Acquire the Knowledge to Achieve Your Goals

Employee Benefits Conference

May 26, 2011 • Orlando

HCPA

Best speakers and topics to keep you up-to-date and help you thrive.

Employee Benefit Plans Conference
Thursday, May 26, 2011
Orlando

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7:30-8:20 a.m.	**Registration and Continental Breakfast**
8:20-8:30 a.m.	**Introduction and Opening Remarks**
8:30-9:20 a.m.	**Department of Labor Update** .....1 Ian Dingwall, CPA Chief Accountant / U.S. Department of Labor Washington, D.C.
9:20-10:10 a.m.	**IRS Update on Employee Benefit Plans** ....21 **Loretta G. Dollar** EP Manager, Gulf Coast Area / Internal Revenue Service Dallas, TX
10:10-10:25 a.m.	**Break**
10:25-11:15 a.m.	**Guidance on Deferred Compensation: 409A & 457** .....33 Marcia S. Wagner, Esq. Founder and President / The Wagner Law Group Boston, MA
11:15 a.m. – 12:05 p.m.	**Accounting & Auditing Update Including Guide Updates** .....52 Marilee Pierotti Lau, CPA EBP Audit and Accounting Consulting & Retired Partner KPMG LLP Kentfield, CA
12:05-1:05 p.m.	**Lunch**
1:05-1:55 p.m.	**Breakout 1: Form 5500 Issues**.....81 Richard A. Cristini CPA Partner / Davidson, Jamieson & Cristini, P.L. Dunedin
	Breakout 2: 403(b) Plans: Surveying the Wreckage.....97 Ian Dingwall, CPA Chief Accountant / U.S. Department of Labor Washington, D.C. and Marilee Pierotti Lau, CPA EBP Audit and Accounting Consulting & Retired Partner KPMG LLP Kentfield, CA

2:00-2:50 p.m.	**Breakout 3: Identifying and Addressing Audit Risks.....113** Diane M. Walker Partner / Johnson Lambert & Co. LLP Reston, VA
	Breakout 4: Investments and Fair Value .....133 Tricia Van Vliet, CPA Director, National Assurance-Aduite of Employee Benefit Plans / BDO Comstock, MI
2:50-3:05 p.m.	**Break**
3:05-3:55 p.m.	**Employee Benefit Plans Audit Quality Center Update.....161** Ian A. MacKay, CPA Director-Federal Regulatory Affairs / AICPA Washington, DC
4:00-4:50 p.m.	**Most Often Asked Question of a Plan Audit Tax Specialist .....172** Carlette Prince, Esq. Tax Senior Manager-Compensation & Benefits / Deloitte Tax, LLP Atlanta

U. S. Department of Labor Update

Ian Dingwall, CPA

Ian Dingwall, CPA

Chief Accountant
Office of the Chief Accountant
Employee Benefits Security Administration
U.S. Department of Labor

Mr. Dingwall assumed the position of the Employee Benefits Security Administration's (EBSA) (formerly the Pension and Welfare Benefits Administration) first chief accountant on July 1, 1988. He serves as EBSA's primary adviser on accounting and auditing issues stemming from EBSA's responsibilities under the Employee Retirement Security Act (ERISA) and the Federal Employee Retirement Security Act (FERSA). Mr. Dingwall was instrumental in developing and implementing the agency's fiduciary audit plan for carrying out its responsibilities for the multi-billion dollar Federal Thrift Savings Plan. In 1984 Mr. Dingwall held the position of treasurer for Jack Kent, Inc. in Middleburg, Virginia. Previously, Mr. Dingwall was a supervisory auditor in the Special Litigation Division of the Office of the Solicitor, where he provided expert advice on accounting and auditing matters involving litigation of employee benefit plan cases. Mr. Dingwall performed the functions of chief accountant to the Enforcement Division of the Federal Energy Regulatory Commission from 1980 to 1982. From 1974 to 1980, he was a senior accountant in the Division of Enforcement at the Securities and Exchange Commission, where he developed numerous cases involving accounting principles and auditing standards. From 1969 to 1974 he was with the accounting firm of Ernst & Young, where he conducted financial audits and performed related tax services for clients. Mr. Dingwall, a graduate of the University of Maryland, is a certified public accountant in Maryland and a member of the American Institute of Certified Public Accountants and the Greater Washington Area Institute of CPAs.

Mr. Dingwall was appointed to the AICPA's first prestigious "Group of 100" to help shape the future role of the CPA profession. Mr. Dingwall received a "Hammer" award from Vice President Gore for helping to "build a government that works better and costs less" and was listed as one of the"1997 Top 100 Most Influential People in Accounting" by the editors of Accounting Today.

Mr. Dingwall is the recipient of the AICPA's 2007 Outstanding CPA in Federal Government Award for his contributions to increased efficiency and effectiveness of government organizations and to the growth and enhancement of the profession. Mr. Dingwall presently serves as an observer "with privileges of the floor" to the Public Company Accounting Oversight Board's Standing Advisory Group.

Department of Labor Update

Ian Dingwall, CPA
Chief Accountant
Employee Benefits Security Administration

The views expressed are those of the speakers and do not necessarily represent the official position of the Department

Overview

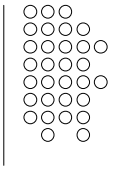
- Regulatory Update
- EFAST2 Update
- Audit Quality Update
- Reporting Compliance Initiatives

Regulatory Update

Informed Decision Making and Excessive Fees – The Three Legged Stool

- Disclosures by plans to participants of certain plan and investment-related information – Interim Final 10/20/10
- Disclosures to plan fiduciaries to assist in assessing 408(b)(2) reasonableness of compensation and potential conflicts of interest – Interim Final 7/16/10
- Disclosures to public and government on electronically filed Form 5500 Annual Report including indirect compensation – Form 5500, Schedule C

Final Regulation to Improve Transparency of Fees and Expenses to Participants

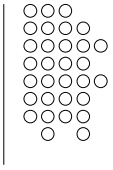


- Published on October 20, 2010

Requires fiduciaries to:

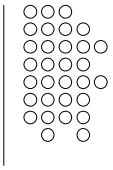
- Give workers quarterly statements of plan fees & expenses deducted from their accounts
- Give workers core information about investments available under the plan
- Use standardized methodologies when calculating and disclosing expense and return information

Final Regulation to Improve Transparency of Fees and Expenses to Participants - continued



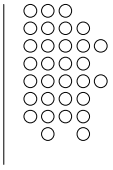
- Centerpiece – a requirement to provide investment-related advice in a format that permits workers to comparison shop among investment options
- DOL has developed a model chart for complying with this requirement
- The reg., model chart, and fact sheet may be viewed at www.dol.gov/ebsa

Disclosure Rules under 408(b)(2)



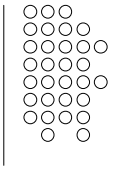
- Brings new transparency to the process of selecting and monitoring of plan service providers
- Establishes comprehensive disclosures from service providers concerning services, fees, and potential conflicts of interest
- Applies to plan contracts or arrangements for services in existence on or after 1/1/12, extended from 7/16/11

408(b)(2) Disclosure Rules – Service Providers Covered



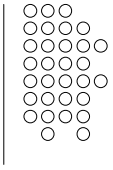
- A service provider who provides any service to a plan as a fiduciary under section 3(21) of ERISA or under the Investment Advisors Act of 1940.
- A service provider who provides banking, consulting, custodial, insurance, investment advisory (plan or participants), investment management, recordkeeping, securities or other investment brokerage or third party administration; or
- A service provider who receives or may receive indirect compensation or fees for the following services: accounting, actuarial, appraisal, auditing, legal, or valuation.

408(b)(2) – Required Disclosures



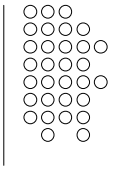
- Service providers are required to disclose (before the parties enter into an agreement for services):
  - All services to be provided under the agreement
  - The compensation or fees to be received for each service
  - The manner of receipt of compensation or fees
  - Information about conflicts of interest.
- Establishes disclosure burden on service provider – integrated with 2009 Form 5500 Schedule C Reporting

Clarification of the Meaning of "*reasonable arrangement*" in 408(b)(2) Disclosure Rules



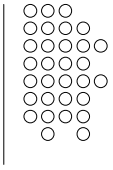
- All service agreements be in writing (no prescribed format)
- Impose new service provider disclosure obligations before or at the time the plan enters a service agreement

Consequences of Non Disclosure = Prohibited Transaction



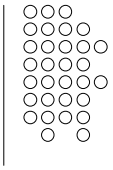
- Contract or arrangement will not be "reasonable" and violates 408 (b) (2)
- Responsible Plan Fiduciary violates 406 (a) (1) (c) by participating in the prohibited transaction
- Service provider is a "disqualified person" under IRS prohibited transaction rules and subject to excise taxes under Code section 4975

Participant Contributions



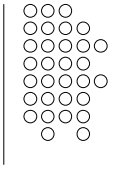
- Federal Register Notice – January 2010
- Applies to plans with fewer than 100 participants at the beginning of the plan year
- Employee contributions considered timely, if deposited within 7 business days

Definition of Fiduciary Project



- Proposed rule published in the Federal Register – October 22, 2010
- Would more broadly define "fiduciary" when a person provides **investment advice, including appraisal or fairness opinions**
- Potential conflicts arise from today's diverse and complex fee practices
- The proposed regulation may be viewed at: www.dol.gov/ebsa.

Final Civil Penalty Rules Under 502(c)(4)



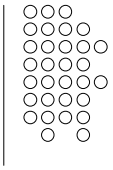
- Final regulation published in Federal Register in January 2009
- Penalties against plan administrators who fail to disclose required information
- PPA disclosures include:
  - Funding limits on benefit accruals
  - Actuarial and financial reports
  - Withdrawal liability amounts (also a FASB project)
- Penalty amount of up to $1,000, per day for failure to meet the disclosure requirements

Annual Funding Notice for DB Plans – Proposed Rule

- Published in Federal Register on 11/18/10
- Applies to all DB plans subject to Title IV
- Annual Funding Notice to PBGC, Ps & Bs, labor organizations representing Ps & Bs, and contributing employers in multi-employer plans
- Previously, only impacted multi-employer plans
- Impacts over 29,000 plans covering 44 million Ps & Bs

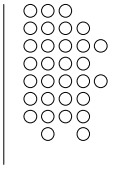
EFAST2 Update

#1 Filing Error: Invalid Electronic Signature



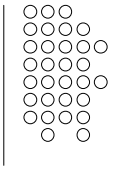
- STOP I-104 Message: *A valid Plan Sponsor's UserID and PIN or Administrator's UserID and PIN must be provided.*
- Avoid this by:
  - Providing a Plan Administrator, not just Plan Sponsor, electronic signature.
  - Verifying the signer has an EFAST2 password. The password ensures they completed EFAST2 registration.
  - Verifying the signer has "Filing Signer" user role checked in their profile.
  - Verifying the signer is using their EFAST2-assigned PIN when signing.

Amending Filings



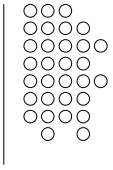
- Amended filings must be electronically filed using EFAST2
- Use most current form available
  - Exception: Schedules B, E, R, P, and T
- See further guidance at the DOL website: www.efast.dol.gov

Do Not Attach SSA Data



- Schedule SSA should not be attached to any e-filing
  - Mail delinquent Schedule SSA to:
    Department of the Treasury
    Internal Revenue Service Center
    Ogden, UT 84201-0024
- Form 8955-SSA replaces Schedule SSA after 2008 plan years

Form 8955-SSA



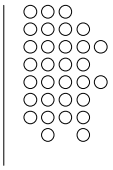
- Replaces Schedule SSA to the Form 5500
- Used to satisfy the reporting requirements of Section 6057(a) of the Internal Revenue Code for plan years beginning on or after January 1, 2009
- The due date for filing the Form 8955-SSA for the 2009 and the 2010 plan years is the later of (1) the due date that generally applies for filing the Form 8955-SSA for the 2010 plan year, and (2) August 1, 2011years.

How to Get Help

- EFAST2 Website www.efast.dol.gov
  - FAQ
  - User Guides
  - Most Common Errors
- EFAST2 Help Desk
  - Call 1.866.GO-EFAST (1.866.463.3278). Live assistance 8am-8pm (Eastern) excluding weekends and holidays
  - Phone lines most busy 11am-3pm (Eastern)
  - Send email to efast2@dol.gov
- Software providers

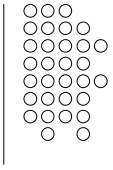
Audit Quality Update

Audit Universe
(2008 Form 5500 Database)



- Approximately 9,500 CPA firms
- Over 77,000 plan audits
- $3.9T in plan assets audited
- Limited Scope Audits 64%

Audit Universe
(2008 Form 5500 Database)



- 30 CPA firms
  - Perform 25% of the audits (19,600 audits)
  - Audit 61% of plan assets under audit
- 9,000 CPA firms
  - Perform 39% of the audits (30,000 audits)
  - Audit 22% of plan assets under audit
  - Approximately 4,400 CPA firms perform one plan audit

Deficient Audits by Strata

	50-99 Audits (17%)	25-49 Audits (21%)	24 or less Audits (36%)
Deficiencies			
1	39%	46%	30%
2	28%	30%	24%
3	17%	12%	15%
4	11%	6%	10%
5+	5%	6%	20%

Deficient Audits
Single vs. Multi-employer

	Single Employer	Multi-employer
Deficiencies	32%	36%
1	34%	20%
2	24%	22%
3	14%	20%
4	10%	12%
5+	17%	27%

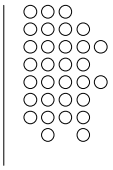
Deficient Audits
Type of Plan

Type of Plan	Single Employer	Multi-employer
DB	26%	41%
DC	33%	31%
HW	35%	37%

Audit Universe
(2008 Form 5500 Database)

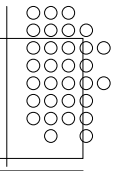
- Enforcement Focus
  - CPA firms performing the most audits
  - CPA firms performing fewer audits
  - Multi-employer plan audits
  - ESOP audits
  - Health and welfare plan audits

Where Are the Deficiencies?



- 71% = Participant Data
- 55% = Contributions
- 52% = Investments
- 37% = Benefit Payments
- 34% = Plan Obligations
- 30% = Party-In-Interest Transactions
- 23% = Planning

EBP Audit Best Practices



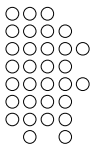
- Commitment to Quality
  - Executive Level
  - Firm-wide
- Importance of EBP Audit Practice
  - Focal point within firm
  - Realistic audit fees
  - Comprehensive EBP specific resources
- Internal Inspection Programs
- Use of Internal Experts

Reporting Compliance Initiatives

Reporting Compliance Initiatives

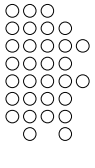
- Stop Filer Program
- Late Filer Program
- Filings with Missing & Invalid Signatures
- Filings with Missing IQPA Reports
- Filings with Missing Schedule C and Schedule C Data

Reporting Compliance Initiatives

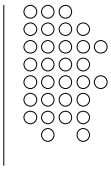


- 403(b) Plan Filings
- Form 5500-SF Eligibility
- Small Plan Audit Waiver Eligibility
- Black-Out Notice Rules
- PPA Funding Certification Requirements

DFVC Program Update



- Still available under EFAST2
- Use of online calculator and electronic payment option encouraged
- New mailing address:
  - DFVC Program – DOL
    P.O. Box 71361
    Philadelphia, PA 19176-1361
- Use of private delivery service no longer permitted



Questions?

IRS Update on Employee Benefit Plans

Loretta G. Dollar

Loretta G. Dollar

EP Manager, Gulf Coast Area

Internal Revenue Service

Loretta Dollar has been an employee of Employee Plans (EP) of the Tax Exempt and Government Entities Division of the Internal Revenue Service for more than 20 years. She is a graduate of Texas Christian University with a BBA in Accounting. Since joining the IRS, Loretta's duties within TE/GE have varied from reviewing determination applications, examining retirement plans, working in Quality Review Section, teaching assignments within the IRS, public speaking assignments outside of the IRS, and as a manager in EP. She recently completed an assignment as lead instructor for new Employee Plans employees in the Gulf Coast area. Loretta is currently manager of EP group 7649 in the Gulf Coast Area.

Loretta Dollar
EP Manager, Gulf Coast Area
1100 Commerce St., MC 4922DAL
Dallas, TX 75242
214-413-5510
Loretta.g.dollar@irs.gov

Retirement Plan Updates

Loretta Dollar
Loretta.G.Dollar@irs.gov

Mistakes Happen

- Numerous rules
- Complexity
- Frequent law changes
- I thought ‘they’ were doing that

Employee Plans Workplan

- Emerging/Abusive Issues
- International Issues
- Governmental Plans
- EPCU Expanded Contacts
- Practitioner Partnering

Audit vs. Compliance Check

- **Revenue Agent** visit
- Determine **tax liability**
- Agent **verifies compliance** in form & operation
- **Inspect** books & records
- **No VCP available** upon notice of audit receipt

- **EPCU** contact
- **NOT** an audit/investigation
- **Verify information** on return filing
- Books/Records **not inspected**
- **Voluntary correction (VCP)** available

EPCU Projects

- 401(k) Compliance Questionnaire
- International Projects
  - Domestic Trusts
  - Foreign Distributions
- Multi-ER Actuarial Certification
- Minimum Funding Deficiency Project
- 403(b) Universal Availability
- SIMPLE Plan Relief Follow-Up
- You must respond to an EPCU contact

EP Examinations

- How plans are selected for an audit
- Current EP Examination Projects
- What if you receive a letter or call from EP Examination
- ***Can I reduce the odds of my plan being selected for audit***

Reduce my Audit Chances?

- Identified problem areas
- What stands out on your Form 5500
- Learn from other's mistakes – Don't wait for an audit
- Practices and procedures in place
- Correction Programs available under EPCRS (Rev. Proc. 2008-50)

Controlled Group

- One business owns at least 80% of another business
- Two or more businesses owned at least 80%
  - By 5 or fewer persons, and
  - Identical interests in any business owned by the group members > 50%
- Affiliated service group

Controlled Group

Who does my plan need to cover?

- Family attribution rules
- Spousal exceptions
- Community property states – really?
- What does this all mean?

Controlled Groups & ASG

- Steps to Take -

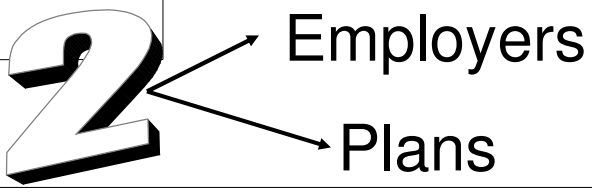
- Questions to ask your clients
- What if you determine a controlled group exists
- When to seek professional help

Maximum Deductible Contributions

(under age 50)

Maximum Contributions			
Compen-sation	SIMPLE IRA	SEP/Profit-Sharing	401(k)
$50,000	$13,000	$12,500	$29,000
100,000	14,500	25,000	41,500
130,000	15,400	32,500	49,000
196,000	17,380	49,000	49,000

www.irs.gov/retirement



- W-2 employee and sole proprietor
  - Unrelated
  - Both have 401(k) plans
  - Can I participate in both plans?
- W-2 employee for unrelated employer, independent contractor for another
  - Participate in employer's 401(k), adopts a SEP for self-employed income
  - How are my contributions limited?

