How to Prepare for an Employee Benefit Plan Audit and Form 5500 Changes

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Learning Objectives

At the end of the session, you will be able to:

- Determine when a Retirement Plan audit is required
- Understand the scope and objectives of a Retirement Plan audit
- Understand unique considerations of a 403(b) Plan audit
- Prepare for and facilitate an effective and efficient audit
- Understand the significant changes to Form 5500

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How to Prepare for an Employee Benefit Plan Audit

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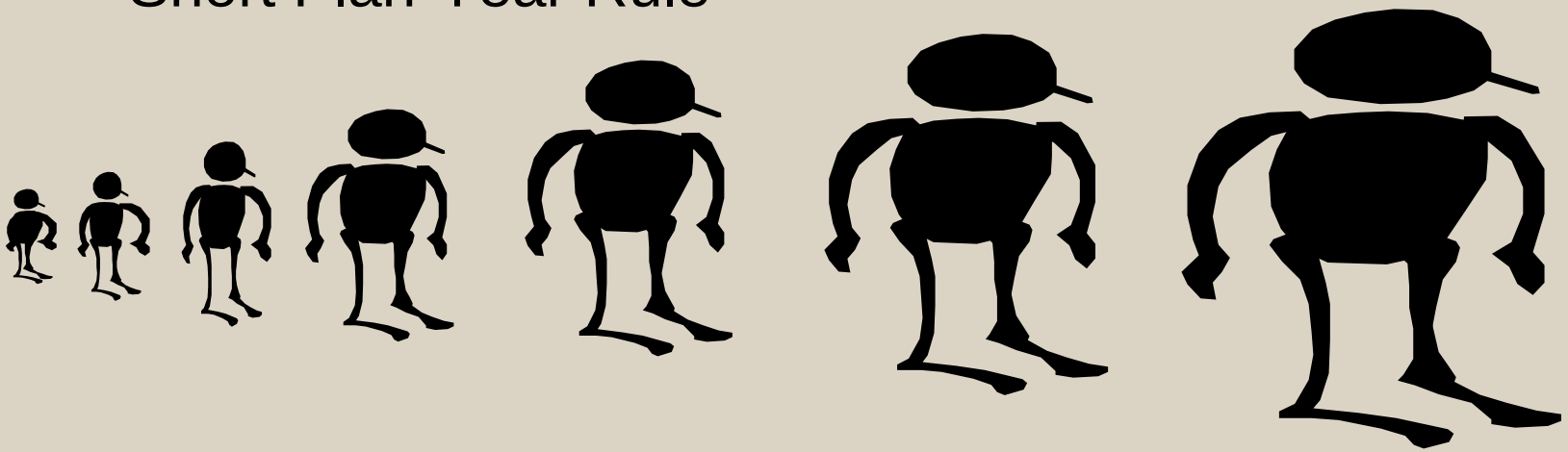
Retirement Plan Audit Requirements

- Outlined in Form 5500 instructions
- Number of Participants
  - 100 or more
    - ◊ First day of plan year
  - 80/120 Rule
    - ◊ Applies for 403(b) Plans
  - Short Plan-Year Rule



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Retirement Plan Audit Requirements

Who is a participant?

1. Employees actively making/receiving contributions
2. Employees that have the right to participate (have met eligibility requirements) that are not
3. Former employees that maintain an account balance in the plan

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Retirement Plan Audit Requirements

403(b) Safe Harbor Exemption (non-ERISA)

- Employee participation is voluntary
- Employee can enforce vendor contract without employer's assistance (individual contracts)
- Employer's involvement is limited to
  - ◊ Letting vendors publicize products to employees
  - ◊ Requesting information
  - ◊ Summarizing or compiling employee information
  - ◊ Collecting and remitting deferrals to vendors
  - ◊ Maintaining records (e.g. deferral / plan records)
  - ◊ Selecting annuity vendors (must be reasonable)
- Employer receives no unreasonable direct or indirect consideration

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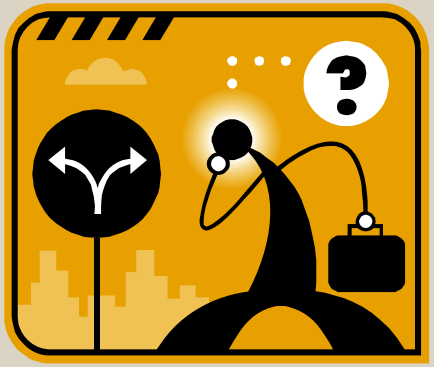
Retirement Plan Audit Requirements

Scenario 1



- Plan effective January 1, 2006
- Calendar year-end
- Had 120 participants on January 1, 2009
- Could have filed as a “small” plan for 2008
- Need an audit for the 2009 plan year?

