Preparing for your annual employee benefit plan audit

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It’s time for your annual employee benefit plan audit. Are you prepared?

Whether this is the first time you’ve gone through the process or the fifteenth, the annual audit of your company’s employee benefit plan can seem overwhelming. But it doesn’t need to be. If you are working with a quality audit firm, and you follow some basic steps to prepare, you can get through the audit timely with minimal disruptions to your already busy schedule.

This article covers the key steps in the process. Information in this article comes from the following publications of the US Department of Labor:

Selecting an Auditor for Your Employee Benefit Plan

Meeting Your Fiduciary Responsibilities

Why does my company need to have an annual audit?

To protect the health and retirement assets of your employees and your company, federal law generally requires employee benefit plans with 100 or more participants to have an audit as part of their obligation to file an annual return/report, the Form 5500. Some pension plans with fewer than 100 participants may also be required to have an audit if they fail to meet certain conditions relating to their plan investments, bonding, and disclosure requirements.

A quality audit serves several purposes. First and foremost, it helps to verify the financial integrity of your plan and ensure that funds will be available when they are needed to pay retirement, health and other promised benefits to your employees. Secondly, it helps fulfill your plan’s legal responsibility to file a complete and accurate annual return or report each year. It’s important to select an experienced, reliable auditor to avoid penalties that could be imposed due to an incomplete, inadequate or untimely audit report.

By uncovering problems, the annual audit reduces fiduciary responsibility risk. The annual audit can help identify compliance problems early. It is always easier to fix an operational failure earlier in the plan life.

What should I expect from the audit?

The annual audit has two main components: compliance and financial reporting. For compliance, the auditor will want to understand plan design and the rules that need to be followed and to know what the plan does to ensure that these rules are followed. The auditor will review a sample of your plan’s data to verify that the rules are being followed. Also, the auditor will review the timeliness of employee contributions made to the plan trust.

The financial reporting component of the audit includes the financial statements and the Form 5500. To make the audit wrap-up process easier for you, the auditor can assist you with drafting financial statements. The auditor will also review and provide feedback on the Form 5500 helping you ensure an accurate filing. However, keep in mind, it is always plan management’s responsibility to ensure that the financial statements and Form 5500 are complete and accurate.

The auditor will issue an opinion on the financial statements. The audited financial statements must be included when the Form 5500 is filed.

What if the auditor finds a problem?

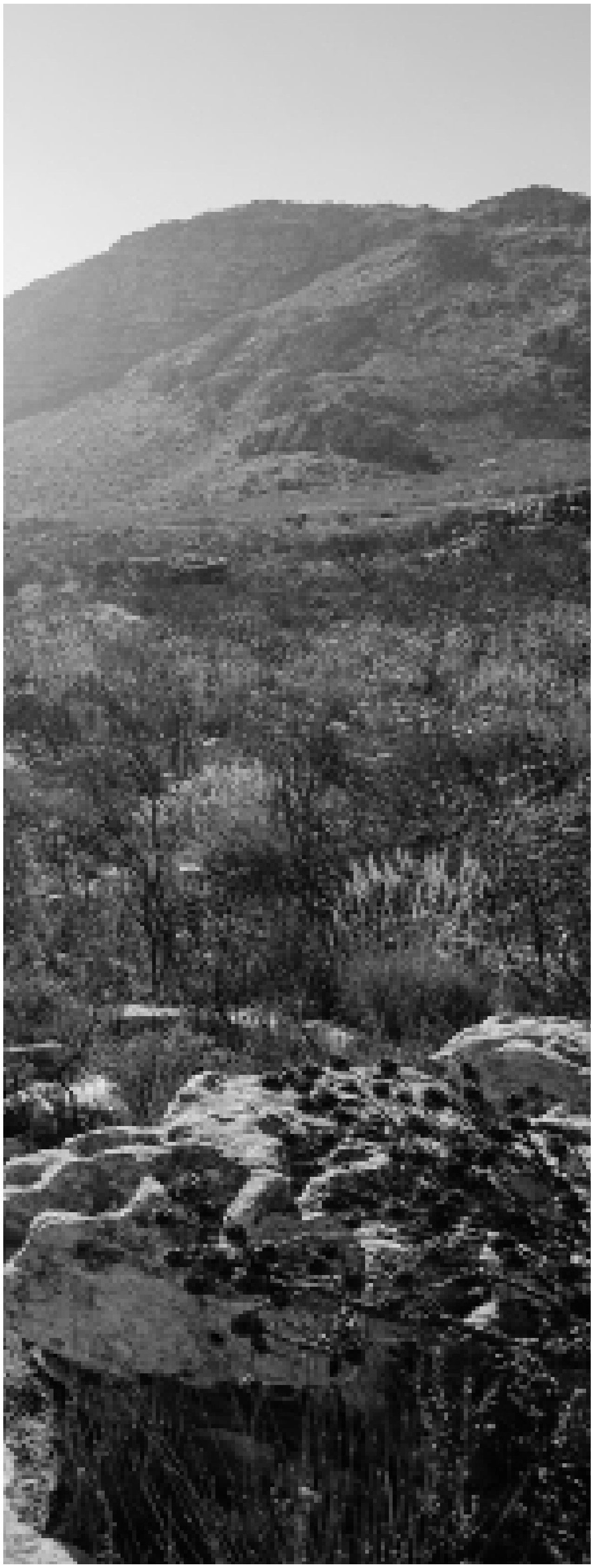
If there is a compliance issue, the auditor will report it to you. Mistakes and operational failures are fairly common, and an experienced auditor will guide you through the process of correction. Common issues that can be fixed in an audit include:

