Accounting for Success

The Five W's of a 401(k) Plan Audit

by
Stacey I. Snyder, CPA, QKA, TGPC
Supervisor - Retirement Plan Audit Services
Belfint Lyons & Shuman, P.A.

"The purpose of a 401(k) plan audit is to verify the plan is operating in compliance with applicable rules and regulations, and in accordance with the provisions of the plan document."

If your client has been informed that their 401(k) plan needs an audit, they probably have many questions if they have never been through a 401(k) audit. Hopefully by answering the five W's (Who? What? When? Where? Why?), we'll cover most of their questions.

WHO? - Who Audits a 401(k) Plan?

The audit of a 401(k) plan must be performed by an independent qualified public accountant. While any independent CPA firm can perform the audit, it is important to evaluate a firm's qualifications. Audits of 401(k) plans differ from financial statement audits since they require specialized knowledge of the applicable rules and regulations related to 401(k) plans that tie into the required audit procedures. Hiring a firm that lacks the appropriate knowledge could result in a deficient audit and create unexpected costs and inconveniences if the Department of Labor (DOL) requires the plan be re-audited.

WHAT? - What is Audited?

The purpose of a 401(k) plan audit is to verify the plan is operating in compliance with applicable rules and regulations, and in accordance with the provisions of the plan document. Therefore, the auditor will need a copy of the plan document and any related amendments to determine which provisions have been adopted by the plan, and the applicable testing procedures to apply to each provision. Generally, the following plan provisions are tested:

- Investments - Unless a limited scope audit is requested, testing of the fair market values as of the last day of the plan year and earnings and transactions during the year will be performed.
- Loans - Testing is performed to verify loans were issued in accordance with plan provisions and applicable regulatory limits.
- Employee Contributions - Testing is performed to verify timeliness of deposits, that participant elections are followed, and that amounts withheld from participants' pay are deposited completely into the plan.
- Employer Contributions - Testing is performed to verify contributions are allocated in accordance with the formula defined by the plan and do not exceed regulatory limits.
- Distributions - Testing is performed to verify eligibility of the distributions, that the amounts distributed are not in excess of plan provisions, that forfeited amounts are determined in accordance with plan provisions, and that distributions were made in accordance with participant elections.
- Rollover Contributions - Testing is performed to ensure the contribution was received from an eligible source and in accordance with the plan document, and that the amount received was deposited into the participant's account completely and in accordance with participant elections.

To complete all the required testing, the auditor will need a variety of reports and supporting documents. The plan's recordkeeper provides an audit package containing a majority of the necessary reports. Payroll reports, personnel file information, and any requests not submitted to the recordkeeper will have to be provided by the plan sponsor.

In addition, if the plan was previously a small plan not subject to the audit requirement, beginning balance testing will also be required. To complete beginning balance testing, the auditor will need historical data for as many years as possible, possibly from inception of the plan.

WHEN? - When is the Audit Due?

Since the audit is required to be attached to the plan's Form 5500, the audit is due by the filing deadline of the Form 5500. The Form 5500 is due the last day of the seventh month following the plan's year end, with an optional two-and-a-half-month extension. For a plan with a December 31 year end, the deadline is July 31 of the following year, or October 15 if an extension is filed.

WHERE? - Where is the Audit Performed?

Audits of 401(k) plans can often be performed remotely. Since reports from the recordkeeper and third-party administrator are already in electronic format, they are provided to the auditor electronically. Any information needed from the plan sponsor may be sent electronically or collected in person.

WHY? - Why Does the Plan Need an Audit?

Plans that have 100 or more eligible participants at the beginning of the plan year are required to undergo audits annually. However, an exception to the requirement is the 80-120 rule. In short, if the plan was previously a small plan (fewer than 100 participants at the beginning of a prior plan year), an audit is not required until the plan reaches 120 participants on the first day of a plan year.