401(k) Plans – Common Errors

- Plan not timely/properly amended (Non-Amender)
- Compensation errors
- Excluding Eligible Employees
- Distributions
  - Plan Loans
  - Hardships

401(k) Plans – Common Errors

- Late Deposits
- Employer Matching Contributions
- ADP and ACP Testing
  - Not completed
  - Not passed
- IRC 402(g) and 415 Limits

Voluntary Correction

- Self-Correction Program (SCP)
  - No IRS contact or fee
  - Practices and Procedures in Place
- Voluntary Correction Program (VCP)
  - IRS approval of correction, $250 fee
- Audit Closing Agreement Program (Audit CAP)
  - Ouch!

Plan Correction Helps

- Fix-it Guides
  - IRA Based Plans
  - 401(k) and 403(b)
- Correcting Plan Errors Webpage
- All can be found at www.irs.gov/ep
- In summary…

Employee Plans Examinations

Fix-It Guides

Now with video!

401(k) SARSEP SEP SIMPLE

---------Trends----------	----------Tips----------			
Potential Mistake	**How to Find the Mistake**	**How to Fix the Mistake**		**How to Avoid the Mistake**
		Corrective Action	**Correction Program(s) Available**	
1) Has your plan document been updated within the past few years to reflect recent law changes? (More)	Review annual cumulative list published close to year-end to see if plan made all required law changes (e.g., Notice 2007-94). (More)	EPCRS Adopt amendments for missed law changes. Appendix D, Part II (More)	VCP Audit CAP (More)	Plan sponsors need to resort to a calendar (tickler) of when amendments must be completed. Review your plan document annually. Maintain regular contact with the company that sold you the plan. (More)

Features Online Comparison Chart

Retirement Plan Assistance

- www.irs.gov/ep
  - Includes pages dedicated to Fix-It Guides and Correcting Plan Errors
- (877) 829-5500
  - Customer Account Services
- RetirementPlanQuestions@irs.gov
- Newsletters

Questions

Loretta.G.Dollar@irs.gov

Guidance on Deferred Compensation: 409A &457

Marcia S. Wagner, Esq.

Marcia S. Wagner, Esq.

Founder

The Wagner Law Group

Marcia S. Wagner is a specialist in pension and employee benefits law, and is the principal of The Wagner Law Group, which she founded 15 years ago. A *summa cum laude* and Phi Beta Kappa graduate of Cornell University and a graduate of Harvard Law School, she has practiced law for over twenty-five years. Ms. Wagner is recognized as an expert in a variety of employee benefits issues and executive compensation matters, including qualified and non-qualified retirement plans, all forms of deferred compensation, and welfare benefit arrangements. Ms. Wagner was appointed to the IRS Tax Exempt & Government Entities Advisory Committee, and ended her three-year term as the Chair of its Employee Plans subcommittee. Ms. Wagner has also been inducted as a Fellow of the American College of Employee Benefits Counsel. For the past four years, 401k Wire has listed Ms. Wagner as one of its 100 Most Influential Persons in the 401(k) industry. Ms. Wagner is widely quoted in such publications as The Wall Street Journal, Financial Times, Pension & Investments, and more, as well as being a frequent guest on FOX Business, CNN, Bloomberg, NBC and other televised media outlets. She resides in Massachusetts with her husband, Craig, and their four wonderful children.

Guidance on Deferred Compensation: IRC 409A and IRC 457

Marcia S. Wagner, Esq.

THE WAGNER LAW GROUP
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Overview of Nonqualified Deferred Compensation

- IRC 409A
  - General Requirements
  - Exclusions From Coverage
- IRC 457
  - 457(f) Plans
  - 457(b) Plans

Qualified Plans v. 409A Plans

Tax-Favored Plans	409A Plans
Discrimination prohibited and benefit limits apply.	Nondiscrimination rules and most limits are n/a.
Minimum standards apply to basic plan features.	ERISA minimum standards do not apply.
Must be funded *(except non-gov. 457(b) plans)*.	Must be unfunded.
Employee not taxed until payment.	Not taxed until payment or "constructive receipt."

NQ Plan Design Practices Prior to Enactment of IRC 409A

- Employee could easily "re-defer" payments.
  - After initial deferral but before payment, employee elects to delay payment again.
- Plan could permit early access to payments.
  - "Haircut" penalty for early payments.
- Plan could help participants avoid loss of benefits when/if employer goes insolvent.
  - Financial triggers accelerate payment before employer enters bankruptcy.

Key Concepts in IRC 409A Rules

- ***American Jobs Protection Act*** adds IRC 409 to federal tax code.
  - Bars employees from accelerating payment.
  - Restricts timing of deferral and re-deferral elections.
- Penalties are severe.
  - Deferred compensation becomes taxable to employee.
  - Subject to additional 20% penalty tax.
  - Premium interest tax may also apply.

IRC 409A Effective Date and Transition Rules

- Effective date was Jan. 1, 2009.
  - Previously, plans had to comply in good faith.
  - 409A plan documents had to be amended to comply by Dec. 31, 2008.
- Grandfathered Plans
  - Plans in effect on Oct. 3, 2004 are exempt from IRC 409A rules.
  - Exemption lost if plan is materially modified.

Deferral Election Rules Under IRC 409A

- General Rule
  - Must make deferral election prior to year compensation is earned.
- Key Exceptions to General Rule
  - New participant may elect to defer within 30 days of becoming eligible.
  - May defer ***annual or long-term*** bonus as late as 6 months prior to end of performance period.
  - May defer ***ad hoc*** bonus if it does not vest for 12 months and election made within 30 days.

Another Exception to 409A Deferral Election Rules

- Excess Plans
  - Excess plans are linked to benefits limit and accruals under tax-qualified plan.
  - Special exception available to new participant in excess plan.
  - New participant may make payment election within first 30 days of 2nd year of participation.
  - All excess plans are ***aggregated*** for purposes of special rule for new participants.

Payment Election Rules Under IRC 409A

- Deferral election must also include payment terms.
  - Employee or plan must specify payment terms.
- Payment must not be earlier than:
  - Separation From Service
  - Disability
  - Death
  - Change of Control
  - Unforeseeable Emergency
  - Fixed Date or Schedule

Other Rules Under IRC 409A

- Anti-Acceleration Rule
  - Employee/plan must specify when deferred compensation will be paid.
  - Thereafter payment cannot be accelerated.
  - Rule examines substance over form.
- Beneficiary Payment Rule
  - Payment election for death benefits must be made when regular payment election is made.
  - Changing identity of beneficiary is permitted.

Other Rules Under IRC 409A *(cont'd)*

- Electing to Change Payment Terms
  - Must be made at least 12 months before first payment.
  - Must postpone first payment at least 5 years.
  - Exemption for electing to change ***annuity*** to another equivalent annuity form.

Coordination of 409A Plan With Qualified Plan

- No Payment Linkage
  - Payments from 409A plan must ***not*** be directly linked to qualified plan payments.
- Amount Linkage
  - 401(k) deferral elections that affect 409A plan deferrals must comply with IRC 409A.
- Funding Restrictions for 409A Plan
  - Funding for top employees restricted when plan is poorly funded or employer is bankrupt
  - Also restricted if underfunded DB plan terminates.

409A Plan Terminations

- Employer can terminate 409A plan without tax penalty if:
  - Unrelated to fiscal downturn.
  - All similar 409A plans terminated.
  - Payments only made between 12 - 24 months after termination.
  - No new 409A plan adopted for 3 years.

Split Dollar Life Insurance

- Generally subject to 409A rules if cash value earned is payable in future year.
  - Deferral election rules are ***not*** applicable if employer pays premiums on non-elective basis.
  - Anti-acceleration rules restricts employee's ability to borrow cash value.

IRS Procedures for Operational Failures

- Eligibility for correction procedures.
  - Failure must be covered by IRS Notice 2008-113.
  - No substantial financial downturn by employer.
  - Other related conditions and limitations.
- Illustration of a correction procedure.
  - Employee elects to defer $20,000 bonus.
  - Operationally, employer improperly pays bonus.
  - Procedures allow employee to quickly repay $20,000 and avoid taxes and 409A penalties.
- Special statements needed for tax returns.

IRS Procedures for Document Failures

- Document failure and IRC 409A.
  - Ordinarily triggers current taxes and 409A penalties on all amounts deferred under plan.
  - IRS relief may be full or partial (*e.g.*, 50% relief).
- Illustration of a correction procedure.
  - Plan pays 10 annual installments at age 65, unless employer pays ***lump sum in its discretion***.
  - Procedures allow plan to be corrected by eliminating employer's lump sum discretion.
  - If employee turns 65 ***within 1 yr of correction***, taxes/penalties only apply to 50% of benefit.

Arrangements Exempt From Coverage By IRC 409A

- IRC 409A broadly covers all types of nonqualified deferred compensation.
  - But 409A reg's provide exemptions for specific types of plans and arrangements.
- 409A exemption for short-term deferrals.
  - Payment must be made within 2 ½ months after tax year.
  - For example, bonus plan for calendar year 2011 pays cash bonuses on March 1, 2012.

409A Exemption for Severance Pay

- "Separation Pay" Exemption
  - Separation must be involuntary, or voluntary for a ***Good Reason***.
  - Permissible benefit amount is lower of:
    - 200% of annual compensation, or
    - 200% of compensation limit for qualified plan.
  - Must be paid by end of 2nd calendar year following year of separation.
- Voluntary separation with ***Good Reason*** must satisfy IRC 409A definition.
  - Other special rules apply to plans that allow voluntary separation with good reason.

409A Exemption for Equity Awards

- Restricted Stock
  - Awards of non-vested employer stock are exempt from IRC 409A.
  - Not taxable so long as award is subject to substantial risk of forfeiture.
- Stock Options
  - ESPP and ISOs are exempt from IRC 409A.
  - Nonstatutory options and SARs are exempt only if granted at FMV exercise price.
  - For terminated employees, option term may be extended (not beyond 10 yrs or original term).

Overview of IRC 457

- Background
  - Governs federal tax treatment of deferred compensation paid by any ***"Eligible Employer."***
- Types of Eligible Employers
  - State and local governmental employers.
  - Tax-exempt organizations.
- Policy Rationale Behind IRC 457
  - Special rules required since Eligible Employers, are not influenced by deduction-based tax rules.

Basic Types of 457 Plans

- 457(b) Plans
  - Referred to as "***Eligible Deferred Comp. Plans***" in IRC 457.
  - Defined to include plans sponsored by Eligible Employers meeting requirements of IRC 457(b).
  - Designed as DC plans.
- 457(f) Plans
  - Broadly includes all other plans sponsored by Eligible Employers.
  - Known as "***Ineligible Deferred Comp. Plans.***"
  - Designed as DC or DB plans.

Scope of 457 Rules

- Plans exempt from IRC 457.
  - Qualified plans, equity plans, secular trusts, gov. excess benefits and retention plans.
  - Plans that do not provide for deferral are also exempt (*e.g.*, vacation, severance, disability).
- Interaction of IRC 457 and IRC 409A
  - 409A rules only apply to 457(f) plans if they provide for deferrals beyond vesting date.
  - IRC 409A does ***not*** apply to 457(b) plans.

Eligibility Rules for 457(f) Plans

- Tax-exempt Organization's 457(f) Plan
  - Must limit participation in 457(f) plan to "***Top Hat***" group of HCEs.
  - Top Hat exclusion allows plan to avoid becoming subject to ERISA funding requirement.
  - Unfavorable tax treatment if 457(f) plan benefits of tax-exempt organization are funded.
- Governmental Employer's 457(f) Plan
  - Special rules exempt governmental plans from ERISA and unfavorable tax rules.
  - No limits on participation in plan.

Rules of Taxation for 457(f) Plans

- Taxation of 457(f) plan benefits.
  - Participants are taxed when benefits are no longer subject to substantial risk of forfeiture.
- Earnings may accumulate on tax-deferred basis after vesting date.
  - Benefits must be ***unfunded*** as provided under Treas. Reg. 1.457-11(a)(1).
- Participants earn benefits on pre-tax basis.
  - Plan may permit pre-tax deferrals or employer contributions.
  - Alternatively, plan may be a DB plan.

409A Deferral Election Rules Applied to 457(f) Plans

- 457(f) plan deferrals are subject to IRC 409A.
  - Generally, election must be made in prior year.
  - New participants may make deferral election within 30 days.
- 409A deferral election rules may (or may not) be applicable to 457(f) plans.
  - IRS Notice 2007-62.
  - Generally, 409A election rules will only apply if plan defers payments beyond vesting date.

How Does 409A Apply to 457(f) Plan?

- IRS Notice states that 409A rules only apply if participants ***defer*** compensation.
  - "***Deferral of Compensation"*** occurs if ***paid*** more than 2 ½ months after end of year it is earned.
  - If benefit is fully paid at vesting, no 409A deferral occurs.
  - If not fully paid at vesting, earnings will grow on tax-deferred basis, and 409A deferral occurs.
- 409A election rules apply when benefits (including earnings) are paid ***after*** vesting.

Past 457(f) Plan Practices

- Plans with ***Rolling Risk of Forfeiture (RRF)***
  - Previously, participants could easily delay vesting at regular intervals to delay taxation.
  - Now, 457(f) plans with RRF feature are viewed as deferred comp. plans under IRC 409A.
  - Thus, RRF feature must now conform to 409A deferral election and payment rules.
- Notice 2007-62
  - IRS will issue 457(f) guidance on "***Substantial Risk of Forfeiture***" to conform to 409A rules.
  - Once issued, RRF feature (even if conformed to 409A) will no longer delay taxes under 457(f).

Funding of 457(f) Plan Benefits

- 457(f) plan benefits must be unfunded.
- May be informally funded with ***rabbi trust***.
  - Assets set aside in a grantor trust.
  - Trust assets remain property of grantor, and trust earnings are taxable to employer.
  - Trust assets remain subject to claims of employer's general creditors.

Distributions from 457(f) Plans

- Alternatives in Plan Design
  - Distribute benefits at or after vesting date.
  - Payment form may be lump sum or installments.
  - Provide for partial lump sum distribution at vesting, sufficient to pay tax withholding due.
- If 457(f) plan provides for ***deferral*** of compensation, 409A payment rules apply.

Introduction to 457(b) Plans

- Governmental 457(b) Plans
  - Governmental employer may include any employees without limitation.
- 457(b) Plans of Tax-exempt Organizations
  - Must limit participation to Top Hat group of HCEs to avoid becoming subject to ERISA.
- Why limit a non-governmental 457(b) plan to Top Hat group only?
  - ERISA requires covered plans to be funded.
  - IRC 457 states that only governmental employers may sponsor funded 457(b) plans.

Contribution Limits for 457(b) Plans

- Deferrals and employer contributions are subject to combined limit of $16,500 (2011).
  - Many plans allow deferrals only.
- Catch-up Limit
  - During 3 years prior to NRA, annual limit is increased by unused limits from prior years.
  - Catch-up Limit may not exceed $33,000 (2011).
- Catch-up Contributions
  - For governmental 457(b) plans only.
  - Participants (age 50+) can contribute higher of Catch-up Limit or Catch-up Contributions.

Vesting and Funding for 457(b) Plans

- Vesting
  - Customarily, deferrals and employer contributions are fully/immediately vested.
  - Amounts are counted against annual limit at vesting, and delayed vesting could violate limit.
- Funding of Benefits
  - Governmental 457(b) plan must be funded through trust.
  - 457(b) plans of tax-exempt organizations must be unfunded (but informal funding is permitted).

Distributions from 457(b) Plan

- Benefits must not be available earlier than
  - Year of attainment of age 70 ½,
  - Severance from employment, and
  - An "***unforeseeable emergency.***"
- Minimum Req. Distributions - IRC 401(a)(9)
- Taxation of 457(b) Plan Benefits
  - If tax-exempt organization, benefits are taxed when distributed or made available.
  - If governmental employer, benefits taxed when actually distributed.

Guidance on Deferred Compensation: IRC 409A and IRC 457

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Accounting & Auditing Update Including Audit Guide Updates

Marilee P. Lau

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Consultant

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Marilee Lau is a founding member and the current Chairperson of the AICPA Employee Benefit Plan Audit Quality Center's Executive Committee which was established in 2004. This committee works closely with the Department of Labor in order to provide appropriate guidance to plan sponsors and their auditors. Marilee is also the chair of the Audit Guide Task Force which updates the accounting and auditing Guide for Audits of Employee Benefit Plans and the Audit Risk Alert.

From 1995-1998 Marilee was the AICPA representative to the ERISA Advisory Council for the Department of Labor in Washington D.C. This Advisory Council provides guidance to the Secretary of Labor on specific issues related to employee benefit plans. She was the Chairperson for the 1998 Council and also was a representative to the President's Saver Summit in 2002. She has served on the AICPA's Employee Benefits Plans Experts Panel and in October, 2007 she concluded her term as the Chair. Marilee is also on the Advisory Board for the Bureau of National Affairs Pension & Benefits Reporter which provides input on various pension issues and is currently serving on the Accountants Committee for the International Foundation of Employee Benefit Plans.

Marilee was KPMG's National Partner in Charge of the Employee Benefit Plan Practice until November 2008 when she transitioned to a consulting role with KPMG dealing with employee benefit plan quality issues related to accounting and auditing of employee benefit plans.

Employee Benefit Plans

…Accounting and Auditing Update

Marilee Lau, CPA
Retired Partner, KPMG
Accounting and Auditing Consultant for Employee Benefit plan audits

Overview

- Industry developments and other "hot topics" affecting employee benefit plans
- New accounting and auditing standards
- Regulatory developments
- Significant issues on the horizon

Employee Benefit Plans Industry Developments – *An Overview*

What happened in 2010?

Economic Issues	Regulatory Changes
Investment performance **Plan amendments** **Continued layoffs** **Going concern and liquidity issues** **Some retirees delaying retirement plans**	**Pension Protection Act** **403(b) Plans** **Form 5500 changes** **Health care reform** **Dodd-Frank Wall Street Reform and Consumer Protection Act** **Defined contribution investment options**

Health Care Legislation

- Affordable Care Act…collectively the…
  - Patient Protection and Affordable Care Act (March 23, 2010)
  - Health Care and Education Reconciliation Act (March 30, 2010)
- Health care reform
  - Medicare Part D federal subsidy deduction
  - Excise tax on high-value health plans ("Cadillac" plans)
  - Many major new requirements
  - Potential impact on the level of benefits offered and contribution rates

Plan design and regulatory changes will likely affect obligation estimates!

