CLARK SCHAEFER HACKETT
BUSINESS ADVISORS

THE TOP 10 ISSUES

Found in Retirement Plan Audits by Regulators

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To avoid financial penalties, compliance corrections and additional time, fiduciaries of retirement plans should consider whether these common issues might impact their plan and take these preventative steps to avoid some of the most common errors found in plan audits by regulators.

Common Issue #1
Failure to Follow the Plan's Definition of Eligible Compensation

Following the definition of eligible compensation is essential for employee and employer contributions to be calculated accurately. With numerous payroll systems and pay codes, it's easy for something to get programmed incorrectly, resulting in improper calculations or limits within the system. This leads to one of the most common problems: misinterpretation of which type of earnings are included or excluded from eligible compensation.

Preventative Steps:

- Plan documents should be very specific about which pay codes are included in eligible compensation and leave nothing to interpretation. If your plan document is unclear, consider amending your plan.
- Plan management and employees responsible for payroll functions should review calculations of eligible compensation and periodically spot-check calculations for accuracy. Any new payroll codes should be reviewed against the provisions of the plan document prior to being used. If there are discrepancies, corrective distributions or contributions may be needed.

Common Issue #2
Delinquent Remittance of Employee Contributions to the Plan

All participant contributions must be remitted to the plan on the earliest date on which they can reasonably be segregated from the company's general assets. In no case can this be later than the 15th business day following the end of the month in which amounts are contributed by employees or withheld from their wages. However, the key consideration is the earliest date that the assets can be reasonably segregated. Once a plan sponsor demonstrates the ability to remit employee deferrals in, for example, three business days, this is the standard which the plan sponsor will be held for all pay periods. In this example, any remittance taking longer than three business days can be considered a late remittance, which will require the plan sponsor to calculate and remit a payment to the plan for lost earnings.

Late payroll deposits are one of the most common Department of Labor audit findings. Even when a plan uses a payroll provider that automatically remits employee contributions to the custodian, late remittances can still arise. Situations such as when an employee responsible for depositing contributions is on vacation (with no backup in place) or when there is a manual payroll run are two of the most common situations.

Preventative Steps:

- Consider your processes and determine the earliest date employee contributions can be segregated and remitted following each payroll cycle.
- Make deposits consistently throughout the year and make sure you have monitoring controls in place to ensure remittances are made according to an established schedule.
- If you do make a late remittance, consider entering the DOL's Voluntary Fiduciary Correction Program, which allows you to calculate lost earnings on the late contributions and make corrective contributions without penalty.
- If a remittance is made later than a plan typically would, but it is not determined to be late, the plan administrator should document the circumstances that accounted for the longer remittance period.
- Ensure a backup employee is trained to remit contributions to the plan. This is particularly important in the case the primary employee with payroll responsibilities takes a vacation or is otherwise unavailable.

Common Issue #3
Lack of Plan Oversight Committee and Meeting Minutes

Every retirement plan should establish an oversight committee that meets regularly to review plan activity. Minutes of the committee's meetings are key documentation to support the committee is performing its fiduciary duty to the plan.

Preventative Steps:

- Establish a plan committee for general oversight, designate an employee as plan administrator to take care of the day-to-day plan operations and ensure fiduciary education is provided regularly.
- Meet at least annually and document individuals attending the meeting.
- Assign responsibility of recording minutes to a specific person.
- Document significant decisions made at each meeting regarding the plan, including:
  - Selection of the plan's trustee, custodian, investment advisors, and other service providers
  - Approval of plan amendments
  - Approval of all discretionary employer contributions (match, profit sharing, etc.)
  - Changes in plan administration policies
  - Review of investment performance (further discussed under Common Issue #4)

Common Issue #4
Failure to Monitor and Review Plan Fees and Investments

Part of a retirement plan sponsor's fiduciary duty is to make sure the services provided to the plan are necessary and the fees paid for those services are reasonable. It's important to remember that reasonable does not mean least expensive. Plan sponsors also have a fiduciary responsibility to review and ensure that investments are diversified.

