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IRS Provides Trends, Tips, Internal Control Questionnaire and Plan Documentation Guide Online

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The Internal Revenue Service (IRS) has recently added important guidance to its Employee Plan Team Audit (EPTA) website that is very helpful to retirement plan sponsors and retirement plan administrators. First, the IRS has released an internal controls questionnaire to assist a plan sponsor in making sure its retirement plans operate in accordance with the plan terms and the Internal Revenue Code (the “Code”). Second, the IRS has released information regarding EPTA trends and tips revealed from audits of large retirement plans. Third, the IRS now provides a tool that assists employers with the documentation needed for an exam by type of plan, including defined contribution and defined benefit plans. This article summarizes the important features of these IRS materials.

Internal Controls Questionnaire

The just released internal controls questionnaire is a tool intended to assist plan sponsors in operating their retirement plans in accordance with the governing plan documents. It is also intended for use by IRS examiners during retirement plan audits. Since the examiners generally cannot review a plan sponsor’s self-audits due in part to attorney/client privilege, the questionnaire assists the examiner on the operation of a plan. The questionnaire is broken up into four topics: Human Resources (HR) personnel; payroll; plan failures; and plan administration.

HR Personnel

The purpose of this questionnaire is to provide the examiner with an understanding of the communications between HR personnel and the plan administrator, as well as the recordkeeping system used by the plan sponsor. This particular questionnaire addresses the HR structure, employment arrangements (including the use of contract employees), rehire issues, change in employee status issues, and data gathering tools. This material should also be valuable in helping a plan sponsor develop a good understanding of the role HR personnel plays in the process with respect to all aspects of a retirement plan.

Payroll

The purpose of this questionnaire is to provide the examiner insight as to how payroll is handled and communicated to the plan administrator and whether the plan sponsor is able to ensure that the data is communicated correctly to the plan administrator. The payroll questionnaire contains 27 questions, many with multiple subquestions. In particular, examiners review the types of payroll services used, the medium for payroll transfers, record retention issues, and payroll control issues. Inconsistent and sloppy payroll practices will lead to further inquiries and possible sanctions if the payroll contributed to the plans at issue cannot be reconciled properly. A plan sponsor's review of this questionnaire should be helpful in its efforts to strengthen any weaknesses in its payroll procedures.

Plan Failures

This questionnaire involves the review of plan operational or plan form failures to determine whether the plan sponsor made adequate corrections and changed its procedures so that errors are less likely to occur. Examiners review whether the self corrections sponsors make to their plans follow the procedures outlined under the Employee Plans Compliance Resolution System (EPCRS) (as set out in Rev. Proc. 2008-50). Based on the questions set out in the questionnaire, plan sponsors should prepare self-correction memoranda that follow the correction guidance for determining whether errors were self correctable and state the methods for the correction. If the examiner determines that the errors are not self correctable, costly penalties may be imposed. Self audits can, if handled properly, be performed under attorney-client privilege. This enables the plan sponsor to take steps to correct problems, and, as a result, be in a far better position in the event of a subsequent examination.

Plan Administration

The purpose of the Plan Administration questionnaire is to allow examiners to understand the processes in place between the plan sponsor and its service providers. Many plan administrative functions are outsourced to third-party vendors. The examiner will review all plan administrative functions to ensure that they are being handled adequately and that nothing is falling through the cracks due to the outsourcing. In addition to the normal plan documentation, examiners review service provider contracts, including record keeper, trustee, custodian, actuary, and consultant contracts. The IRS is keenly aware that most retirement plans are being serviced by many parties even though the plan sponsor is responsible for the ultimate plan administration.

Based on the exhaustive list of exam questions, plan sponsors should review all vendor contracts to identify what services are being provided, to confirm that no administrative duties are lacking, and to ensure that all features of the plan are being monitored on a timely basis.

Tips and Trends on Retirement Plan Compliance

The IRS EPTA Program website contains numerous examples of plan errors found in examinations of large plans and in voluntary submissions. This material also provides guidance regarding appropriate solutions for such errors.

The site categorizes the trends by plan types, including 401(k) plans, defined benefit plans, multiemployer plans, 403(b) plans, 457 plans, and other governmental plans. The site also has a category for common errors across all plan types. Moreover, the site links sponsors to a taxpayer documentation guide, videos from the IRS about their mission, and checklists that assist in finding, fixing, and avoiding plan errors. The Tips and Trends site is extremely useful for assisting plan sponsors with all types of plan compliance issues.

Taxpayer Documentation Guide

The Taxpayer Documentation Guide was developed by EPTA agents and outside practitioners to provide a comprehensive list of documents needed for a full and proper examination of issues identified for an audit. The guide also helps plan sponsors determine the nature and scope of documentation and other information that should be maintained and readily available in the event a plan is subject to an IRS examination. There are separate guides for defined contribution and defined benefit plans, each of which covers the life cycle

of the plans from plan formation to termination. The guide cannot be construed as official guidance, however, and is valid only for plan years 2003 through 2005. EPTA is currently updating this guide for later years.

Record retention is also a significant concern for EPTA. As highlighted in the guide, ERISA requires employers to retain records sufficient to determine benefits that are due or that may become due. Records of transactions for retirement plans may cover a significant amount of time. The IRS cautions that records of retirement plans should be retained until all benefits have been paid, the trust has been liquidated, and a sufficient amount of time has passed such that the plan will not be the subject of an audit.

Plan sponsors should review all of their vendors' record retention policies to make certain records are kept for the life of the plan, plus seven years. If a plan sponsor changes service providers, the plan sponsor must make sure the new provider takes over the prior records or the former provider maintains the records to comply with ERISA.

The IRS website also describes the requirement for record retention in an electronic media. The IRS reminds plan sponsors that it is their responsibility to work with vendors to satisfy the IRS record retention requirements, and that the IRS is able to issue a Notice of Inadequate Records and/or pursue other available legal remedies.

What Plan Sponsors Should Do Now

With the publication of this guidance, the IRS has facilitated self-audits of plans by employers. It is recommended that a self-audit be performed at least annually. Regular self-audits should enable plan sponsors to demonstrate compliance with applicable ERISA and tax requirements more easily. A self-audit is generally performed using a mix of internal and external resources. A plan self-audit may be structured so that results are attorney/client privileged communications. Littler is available to draft self-audit procedures that can help you accomplish this goal. Littler develops procedures based on the specific provisions of your plan document action, the applicable requirements under the Internal Revenue Code of 1986 (as amended), and ERISA, and available IRS and DOL guidance.

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Melissa B. Kurtzman is a Shareholder in Littler's Philadelphia office. For additional information about how Littler can assist you in the operation of your tax-qualified retirement plans, or for any other employee benefits concerns, please contact a member of Littler's Employee Benefits and Executive Compensation Practice Group. If you would like further information, please contact your Littler attorney at 1.888.Littler, info@littler.com or Ms. Kurtzman at mkurtzman@littler.com.