Medicare Part D Subsidy

- Subsidy from Federal government for providing retiree prescription drug coverage continues
- Taxable years beginning after December 31, 2012 Medicare Part D subsidy deduction no longer allowed
- Health care reform change

Current Law	New Law
Subsidy not treated as income to employer	**Same as current law**
Employer deducts full cost of prescription drug coverage	**Employer** cannot **deduct portion of cost that is subsidized**

- Consider the effect on accounting for post-employment benefits under ASC 740

Overview of new requirements related to benefit plans

- Currently in effect
  - FSA reimbursements for over-the-counter drugs
- Plan years beginning on or after September 23, 2010
  - Dependent coverage to age 26
  - Pre-existing conditions for children under age 19
  - Lifetime maximum benefits
  - Annual limits
  - Rescissions
  - Annual rebates for fully-insured plans

Overview of new requirements related to benefit plans (continued)

- January 1, 2012
  - Form W-2 reporting on cost of coverage
- January 1, 2013
  - Limit on employee contributions to FSAs
  - Medicare tax increase for certain individuals
- Taxable years beginning after December 31, 2012
  - Medicare Part D subsidy deduction no longer allowed

Overview of new requirements related to benefit plans (continued)

- January 1, 2014
  - Individual mandate and assistance
  - Employer penalties for no coverage or inadequate coverage
  - Free-choice vouchers issued by employers
- Taxable years beginning after December 31, 2017
  - Excise tax on high-cost plans
- Additional requirements apply to plans started or modified significantly after March 23, 2010 (non-grandfathered plans)

Accounting and Auditing Update

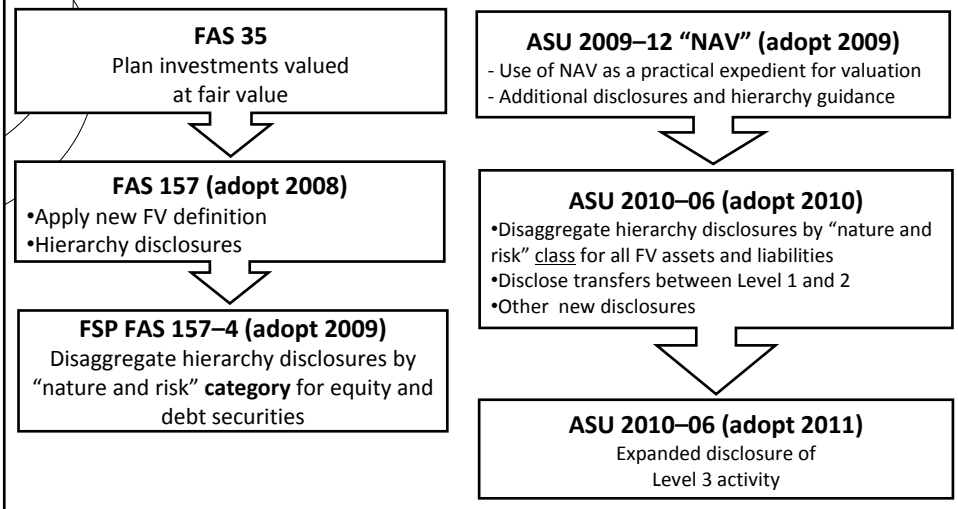
Participant loans: Key provisions of FASB ASU 2010-25

- Effective for fiscal years ending after December 15, 2010 (early adoption permitted)
- Apply retrospectively to all prior periods presented
- All defined contribution plans that allow for participant loans will be affected
- Participant loans are classified as "notes receivable from participants"
  - **No longer considered a plan investment for GAAP purposes, although DOL still considers them an investment**
- Measured at unpaid principal balance plus accrued interest

Participant loans: Implementation of FASB ASU 2010-25

- Segregate participant loans from plan investments on the Statement of Net Assets Available for Benefits and classify them with receivables
- Segregate related interest income from investment income on the Statement of Changes in Net Assets Available for Benefits
- Reclassify participant loans and interest income for prior period presented, if applicable
- Remove participant loans
  - from the fair value hierarchy disclosure
  - from fair value measurements disclosure
- Consider certain disclosures required under ASC 310, *Receivables*
- Continue to include participant loans on the supplemental schedule of assets held at end of year
- Continue to include participant loans in the limited scope disclosure (if applicable)

Plan financial statements
Adoption timeline- fair value measurements



Fair value measurements and disclosures

- FASB ASC 820 amendments
  - FSP 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*
  - FASB ASU 2009-12, *Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*
  - FASB ASU 2010-06, *Improving Disclosures about Fair Value Measurements*

FSP 157- 4: Key provisions

- Clarified objective of fair value measurements even when level of activity has decreased (including guidance on determining when market is not active and when transactions may not be orderly)
- Provided additional guidance on defining major categories, for fair value disclosure purposes, based on nature and risk of securities
- For determining appropriate level of disaggregation for fair value disclosures under ASC 820, examples of factors that may be considered include
  - Shared activity or business sector
  - Vintage
  - Geographic concentration
  - Credit quality
  - Economic characteristic

FASB ASU 2009-12 (ASC 820-10-35)

- Provided additional guidance on measuring fair value of investments in certain entities that calculate NAV per share (or its equivalent)
  - **Use of NAV as a "practical expedient"**
  - **NAV calculated in a manner consistent with FASB ASC 946, Financial Services – Investment Companies**
  - **NAV calculated as of the reporting entity's measurement date**

FASB ASU 2009-12: Disclosures (ASC 820-10-50-6A)

- Enables users of the financial statements to understand the nature and risks of the investments and whether the investments are probable of being sold at amounts different from NAV per share (or its equivalent)
- Disclosures are required for each class of investment (class of investment shall be determined on the basis of the nature and risks of the investments) within the scope of ASU 2009-12 regardless of whether the practical expedient is applied
- Most common applicable disclosures
  - The fair value of the investments, and a description of the significant investment strategies of the investee(s)
  - A general description of the terms and conditions upon which the investor may redeem the investments (e.g., quarterly redemption with 60 days notice)
  - Unfunded commitments

FASB ASU 2009-12: Hierarchy considerations (ASC 820-10-35-58)

Investments measured at NAV per share, as a practical expedient, are still subject to the fair value disclosures requirement of ASC 820 (fair value hierarchy)

Reporting entity's ability to redeem investment	Categorization of fair value measurement of the investment	Example
Entity has the ability to redeem **its investment with the investee at NAV per share (or its equivalent) at the measurement date**	Level 2	**An investment in a hedge fund where initial lockup period has expired**
Entity will **never have the ability to redeem** its investment with the investee at NAV per share (or its equivalent)	Level 3	**An investment in private equity fund**
Entity cannot redeem its investment with the investee at NAV per share (or its equivalent) at the measurement date but the investment **may be redeemable with the investee at a future date**	Reporting entity considers the length of time until the investment will become redeemable; determines whether the fair value measurement of the investment shall be categorized as a **Level 2 or a Level 3**	**Investments subject to a lockup or gate or investments whose redemption period does not coincide with the measurement date**

Slide 18

FASB ASU 2010-06: Key provisions

- Added new fair value disclosure requirements and clarified certain existing disclosures
- Clarifications of existing requirements are effective for all reporting periods beginning after December 15, 2009
  - Fair value disclosures are to be made separately for each "class" of assets and liabilities instead of "major category"
  - Additional guidance regarding the disclosure of valuation techniques and inputs used in estimating the fair value of Level 2 and Level 3 measurements
- New disclosure requirements
  - Information about significant transfers between fair value hierarchy levels (effective for all reporting periods beginning after December 15, 2009)
  - Separate presentation of purchases, sales, issuances and settlements in the reconciliation of recurring Level 3 measurements on a gross basis (effective for fiscal years beginning after December 15, 2010)

FASB ASU 2010-06: Disclosures

- The amounts of significant transfers between Level 1 and Level 2 of the fair value hierarchy and the reasons for the transfers
  - Significant transfers into each level shall be disclosed separately from transfers out of each level
  - A reporting entity shall disclose and consistently follow its policy for determining when transfers between levels are recognized
- Transfers in and/or out of Level 3 and the reasons for those transfers
  - Significant transfers into Level 3 shall be disclosed separately from significant transfers out of Level 3
  - A reporting entity shall disclose and consistently follow its policy for determining when transfers between levels are recognized
- For fair value measurements using Level 2 inputs and Level 3 inputs, disclose a description of the valuation technique used and the inputs used in determining the fair values of each class of assets or liabilities

FASB ASU 2010-06: Level of disaggregation

- Not intended to mean a line item in the statement of net assets
  - Class is often a subset of assets or liabilities within a line item on the statement of net assets
- Affects the level of disaggregation in all fair value disclosures, including the additional disclosures in ASU 2009-12
- Requires sufficient information be provided to permit a reconciliation of the fair value disclosures presented to the line items in the statement of net assets

Effect on benefit plans

- Plan management is responsible for valuation of investments and presenting the f/s in accordance with GAAP
  - May use outside service provider or pricing service
  - Requires sufficient understanding of the nature of the plan's investments
- Limited scope audit
  - Certification does not change management's responsibilities
- Auditor should obtain an understanding of entity's process for determining
  - Fair value measurements
  - Fair value disclosures, including fair value hierarchy levels

Uncertain tax positions

- AICPA TIS Section 5250.15 Application of Certain FASB Interpretation No. 48 (codified in FASB ASC 740-10) Disclosure Requirements to Nonpublic Entities That Do Not Have Uncertain Tax Positions
  - Clarified that the disclosures required by FASB ASC 740-10-50-15c-e remain in effect (if applicable), regardless of whether the entity has any uncertain tax positions
  - Typically, plan tax years will remain open for 3 years

Uncertain tax positions – example disclosure

Accounting principles generally accepted in the United States of America require plan management to evaluate tax positions taken by the plan and recognize a tax liability if the plan has taken an uncertain position that more likely than not would not be sustained upon examination by the [*Identify applicable taxing authorities*]. The plan administrator has analyzed the tax positions taken by the plan, and has concluded that as of December 31, 2010, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the financial statements. The plan is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The plan administrator believes it is no longer subject to income tax examinations for years prior to 2008.

Service organization control reports (SOC 1 Reports)

- SSAE No. 16, *Reporting on Controls at a Service Organization*
  - Supersedes SAS 70
  - Effective for report periods ending on or after June 15, 2011 (with early implementation permitted)
- What is similar
  - Type 1 and Type 2 reports
  - Service auditor obtains the same level of evidence and issues examination level opinion
  - Restricted to user entities that are customers of the service organization and user auditors
  - Primarily an auditor to auditor communication
  - Provides user auditors with information about controls at a service organization that are relevant to the user entities' financial statements

Service organization control reports (SOC 1 Reports) (continued)

- What has changed
  - Guidance moved from the auditing standards to the attestation standards
  - A written assertion by management of the service organization
    - Fairness of the presentation of the description of the system
    - Suitability of the design (Types 1 and 2) and effectiveness of the controls (Type 2)
  - Description of the system and the service auditor's opinion on the description will cover a period of time rather than as of a specified date
- New user auditor guidance will be effective for 2012 calendar audits
  - User auditors continue to use guidance in AU section 324 until new guidance is effective
  - New guidance will remain in the auditing standards
  - New guidance does not contain any significant changes for user auditors

PCAOB Auditing Standards (AS) Updates

- AS No. 7 Engagement Quality Review
  - Effective for audits of fiscal years beginning on or after December 15, 2009
- AS Nos. 8-15 "Risk Assessment Standards"
  - Effective for audits of fiscal years beginning on or after December 15, 2010

PCAOB Auditing Standards Nos. 8-15 “Risk Assessment Standards”

- Suite of seven standards patterned after IAASB (International) clarified standards
  - AS No. 8, *Audit Risk*
  - AS No. 9, *Audit Planning*
  - AS No. 10, *Supervision of the Audit Engagement*
  - AS No. 11, *Consideration of Materiality in Planning and Performing an Audit*
  - AS No. 12, *Identifying and Assessing Risks of Material Misstatement*
  - AS No. 13, *The Auditor's Responses to the Risks of Material Misstatement*
  - AS No. 14, *Evaluating Audit Results*
  - AS No. 15, *Audit Evidence*
- Similar to the AICPA Accounting Standards Board SAS # 104-111 Risk Assessment Standards
- The standards address many fundamental aspects of the audit process and are expected to serve as a foundation for future standards-setting

PCAOB Auditing Standard No. 7

Engagement Quality Review

- Designed to give investors assurance about engagement quality
- Requires a rigorous review to serve as a meaningful check on the work performed by the audit team
- Increase likelihood that significant engagement deficiencies will be caught BEFORE issuing the report

Hot Topics . . .

for the Current Year

PCAOB Release 2010-006
Fair Value Measurement Deficiencies

- PCAOB Report on Observations of PCAOB Inspectors Related to Audit Risk Areas Affected by the Economic Crisis (September 29, 2010)
- Issues noted
  - Failure to evaluate whether FV measurements were determined using appropriate valuation methods or adequately test controls over issuer's valuation process
  - Failure to evaluate, or evaluate sufficiently, the reasonableness of management's significant assumptions, including tests beyond inquiries of management
  - Failure to evaluate available evidence that was inconsistent with issuers' fair value estimates
  - Failure to test, or test sufficiently, significant, difficult-to-value securities

403(b) plan audits

A look back on 2009 audits…

Examples of what we dealt with	What we found in many instances
Issues defining "The Plan"	**Lack of historical records and insufficient audit evidence**
Field Assistance Bulletins	**Lack of internal controls over the plan**
Allocated vs. unallocated contracts	**Lack of understanding re: fiduciary responsibilities**
Fair value measurement issues	**Operational errors**
Participant Loans vs. Loans to Participants	**Non-timely contributions**
"Good Faith" efforts to comply	**"Good Faith" efforts to comply**

403(b) plan audits (continued)

- Audit Effort and Results
  - Sought sufficient appropriate audit evidence
  - Often resulted in frequent and difficult client conversations
  - Modified opinions
  - SAS 115 communications
- Now what?
  - DOL 403(b) website: http://www.dol.gov/ebsa/w03b.html
  - Auditors
    - What will happen for the 2010 plan year?
  - AICPA 403(b) Audit Task Force

ASC 815, *Derivatives and Hedging*

- Entities are required to provide enhanced disclosures
  - How and why an entity uses derivative instruments
  - How derivative instruments are accounted for under the standard
  - How derivative instruments are recorded in the financial statements
  - Concentrations of credit-risk in derivative agreements
  - Categories of derivatives by type of risk (e.g., interest, credit or foreign exchange rate)

ASC 815, *Derivatives and Hedging*

- Materiality considerations include
  - Gross amounts (e.g., notional values)
  - Volume of activity during the period
  - Outstanding positions at year end (not just the fair value)
  - Gain or loss from derivatives during the year
  - Overall risk relative to the entire investment portfolio
- Generally management needs to obtain information from the investment manager to assess the materiality of the derivatives and comply with the disclosure requirements
- SEC letter regarding disclosures (July 2010)
  - How and why derivatives were used rather than how they "may" be used
  - Volume disclosures
  - Identification between purchased and written derivatives

FASB Exposure Draft

Disclosures for Employers Participating in Multiemployer Plans

- FASB issued an Exposure Draft (ED) in September 2010
- Proposed significantly enhancing financial statement disclosure requirements for employers participating in multiemployer defined benefit plans
- FASB received a lot of feedback on ED
- Final standard expected in 3rd quarter of 2011

EBP Guide Overhaul

- Guide last issued 1991
- Has not been revised or amended other than for conforming changes
- Significant changes have occurred
  - Types of retirement plans offered
  - Ways plans are administered
  - Types of investments plans are holding
  - Numerous changes to the rules and regulations by the DOL, IRS and PBGC

EBP Guide Overhaul

- Various accounting issues were brought to FinREC (formerly AcSEC) beginning in March of 2006
- Working Draft of accounting chapters posted for comment on AICPA website http://www.aicpa.org/InterestAreas/AccountingAndAuditing/Community/EMPLOYEEBENEFITPLAN/Pages/WorkingDraftEmployeeBenefitPlans.aspx
- Comment Period Ended June 10, 2011
- Preliminary results of comments

EBP Guide Overhaul

- Accounting Chapters include:
  - Defined Contribution Retirement Plans
  - Defined Benefit Pension Plans
  - Health and Welfare Plans
  - Investments
  - Illustrative financial statements
- Chapters containing auditing guidance will be reviewed and cleared by the ASB
- Guide expected to be released Spring 2012

EBP Guide Overhaul

- New Guide will contain –
  - Introduction and Background
  - Planning and General Auditing Considerations
  - Internal Control
  - Accounting, reporting and auditing guidance specific for DC, DB and HWF plans

EBP Guide Overhaul

- Related Parties and Parties-in-Interest
- Other Auditing Considerations and Audit Completion
- Auditor's Reports
- Added practice tips to each chapter
- Newly revised financial statements

Accounting Topics

Accounting Topics

- Enhancements and New Accounting Topics for DC Plans:
  - Cash balances
  - Excess Contributions
  - Corrective Contributions
  - Forfeitures
  - Rollovers
  - Presentation of certain items in the statement of changes in net assets
  - Plan Mergers

Accounting Topics

- DC plans (continued)
  - New recommended disclosures
    - Significant terms of expense offset arrangements
- DB Plans
  - Contributions receivable
  - Funding waivers

Accounting Topics

- Health and Welfare Plans
  - Defining the Reporting Entity
  - FSAs, HRAs, HSAs
  - Contributions Receivable
  - Refunds and Rebates
  - Stop-loss arrangements
  - Claims
  - Tax-favored Arrangements
  - Benefit Obligations
  - Plan mergers, spinoffs, and terminating trusts

Accounting Topics

- HWF Plans
  - The annual health care process
  - Examples of HWF arrangements
- Added practice tips to each chapter
- Newly revised financial statements

New Chapters

- Will be adding
  - Multiemployer chapter
  - Multiemployer information
  - Employee Stock Option Plans

Auditing Topics

Auditing Topics

- Audit areas being considered for enhancement:
  - Risk assessment considerations
  - Payroll
  - Receipt of benefit payments
  - Allocations to individual participants
  - Investment and Investment income
  - Claims
  - Distributions and census data
  - Other

Update on EBP Audit Guide Overhaul

- Various accounting issues were brought to FinREC (formerly AcSEC) beginning in March of 2006
- Working draft of accounting chapters posted for comment on AICPA website
  http://www.aicpa.org/InterestAreas/AccountingAndAuditing/Community/EMPLOYEEBENEFITPLAN/Pages/WorkingDraftEmployeeBenefitPlans.aspx
- Comment period ends June 10, 2011
- Chapters containing auditing guidance will be reviewed and cleared by the ASB
- Guide expected to be released Spring 2012

What's on the Horizon?

On the Horizon

- Auditing Standards Board Clarity Project
  - AICPA Auditing Standards Board (standards issued by the ASB apply to nonpublic companies or nonissuers) - www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/AudAttest/AudAttestStndrds/Pages/AuditandAttestServices-Standards.aspx
- FASB projects
  - Financial Accounting Standards Board - www.fasb.org
- Other Standard Setting Bodies
  - AICPA Professional Ethics Executive Committee
    - www.aicpa.org/members/div/ethics/index.htm
  - Public Company Accounting Oversight Board
    - www.pcaob.org

Summary & Questions

Form 5500 Issues

Richard A. Cristini, CPA

Richard A. Cristini, CPA, CGFM, CPPT

Partner

Davidson, Jamieson & Cristini, P.L.