Preventative Steps:

- Develop an effective governance framework to assess plan investment, administrative, and professional fees.
- Review service agreements to verify fees charged are allowable and follow the terms of the agreement.
- Document how to benchmark fees against other options.
- Document the decision-making process for why a particular investment class was selected versus other options that might have lower fees.
- Ensure participants are receiving the required investment and fee disclosures.
- Establish an investment policy that includes:
  - Identification of the body responsible for investment monitoring
  - Investment options available to participants
  - Specific procedures used to monitor the performance of funds
  - Criteria used to evaluate fund performance
  - Schedule a review of your plan's investment options at least annually and document this evaluation

Common Issue #5
Nondiscrimination Testing Failures

Nondiscrimination testing is one of the most critical aspects of plan administration for sponsors. Maintaining a tax-qualified plan provides significant tax advantages to both the plan sponsor and the plan participants. Failure to comply with the nondiscrimination testing requirements may jeopardize the tax-qualified status of the plan, lead to IRS penalties, or result in missed tax deductions.

Preventative Steps:

- Verify the accuracy of the employee census data used to perform the nondiscrimination testing, including looking for employees listed with zero compensation or employees on the census who have deferral amounts greater than plan limits.
- Conduct plan testing throughout the year to avoid surprises.
- Review the test results in detail with your service provider to verify pass/fail status and ensure corrective distributions or contributions happen before the IRS deadline.

Common Issue #6
Failure to Use or Allocate Forfeitures

If an employee is not fully vested upon termination, employer contributions are forfeited based on plan rules. The Internal Revenue Service requires that forfeitures be used in the plan year in which the forfeitures occur. Most plan documents provide for this account to be used to pay plan expenses or reduce future employer contributors. In some cases, they may also be reallocated to plan participants.

Preventative Steps:

- Refer to your plan document regarding how the forfeitures should be used.
- Ensure the balance in the forfeiture account is reduced to zero at least once during the plan year.

Common Issue #7
Insufficient Cybersecurity Controls

Cybersecurity is a fiduciary obligation and plan fiduciaries should take reasonable and appropriate steps to protect their retirement plans from cybersecurity breaches. Plan sponsors should also consider their service provider's use of sensitive personnel information, such as Social Security numbers, date of birth, home address, salary, passwords and general payroll information.

Preventative Steps:

- Establish a formal cybersecurity program.
- Consider controls over data not only on the company's network, but also for every service provider that receives data related to the plan or payroll. This includes obtaining an understanding of the security for data transmissions, how data is stored and how data is protected at each service provider.
- Conduct periodic cybersecurity awareness training (at least annually).
- Educate participants on the importance of online security.
- Obtain cyberliability insurance coverage, which can help offset some of the significant costs associated with a data breach.

Common Issue #8
Lack of Review of the SOC 1 Reports for Service Providers

Most retirement plan sponsors outsource their plan operations and payroll functions to third-party administrators and service providers. Given the significance of these operations to the plan, plan management should obtain a System and Organization Controls 1 Report from the plan's recordkeeper and payroll provider. These reports document internal controls over financial reporting as well as results of tests of control for operating effectiveness. As the internal controls of the service organizations become an extension of the plan's controls, plan management should review the key components of the SOC 1 report and implement effective internal controls over outsourced functions.

Preventative Steps:

- Obtain and review SOC 1 reports annually to ensure there are no problems with internal controls that may affect the plan.
- Document the review of the SOC 1 reports in meeting minutes, including how management responded to any issues the SOC 1 report noted.
- Make inquires with third-party administrators and service providers regarding their cybersecurity policies.

Common Issue #9
Failure to Update Contribution Limits

Elective deferral contributions are subject to an IRS limit each calendar year. Plan participants age 50 and older may also make catch-up contributions, subject to a separate, annual IRS limit. These dollar limits are moving targets, as they are subject to annual adjustment by the IRS based on changes in the cost of living.

Preventative Steps:

- Review the payroll system annually to ensure that caps have been implemented and updated for the IRS limit.
- Communicate IRS limits annually to the payroll administrator.
- Establish protocols that trigger an alert when a participant exceeds the annual contribution amount.

Common Issue #10
Lack of an ERISA Fidelity Bond

Most qualified retirement plans require a fidelity bond. The purpose of a fidelity bond is to protect a plan against losses resulting from acts of fraud or dishonesty by plan fiduciaries and others who oversee plan funds. Typically, the bond needs to be at least 10% of the value of the plan assets, with a maximum of $500,000, or $1 million if a plan contains employer securities.

Preventative Steps:

- Make sure you have a copy of your ERISA fidelity bond and fiduciary insurance policy.
- Review the ERISA fidelity bond annually to ensure compliance.

By adopting these preventative steps and committing to regular plan checkups, an employer can comply with current regulations, optimize plan benefits for employees, and avoid unnecessary time and expense.

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