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Retirement Plan Audit Requirements

Scenario 2

- Plan effective January 1, 2006
- Calendar year-end
- Had 110 participants on January 1, 2009
- Could have filed as a “small” plan for 2008
- Need an audit for the 2009 plan year?

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Retirement Plan Audit Requirements

Scenario 3

- Plan effective January 1, 2009
- Calendar year-end
- Had 100 participants on January 1, 2009
- Since new plan, no 2008 filing requirement
- Need an audit for the 2009 plan year?

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Audit Objective

- Established by Generally Accepted Auditing Standards (GAAS)
  - Express an opinion on financial statements and supplement schedules
    - ◊ Whether fairly stated in conformity with Generally Accepted Accounting Principals (GAAP)
      - In all material respects
- GAAS audit is NOT designed to ensure compliance with ERISA
- Objectives influenced by Department of Labor (DOL) and Internal Revenue Service (IRS)

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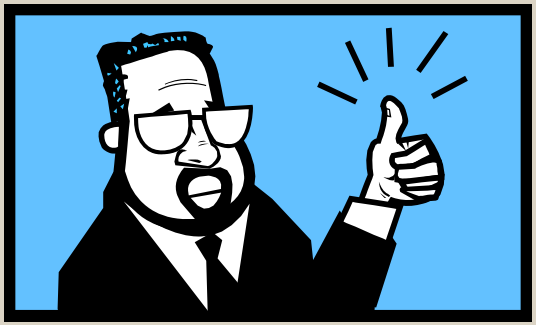
Audit Objective

- Types of Audit Opinions
  - Unqualified
    - ◊ Accepted by DOL
  - Qualified
    - ◊ Not accepted by DOL*
    - ◊ May result in rejection of Form 5500
  - Adverse
    - ◊ Not accepted by DOL*
    - ◊ May result in rejection of Form 5500
  - Disclaimer
    - ◊ Accepted by DOL in the case of limited-scope audits
    - ◊ Otherwise, not accepted by DOL*
      - May result in rejection of Form 5500



*Certain exceptions are available for 403(b) Plans

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What is Audited?

- Limited-scope audit
  - Contributions
    - ◊ Plan level
  - Benefit Payments
  - Participant Data
    - ◊ Eligibility
  - Plan Obligations
    - ◊ Participant Accounts
  - Other
  - Participant Loans?

- Full-scope audit
  - Everything in left column
  - Investments
    - ◊ Valuation
    - ◊ Income

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Key Audit Areas

- Internal Controls
  - Assessment of Plan's control environment
  - Control walk-throughs of significant transaction classes
- Contributions (Plan level)
  - Timely remittances of employee contributions
  - Reconciliation between trust, payroll and recordkeeping
- Benefit Payments
  - Detail listing matches trust statement
  - Meet eligibility standards to receive benefits
  - Vesting

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Key Audit Areas

- Participant Data
  - Integrity of data used to determine eligibility
  - Recalculate eligibility and compare to actual
- Plan Obligations
  - Reconciliation of activity and balances between trust/insurance statements and recordkeeping
  - Investment Elections
  - Income Allocation

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Key Audit Areas

- Other
  - Expenses
  - Non-discrimination testing
  - Mergers
  - Change in Service Providers
  - Subsequent Events
- Investments (full-scope only)
  - Valuation
    - ◊ Hard to value assets
  - Income
  - Participant Loans

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Role of SAS 70

- Important in electronic environment
- Report on the Processing of Transactions by Service Organizations
  - Auditor audits and assesses internal controls of a service organization
  - Auditor issues a report called the “Service Auditor's Report”
  - Internal controls evaluated are set by service organization

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Role of SAS 70

- Two Types
  - Type I
    - ◊ Report on controls regarding
      - *Description*
      - *Design*
    - ◊ May be used to gain an understanding of controls
  - Type II
    - ◊ Report on controls regarding
      - Description
      - Design
      - *Effectiveness*
    - ◊ May be used to gain an understanding of controls
    - ◊ May be used to reduce testing

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Role of Third-Party Administrators

- Involvement can vary greatly between third-party administrators
- Source of a significant amount of audit information
  - Audit Package
  - Additional information
- Ultimately responsibility is with Plan Sponsor

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Unique 403(b) Audit Considerations

- Safe Harbor Exemption
- First time subject to full reporting (Form 5500) reporting requirements
- Shift in understanding of Plan oversight responsibility – fiduciary
  - "Not our money"
- New experience for Plan Sponsor personnel and TPA

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Unique 403(b) Audit Considerations

- Plan Sponsor historical reliance on TPA
  - Plan design
  - Responsibility
  - Audit scope/objective
- Availability of historical data
  - Impact on opinion
- DOL / GAAP reporting differences
  - Impact on opinion

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Unique 403(b) Audit Considerations

403(b) Audit Opinion

- Unqualified = GOOD!
- Disclaimer due to limited-scope = GOOD!
- Qualified, adverse or disclaimer due to pre-2009 contracts not covered = ACCEPTABLE
- Qualified, adverse or disclaimer due to inability to verify beginning balances of contracts covered = ?