Richard A. Cristini, CPA, CGFM, CPPT is the Partner in charge of the audit division for the accounting firm of Davidson, Jamieson & Cristini, P.L. He has been the partner in charge of audits for eleven municipalities and twenty-two municipal Pension Trust Funds. Six of these municipal clients have been awarded the Certificate of Achievement for Excellence in Financial Reporting by the Government Finance Officers Association (GFOA). Four of these cities have received the GFOA's Distinguished Budget Presentation Award. Richard is also a participant in the GFOA's program as a Certificate reviewer for municipalities in other states. Richard was a member of the GASB task force on the first GASB 34 implementation guide and has participated in the conversion of seven municipal CAFR's to the new reporting model.

In the role of a consultant, Richard has been the facilitator for strategic long-term financial plans for five municipalities. One of these clients has recently published the fifteenth annual update of their strategic plan. Richard has completed courses in strategic planning offered by local universities and the American Management Association.

Florida Institute of Certified Public Accountants
2011 Employee Benefits Conference

FORM 5500

Annual Return/Report of Employee Benefit Plan

May 26, 2011

Presented by

Richard A. Cristini, CPA, CGFM, CPPT
Davidson, Jamieson & Cristini, P.L.

WHO MUST FILE

- Profit sharing plans, 401(k) plans, stock bonus plans, money purchase plans, defined benefit plans, certain welfare benefit plans, etc.
- Annuity arrangements under Code Section 403(b)(1)
- Church pension plans electing coverage under code 410(d)
- Pension benefit plans covering residents of Puerto Rico, U.S. Virgin Island, Guam, Wake Island, or American Samoa
- Plans that satisfy the actual deferral percentage test by adopting the provisions of Section 401(k)(11)

*WHO DOES **NOT** FILE*

- Unfunded excess benefit plan
- SIMPLE plans using SIMPLE IRAS
- SEP plans
- Church pension plans NOT electing coverage under code 410(d)
- IRA's not considered pension plans
- Governmental plans

WHEN TO FILE

- By the last day of the 7th calendar month after the end of the plan year
- Extensions:
  - For 2 ½ months, submit Form 5558 to the IRS (keep copy), or
  - Automatically granted if plan sponsor's corporate return is on extension for same year period, but only to the corporate extension date
- Short Years – plan year < 12 months: file by the last day of the 7th calendar month, plus extensions after the short plan year ends

TERMINATED PLANS/MERGERS

Terminated Plans:

- Continue filing until all assets have been distributed
- Final return filed when all liabilities for which benefits may be paid have been satisfied

Merger:

- Final return filed for the plan year that ends when all plan assets were legally transferred to the control of another plan

FORM 5500-EZ

. Form 5500-EZ: One-Participant Plan covers:

1) only an individual (or plus spouse); or

2) a partnership that covers only the partners (or plus spouses)

- May not be used if plan covers a business that is a member of an affiliated service group, or a controlled group of corporations.
- Not filed using EFAST2
- Filed directly with IRS

FORM 5500 or FORM 5500-SF

- Form 5500, Form 5500-SF and Schedules ***must*** be submitted through EFAST2 effective with 2009 filings
- EFAST2: Electronic submissions of Returns/Reports (new for 2009 returns)
- EFAST2 website at www.efast.dol.gov or 1-866-GO-EFAST

FORM 5500 or FORM 5500-SF

- Small Plan – generally, plan covering fewer than 100 participants as of the beginning of the plan year
- 80 – 120 Rule – Small or Large
  - Based on number of participants reported on line 5 count at beginning of plan year
  - If prior return was filed, you may choose either
  - If first return, must file as large plan

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)

All pension and welfare plans and DFEs that are required to submit an annual return/report under Title I of ERISA (Form 5500-SF) must do so electronically for all plan years. Beginning January 2010, an all electronic system called EFAST2 began processing those electronic annual returns/reports. Prior year delinquent of amended Form 5500 annual return/reports must be filed electronically through EFAST 2.

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

The Form 5500-EZ cannot be submitted electronically. A "one-participant" plan that is eligible to file Form 5500-EZ and is not required to file under Title I of ERISA may elect to file Form 5500-SF electronically with EFAST2 rather than filing a Form 5500-EZ on paper with the IRS. Such a "one-participant plan" that is not eligible to file Form 5500-SF must file Form 5500-EZ on paper with the IRS.

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

You have two options to file the Plan year 2009 or 2010 annual return/report.

1. You can electronically prepare and submit a plan year 2009/2010 annual return/report using EFAST2-approved third-party software. A list of such software is available.

2. You can electronically prepare and submit a plan year 2009/2010 return/report using IFILE.

IFILE is the Form 5500 and Form 5500-SF annual return/report preparation and submission applicabion that is on DOL's Web site www.efast.dol.gov

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

IFILE is offered as an alternative to EFAST2-approved third-party software.

A list of EFAST2-approved third-party software will be posted on www.efast.dol.gov. There will be two types of software certification in EFAST2: certification for software to prepare filings and certification for software to submit filings. Make sure the software you are using is approved for the function(s) you will need to have performed by the software (i.e., filing preparation and/or submission).

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

IFILE cannot be used to transmit batches of filings; it can only be used to transmit single filings. Many third-party preparers benefit from transmitting batches of filings. Some EFAST2-approved third-party software may support transmission of batches of filings.

IFILE does not help you prepare an annual return/report. Some EFAST2-approved third-party software may integrate with your systems to automatically populate some of the information required.

IFILE does not contain filing assistance or integrated instructions. Some EFAST2-approved third-party software may provide such value-added support.

IFILE does not allow more than one individual to edit a filing without exporting, downloading, importing, etc., whereas, some EFAST2-approved third-party software may provide such file sharing functionality. With file sharing as part of the software, different people can work on a single filing in a coordinated and streamlined manner.

You can register for electronic credentials through the EFAST2 web site www.efast.dol.gov.

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

When registering for electronic credentials through the EFAST2 Web site, what are the different user types and what type(s) of user should I select?

There are five user types under EFAST2. You can check as many as apply to you. You may associate more than one user type under your registration if you will be performing multiple functions:

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

Filing Author: Filing Authors can complete Form 5500/5500-SF and the accompanying schedules, submit the filing, and check filing status. Filing Authors cannot sign filings unless they also have the "Filing Signer" type. If you are using EFAST2-approved third-party software to author your filing rather than IFILE, you do not need to check this box.

Filing Signer: Filing signers are Plan Administrators, Employers/Plan Sponsors, or Direct Filing Entities who electronically sign the Form 5500/5500-SF. This role should also be selected by plan service providers that have written authorization to file on behalf of the plan administrator under the EFAST2 e-signature option. No other filing-related functions may be performed by selecting this user type alone.

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

Schedule Author: Schedule Authors can complete one or more of the schedules that accompany Form 5500/5500-SF. Schedules created by a Schedule Author are not associated with a filing. For a schedule created by a Schedule Author to be used in a filing, the schedule must be exported. This exported file will then be imported by the Filing Author to the correct filing. Schedule Authors cannot initiate, sign, or submit a filing. If the Filing Author is using EFAST2-approved third-party software to author your filing rather than IFILE, then you do not need to check this box.

Transmitter: Transmitters can transmit Form 5500/5500-SF filings to the EFAST2 system for processing on behalf of others. Transmitters are responsible for the security of all filing information prior to and during its transmission. A Transmitter can be a company, trade, business, or individual.

Third-Party Software Developer: Third-party Software Developers make Form 5500 filing preparation or transmission software for use in the EFAST2 system. They submit test cases using their software to the Participant Acceptance Testing System (PATS) Team. The PATS Certification Team will then review their submissions and provide feedback or approve and certify the software. A Third-Party Software Developer can be a company, trade, business, or individual.

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

You do not need to register for EFAST2 electronic credentials just to complete the annual return/report using third-party software. If you will be submitting the filing to EFAST2, however, you may need to register for credentials as a "Transmitter" user type. If you will be signing the filing, you will need to register for credentials as the "Filing Signer" user type.

A filing Author is the person who initiates (including filling out) the Form 5500 or Form 5500-SF and the schedules and attachments on IFILE. A Transmitter is the person or organization who actually submits the completed annual return/report to EFAST2.

EFAST2 is a completely separate system from EFAST. You will need to register for and obtain new electronic credential under EFAST2.

EFAST 2

(ERISA FILING ACCEPTANCE SYSTEM II)
(Continued)

The IQPA report needs to be documented on letterhead, signed, and then saved as a single Portable Document Format (PDF) file. That PDF file then needs to be attached to the Form 5500 annual return/report. When you submit the Form 5500 annual return/report, the attachments will be transmitted to EFAST2 along with the rest of the information in the annual return/report.

CONTENTS OF THE ANNUAL REPORT

The contents of the annual report (i.e., Form 5500) vary depending on the type and size of the employee benefit plan the report covers.

A summary of each of the components of the annual report (i.e., Form 5500) follows:

1. Form 5500.
2. Schedule A (Insurance Information).
3. Schedule C (Service Provider Information).
4. Schedule D (DFE/Participating Plan information.
5. Schedule E (Now reported on Schedule R).
6. Schedule G (Financial Transaction Schedules).
7. Schedule H (Financial Information).
8. Schedule I (Financial Information – Small Plan).
9. Schedule MB (Multi employer Actuarial Information) and SB (Single-employer Actuarial information.
10. Schedule R (Retirement Plan and ESOP Information).

RISK ASSESSMENT PROGRAM
Form 5500 – 401(k)

COMMON FAILURES:

The most common failures involve errors in (1) the ADP/ACP testing, and (2) the timely payment of the 401(k) deferrals.

The other most prevalent failure involved contribution allocation errors, which occur when the amount of contribution required by the formula in the plan document (e.g., 10% of participant's compensation) is not made. This could be for one participant or many participants. It could be caused by an administrative error (i.e., not deposited timely) or due to negligence or oversight (i.e., wrong participant compensation used).

RISK ASSESSMENT PROGRAM
Form 5500 – 401(k)
(Continued)

COMMON FAILURES (continued):

Avoiding the Error:

ADP/ACP Testing et al:
The best way to avoid these problems is to make sure all the people responsible for running the tests are knowledgeable with the law (Internal Revenue Code section 401(k)(m). This includes knowing what contribution amounts and what employee compensation to use in applying the tests.

Contribution Allocations:

401(k) plans can have multiple types of contributions being allocated to the plan. In addition to tax deferred contributions, there could be employee after-tax contributions, employer matching contributions, and employer discretionary contributions. The best way to avoid allocation problems is to make sure all the people responsible for the allocation know the correct and most current allocation formulas. They must also know whether or not forfeitures are allocated to participants, and if so, what is the allocation formula. Finally, they must know the correct and most current definition of compensation being used in the formulas and ensure that it is used in the calculations.

RISK ASSESSMENT RESULTS
FORM 5500 - PROFIT SHARING PLANS

The most common failure involves inadequate bonding of plan fiduciaries and persons who handle pension funds, as required by Title I of ERISA, unless one of the limited exceptions is met. The amount of bonding should not be less than ten percent of the amount of funds handled, but in no event less than $1,000, nor more than $500,000.

The 2nd most prevalent failure involves contribution allocation errors. Such errors occur whenever the amount of contribution required by the formula in the plan document (i.e., 10% of participant's compensation) is not made. This could be for one participant or many participants. It could be caused by an administrative error (e.g., not deposited timely) or due to negligence or oversight (e.g., incorrect participant compensation used).

The 3rd most prevalent failure involves participation and/or coverage. Participation errors (Internal Revenue Code §410(a) occur when a plan does not bring an employee into the plan when the plan document states they should, or brings an ineligible employee into the plan contrary to the plan document (e.g., the plan provides that an employee enters the plan only after completing a year of service). Coverage errors occur when the plan does not "cover" (meaning they are a benefitting participant) a certain amount of employees as required by Internal Revenue Code §410(b).

RISK ASSESSMENT RESULTS
FORM 5500 – PROFIT SHARING PLANS
(Continued)

The 4th most prevalent failure involves vesting. A vesting error can occur whenever a plan does not count a participant's vesting service correctly per the plan document, and/or incorrectly applies the plan's vesting percentage schedule. Errors in vesting can result in the participant receiving less than their entitled pension benefits.

The last most prevalent failure involves not timely amending the plan to comply with changes in current law and/or regulatory guidance. The failure specifically affects the qualified status of the plan, so care should be taken to ensure that timely amendments are made to ensure that the plan remains qualified. Timely amending the plan includes the necessity to ensure the timely adoption of both interim and discretionary amendments, as well as for changes in law.

RISK ASSESSMENT RESULTS
FORM 5500 – PROFIT SHARING PLANS

(Continued)

AVOIDING THE ERROR:

Fidelity Bonds:

Make sure the person responsible for obtaining/maintaining your Fidelity Bond knows the rules for adequate bonding. Plan fiduciaries and persons who handle pension funds are required by Title I of ERISA to be bonded unless one of the limited exceptions is met. The amount of bonding should not be less than ten percent of the amount of funds handled, but in no event less than $1,000, nor more than $500,000.

Contribution/Allocations:

Profit sharing plans can have multiple types of contributions being allocated in the plan. Most of these plans have employee discretionary contributions which are allocated based on a specific formula. There could also be employee after-tax (voluntary) contributions. The best way to avoid problems is to ensure that the parties who are responsible for the allocations know the correct and most current allocation formulas. They must also know whether or not forfeitures are allocated to participants and, if so, what the allocation formula is. Finally, they must know the correct and most current definition of compensation being used in the formulas to ensure it is properly used in the calculations.

RISK ASSESSMENT RESULTS
FORM 5500 – PROFIT SHARING PLANS
(Continued)

Participation/Coverage:

Errors involving participation and/or coverage can be caused by a number of things. Poor recordkeeping and/or lack of knowledge regarding such are the two most common errors. Participation is generally based upon an employee's date of hire, the amount of service completed from the date of hire, and possibly the age of the employee. If records are not maintained properly, errors will occur. Here again, the best way to avoid participation problems is to make sure that the parties responsible for administering plan participation know the correct and most current eligibility provisions in the plan.

In order to make sure your plan does not have coverage errors, it is essential that whoever is responsible for plan administration has an in-depth knowledge of Internal Revenue Code Section §410(b), which contains the coverage requirements every plan must meet. As part of this , they must also know exactly who is in the plan and who is not.

RISK ASSESSMENT RESULTS
FORM 5500 – PROFIT SHARING PLANS
(Continued)

Vesting:

Errors including vesting can be caused by a number of things. Poor recordkeeping and/or lack of knowledge regarding vesting are the two most common errors. In some plans, a participant becomes 100% vested as soon as they enter the plan. For the majority of plans, vesting percentage is based on an employee's years of vesting service as defined by the plan document. Depending on the number of years of vesting service completed, a participant is entitled to a certain vesting percentage as defined in the vesting schedule in the plan document. So, if errors are made in calculating years of service or the wrong schedule is used, a participant could receive the wrong amount of their pension benefits. Once again, the best way to avoid these problems is to make sure that the parties responsible for administering the plan's vesting know the correct and most current vesting provisions in the plan.

RISK ASSESSMENT RESULTS
FORM 5500 – PROFIT SHARING PLANS

(Continued)

Non-Timely Plan Amendments:

Discuss with your plan administrator or pension professional as to whether the plan is currently up to date with current law changes. Setting up operating procedures and appropriate internal control for the plan is an important first step. Administrative problems cause a high percentage of pension plan errors. Many times, there is a communication breakdown between attorneys, accountants, trustees, and employees helping administer the plan that can cause mistakes to be made.

403(b) Plans: Surveying the Wreckage

Ian Dingwall, CPA
Marilee Pierotti Lau, CPA (Retired)

Ian Dingwall, CPA

Chief Accountant

Office of the Chief Accountant
Employee Benefits Security Administration
U.S. Department of Labor

Mr. Dingwall assumed the position of the Employee Benefits Security Administration's (EBSA) (formerly the Pension and Welfare Benefits Administration) first chief accountant on July 1, 1988. He serves as EBSA's primary adviser on accounting and auditing issues stemming from EBSA's responsibilities under the Employee Retirement Security Act (ERISA) and the Federal Employee Retirement Security Act (FERSA). Mr. Dingwall was instrumental in developing and implementing the agency's fiduciary audit plan for carrying out its responsibilities for the multi-billion dollar Federal Thrift Savings Plan. In 1984 Mr. Dingwall held the position of treasurer for Jack Kent, Inc. in Middleburg, Virginia. Previously, Mr. Dingwall was a supervisory auditor in the Special Litigation Division of the Office of the Solicitor, where he provided expert advice on accounting and auditing matters involving litigation of employee benefit plan cases. Mr. Dingwall performed the functions of chief accountant to the Enforcement Division of the Federal Energy Regulatory Commission from 1980 to 1982. From 1974 to 1980, he was a senior accountant in the Division of Enforcement at the Securities and Exchange Commission, where he developed numerous cases involving accounting principles and auditing standards. From 1969 to 1974 he was with the accounting firm of Ernst & Young, where he conducted financial audits and performed related tax services for clients. Mr. Dingwall, a graduate of the University of Maryland, is a certified public accountant in Maryland and a member of the American Institute of Certified Public Accountants and the Greater Washington Area Institute of CPAs.

Mr. Dingwall was appointed to the AICPA's first prestigious "Group of 100" to help shape the future role of the CPA profession. Mr. Dingwall received a "Hammer" award from Vice President Gore for helping to "build a government that works better and costs less" and was listed as one of the"1997 Top 100 Most Influential People in Accounting" by the editors of Accounting Today.

Mr. Dingwall is the recipient of the AICPA's 2007 Outstanding CPA in Federal Government Award for his contributions to increased efficiency and effectiveness of government organizations and to the growth and enhancement of the profession. Mr. Dingwall presently serves as an observer "with privileges of the floor" to the Public Company Accounting Oversight Board's Standing Advisory Group.

Marilee P. Lau

Consultant

KPMG LLP

Marilee Lau is a founding member and the current Chairperson of the AICPA Employee Benefit Plan Audit Quality Center's Executive Committee which was established in 2004. This committee works closely with the Department of Labor in order to provide appropriate guidance to plan sponsors and their auditors. Marilee is also the chair of the Audit Guide Task Force which updates the accounting and auditing Guide for Audits of Employee Benefit Plans and the Audit Risk Alert.

From 1995-1998 Marilee was the AICPA representative to the ERISA Advisory Council for the Department of Labor in Washington D.C. This Advisory Council provides guidance to the Secretary of Labor on specific issues related to employee benefit plans. She was the Chairperson for the 1998 Council and also was a representative to the President's Saver Summit in 2002. She has served on the AICPA's Employee Benefits Plans Experts Panel and in October, 2007 she concluded her term as the Chair. Marilee is also on the Advisory Board for the Bureau of National Affairs Pension & Benefits Reporter which provides input on various pension issues and is currently serving on the Accountants Committee for the International Foundation of Employee Benefit Plans.

