Modifications to EPCRS Corrective Procedures

Notice 2024-77 makes several modifications to the EPCRS corrective procedures as outlined in Rev. Proc. 2021-30. These modifications include the following items.

- The definition of an overpayment (if an inadvertent benefit overpayment) in certain sections of Rev. Proc. 2021-30 (as described above).
- A plan sponsor is no longer required to notify an individual that an overpayment is a NERD if recoupment of an inadvertent benefit overpayment *is not* sought.
- The requirement for a corrective payment does *not* apply, except for failures caused by
 - overpayments that exceed the limits defined in IRC Secs. 401(a)(17) and 415, or
 - IRC Sec. 436 failures resulting from an inadvertent benefit overpayment that is *not* recouped from the recipient.
- In the event an inadvertent benefit overpayment is treated as an ERD, there is no need to apply for a waiver of the
 - 6 percent excess contribution penalty tax (if applicable), or
 - 10 percent early distribution penalty tax.

Application of Guidance

The interim guidance provided in Notice 2024-77 is effective for operational failures caused by inadvertent benefit overpayments that occurred on or after October 15, 2024, and allows plan sponsors to rely on a reasonable, good faith interpretation of IRC Secs. 414(aa) and 402(c)(12) for failures that occurred before this date.

The following chart describes guidance applicable to operational failures caused by inadvertent benefit overpayments that occurred before October 15, 2024.

Date of Occurrence	Inadvertent Benefit Overpayment	Guidance Application
On or after October 15, 2024	Operational Failure	Interim Guidance provided by Notice 2024-77
December 29, 2022 to October 14, 2024	Operational Failure	Reasonable, good faith interpretation of IRC Secs. 414(aa) and 402(c)(12)
	Operational Failure	Reasonable, good faith interpretation of the existing administrative guidance at the time
Before December 29, 2022	Determinations to Not Seek Recoupment or Recovery of All or Part of an Inadvertent Benefit Overpayment	May rely on determinations made not to seek recoupment or recovery
	Installment Payments or Reductions in Periodic Benefit Payments	These payments or reductions in periodic benefit payments may continue after December 29, 2022

Next Steps

The IRS has requested general comments on or before December 16, 2024, regarding the interim guidance provided in Notice 2024-77. The Agency also invites comments regarding the application of IRC Sec. 414(aa) and IRC Sec. 402(c)(12) to EPCRS correction methods as provided by Section 301 of SECURE 2.0.

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