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DOL, IRS Plan Audits Becoming More Frequent and Thorny

There are a wide variety of mistakes plan fiduciaries can make; getting it all right is an ongoing team effort.

By Lee Barney EDITORS@ASSETINTERNATIONAL.COM | December 15, 2016

The Department of Labor (DOL) and the Internal Revenue Service (IRS) both frequently find numerous mistakes that retirement plan sponsors make in running their plans, and, as a result, they are conducting audits more frequently, experts say.

"The DOL and IRS are truly diving deep into the operations of employee benefit plans," says Lisa Canafax, senior retirement consultant with Willis Towers Watson in Chicago. "We have seen a deeper dive into the operations of plans, particularly with data requests. Plans may be asked for a full census file on the transactions for each participant. Expect the DOL and IRS to do a lot of data mining."

The number one violation the auditors find with plans is the timely remittance of employee deferrals, says Rick Skelly, client executive at Barney & Barney LLC in San Diego, California. "This causes plan sponsors to pay lost earnings and an excise tax on late deposits. The regulations require plans with fewer than 100 participants to make the deferrals within seven days. For larger plans, they must do so as soon as administratively feasible after each payroll, typically within three to five days."

And if a sponsor is inconsistent about deferrals, that will also be seen as a major error, says Heidi LaMarca, head of the Employee Benefit Plan Service Practice at accounting and auditing firm Windham Brannon, in Atlanta. For instance, if the sponsor makes a deferral for some participants within two days but others within five days, that will be a red flag for both the DOL and the IRS, LaMarca says.

The second most common mistake found in audits is in the application of various definitions of compensation, Canafax says. "Payroll is enormously complex, and depending on the organization, it can be derived from up to 100 payroll buckets, such as base pay, bonus, overtime and moving expenses."

"There are multiple types of compensation that can be considered as eligible for an employee to contribute from," Skelly agrees. "Some of the most common are W2, 415 or 3401, and the plan documents usually dictate which one the sponsor has to use."

Then there is the surprisingly common issue of the plan simply not following its own directives, says Ellen Bartholemy, accounting services principal at Hall & Company CPAs in Irvine, California. Plan sponsors and advisers should "ensure the administration of the plan conforms to the written plan document and any administrative policies and procedures of the plan," Bartholemy notes. "Maintain up-to-date plan documents and conduct periodic compliance reviews."

NEXT: Monitoring investments

Of course, it is incumbent on plan sponsors and their advisers to meticulously monitor investments, says Hal Hunt, head of the Employee Benefit Plan Audit Practice at accounting and auditing firm Mayer Hoffman McCann in Kansas City, Kansas. It is important for sponsors to keep detailed minutes of the retirement plan committee meetings where investments are reviewed. "There should be a watch list for investments that are not performing well, and action should be taken when needed," Hunt says.

Related to this, the DOL and IRS want to make sure that plans with self-directed brokerage accounts educate participants about the risks of investing in individual stocks, LaMarca says. "The DOL is concerned about whether participants understand the

risks and know enough about equity investments to make an informed choice, particularly if they are directing 100% of their portfolio into the self-directed brokerage account."

If the plan has an employee stock ownership plan, the DOL wants to ensure that the stock is properly valued, Hunt says. "The DOL believes that the valuation firms will do the bidding of the sellers," he says.

Another "marquee issue for DOL and IRS audits," Canafax says, "is payment of benefits to vested terminated participants. When the DOL started with its deep dive audits, it found that many organizations didn't have strong—or in some cases, any—processes to keep track of people's addresses 20 to 30 years out. The DOL is now focusing on this. It is a big issue that has risen to the level of being included in Form 5500 reporting."

NEXT: Health and welfare plans

The DOL has also recently discovered that sponsors that file Form 5500 for their 401(k) plans fail to file for their health and welfare plans, LaMarca says. "A lot of plan sponsors do not realize that they have to file for these plans," she says.

And when they file for their health and welfare plans, the DOL will look to see whether they comply with the Health Insurance Portability and Accountability Act (HIPAA), the Consolidated Omnibus Budget Reconciliation Act (COBRA) and the Affordable Care Act (ACA), Hunt says.

The DOL also wants to ensure that plans are insured with a fidelity bond and that it provides adequate coverage, LaMarca says.

Ensuring that participant loans and hardship withdrawals are being properly administered is yet another area both the IRS and the DOL find many problems, says Paula Calimafde, a principal with Paley Rothman in Bethesda, Maryland. They frequently find that plans are charging an incorrect interest rate, do not ensure that the funds are being used for the requested purpose or permit a loan to exceed the statutory limits of the lesser of $50,000 or 50% of the vested account balance, she says.

Last but not least, the DOL wants to know whether plans are monitoring their service provider fees to ensure that they are reasonable, Hunt says.

The best way to avoid these errors is to conduct regular self-assessments to get in front of potential errors, Canafax says. "Doing regular self-checks on a rolling basis is much less disruptive than going through an IRS or DOL audit," she says.

To help with this, plan sponsors can partner with an Employee Retirement Income Security Act (ERISA) lawyer, an auditing firm, a knowledgeable recordkeeper and a retirement plan adviser specialist, experts agree. And the retirement plan committee should meet regularly. "Quarterly is a best practice," LaMarca says.

Sponsors should be made aware of all of the aforementioned common mistakes and educate their payroll and finance departments—and the plan fiduciaries—about them, Skelly concludes.