Marilee was KPMG's National Partner in Charge of the Employee Benefit Plan Practice until November 2008 when she transitioned to a consulting role with KPMG dealing with employee benefit plan quality issues related to accounting and auditing of employee benefit plans.

403(b) PLAN AUDITS: YEAR 2 – NOW WHAT?

Ian Dingwall, Chief Accountant
Department of Labor—EBSA
Marilee Lau, CPA
Retired Partner KPMG

Looking Back

- 2009 Form 5500s Filed By October 15th
  - Total 5500s filed: ~675,000
  - Total 5500s expected: ~695,000
- Large Retirement Plans – Auditors' Report
  - Unqualified: =17,000 (20%)
  - Limited Scope Disclaimer: = 67,000 (80%)
    - (29 CFR 2520.103-8)

Interesting to Note

- Per DOL statistics: ~9,500 EINs related to ERISA plan audits
- Of those: =4,500 are AICPA Members
- Of those: =2,000 are AICPA Employee Benefit Plan Audit Quality Center Members

403(b) Form 5500s Filed

- Total: =19,200
- Large: =7,200
- Small: =12,000
- Filed with Schedule H: = 5,100

Large 403(b) Plan Filings

- A number filed without financial data
  - No Schedule I OR Schedule H Attached
  - Filed as in prior years – except through EFAST2
- A number filed without audited financial statements attached

Large 403(b) Plan Filings – Auditors' Report

- Unqualified
- Qualified
- Adverse
- "Standard" limited scope
- "Full" disclaimer
- Number citing the Field Assistance Bulletins (FABs)
- Compiled December 31, 2008

DOL Action Steps For 403(b) Plans

- Some analysis of filing data
- 45-Day Letters for:
  - Incorrectly filed
  - Missing audited financial statements
  - Other Deficiencies
  - Non-filers

ASPPA Letter to DOL

- American Society of Pension Professionals and Actuaries (ASPPA) and the National Tax Sheltered Accounts Association (NTSAA) Task Force on 403(b) Audits letter dated February 17, 2011 to Assistant Secretary Borzi
  - ***Opening Balance Relief - ASPPA and NTSAA recommend:*** that a rule be developed under which the auditor of the financial statements of a 403(b) plan can rely upon an employer's documented good faith effort, whether successful or not …
  - ***Disclaimed Audit Relief - ASPPA and NTSAA recommend:*** that a rule be developed to ensure that the audit will provide useful information to the fiduciaries, Department and participants, while substantially reducing expenses. We propose that, … the plan, in the alternative, can engage the auditor to opine on the business controls of the plan sponsor in handling the assets or other financial matters of the plan within the control of the sponsor.

ASPPA Letter to DOL (continued)

- ***ASPPA and NTSAA recommend:*** that a committee of industry experts be established to suggest, review and modify the existing audit guidelines for 403(b) plans. The committee should specifically consider:
  - The differences between group annuities, individual contracts, and individual custodial agreements and the potential for different audit requirements for each;
  - The need for relief and clarification that beginning balances as of January 1, 2009, are absolute for all purposes under applicable auditing standards, and that auditors may modify their standard procedures and accept data provided as of January 1, 2010;
  - Creation of a model "Audit Checklist" for 403(b) plans that is specific to 403(b)s and does not contain qualified plan requirements; and
  - Better coordination between the Department's rules and the Internal Revenue Service compliance rules by creating educational communications and training materials specifically focusing on 403(b) plans for employers, vendors, auditors and administrators.

ASPPA Letter to DOL (continued)

- ***ASPPA and NTSAA further recommend:*** that the Department use its regulatory authority to establish specific auditing standards under ERISA for 403(b) plans that:
  - Consider the existing regulatory requirements of the issuers of 403(b) annuity and custodial account products;
  - Audit the plan at the employer level rather than at the financial institution level, taking into account the internal controls of the employer in lieu of the financial institutions; and
  - Establish an absolute starting date for contracts/accounts to be included under the plan for ERISA enforcement purposes and direct auditors to disregard balances and transactions that predate the specified date.
- Any such standard must take into account the differences between group annuities, individual annuities and custodial accounts.

Looking Back - Auditors

- What we found
- What we didn't find
- What we did about it

What We Found – Defining "The Plan"

- How many plans are there?
  - Multiple plans vs. multiple vendors
  - "Old" Plan vs. "New" Plan
  - 403(b) "Safe Harbor Plan" plus 401(a) Plan
  - 401(a) with Profit Sharing formula (Discretionary)
  - 401(a) with a Money Purchase Plan formula (Fixed %)
  - 401(a) with a Matching formula (Based on the 403(b) Plan)

What We Found – Defining "The Plan" (continued)

- ERISA vs. Non-ERISA
  - Governmental plans (ERISA section 3(32))
  - Church plans (ERISA section 3(33))
  - "Safe Harbor" Plans
    - DOL regulation 29 C.F.R. § 2510.3-2(f)
- "Improper" plan documents
  - Safe Harbor plans with "ERISA" documents
- Safe Harbor plans that filed 5500s
- ERISA plans that never filed 5500s

What We Found - Generally

- FAB reduced the number of participants
- Issues related to:
  - Allocated vs. unallocated contracts
    - DOL Advisory Opinion 2010-10A
  - Fair Value – equals Contract Value?
  - Participant loans vs. Loans to Participants
    - Loans 'inside' and/or 'outside' of the plan
- "Good Faith" efforts to comply

What We Didn't Find!

- Historical records!
  - Plan Sponsor
  - Vendor(s)
- Lack of internal controls over the plan
- Lack of understanding about and applicability of fiduciary responsibility requirements
  - "Who knew?"
  - "That's why we hired the vendor(s)!"

What We Didn't Find! (continued)

- Sufficient audit evidence to support:
  - Completeness assertion
    - Generally, only 2008 and 2009 data made available
  - Consistency
    - Lack of records
    - Change(s) in vendor(s)
    - Change(s) in Plan Sponsor personnel
- "Good Faith" efforts to comply

What We Did About It

- Sought alternative auditable evidence
- Had long, and frequently difficult client conversations
- Modified our opinions

Then What?

- SAS 115 Communications – Does a Disclaimer result in a Material Weakness?
  - "How can we disclaim an opinion and ***NOT*** have a Material Weakness?"
  - "Generally, a Material Weakness includes an expectation of correction. How can the client ***ever*** correct the past?"
  - "Won't the Material Weakness continue to be included in the 115 communications for as long as we disclaim an opinion?"

Looking Forward - DOL

- Continue to monitor compliance
- Continue to discuss issues going forward
- DOL 403(b) Website:
  http://www.dol.gov/ebsa/403b.html

Looking Forward - Auditors

- What will happen for the 2010 plan year?
- What happens when plans change auditors and the new auditor doesn't agree with the prior auditor's report?
  - Prior auditor issued 'clean' report
  - Prior auditor issued a modified report
- How will restatements be handled?

Looking Forward – Auditors (continued)

- AICPA Joint 403(b) Audit Task Force
  - Work with DOL to monitor compliance
  - Work with DOL and others to develop and recommend alternative reporting compliance
  - Continue outreach with additional tools and presentations

Looking Back and Forward – Typical Compliance Issues

- Late Deposit of Participant Deferrals & Loan Repayments
- Failure to Properly Apply Plan's Definition of Compensation
- Failure to Properly Update the Plan Document
- Failure to Follow Eligibility Provisions
  - Universal Availability vs. Employer contribution eligibility
- Incorrect Employer Contributions
- Failure to Properly Apply Plan's Vesting Provisions
- Improper Use of Plan Forfeitures

What Did You Find?

- What is your biggest concern for year 2 audits? What is your client's biggest concern?
- What is the most important thing you learned from last year's audit that you would change this year, and how?
- How will you be communicating differently with your clients? Service providers?
- How will you plan to conduct your audits more efficiently?
- What can your clients do to make the audit process more effective? More efficient?

Questions?

Speaker Biography

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- Mr. Albert has been the Chief of the Division of Reporting Compliance since 2000. He has over ten years of public accounting experience managing audits of qualified employee benefit plans, P & C insurance companies and health care providers. His current responsibilities include maintaining a multifaceted reporting compliance program that utilizes compliance assistance, voluntary compliance and traditional enforcement strategies. Scott also provides technical

SPEAKER BIOGRAPHY

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- Bob Lavenberg has more than 24 years of experience with the Employee Retirement Income Security Act of 1974 (ERISA) and related business advisory services. His expertise spans reporting, government compliance and assessment of tax implications for plans, including employee benefits, qualified retirement, health, welfare, and fringe benefits. A former member of the AICPA Employee Benefit Plan Audit Expert Panel, Bob currently serves as the vice-chair of the AICPA Employee Benefit Plan Audit Quality Center Executive Committee.

Identifying and Addressing Audit Risks

Diane Marotta Walker, CPA

Diane Marotta Walker, CPA

Partner

Johnson Lambert & Co. LLP

Diane Marotta Walker is a partner in Johnson Lambert & Co. LLP's Virginia office.

Diane serves as audit engagement partner or concurring partner for numerous insurance companies, employee benefit plans, and not-for-profit organizations. In addition to experience with US generally accepted auditing standards, she has significant experience with PCAOB auditing standards.

Diane has significant leadership roles in Johnson Lambert & Co. LLP's audit practice including serving as Partner in Charge of Quality Control and Co-Chair of the firm's Technical Committee. She served as the lead for the firm wide electronic workpaper implementation and continues to have oversight responsibility for improvement of related processes. Diane also leads all aspects of Johnson Lambert & Co. LLP's growing employee benefit plan audit practice.

Diane is a graduate of The College of William and Mary with a BBA in Accounting. Diane began her career at Johnson Lambert & Co. LLP as an intern in 1997.

Diane lives in Arlington, Virginia and enjoys travel.

Identifying and Addressing Audit Risks

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May 26, 2011

Agenda

Risk Assessment Considerations

Hot topics in employee benefit plan audits

Changes in accounting standards

Auditing Standards Update

Risk Assessment Considerations

Changes from the Prior Year

Plan amendments or restatements

Changes in vesting provisions

Elimination, reinstatement or change in amount of matching contributions

Auto enrollment

Audit risks:

Plan provisions are not being applied correctly by plan sponsor and/or service providers

Changes from the Prior Year

New plan personnel or service providers

Lose understanding of plan and its provisions

Audit Risks:

Errors in calculating or remitting contributions

Errors in transfers to new service provider

Plan sponsor's intentions regarding plan provisions not properly communicated to new service provider

Changes from the Prior Year

Corporate events impacting the plan

Mergers\Acquisitions

Audit Risks

Proper treatment of 2 plans merging

Proper inclusion or exclusion of plan participants

Economic impacts

Financial strain at plan sponsor

Timeliness of remittance of participant contributions

Impact on underfunded defined benefit or health and welfare plans

Going concern considerations

Incentive to manipulate estimates that have impact on plan sponsor's financial statements (benefit obligations)

Economic impacts

Turnover in plan personnel

Lack of understanding of plan, provisions and ERISA increases risk of error

Layoffs

May trigger partial plan termination

100% vesting for impacted participants (plans that have a vesting schedule)

Hardship Withdrawals

Must meet standards

Use of SAS 70s

Tool to assist in understanding and evaluating design of internal controls at service providers

Help reduce, not eliminate, testing

Critical to obtain correct SAS 70 report (and all applicable to the plan)

Some organizations have multiple SAS 70s

Use of SAS 70s

User control considerations

Controls that service provider has specified should be in place at plan sponsor

To rely on SAS 70 need to:

Verify control in place at plan sponsor to satisfy

Test operating effectiveness as appropriate

Exceptions and carve outs

Seeing more of these in SAS 70s

Use of SAS 70s – Carve outs

Sub-service providers not included in scope – typically stated in opinion

- Sources of investment prices
- Eligibility determination
- Vesting

Use of SAS 70s - Exceptions

Are there mitigating controls in place at service provider?

- Other levels of review such as quality control reviews
- Different access levels (physical vs logical)

Does the plan sponsor perform a control to mitigate?

- Review and approval – vesting calculation

Evaluation will be different depending on plan's controls and reliance on service provider

Use of SAS 70s – Audit Risks

Evaluation of SAS 70 should occur as part of risk assessment process

Appropriate audit strategy should be designed given what is covered and any exceptions or qualifications

Be careful of overreliance on the SAS 70

SSAE 16 – SAS 70 Replacement

Statement on Standards for Attestation Engagements (SSAE) 16 – Reporting on Controls at a Service Organization

Effective for service auditor's reports for periods ending on or after June 15, 2011

Guidance for performing the attestation report – not for using it

New guidance for use of SAS 70 will come as part of the Clarity Project (effective in 2012)

Not expected to significantly impact plan audits

SSAE 16 – SAS 70 Replacement

SAS 70 reports will be known as “SOC 1” reports

Still Type 1 and Type 2

Will also be other types of reports

SOC 2 – intended for stakeholders; controls relevant to security, availability, processing integrity, confidentiality, or privacy

SOC 3 – general use reports on controls relevant to security, availability, processing integrity, confidentiality, or privacy

Participant Loans (ASU 2010-25)

Considered notes receivable rather than an investment

No longer carried at fair value, so fair value disclosures not applicable

On Form 5500- Schedule H – still classified as investment

no reconciling footnote needed

Limited scope certification may cover (no change)

Fair value measurements

Limited scope audit considerations & risks

Full scope audit considerations & risks

Disclosures

Fair Value – Limited Scope

Are all investments covered in the certification?

Participant loans?

Carefully read the certification – some trustees and custodians are changing the wording

Management's reliance on certification becoming more challenging with alternative investments/hard to value securities

Are they reported at fair value as of plan's year end?

Fair Value – Full Scope

Process of management and service providers for obtaining fair values

Management can use outsourced service providers to assist, but still responsible for fair values reported in the financial statements

Nature of the investments

Any new or hard to value investments?

Fair Value - Disclosures

New disclosures related to fair value measurements required for 2009 plan year ends

Wide divergence in practice

Look again as compared to the standards as we approach 2010 plan year ends

Additional new disclosures required for 2010 plan year ends

Fair Value - Disclosures

Investments in certain entities that calculate NAV

Disaggregation of investments by major security type, determined based on the nature and risks of the securities

schedule of assets held is not a substitute

Clarification about fair value methodologies and inputs for Level 2 and 3

Transfers in and out of Levels, and describe reasons

Insurance Company Products

Critical to read and understand contracts

Products can be complex and vary significantly from plan to plan (with same insurance company)

Need to understand the plan's investment options to determine financial statement presentation and footnote disclosures are appropriate

Also, how audit in full scope

Insurance Company Products

Allocated vs Unallocated Contracts

Allocated – not a plan asset; insurance company has assumed the risk\liability

Unallocated- plan asset; plan retains the obligation to pay the benefits

Pooled separate accounts vs mutual funds

PSA – no public price

Practical expedient of ASU 2009-12, including required disclosures

Initial Audit of a Plan

First year audit is required, prior year statement of net assets available for benefits must be presented

Can be compiled, reviewed or audited

Remember- opinion should be issued to highest level of assurance performed

Must apply appropriate audit tests to opening balances

AICPA guidance: TIS Section 6933.01

Uncertainty in Income Taxes

Management's determination of the taxable status of an entity is a tax position subject to required disclosures

Add to Tax Status note

Whether any uncertain tax positions

Whether any tax audits in progress

Description of tax years open to examination

See AICPA Audit Guide and Audit Risk Alert for sample wording

Uncertainty in Income Taxes

Plans may be subject to Unrelated Business Income Tax (UBIT) in certain situations

Items to look at further:

Welfare plans – assets > allowable reserves

Investments in partnerships, real estate investment trusts, loans or mortgages

Health & Welfare Plans

Health Care Reform provisions may impact a welfare benefit plan's obligations

Discuss with management and the plan's actuary to determine that the impact has been properly considered in the determination of the benefit obligation

- Plan amendments should be considered in the calculation as soon as contractually agreed to, even if not effective until future periods

Developing Your Testing Strategy

Modify audit approach to address risks:

- Nature, timing and extent of audit procedures

Focus on areas with significant risks

Would not expect audit approach and sample sizes to be the same on every audit

- More robust audit procedures in areas with significant risks

Auditing Standards Update

Clarity Project\Clarified Standards

Goal to clarify and converge ASB audit, attest, and quality control standards with those of the International Auditing and Assurance Standards Board (IAASB)

Resulting standards should be easier to read and apply

Clarity Project\Clarified Standards

Over 35 standards have been approved and are “finalized but not yet issued”

Will be issued as a single SAS in a codified AU section format in 2011

Effective for periods ending on or after December 15, 2012

Recently Issued Standards

SAS 117-121 issued separately to deal with certain practice issues

New standards <u>effective for periods beginning on or after December 15, 2010</u> related to:

other information (SAS 118)

supplementary information (SAS 119)

required supplementary information (SAS 120) – N/A to plans

SAS 118

Other Information in Documents Containing Audited Financial Statements

Auditor's responsibility for "other information" in documents containing audited financial statements and auditor's report

Applicable to Form 5500

Information may be relevant to audit

Read for material inconsistencies

Prior to report release or as soon as practicable

SAS 119

Supplementary Information in Relation to the Financial Statements as a Whole

Auditor's responsibility when engaged to report on whether *supplementary information* is fairly stated, in all material respects, in relation to the financial statements as a whole

Applicable to ERISA required supplemental schedules

Wording in audit opinions and representation letters will be changing

QUESTIONS

Investments & Fair Value

Tricia Van Vliet, CPA

Tricia A. Van Vliet, CPA

Director National Assurance
Employee Benefit Plan Audit Practice
BDO USA, LLP

Experience Summary

Tricia Van Vliet is a Director in the National Assurance Department of BDO USA, LLP, with responsibilities primarily related to ERISA audit quality and risk management. She also plays a key role in the Firm's national initiatives related to investment fair valuation, supporting all industry groups in this regard. In addition to her national responsibilities she also serves as technical or engagement quality control reviewer on nearly 20 complex employee benefit plan audit engagements, including health & welfare and multi-employer plans. She has over 16 years of public accounting experience, with a specialization in the employee benefit plan industry.

Tricia's employee benefit plan audit experience is complimented with more than 8 years of experience auditing in the investment company and securities industries. The majority of her time is dedicated to development of audit guidance, resources and training for BDO employee benefit plan auditors, in addition to technical consultations and communications for the Firm's national employee benefit plan audit practice. Tricia instructs national training courses and has presented numerous client seminars. She speaks regularly at the AICPA National Conference on Employee Benefit Plans and Employee Benefit Plan Audit Forums offered by the Michigan Association of Certified Public Accountants (MACPA). Tricia currently serves the profession as a member of the AICPA Technical Standards Subcommittee, and the MACPA Employee Benefits Task Force.