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How Do I Effectively Prepare for an Audit?

- Establish a timetable that is mutually agreeable to
  - You
  - Auditor
  - Other Service Organizations
- Obtain request letter sufficiently in advance
  - Work with auditor to understand exactly what they are requesting
- Pull information prior to auditor site visit
  - Provide information in advance
  - Have ready/organized when they walk in your office

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How Do I Effectively Prepare for an Audit?

- Facilitate auditor on-line access to your Plan if possible
- Prepare reconciliations
  - Investigate variances and irregularities prior to start of audit fieldwork

BE READY!

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How Do I Effectively Facilitate an Audit?

- Make audit a priority once it commences
  - Be available to auditors during site visit
  - Respond to additional requests/inquiries timely
- Monitor progress on a periodic basis
  - Weekly updates?
- Obtain support from organization's financial department
  - Bring Controller/CFO into process

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How Do I Effectively Facilitate an Audit?

- Re-establish timetable if off-course
- Closing Meeting
  - Discuss audit findings
  - Discuss process improvement

COMMUNICATE!

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Auditor Selection

- Important to select auditor familiar with plan audits
  - Deficient audit may result in rejection of Form 5500
    - ◊ Becomes Plan Sponsor's issue
- Referral sources
  - Peers
  - Third-party administrator
  - Other Plan Professionals
  - American Institute of Certified Public Accountants Employee Benefit Plan Audit Quality Center (AICPA EBPAQC)

Employee Benefit Plan Audit Quality Center
AICPA

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Form 5500 Changes

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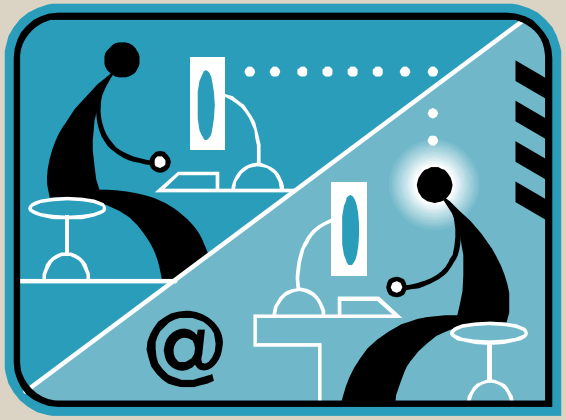
Electronic Filing

- Electronic filing ***required*** beginning with 2009 filings
  - EFAST2
- Amended returns or delinquent filer (DFVC) filings after must be prepared and submitted through the EFAST2
  - Regardless of Plan year



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Electronic Filing

- Filers and preparers can continue to use third party software to complete the forms
  - Needs to be EFAST2 approved
- As an alternative, plan sponsors can fill out the forms directly on the EFAST website
  - IFILE
    - ◊ barebones/no-frills electronic filing system
- Plan Sponsors/preparers may be able to use a combination of systems

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Electronic Filing

- Need credentials to sign and submit returns
  - www.efast.dol.gov
- All related schedules/attachments need to be submitted electronically
  - Accountant's Opinion and Schedule MB/SB must be in PDF format and have signatures
  - Other attachment types can be TXT or PDF formats
- Immediate edit checks
- Posted to EFAST website within 24 hours of transmittal

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New Form 5500-SF

- New Form for 2009
- Two page “Short Form” 5500 for small plans (under 100 participants). Can use if
  - Exempt from annual audit requirement
  - 100% invested in secure investments that have a readily determinable fair value at all times during plan year
  - Held no employer securities at any time during the plan year
  - Not multiemployer plan
- No schedules required except DB plans required to file actuarial schedule.

