

# Safety net

How audits can help ensure your benefits plans are in compliance **Interviewed by Sue Ostrowski**

If your company offers a defined contribution plan or a less common defined benefit plan, those plans may be subject to an annual audit by an independent CPA, says Ken Levine, a director of assurance services at SS&G Financial Services, Inc.

“An audit is a test to determine if the financial statements of the plan are accurate and if the plan is operating in compliance with the provisions of the plan and the law,” says Levine. “Think of it from the participant’s perspective, as a safety net. You want to know that the part of your paycheck you are asking your company to contribute to your 401(k) is actually going where you want it to go.”

The audited statements are attached to Form 5500, which all companies with defined contribution, defined benefit, or certain other types of employee benefit plan, must file. However, only companies with about 120 employees or more must attach audited statements to the form.

*Smart Business* spoke with Levine about what plans must be audited and how to prepare for the annual event.

## What kinds of plans must be audited?

Defined contribution and defined benefit plans, as well as certain other types of employee benefit plans, must be audited if they meet certain criteria as proscribed by law. In a defined contribution plan, such as a 401(K) plan, participants define what their contribution is and where it’s invested, and they are entitled to what’s in their account when they retire. These plans are audited to ensure participants’ money is being deposited in a timely manner in the funds they want it to go in and that the earnings on their investments are properly allocated to their accounts.

Defined benefit plans, usually entirely funded by the company, are also covered. In these, participants get a defined amount per year after they retire, based primarily on salary and years of service. An audit helps ensure a company is putting away enough money to cover the entire population of eligible employees.

Both types of plans are separate legal entities from the plan sponsor, so if the employer runs into trouble, the assets of participants are outside the company.

## How can a business prepare for an audit?

You need to have your books and records together. You’ll need an annual trustee statement from the organization holding the ac-



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counts. The business leader should also make available participant information so the auditor can ensure that everyone who is participating qualifies and that no one who qualifies is being excluded.

Throughout the process, the CFO or CEO should be available to answer questions and help track down data. It’s more cost-effective for the plan sponsor to track down the data than to have the auditor do so.

## What will the auditor look for?

The auditor wants to make sure participants’ money is going where they want it to go. If someone wants his money to go into mutual funds 1, 2, 3 and 4, it should be going there and not into funds 2, 3, 5 and 6. It’s up to the custodian to get the money into the right place.

Also, if there’s a company match, the auditor ensures that participants are getting the proper match. He or she also looks at when the money is coming out of employees’ paychecks and whether it’s being remitted to the plan as quickly as possible. There’s no hard and fast deadline on the number of days it should take, but it should happen very quickly so that employees’ money is going to work for them as fast as it can.

In a defined benefit plan, the auditor is making sure that in good years and in bad, the company is putting into the plan the

amount determined by an actuary to cover all eligible participants.

## If errors are detected during an audit, who is responsible — the plan sponsor or the custodian of the funds?

It could be both. If a company is not remitting funds as quickly as it’s supposed to be, that is clearly the company’s responsibility. But if participants are saying they want their money in one set of funds and the custodian of the accounts is making the mistake and putting it in different funds, that is the responsibility of the custodian. But even if it’s the custodian’s mistake, that doesn’t necessarily alleviate the plan sponsor from responsibility because that company is responsible for choosing, overseeing and managing a qualified custodian.

Usually the penalties are relatively small, but if a company does something intentional — say the plan sponsor hangs on to its participants’ money to help pay the bills — the penalties and the consequences can be severe. There are also penalties for noncompliance and for failing to file on time.

## What should a business leader look for when hiring an independent auditor?

First and foremost, retain a firm that has experience in auditing benefits plans. You don’t want to be the only company or one of only a few companies that the firm audits, because an incomplete or inadequate audit can result in penalties against the plan sponsor.

Ask how many plans the firm audited and what is the size of those plans. A large public company could have a plan or plans with billions of dollars, while a private company might have a plan with a few million dollars, and there can be a big difference in the complexity of the audit. You want a firm that has experience auditing within the general ranges of your size plan.

Look at the combination of experience, skill and cost. You can always find someone who will do an audit inexpensively, but you get what you pay for. The cost of errors can be expensive. A good auditor will bring discrepancies to the attention of the business owners and help them correct those discrepancies.

A firm that doesn’t know as much is much less likely to identify the problem and then be able to help the company through the correction process. <<

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