Professional Affiliations

American Institute of Certified Public Accountants
Michigan Association of Certified Public Accountants

Education

B.S., Business Administration, Aquinas College

Investments and Fair Value

Understanding Investments Found in Employee Benefit Plan Portfolios

FICPA Employee Benefits Conference
May 26, 2011

Tricia A. Van Vliet, CPA
BDO USA, LLP

Course Objectives

- Provide auditors with an overview of investments held in employee benefit plan portfolios
- Highlight investment reporting and disclosure requirements
- Discuss audit issues, pitfalls and best practices associated with various plan investments

Common Investments Found in Employee Benefit Plans

- Common Stock
- Bonds
- Mutual Funds
- Bank Collective Investment Funds
- Insurance Company Investment Products
- Master Trusts
- Alternative/Hard-to-Value Investments
- Self Directed Brokerage Accounts
- Separately Managed Funds

Common Stock

- Equity investment security
  - Ownership in a corporation
  - May be publicly traded or closely held
- Publicly traded shares
  - generally valued at quoted market price based upon close of a national exchange
- Closely held shares
  - most commonly found in ESOP
  - generally measured based upon an independent valuation

Bonds

- Debt/fixed income security
  - Corporation or government/agencies issue bonds to raise cash
  - Certain U.S. Treasuries available to public for direct investments
  - Most trade in secondary market through brokers
    - Complexities often lead to confusion over these investments
      - Valuation, including fair value hierarchy
    - Numerous resources available to assist engagement teams

Mutual Funds

- Also known as registered investment companies
  - Registered with the SEC, annual audit and periodic filing requirements
- Plan holds shares in mutual funds
  - Money invested is pooled with that of other investors, not limited to plans
  - Underlying portfolio of investments managed by a adviser based upon the fund's objective
  - Offers diversification to shareholders
  - Varying levels of risk associated with nature of underlying investments
- Shares are generally valued at Net Asset Value Per Share (NAVPS) based upon net asset value of underlying portfolio securities and are published on a national exchange

Bank Collective Investment Funds

- Primer issued by the AICPA EBPAQC in December 2010
- Historically and most commonly referred to as a common/collective trust (CCT)
- A trust that combines and collectively invests the assets of multiple qualified retirement plans
- Often times looks like a mutual fund
  - May hold investment in mutual funds
  - Cash holdings and expense arrangements impact unit price
- Plan holds investment units or units of participation
- Units represent the undivided interest in the underlying assets of the trust
- The purchase or redemption price of the units is determined periodically by the trustee, based on the current market values of the underlying assets of the fund
- Audited financial statements generally available
  - Date of audited financial statements may differ from plan year end

Separate Account Investments Offered by Insurance Companies

- Separate Accounts – often look like mutual funds
  - May be Registered or Unregistered
    - Pooled
    - Individual
- Significant challenge for plan sponsor and auditors
  - Misconceptions regarding nature of individual plan investments
  - Lack of transparency and inconsistencies among insurance companies
- Name may be based on the underlying mutual funds
- Unit value of separate account is generally different than the NAV of the underlying mutual fund
  - Impact of insurance contract's expense structure
- Recognizing a separate account
  - Presence of an insurance contract
  - Plan assets issued by an insurance company

Distinguishing Common Fund-Type Investments

Separate Account	Mutual Fund	Bank Collective Investment Fund
Unit value	Share price/NAVPS	
Portfolio holdings; may hold a single mutual fund or numerous securities	Portfolio holdings	Portfolio holdings; generally marketable securities, but may invest in other collective investment funds or mutual funds
No quoted market price	Generally quoted market price; close of exchange	No quoted market price; often valued daily to allow for daily purchases & sales
Part of investment contract	Held in separate trust	Held in separate trust
An asset/liability of the insurance company	May be traded at Omnibus or Plan level	Bank, as trustee, owns underlying assets of the fund
May be audited; often unaudited	Audited	Audited financial statements largely available

Other Insurance Company Investment Products

- Primer on products from AICPA EBPAQC – expected later in 2011
- Contracts may be allocated or unallocated
  - Caution to be exercised
  - DOL Advisory Opinion – 2010-01A – *issued March 4, 2010*
    - Contains a summary specific to one service provider, but may be considered for similar contracts
- General Account Products
  - Backed by general assets of insurance company
    - Administration Contracts (DA)
    - Immediate Participation Guarantee Contracts (IPG)
    - Guaranteed Investment Contracts (GIC)
- Synthetic GICs
- Other annuities

Fixed Interest Accounts

- Various mechanics for interest determination as defined in the contract
  - Average rate based on deposit timing
  - Fixed rate for a certain period
  - Plan owns the contract
- Deposit Administration Contracts
- Immediate Participation Guarantee Contract

Deposit Administration Contracts

- Contributions applied to future benefits of a participant
- Looks like a money market account with a bank
- Insurance company promises to pay a rate of interest, but not a specified benefit
- No guarantee that funds will be sufficient to pay for future annuities
- Insurance contract may or may not pay experience rated dividends

Immediate Participation Guarantee Contract

- Variation of a Deposit Administration Contract
- Typically two forms of contracts
  - Contract provides that annuities are purchased when a participant retires
    - Experience credit/debits adjust the account balance
  - Contract provides that pension payments are made under the contract without the purchase of an annuity
    - Sufficient account balance must be maintained to fund remaining benefits of all current retirees

Guaranteed Investment Contracts (GIC)

- Investment contract that provides a guaranteed return on principal
- Plan owns the contract
- Individually negotiated – terms specific to that plan
- Benefit responsive vs. non-benefit responsive
  - Benefit responsive generally refers to the ability of plan participants to transact at book value (principal plus accrued interest)
    - Compliance will all criteria in the standard are necessary for a contract to be considered benefit responsive
    - Must be evaluated on an individual contract basis
  - Determining whether a specific contract is benefit responsive or not continues to create challenges for auditors and plan management

Synthetic GIC

- Investments with a "wrapper" contract stabilizes investment return
  - Simulates performance of a 'traditional' GIC
- Value of the wrapper is the difference between the assets underlying the GIC and the value of the principal plus the guaranteed interest
- Plan owns the wrapped investments

How Are Contracts Valued?

Separate Accounts

NAVPS for individual funds may be different

- Not exchange traded
- Little or no transparency

May or may not be valued using the principles of the investment company audit guide

Guaranteed Rate Products

Limited visibility into valuation inputs

Judgment involved

Issuers do not always provide information to value the contracts

Multiple valuation techniques are used

Master Trusts

- Trust account that holds the assets of multiple plans under common control
- Each plan generally has an undivided interest in the assets of the trust
- Ownership is represented by
  - Record of proportionate dollar interest
    or
  - By units of participation

Other Hard-to-Value and Complex Plan Investments

- Other alternative and/or otherwise complex investments commonly found in EBP portfolios
  - Derivative Investments
  - Stable value funds
  - Limited partnerships
  - Hedge funds
  - Real estate

Self Directed Brokerage Accounts

- Allows participants to invest their account balances in any investment desired, within specified limitations
- May contain hard-to-value investments, such as real estate and mortgages
- Viewed as individual investments for auditing purposes
- Obtaining certification as to the accuracy and completeness of the accounts may pose a significant challenge
  - Often no certification available
  - May require multiple certifications

Self Directed Brokerage Accounts

- All parties must be identified to determine which investments are covered by a limited-scope certification and which investments are subject to full-scope procedures
  - Several custodians may be involved as some plans allow personal brokers to be used
- ASC 820 requires disclosure of level for each type (i.e., mutual funds, common stock, etc.) of investment within the self-directed account
- Information necessary for required disclosure of net appreciation/depreciation by investment type often a challenge to obtain from service providers
- Form 5500 Schedule H (Financial Information) and related schedule of assets permits aggregate reporting (single line item) of certain self-directed accounts

Separately Managed Accounts

- Commonly mistaken as a fund-type investments
- Plan owns individual investments rather than an interest (i.e., shares or units) in a fund
- Related investment agreements critical to understanding the nature of the plan's investments and their management
- Reporting and disclosure in financial statements, as well as full scope audit procedures if applicable, at the individual investment level

Fair Value Measurements- ASC 820 Continues to Evolve

- Recent culprits include
  - ASC 820-10-65-4 (FSP FAS 157-4); greatest impact on plans: disaggregation of investments by major category based upon nature & risk
    - Effective for interim and annual reporting periods after June 15, 2009
  - ASU 2009-12; practical expedient applicable to many common alternative/non-publicly traded plan investments measured at net asset value per share (NAVPS); additional disclosures (e.g., investment strategies, capital commitments, restrictions, etc.)
    - Effective for interim and annual reporting periods ending after December 15, 2009
  - ASU 2010-06; much needed clarification regarding disaggregation of investments by class based upon nature and risk and further expands required disclosures
    - Majority of provisions effective for interim and annual reporting periods beginning after December 15, 2009; exception related to level 3 rollforward fiscal years beginning after December 15, 2010

Fair Value Measurements– ASC 820 Continues to Evolve

- Expands the disclosure requirements
- Ultimately aimed at increasing transparency and improving comparability
- Creating very real challenges for those responsible for the preparation of plan financial statements and related footnote disclosures
- Forces Plan management to understand the nature and risks related to the investments

Let's take a look at how this translates into a plan footnote disclosure…

Fair Value – Disclosure Example

	Assets at Fair Value as of December 31, 20XX			
	Level 1	**Level 2**	**Level 3**	**Total**
Government Securities:				
US Treasury	$28,155,000	$ -	$ -	$ 28,155,000
Federal Home Loan Mtg Co	-	1,065,000	-	1,065,000
Federal National Mortgage Association	-	2,000,000	-	2,000,000
Real Estate			15,000,000	15,000,000
Guaranteed Investment Contract			20,000,000	20,000,000
Mutual Funds:				
Balanced funds	1,018,000		-	1,018,000
Growth Funds	3,000,000			3,000,000
Common Collective Trusts:				
Fixed Income - US	-	25,000,000	-	25,000,000
Equity - US	-	38,500,000	-	38,500,000
Total investments at fair value	$32,173,000	$66,565,000	$35,000,000	$ 133,738,000

Fair Value – Disclosure Example

Level 3 Gains and Losses
The following table sets forth a summary of changes in the fair value of the plan's level 3 assets for the year ended December 31, 20XX.

	Level 3 Investments	
	Real Estate	Guaranteed Investment Contract
Balance, beginning of year	20,000,000	24,400,000
Realized gains (losses)	(4,000,000)	600,000
Unrealized gains (losses) relating to assets still held at end of year	(2,000,000)	-
Purchases, sales, issuances, settlements (net)	1,000,000	(5,000,000)
Balance, end of year	$15,000,000	$20,000,000

Total amount of gains (losses) for the period included in changes in net assets attributed to unrealized gains (losses) relating to assets held at end of reporting period.	(2,000,000)	-

ASU 2010-25

- ASU 2010-25 – *Reporting Loans to Participants by Defined Contribution Plans*
  - Effective for fiscal years ending after 12.15.2010
  - Retrospective adoption to all prior periods presented
  - No longer an investment for GAAP purposes
    - Record as notes receivable from participants
      - Outstanding balance plus accrued unpaid interest
    - Fair value disclosures no longer applicable
    - Exempted from credit quality disclosures in ASU 2010-20
  - Continues to be an investment for ERISA purposes
    - Report as investment on Form 5500, Schedule H and required ERISA supplemental schedule of assets (held at end of year)

ASU 2010-25

- Implementation
  - Segregate participant loans from plan investments and investment income
  - Reclassify participant loans and interest income for all prior periods presented
  - Include disclosure regarding adoption/reclassification
  - Consider ASC 320, *Receivables*
    - Accounting policy
    - Allowance for credit losses and impairment, if applicable
  - Limited scope certification disclosure considerations – may continue to include
  - Remove participant loans from the fair value disclosures & hierarchy
  - Auditor's report may be modified to emphasize adoption
    - Reclassification only and generally expect no change in valuation methodology; engagement team may conclude that change is neither quantitatively nor qualitatively material

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- Understanding differences that may exist between GAAP and Form 5500 reporting for plan investments
  - Consider financial statement presentation and disclosure vs. Schedule H classifications and related handling of ERISA supplemental schedules
    - Insurance products – fair value vs. contract value
    - Investment funds
      - Direct Filing Entity (DFE) vs. non-DFE
    - Participant loans
      - Investment vs. receivable

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- **Distinguishing between Management & Auditor Responsibilities**
  - **Management**
    - **Understand, be able to articulate and support fair value measurements**
    - **Determining that the plan investments are measured at fair value and disclosed in accordance with ASC 820**
      - **Be wary of valuation timing lags especially for non-publicly traded investments**
    - **Determining the classifications of investments**
      - **Within the fair value hierarchy (Level 1, 2 or 3)**
      - **Disaggregation by class based upon nature and risk**
    - **Assistance may be provided by a 3rd party, but this does not relieve management of their responsibilities**
      - **Understand valuation methods, and related inputs/assumptions**
      - **Engage in meaningful discussion and be able to challenge the service provider when necessary**

Note: Independence issues- auditor cannot perform these management functions

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- Distinguishing between Management & Auditor Responsibilities (continued)
  - Auditor
    - Full vs. Limited scope engagements
      - Most significant distinguishing characteristics related to existence and valuation assertions
      - ASC 820 does not change the auditor's responsibility for investment information in a limited scope audit
    - Regardless of scope auditor is responsible for assessing form and content; need to conclude on adequacy of disclosures in accordance with GAAP
    - Understand management's processes and procedures for fair value reporting and disclosure
    - Demonstrate a comprehension of plan investments
    - Be able to assess management's knowledge of the investments contained in the plan's portfolio

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- So what could it mean if management fails to fulfill their responsibilities?
  - Lack sufficient knowledge/understanding of plan investments
    - Need to obtain an understanding of the investments and risks; auditor cannot do this for management
  - Lack sufficient knowledge/skill necessary to measure investments at fair value
    - Must work with advisors and other 3rd party service providers, as necessary, to obtain such knowledge and skill
  - Inability to provide sufficient audit evidence for auditor to conclude
    - Must obtain and provide such evidence or this may represent a scope limitation

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- Gather all available information
  - May be very accessible and not as difficult as it may seem
    - Sources of Data
      - What do you give your participants to help them understand options when directing the investment of their contributions?
      - Investment prospectus or similar documents
      - Annual and other periodic filings for publicly traded investments
      - Audited financial statements of investments
      - Summaries and other information supplied by record-keeper, trustee, or custodian
      - Are you employing sophisticated professional investment managers/advisors?
        - May be the source of a wealth of information
        - Periodic performance analysis
        - Investment strategies/objectives
        - Allocation decisions within allowable ranges per investment policy
        - Established benchmarks

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- Disclosures and required classifications involve significant judgment
  - Many tools and resources available to assist
    - AICPA
    - AICPA Employee Benefit Plan Audit Quality Center
  - Valuation
  - Unit of account
  - Classification within the ASC 820 hierarchy (level 1, 2 or 3)
  - Disaggregation by class based upon nature and risk

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- What we are seeing in practice
  - Valuation methodology, inputs/assumptions
    - Common Stock
    - Bonds
    - Mutual Funds
    - Bank Collective Investment Funds
    - Insurance Company Investment Products
    - Master Trusts
    - Alternative/Hard-to-Value Investments
    - Self Directed Brokerage & Separately Managed Accounts

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- What we are seeing in practice (continued)
  - Determining the plan's unit of account
    - Common Stock
    - Bonds
    - Mutual Funds
    - Bank Collective Investment Funds
    - Insurance Company Investment Products
    - Master Trusts
    - Alternative/Hard-to-Value Investments
    - Self Directed Brokerage & Separately Managed Accounts

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- What we are seeing in practice (continued)
  - Determination of levels within the hierarchy
    - Common Stock
    - Bonds
    - Mutual Funds
    - Bank Collective Investment Funds
    - Insurance Company Investment Products
    - Master Trusts
    - Alternative/Hard-to-Value Investments
    - Self Directed Brokerage & Separately Managed Accounts

Navigating Fair Value Measurements, Disclosures and Your Responsibilities

- What we are seeing in practice (continued)
  - Disaggregation based upon nature & risk
    - Common Stock
    - Bonds
    - Mutual Funds
    - Bank Collective Investment Funds
    - Insurance Company Investment Products
    - Master Trusts
    - Alternative/Hard-to-Value Investments
    - Self Directed Brokerage & Separately Managed Accounts

Open Forum – Q&A

Appendix

Example Planned Audit Approach for Fund Investments Measured at NAVPS

Note: these examples are intended for illustrative purposes only; auditors will customize their planned audit procedures in response to the nature of the investments and risk assessment specific to the individual plan

Example Planned Audit Approach – Audited Collective Investment Funds

- Obtain
  - Audited financial statements (AFS) prepared in accordance with investment company GAAP
    - Evaluate impact on NAVPS where prepared on another basis (caution: insurance company investment fund financials may follow statutory accounting principles)
  - SAS 70 report covering portfolio investment valuation and calculation of NAVPS, if available

Example Planned Audit Approach – Audited Collective Investment Funds

- Where fund AFS and plan measurement dates are the same
  - Expectation generally such that NAVPS will agree without exception to AFS
  - Evaluate available evidence, and agree plan investment NAVPS to fund per AFS
  - Document conclusion or need for further audit procedures (e.g., where audit evidence contradicts auditor's expectations)

Example Planned Audit Approach – Audited Collective Investment Funds

- Where fund AFS and plan measurement dates are different
  - Consider description of controls and tests of operating effectiveness included in applicable SAS 70 report(s)
  - Assess risk associated with gap in measurement dates
    - Consider investment adv/mgr performance analysis (generally quarterly, may be available monthly)
    - Consider established benchmarks, such as:
      - S&P 500 Index – stock funds
      - MSCI EAFE Index – international stock funds
      - Wilshire US REIT – real estate investment trusts

Example Planned Audit Approach – Audited Collective Investment Funds

- Where fund AFS and plan measurement dates are different (continued)
  - Obtain periodic internal/unaudited financial statements or other reporting for the funds and holdings for gap period
  - Compare fund performance to established benchmark/robust analytics may be effective as a substantive audit procedure (critical the auditor expectations are developed and documented)
  - Evaluate evidence supporting consistency in reporting/valuation, fund investment strategy, etc.