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Form 5500 Revisions

- Part I:
  - Modified extension box to now be 4 boxes
    - ◊ Filing under Normal Extension (Form 5558)
    - ◊ Filing under Automatic extension (Employer Federal Tax Extension)
    - ◊ Filing under the DFVC Program
    - ◊ Filing under a Special Extension (Announced by IRS, DOL or PBGC)
- Part II Signatures
  - Box added for signature of DFE
    - ◊ If Plan Administrator is same signature of Employer/Plan Sponsor box only need to sign for Plan Administrator
- Part II, Line 8a and 8b
  - Certain new codes added

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Schedule A Revisions

- Added Part IV Provision of Information Section
  - Identifies any insurance company that fails to provide any information necessary to complete the Schedule A
  - Before reporting them, plan sponsor must contact the provider and advise them that they intend to list them on the Schedule A in Part IV

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Schedule C Revisions

- Report entities that received $5,000 or more in total direct or indirect compensation (money or fair value of items) in connection with services rendered to the plan
- Additional reporting of indirect compensation for certain service providers
- Alternative reporting option of “eligible indirect compensation”
- Report service providers who fail or refuse to provide information for reporting
- “Top 40” is eliminated
- There are some new service and fee codes
- Reportable compensation now includes brokerage fees & commissions regardless of whether broker has discretion

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Schedule C Revisions

- Direct compensation
  - Payments made directly by the plan for services rendered to the plan or because of a person's position with the plan are reportable as direct compensation
- Examples
  - Direct payments by the plan out of a plan account.
  - Charges to a plan forfeiture accounts and fee recapture accounts
  - Charges to a plan's trust account before allocations are made to individual participant accounts
  - Direct charges to plan participant individual accounts

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Schedule C Revisions

- Indirect compensation
  - Compensation received from sources other than directly from the plan or plan sponsor in connection with services rendered to the plan during the plan year or person's position with the plan
- Example
  - Fee and expense reimbursement payments received by a person from an investment in which the plan invests in that are charged against the fund or account and reflected in the value of the plan's investment. This may include:
    - ◊ Management fees paid by a mutual to its investment advisor
    - ◊ Sub-transfer agency fees
    - ◊ Shareholder servicing fees
    - ◊ Account maintenance fees
    - ◊ 12b-1 distribution fees

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Schedule C Revisions

- Additional reporting of indirect compensation for certain service providers
  - For “key service providers” must report each source from whom the person received indirect compensation of
    - ◊ $1,000 or more, or
    - ◊ The plan was given a formula or other description of how compensation is determined instead of dollar amount
  - “Key service providers” is each person identified in Line 2 of Schedule C who is a fiduciary to the plan or provides one or more of the following services to the plan
    - ◊ Contract Administrator
    - ◊ Consulting
    - ◊ Investment Advisory or management
    - ◊ Securities Brokerage
    - ◊ Recordkeeping

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Schedule C Revisions

- "Eligible indirect compensation" alternative reporting option
  - For indirect compensation to be "eligible indirect compensation"
    - ◊ Plan Sponsor must receive written materials that disclose and describe all of the following
      - The existence of the indirect compensation
      - The services provided for the indirect compensation or the purpose for payment
      - The amount (or estimate) of the compensation or description of the formula used to calculate or determine the compensation
      - The identity of the party or parties paying and receiving the compensation

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Schedule C Revisions

- Reporting service providers who fail or refuse to provide information for reporting
  - Plan sponsor must contact the provider before reporting them and advise them that they intend to list them

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Schedule H Revisions

- Part II: Added a line item for dividends related to mutual funds (line 2b(2)(C))
- Part IV: Added question 4l - “Has the plan failed to provide any benefit when due under the plan?”
- Part IV: Added question 4m - “If this is an individual account plan, was there a blackout period?”
- Part IV: Added question 4n - “If 4m was answered yes, was the required notice supplied to participants or an exception applied under 29 CFR 2520.101-3?”
- Enhanced supplemental schedule of delinquent participant contributions (Part IV, line 4a)

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Schedule I Revisions

- Part I: Added a line item for expenses paid to administrative service providers (line 2h)
- Part IV: Added question 4l - “Has the plan failed to provide any benefit when due under the plan?”
- Part IV: Added question 4m - “If this is an individual account plan, was there a blackout period?”
- Part IV: Added question 4n - “If 4m was answered yes, was the required notice supplied to participants or an exception applied under 29 CFR 2520.101-3?”

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Schedule R Revisions

- Added Part IV related to ESOP's (as Schedule E was eliminated in 2009)
- Added Part V related to Multiemployer Defined Benefit Pension Plans
- Added Part VI related to Single-Employer and Multiemployer Defined Benefit Pension Plans for more than 1,000 participants

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Schedules Eliminated

- Schedule E – ESOP Annual Information
  - Was eliminated in 2009 (certain limited questions moved to Schedule R)
- Schedule SSA – Annual Registration Statement Identifying Separated Participants with Deferred Vested Benefits
  - Was eliminated in 2009
  - Information on this Form will <u>not</u> be filed with EBSA (due to confidentiality of SSN information
  - Will be a required plan filing with the IRS on Form 8955-SSA (not available yet)

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Questions and Discussion

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