- Untimely remittance of participant contributions. Employers of all sizes are required to transmit employee contributions or loan repayments to retirement plans as soon as they can be reasonably segregated from the employer's general assets. A good rule of thumb is that you should be able to submit the contributions that have been withheld in the same amount of days it takes you to submit your payroll taxes.
- Operational errors arising from failing to follow plan terms, such as incorrect compensation used in the calculation of contributions (wrong definition of compensation), improper match allocations, incorrect application of the participant eligibility terms, and improper determination of vesting for participant distributions.
- Late or Missed Filing of Form 5500.
- Participant Loan Failures such as loans that exceed the maximum permitted dollar amount or providing loans that are not allowed by the Plan.
- Failure to timely amend the Plan to keep it updated with changes in the Law.

How can I prepare?

The first step in preparing for your audit is to establish a timeline with the auditor. During the week the auditor is working, block time in your schedule for questions/requests. The audit will proceed more quickly if you are prompt in responding to requests and providing information.

Communicate early and often with the auditor as well as others who are assisting you. Ask the auditor to let you know regularly which requests are still open so you can work with others to make sure the information is provided.



What's the best way to determine the quality of an outside auditor?

First, make sure the auditor has the right certification. Under federal law, an auditor engaged for an employee benefit plan must be licensed and/or certified as a public accountant by a state regulatory authority. Auditors should also be independent, meaning they do not have any financial interests in the plan or the plan sponsor that would affect their ability to render an objective, unbiased opinion about the plan's financial condition.

Next, be sure to find out about the auditor's experience. An auditor's failure to perform tests in areas unique to employee benefit plan audits is one of the most common reasons for a deficient audit report. Look for an auditor who has solid training and extensive experience with employee benefit plan audits, familiarity with benefit plan practices and operations, as well as the special auditing standards and rules that apply to these plans. If you hire an audit firm with a dedicated employee benefit plan team, your fiduciary liability risk in regards to the audit will be reduced.

What other outside parties will be involved?

You will likely rely on several outside parties during the audit, and they should make themselves available to work directly with your auditor. Make sure you have the appropriate user controls in place and follow your organization's best practices for outside parties.

Your plan's third party administrator (TPA) will likely be a key part of the process. Your auditor will probably work directly with the TPA to obtain most of the documents and recordkeeping reports, many of which the auditor will download directly from the TPA.

Other outside parties may include your plan's investment adviser or a plan consultant, who can help complete many of the questions related to your plan's investment performance and plan administration.

How do I know if I'm a fiduciary?

You are a fiduciary if your job involves operating a plan. It is determined based on the functions you perform for the plan, not on your job title. For example, if you, or a committee, administer and manage a plan or the plan's investments, this makes you, or the committee, a fiduciary.

A plan must have at least one fiduciary. It could be a person, entity, board of directors or committee, and it must be named in the written plan document or through a process, such as having control over the plan's operation.

Examples of fiduciaries include trustee, investment advisors, plan administrator, a Plan's administrative or investment committee and those who select committee officials.

A key component to determining fiduciary responsibility is whether someone or something exercises discretion or control over the Plan.

What are my responsibilities as a fiduciary?

The main responsibility, of course, is to carry out your duties prudently. You must act solely in the interest of your plan participants and their beneficiaries with the exclusive purpose of providing benefits to them. You are responsible for following the plan documents, unless they are inconsistent with ERISA, ensuring that plan investments are diversified, paying reasonable plan expenses and benchmarking fees.

An investment advisor can help you carry out the functions of your Plan that require specific expertise, not just with investments but other related areas.

Do I have personal liability as a fiduciary?

If you do not follow the basic standards of conduct, you may be personally liable to restore any losses to the plan, or to restore any profits made through improper use of the plan's assets resulting from your actions.

Here are some ways you can limit your liability as a fiduciary:

- Document the processes you used to properly carry out your fiduciary responsibilities.
- Give participants control over the investments in their accounts, therby limiting your liability for your plan participants' investment decisions
- Hire a service provider or providers to handle fiduciary functions, so that the person or entitiy then assumes liability for those selected functions. You are still responsible for the selection of the manager, but you are not liable for the individual investment decisions fo that manager. You are also responsible for periodically monitoring the manager to ensure that the plan's investments are being handled prudently and in accordance with the contract or agreement.

Employee Benefit Plan Audit Checklist

What items can I expect the auditor to request?

The auditor will need most or all of the following documents to conduct the audit and draft the financial statements, which must undergo management review:

Documents

- ☐ Adoption Agreement
- ☐ Plan Document
- ☐ Fidelity Bond
- ☐ IRS Determination Letter
- ☐ Plan amendments
- ☐ Participant notices
- ☐ Investment Committee minutes
- ☐ Summary Plan description
- ☐ Fee disclosures

Payroll Information

- ☐ Payroll register
- ☐ Census
- ☐ Contribution deposit report that includes:
  - ☐ Transmission amounts
  - ☐ Transmission times
- ☐ Participant level data

Trustee/Recordkeeping

- ☐ Certified Trust report
- ☐ Investment Certification
- ☐ Participant Accounting Report
- ☐ Participant Contribution report
- ☐ Trust Reconciliation
- ☐ Loan Report
- ☐ Distribution Report
- ☐ Rollover Report
- ☐ Compliance Testing

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