Example Planned Audit Approach – Audited Collective Investment Funds

- Where fund AFS and plan measurement dates are different (continued)
  - Absent evidence to the contrary, document conclusion regarding consistency in valuation and calculation of NAVPS at fund level and agree fund NAVPS to plan management's accounting/reporting (e.g., trust/custodial statements) as of the financial statement date
    - Where we are unable to conclude based upon the above approach – price testing of underlying portfolio holdings may be necessary; see further procedures related to risk assessment and sampling under 'unaudited investment funds' in the following illustration

Example Planned Audit Approach – Unaudited Investment Funds

- Obtain
  - Internally prepared/unaudited financial reports, if available
  - SAS 70 report covering portfolio investment valuation and calculation of NAVPS, if available
  - Other documentation supporting/describing underlying portfolio investment holdings and valuation methodology

Example Planned Audit Approach – Unaudited Investment Funds

- Consider any available fund performance analysis and established benchmarks
  - Often investment entity internal audit/compliance department may be a good source of information and/or starting point; client service rep will generally not be expected to provide audit support needed

Example Planned Audit Approach – Unaudited Investment Funds

- Disaggregate plan investments/underlying investment portfolios based upon nature and risk in order to perform appropriate risk assessment and design appropriate substantive audit procedures
  - Due to the fact that it may be difficult to establish an appropriate level of TOCs assurance; generally will require a monetary sample for purposes of price testing underlying portfolio investment valuation

Example Planned Audit Approach – Unaudited Investment Funds

- Sample size will be driven by assessed risk level and performance materiality
- Risk assessment may include
  - Evidence of controls (consider design/implementation vs. operating effectiveness) at investment entity level related to portfolio holding valuation and calculation of NAVPS
  - Plan sponsor level monitoring controls (design/implementation per risk assessment process)
  - Nature/complexity of portfolio investment strategy and underlying holdings
- Domestic equities/mutual funds vs. debt instruments vs. alternative/complex financial instruments vs. real estate, etc.

Example Planned Audit Approach – Unaudited Investment Funds

- Risk assessment may include (continued)
  - Transparency related to other factors involved in calculating NAVPS at fund vs. plan level
- Consider expense formulas, cash holdings, etc.
  - Sophistication of fund accounting personnel (in-house vs. outsourced to professional fund accounting organization)
  - Frequency of the valuation process
  - Manual vs. automated nature of calculation and related inputs
  - Historical errors

Example Planned Audit Approach – Unaudited Investment Funds

- Performance materiality calculated at the plan level
  - Further consider
- Materiality of plan's individual investment holdings
- When taking a deeper dive into the underlying investment portfolios of the plan's individual investments, consider value of portfolio holdings relative to impact on NAV/NAVPS and then compare to plan level performance materiality for purposes of identifying any underlying portfolio investments that may require 100% testing prior to calculating the required sample size from remaining population (i.e., after identifying individually significant items)

Example Planned Audit Approach – Unaudited Investment Funds

- Note: Due to the varying levels of complexity and number of portfolio holdings among such investment funds, it is unlikely that one can arrive at a 'one-size-fits-all' approach; will require auditor judgment based upon the risk assessment performed in order to arrive at appropriate further audit procedures in response to the risks identified for the plan and the individual investments

Employee Benefit Plans Audit Quality Center Update

Ian A. MacKay, CPA

Ian A. MacKay, CPA

Director, Federal Regulatory Affairs
AICPA

Mr. MacKay is responsible for directing the Employee Benefit Plan Audit Quality Center; monitoring Federal government activities (other than tax and governmental accounting) and communicating issues to AICPA members, providing technical assistance on federal legislation; liaising with Federal government agencies on audit and accounting matters, and monitoring and commenting on proposed regulation.

Mr. MacKay is a graduate of the College of William and Mary and an adjunct professor at George Washington University.

AICPA Employee Benefit Plan Audit Quality Center

Employee Benefit Plan Audit Quality Center Update

Ian MacKay, Director, EBPAQC

EBPAQC Executive Committee

Bob Lavenberg, *Chair*	**BDO USA, LLP**
Michael Cecere	**Gray, Gray & Gray, LLP**
James Haubrock	**Clark, Schaefer, Hackett & Co.**
Don Holmes	**PricewaterhouseCoopers LLP**
Hal Hunt	**Mayer Hoffman McCann P.C.**
Ilene Kassman	**KPMG LLP**
Heidi LaMarca	**Windham Brannon PC**
Bertha Minnihan	**Moss Adams LLP**
Lynne McMennamin	**McGladrey and Pullen LLP**
Susan Peirce	**Apple Growth Partners**
Patricia Schmitt	**Perkins & Company, P.C.**
Darrell Schubert	**Ernst & Young LLP**
William Seymour	**SB & Company, LLP**
Alice Wunderlich	**Deloitte & Touche LLP**

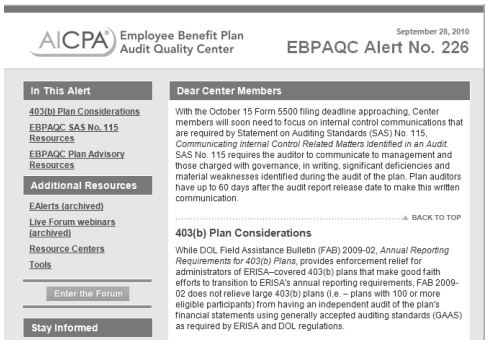
Ian MacKay, Director
Sue Hicks, Senior Manager
Shelly Desbois, Manager
Cynthia Dillon, Administrator

EBPAQC Membership

- **2,069 firm members**
  - Over 200 new member firms in past year
  - 100% of firms that perform over 100 ERISA audits are members (82 firms)
  - 33% of member firms perform 5 or less ERISA audits
- **Member firms audit over 75% of all ERISA plans**
- **82 firms from Florida**

EBPAQC EAlerts

- 40 EAlerts issued in the past year
- Are you sharing them with your staff?
- Also archived on EBPAQC website



AICPA Employee Benefit Plan Audit Quality Center

September 28, 2010

EBPAQC Alert No. 226

In This Alert

403(b) Plan Considerations

EBPAQC SAS No. 115 Resources

EBPAQC Plan Advisory Resources

Additional Resources

EAlerts (archived)

Live Forum webinars (archived)

Resource Centers

Tools

Enter the Forum

Stay Informed

Dear Center Members

With the October 15 Form 5500 filing deadline approaching, Center members will soon need to focus on internal control communications that are required by Statement on Auditing Standards (SAS) No. 115, *Communicating Internal Control Related Matters Identified in an Audit*. SAS No. 115 requires the auditor to communicate to management and those charged with governance, in writing, significant deficiencies and material weaknesses identified during the audit of the plan. Plan auditors have up to 60 days after the audit report release date to make this written communication.

BACK TO TOP

403(b) Plan Considerations

While DOL Field Assistance Bulletin (FAB) 2009-02, *Annual Reporting Requirements for 403(b) Plans*, provides enforcement relief for administrators of ERISA–covered 403(b) plans that make good faith efforts to transition to ERISA's annual reporting requirements, FAB 2009-02 does not relieve large 403(b) plans (i.e. – plans with 100 or more eligible participants) from having an independent audit of the plan's financial statements using generally accepted auditing standards (GAAS) as required by ERISA and DOL regulations.

Live Forum Webinars

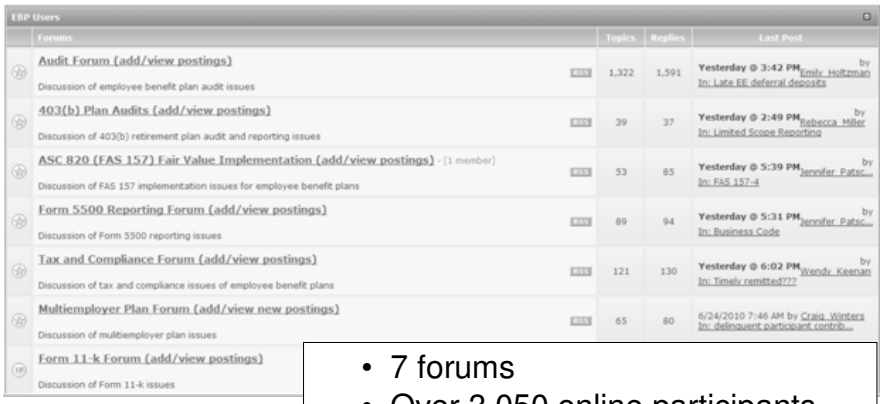
- **Hosted 10 webinar events in past year**
  - Archived (audio and presentation)
  - Very popular
  - CPE option

  - Audit Sampling in Employee Benefit Plan Audits- Roundtable Discussion (June 8)

More webinars to be announced…

- Investment products
- Tax compliance testing
- Others

Member-to-Member Discussion Forum

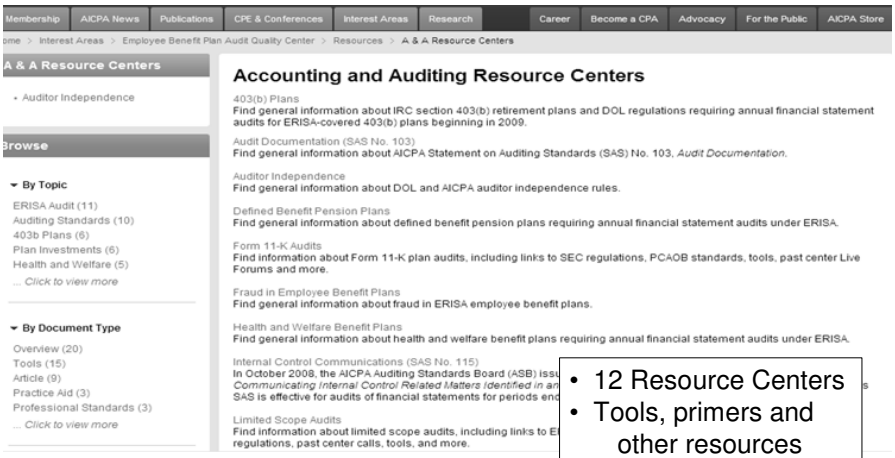


EBP Users

Forums	Topics	Replies	Last Post
Audit Forum (add/view postings) Discussion of employee benefit plan audit issues	1,322	1,591	Yesterday @ 3:42 PM by Emily Holtzman In: Late EE deferral deposits
403(b) Plan Audits (add/view postings) Discussion of 403(b) retirement plan audit and reporting issues	39	37	Yesterday @ 2:49 PM by Rebecca Miller In: Limited Scope Reporting
ASC 820 (FAS 157) Fair Value Implementation (add/view postings) · [1 member] Discussion of FAS 157 implementation issues for employee benefit plans	53	85	Yesterday @ 5:39 PM by Jennifer Patsc... In: FAS 157-4
Form 5500 Reporting Forum (add/view postings) Discussion of Form 5500 reporting issues	89	94	Yesterday @ 5:31 PM by Jennifer Patsc... In: Business Code
Tax and Compliance Forum (add/view postings) Discussion of tax and compliance issues of employee benefit plans	121	130	Yesterday @ 6:02 PM by Wendy Keenan In: Timely remitted???
Multiemployer Plan Forum (add/view new postings) Discussion of multiemployer plan issues	65	80	6/24/2010 7:46 AM by Craig Winters In: delinquent participant contrib...
Form 11-k Forum (add/view postings) Discussion of Form 11-k issues			

- 7 forums
- Over 3,050 online participants
- 1,950 topics posted
- Valuable resource for smaller firms

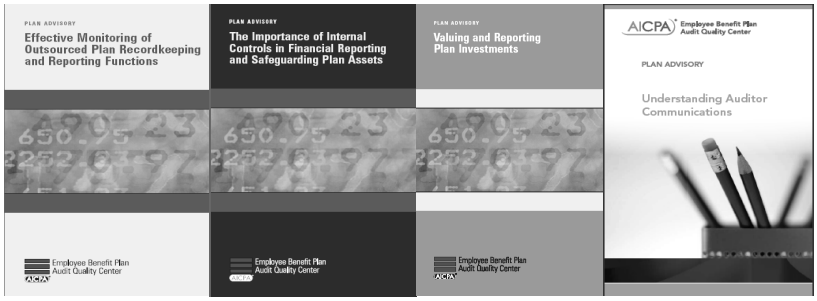
Online Resource Centers



- 12 Resource Centers
- Tools, primers and other resources
- Plan Sponsor resource center

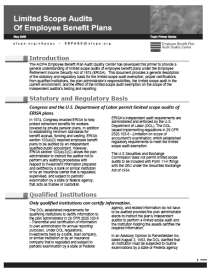
Plan Advisories

- **Monitoring Outsourced Recordkeeping and Reporting**
- **Internal Controls**
- **Plan Investments**
- **Understanding Auditor Communications**



EBPAQC "Topix" Primers

- Plan Investments in Bank Collective Investment Funds
- Limited Scope Audits
- 403(b) Plans
- Alternative Investments in Employee Benefit Plans
- Stable Value Funds and Investment Contracts
- Plan Sponsor Subsidies Under the Medicare Prescription Act
- Cash Balance Plans


Limited Scope Audits
Of Employee Benefit Plans

Introduction

Statutory and Regulatory Basis

Qualified Institutions

EBPAQC Tools and Aids

- Responding to Requests for Proposals
- Firm Preparedness Checklist for Employee Benefit Plans
- Common EBP Audit Deficiencies
- ERISA Audit Inventory and Staffing Schedule
- Internal Inspection Tool
- SAS No. 70 Review Checklist
- FASB Accounting Standards Codification™

Plan Investment Resources

- **Assessing the Fair Values of Your Plan Investments: Considerations for Plan Management in Understanding How Fair Values Are Determined under FASB Statement No. 157, Fair Value Measurements**
- **Illustrative Fair Value Disclosures**
- **FASB ASC 820 Plan Sponsor FAQs**
- **Archived EBPAQC Live Forum webinars – FAS 157 Q&A; FAS 157 Implications to Employee Benefit Plans;**
- **Plan Advisory, Valuing and Reporting Plan Investments**
- **“Topix” Primer, Alternative Investments in Employee Benefit Plans**
- **"Topix" Primer, Stable Value Funds and Investment Contracts—An Overview**
- **AICPA Alternative Investments – Audit Considerations, A Practice Aid for Auditors**

Limited Scope Audit Resources

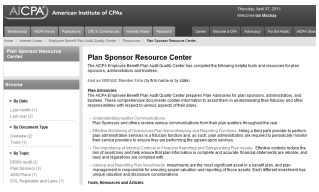
- **“Topix” Primer, Limited Scope Audits of Employee Benefit Plans**
- **Limited Scope Decision Tree**
- **Excerpts from past employee benefit plan audit risk alerts**
- **EBPAQC Live Forum webinar archive-Limited Scope Audits, Basics and Beyond**
- **Links to DOL regulatory information**

403(b) Plan Resources

- 403(b) Plan Audit Frequently Asked Questions
- "Topix" Primer, 403(b) Plans
- 403(b) Filing and Audit Requirements
- 403(b) Getting Started: Meeting the New Form 5500 Reporting and Audit Requirements
- 403(b) Questions to Expect from Your Plan Auditor
- 403(b) Sample Auditor Request List for Plan Information
- EBPAQC 403(b) Plan Audit Live Forum archives (2 Webinars)
- DOL contact information for 403(b) questions
- Links to other resources

Plan Sponsor Resources

- Audit Quality and Auditor Selection
- Article: Quality Counts for Your Plan's Financial Statement Audit
- RFP and Auditor Evaluation Process Checklist
- Find a Center Member by firm (alpha or state name)
- Plan Advisories
- DOL/Regulatory Resources



EBPAQC Marketing Toolkit

- Sample General Announcement to All Firm Staff
- Sample Announcement to Employee Benefit Plan Audit Staff (granting access to website)
- EPBAQC Press Release and Press Relations Guidelines
- EBPAQC Logo Usage and Guidelines
- Client Communication
- Client Talking Points
- Newsletter Sample
- Sample Web site Text
- Networking Strategies
- Marketing Strategies

Audit Quality and Auditor Qualifications

" Many of the annual reports filed contain substandard audit reports…The Department believes that the integrity of the annual report would be improved and Congressional intent better served if the Secretary were permitted to set certain qualification standards for IQPAs who seek to audit employee benefit plans as well as provide accountability for accountants and others responsible for the integrity of the annual report."

DOL Assistant Secretary Phyllis Borzi before the Senate Committee on Health, Education, Labor and Pension October 7, 2010

EBPAQC Task Forces

EBP Auditor Qualifications Task Force- Develop an AICPA/EBPAQC position paper and strategy for recommending enhanced ERISA plan auditor qualifications.

Limited Scope Audit Task Force- Work with the DOL EBSA and industry groups to implement recommendations related to limited scope audits.

403(b) Audit Alternatives Task Force - Work with the DOL EBSA to analyze and evaluate the results of 2009 plan year 403(b) audit filings and develop recommendations for alternative approaches to a GAAS/GAAP audit of 403(b) plans.

SAS 70/SSAE 16 Task Force – Address EBP implementation issues with new service auditor attestation and audit standards.

Questions?

AICPA® Employee Benefit Plan Audit Quality Center

Most Often Asked Questions of Plan Audit Tax Specialist

Carlette Prince, Esq.

Carlette Prince, Esquire

Senior Manager

Deloitte Tax LLP

Global Employer Services/Compensation & Benefits

Carlette has more than eleven years of experience in public accounting, the last nine of which have been focused exclusively in the employee benefits and executive compensation areas. Carlette provides assistance to clients with respect to retirement plan compliance reviews including assisting with corrections under IRS' Employee Plans Compliance Resolution System, tax compliance reviews of benefit plans in conjunction with the annual employee benefit plan audit, retirement plan consulting such as plan drafting and vendor searches as well as Forms 5500 and Forms 990/990-T compliance.

Carlette currently serves as engagement manager for over 600 Signature-Ready Forms 5500 for a large retirement plan vendor.

Deloitte.

2011 FICPA Employee Benefit Plans Conference Most often asked questions of plan audit tax specialists

May 26, 2011

Carlette Prince
Global Employer Services
Deloitte Tax LLP

Agenda

Why do I need the tax specialist in my audit?

Top 10 compliance issues

Most frequently asked questions
- Mergers & acquisitions
- Forfeitures
- 403(b) related
- UBIT
- Schedule C
- Late deposits of deferrals
- Definition of compensation
- Nondiscrimination testing

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Agenda (cont.)

Additional considerations
- Footnotes to the financial statements
- E-filing
- Audit report
- Preparing the return for submission
- Required amendments
- IRS determination letter
- Form 8955-SSA

Annual review of plan by tax specialist

Background

- Basic audit requirement
  - Retirement plans with 100 or more participants, where the 80-120 rule does not apply
  - Funded health and welfare benefit plans with 100 or more participants, where the 80-120 rule does not apply

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Why do I need the tax specialist in my audit?

Why do I need the tax specialist in my audit?

- Assess tax status
  - Department of Labor regulation merely requires that notes to the financial statements provide “information whether or not a tax ruling or determination letter has been obtained”
  - Tax status of plan must be considered to determine whether there is a possibility of claims and assessments affecting plan assets resulting from a loss in tax exemption

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Why do I need the tax specialist in my audit? (cont.)

- Assess tax status (cont.)
- AICPA suggests:
  - Reviewing IRS determination letter or opinion letter from counsel. If plan is amended subsequent to IRS letter, review aspects of plan relevant to plan's tax-exempt status
  - Inquiring about the plan's operations regarding;
    - Minimum coverage
    - Minimum participation
    - Nondiscrimination testing
    - Limitations on contributions
    - Top heavy testing
    - Exclusive benefit rule
    - Diversification of certain employer security holdings
  - Reviewing other audit findings and considering tax impact

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Why do I need the tax specialist in my audit? (cont.)

- Tax specialist role
  - Assess compliance with rules and regulations and note red flags that may indicate noncompliance
  - For red flags, assess whether an operational or documentary violation has actually occurred
  - For actual violations, help assess impact on the plan and analyze plan sponsor's response
  - Form 5500 reconciliation and reporting questions

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Top 10 compliance issues

Top 10 issues compliance issues

- Compliance issues
  - The IRS has issued “Top 10” lists that summarize issues of focus during an IRS audit and common compliance issues:
    - Top 10 issues — EPTA
      - IRS list developed to focus IRS audits of plans with 2,500 or more participants
      - “Top 10” items IRS considers in big case audits
    - Top 10 Issues — VCP
      - IRS list of top 10 issues identified in applications to approve corrections of significant plan errors

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IRS top 10 issues lists

Employee plan team audits

1. Termination or partial termination
2. Acquisitions
3. Nondiscrimination tests
4. Compensation
5. Plan document — Updates for new laws/regs
6. Vesting
7. Distributions and loans
8. Assets — Lack of diversification
9. Limits (415–402(g))
10. Plan internal controls

Voluntary correction program

1. Plan document — Updates for new laws/regs
2. Compensation
3. Inclusion/Exclusion participants
4. Plan loans
5. Impermissible in-service distributions
6. Minimum distributions failure
7. Employer eligibility issues
8. Nondiscrimination tests
9. Top-heavy tests
10. 415 Limit violations

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Most frequently asked questions

Question #1

If the company had a merger/termination during the year, what should we consider regarding its benefit plan(s)?

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Answer #1: Merger considerations

- Risks/exposure (reasons for due diligence)
  - Technical exposure: risk of inconsistent or incorrect plan terms, discrimination tests, or operation
    - Potential issue: the possibility of disqualification by the IRS, if the plan is a qualified retirement plan, or investigation by the U.S. Department of Labor for ERISA violations
    - Don't forget the final Form 5500 if there is a short plan year as a result of the company transaction
  - Economic exposure: risk of additional payments by the acquiror above the true value of the company
    - Potential issue: additional payments for retiree medical expenses, employee benefits, and golden parachute payments

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Answer #1: Items for consideration

- Due diligence checklist:
  - Asset, merger or stock purchase
  - Document review
    - Plan document, summary plan description, loan program, etc.
  - Operational review of plans
    - Compliance with terms and rules under IRS regulations and ERISA
    - Defined contribution — check nondiscrimination testing, compliance with IRS/ERISA, contribution limits, timeliness of deferral remittance
    - Defined benefit — minimum funding standards, PBGC reporting and annual benefit limits

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Answer #1: Additional considerations

- Termination of plan:
  - Can the plan be terminated?
  - File Form 5310
    - Voluntary filing with IRS for determination letter on termination of plan
    - Provides comfort regarding the termination
- Merger of plan:
  - Make sure no cut-back of benefit (anti-cutback)
  - Maintain records, IRS/DOL can audit up to 3 years after final Form 5500 is filed
  - Continued separate operation
  - Will the plan(s) pass nondiscrimination testing?

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Question #2

What are some items we need to consider regarding the treatment of plan forfeitures?

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Answer #2: Know how forfeitures are used

- Plans may use forfeitures to:
- Reduce future employer contributions
- Allocate as an additional contribution (similar to an additional profit sharing or discretionary contribution)
- Pay plan expenses
- Use of forfeitures must comply with plan document's terms:
- Plan may provide for different treatment for different types of forfeitures (e.g., use forfeited match to offset future match, but allocate forfeited discretionary contributions)
- Plan may stipulate period in which allocation must occur
- Master trusts
  - Track forfeitures by plan so that one plan's forfeitures are not used for another plan
- Annual allocation to $0 is required (not a 12/31 $0)

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Answer #2: Forfeiture issues — Prevention and correction

- Know what the plan document says regarding use of forfeitures
- If forfeitures have been accumulated in plan for years:
  - Use all in the current year in accordance with the plan document
- For forfeitures used to pay unreasonable plan expenses, make the plan whole from the sponsor's assets
  - DOL's Voluntary Fiduciary Correction Program, published April 19, 2006

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Question #3

Are there any items we should consider specific to the 403(b)?

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Answer #3: 403(b) Considerations

- New reporting rules for 403(b) plans (2009)
  - DOL final regulations remove limited reporting exemption for 403(b) plans
  - 403(b) plans that are subject to ERISA have the same reporting requirements as qualified plans
- DOL Field Assistance Bulletin 2009–2: Excludes contracts from plan assets which meet all of the following:
  - Contract issued prior to January 1, 2009
  - No contribution obligation and no contributions after December 31, 2008
  - All rights under the contract are enforceable solely by the employee/beneficiary
  - Employee is fully vested in the contract

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Answer #3: 403(b) Considerations (cont.)

- Audit concerns
  - How to identify contracts that are part of the plan:
    - Contracts issued by providers no longer providing plan services
    - Contracts issued to participants no longer employed
    - Assets not held in "trust" — individual annuity/custodial contracts
  - Validating opening balance
  - Multiple vendors may be involved
    - How are plan limits monitored
    - May need to consider condition of records and controls over multiple vendors for risk assessment
  - Differences between 403(b) plans and qualified plans
    - Eligibility/testing/limits
    - Loans by the vendor to participants (vs. participant loans)

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Question #4

Is the VEBA or qualified plan subject to Unrelated Business Income Tax?

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Answer #4: UBTI can sometimes be generated

- Qualified plans are not subject to income tax
- Certain circumstances may give rise to Unrelated Business Income Tax in an otherwise tax-qualified plan
- Required filing: Form 990-T and, in many cases (including Florida), a state tax return
  - Note: earlier filing date for 990-T's for a 401(a) trust than for a 501 trust

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Answer #4: How UBTI can be generated

- Funded welfare plans — VEBA overfunding
  - If year end assets exceed actual claims payable plus IBNR, the excess (or trust earnings, if lower) for the year is subject to UBIT
    - Postretirement medical liabilities are not counted
    - Assume postretirement welfare benefits cause UBTI unless employer submits evidence otherwise
- All plans subject to audit
  - Limited partnerships, mortgage-backed securities, etc.
  - Examine K-1 — usually found in the notes to the K-1 (check line 20, particularly Code V)

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Answer #4: UBTI exclusions

- Excluded from UBTI
  - Employee-pay-all VEBA
  - Union VEBA (must be a separate trust from non-union)
  - Incurred but not yet reported claims
  - Retiree life insurance set aside (should be evidenced by actuarial report)
  - Disability claims incurred during year but not yet paid
  - Investments all in municipal bonds
  - 419A limits for welfare benefits may be combined. This combination may exclude additional income from taxation

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Answer #4: Sample rep language if plan is subject to UBIT

- Sample UBTI rep
  - We are aware that during 2010 our VEBA trust was overfunded and subject to Unrelated Business Income Tax (UBIT). We represent that we will file the Form 990 and 990T, if applicable, and pay the UBIT in a timely manner

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Question #5

Why is the plan we are auditing requesting Schedule C information and what do we need to provide?

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Answer #5: What do we need to provide?

- Typically will need to provide the following:
  - Accounting firm name
  - Accounting firm EIN/address
  - Amount of direct fees/Expenses
  - Whether or not received any indirect compensation (note: audit firms typically would not receive indirect compensation)
  - Also confirm if we paid any non-monetary compensation in connection with the plan

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Answer #5: Challenges to new Schedule C

- Plan sponsor challenges
  - Learning e-filing process and technology
  - Understanding how the form has changed
  - Collection of additional Schedule C information
  - Reporting service providers who don't comply
- How audit can help
  - Remind plan sponsors to reach out now to service providers who might not be aware of these rules
  - Encourage plan sponsors to review fee information provided and question missing or incomplete information

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Question #6

How do late deposits of 401(k) deferrals and participant loan repayments impact the financial statements?

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Answer #6: When is a deferral "late"

- 29 CFR §2510.3-102 Definition of "plan assets"— participant contributions
- Maximum time period for pension benefit plans
  - In no event shall the date occur later than the 15th business day of the month following the month in which the participant contribution amounts are received by the employer
  - This 15 day rules is not a safe harbor

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Answer #6: When is a deferral "late" (cont.)

- DOL view for determining late deposits
  - Determination is based on how quickly an employer can deposit money. If within 1 business day, deposits after 1 day are generally late. If within 5 business days, then 5 business days would be the standard
  - Also look for consistency throughout the year

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Answer #6: Late deposit — Safe harbors

- Safe harbors?
  - For small plans (< 100 participants) — regulations include 7 business day safe harbor
  - For large plans (> 100 participants) — DOL is considering
    - Large companies tend to have more sophisticated payroll systems
    - Have back-up employees for payroll processes

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Answer #6: Prevention and correction

- Set a policy and follow it
- Prohibited transaction subject to 15% excise tax under Internal Revenue Code ("Code") §4975 — report and pay via Form 5330
  - Potential additional step: use DOL's correction program (see DOL's Voluntary Fiduciary Correction Program — VFCP) Does not exempt employer from filing. Provides additional security around resolution
- Lost earnings must be funded to the plan and allocated to participant accounts for the time period between the administratively feasible date and the date actually remitted

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Answer #6: Sample rep language (questionable contributions are not late)

- On late deposit of deferrals
  - We have consulted with our ERISA counsel regarding the timing of our deferral contribution deposits and in our counsel's opinion the timing of our deposits would not be considered late. Accordingly we do not believe that these contributions would constitute a prohibited transaction

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Answer #6: Sample note disclosure (late deposit)

- Note X. Nonexempt party-in-interest transactions
  - ABC Company remitted the January XX, 2009 participant contributions of $25,000 to the trustee on March XX, 2010, which was later than required by the U.S. Department of Labor Regulation 2510.3-102. The Company filed Form 5330 with the Internal Revenue Service and paid the required excise tax on the transaction. In addition, participant accounts were credited with the amount of investment income that would have been earned had the participant contribution been remitted on a timely basis

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Answer #6: Sample attachment (late deposit)

- Plans disclosing delinquent participant contributions on line 4a must attach the following supplemental schedule
  - Loan repayments may be reported on line 4a (delinquent contributions) or 4d (non-exempt transactions)
  - Report delinquent contributions in year of error and every year thereafter until corrected

Schedule H Line 4a — Schedule of delinquent participant contributions				
Participant contributions transferred late to plan	Total that constitute nonexempt Prohibited Transactions			Total fully corrected under VFCP and PTE 2002-51
Check here if late participant loan contributions are included	Contributions not corrected	Contributions corrected outside VFCP	Contributions pending correction in VFCP	

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Question #7

What should we consider if the plan uses the incorrect definition of compensation?

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Answer #7: Failure to apply Plan's Definition(s) of Compensation

- "Compensation" definition(s) are critical for accurately calculating participant deferrals, employer contributions, ADP and ACP tests
- Know the definition of compensation
  - Does the plan use multiple definitions
  - For initial year of participation (Full year or from entry date)
- Know which "compensation" elements are included and excluded for various plan purposes
  - Bonus pay
  - Vacation pay
  - Elective deferrals
  - Overtime pay
  - Commission pay

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Answer #7: Failure to apply Plan's Definition(s) of Compensation — Prevention and correction

- Did the plan's payroll service provider code eligible compensation to match the plan's provision?
- When payroll conversions/upgrades occur was coding verified?
- If an error occurred, what should we consider
  - Were participants made whole
  - Was the plan document amended (if necessary)

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Answer #7: Sample rep language (over contribution)

- Sample ER contribution error
  - We are aware that during 2010 we over contributed the employer portion of the contributions to a few employees resulting in an amount being improperly credited to the employee's account. In order to avoid jeopardizing the Plan's tax status, we have calculated the amount(s) to be distributed from the employees accounts into the forfeiture account and will use these amounts, including allocable earnings, to reduce future employer contributions as soon as possible

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Answer #7: Sample footnote disclosure (under-contribution)

- Note X. Federal Income Tax Status
- The Internal Revenue Service has determined and informed the Company by a letter dated August 9, 20XX, that the Plan and related trust were designed in accordance with the applicable regulations of the IRC. **During 2010, incorrect eligible earnings were used to calculate contribution amounts for certain employees. The Plan Sponsor has taken the necessary corrective action in accordance with the acceptable correction methods of the Employee Plans Compliance Resolution System ("EPCRS"), including repayment of lost earnings on these amounts.** The Plan Sponsor believes the Plan has maintained its tax-exempt status. Therefore, no provision for income taxes has been included in the Plan's financial statements

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Question #8

What if the plan fails nondiscrimination testing?

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Nondiscrimination testing — In general

- Consider which tests are required (depending on the plan's provisions)
  - ADP Test (employee pre-tax deferrals)
  - ACP Test (employee post-tax deferrals and employer matching contributions)
  - 401(a)4 General Test
  - Code §415 test (lesser of $49,000 or 100% of comp for 2010)
- If failure occurs, confirm correction was made timely
- For Safe harbor 401(k) plans, consider which tests (if any) are required

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Additional considerations: Nondiscrimination testing failures — Prevention and correction

- Other testing issues
  - Were all members of the controlled group considered for testing purposes
  - When should employees of newly-acquired entities be included in the tests
  - If the 3-year testing cycle is utilized, consider if it was appropriate

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Additional considerations

Additional considerations

- Check prior year management representation
  - Are there any action items the plan sponsor should have completed during the year
- Proposed ASC 74/wording for tax status note
  - "Accounting principles generally accepted in the United States of America require plan management to evaluate tax positions taken by the plan and recognize a tax liability (or asset) if the plan has taken an uncertain position that more likely than not would not be sustained upon examination by the [Identify applicable taxing authorities]. **The plan administrator has analyzed the tax positions taken by the plan, and has concluded that as of December 31, 20X1, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements. The plan is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The plan administrator believes it is no longer subject to income tax examinations for years prior to 20XX.**"

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Additional considerations (cont.)

- Schedule of assets held attached to financials
  - Do not consolidate similar assets into one line (i.e. Bank Collective Fund A, Bank Collective Fund B, etc. should not be reported on one Collective Fund line)
  - Stable value funds (may need to break down underlying assets)
- Check Form 5500 for reasonableness
  - Does the Schedule H tie to the financials
    - If not, is there a reconciling footnote
  - Are there indirect fees reported on the Schedule C
    - If so, confirm F/S don't say that the Company pays all fees

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Additional consideration: Sample footnote disclosure (expenses)

- Note X. Description of the Plan
- **Expenses** — Certain [enter fee types] fees are paid by the Plan; all other [enter type (e.g. administrative)] expenses are paid by the Company
- Consider the following additional disclosure (if applicable):
- **Investment Valuation and Income Recognition** (include at end of section)
- Management fees and operating expenses charged to the Plan for investments in the mutual funds are deducted from income earned on a daily basis and are not separately reflected. Consequently, management fees and operating expenses are reflected as a reduction of investment return for such investments

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Additional considerations: Electronic filing

- DOL has mandated electronic filing for all Form 5500 filers for plan years beginning on or after January 1, 2009
  - Amended (or delinquent) returns:
  - EFAST2 — Input correct plan year on 2010 Form
- Exception — Certain prior year schedules must be included as "other attachments" (B, SB, MB, E, P, R T)
  - DOL Notices
  - E-file amended return through EFAST2
  - Send copy to separate DOL address

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Additional considerations: Audit report

- DOL FAQ 24 provides that an audit report from an IQPA must be attached
  - As PDF
  - On auditor's letterhead (with auditor's address)
  - Signed/dated
- Issues arose under EFAST2 due to:
  - Encrypted or password protected audit reports (causes rejection of 5500 filing)
  - DOL also wants the audit report to be "searchable"
  - Preparer best practice: check final audit reports ahead of time, alert plan sponsors and auditors of risk of rejection
- Dilemma — Auditors don't want audit report "separated" though Sch. H, but some e-filing programs (ex. Relius) may require separate attachments
- Consider developing standard best practice such as attaching the entire audit report where attachments are called for

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Additional considerations: Preparing the return for submission

- Attachment formats (low resolution settings suggested)
  - Audited financial statements on letterhead with “wet” signature and in PDF format
  - Actuarial schedules signed by actuary in PDF format
  - All other attachments can be in TXT or PDF format
  - Do not attach Form 5558 Extension (filed with IRS)
  - Do not attach Schedule SSA (Form 8955-SSA filed with IRS)
    - Generally will no longer have PII issue
    - Be on the lookout for service providers who inadvertently include SSA information

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Additional considerations: Required amendments

- Pension Protection Act of 2006 (PPA)
  - Deadline for most amendments — last day of the first plan year that began on or after January 1, 2009
  - Notice 2009-97 extended some to the last day of the first plan year that begins on or after January 1, 2010
    - Limits on benefits and accruals for single-employer DB plans
    - Vesting, ceasing or limiting accruals applicable to cash balance & other DB plans
    - Diversification requirements for DC plans

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Additional considerations: Required amendments (cont.)

- Heroes Earnings Assistance and Relief Tax Act of 2008 (HEART)
  - Deadline for most amendments — last day of the first plan year that began on or after January 1, 2010
    - Inclusion of differential wage payments for purposes of Code section 415
    - Optional inclusion of differential wage payments — calculate benefits/contributions/non-discrimination testing
    - Eligibility of >30 days active duty receive distributions of elective deferrals
    - Additional benefits for survivors of participants who die while performing military service
    - Optional benefit accruals for disability/death while performing military service

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Additional considerations: Required amendments (cont.)

- Worker, Retiree and Employer Recovery Act of 2008 (WRERA)
  - Adopt suspension of required minimum distributions in 2009
    - Last day of the first plan year that began on or after January 1, 2011
    - Can choose to adopt at the same time as the HEART amendments

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Additional considerations: IRS determination letter — Individually designed plans

Employer EIN ends in	Plans cycle is	Last day of EGTRRA amendment period	Next 5 year cycle ends
1 or 6	Cycle A	January 31,2007	January 31, 2012
2 or 7	Cycle B	January 31, 2008	January 31, 2013
3 or 8	Cycle C	January 31, 2009	January 31, 2014
4 or 9	Cycle D	January 31, 2010	January 31, 2015
5 or 0	Cycle E	January 31, 2011	January 31, 2016

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Additional considerations: IRS determination letter — Prototype plans

Type of prototype document	Initial cycle began	Initial cycle ends	Next 6 year cycle ends
Defined contribution	February 1, 2005	January 31, 2006	January 31, 2011
Defined benefit	February 1, 2007	January 31, 2008	January 31, 2013

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Additional considerations: IRS Form 8955-SSA

- Form 8955-SSA replace Schedule SSA
  - Filed separately with the IRS, not DOL
  - Due date: same as Form 5500, last day of 7th month following end of plan year
  - Extension can be obtained — Form 5558 (revised draft requires signature for extension of 8955-SSA but not 5500)
  - Special due date for 2009 — the later of the due date for the 2010 Form 5500 or August 1, 2011
  - Form 8955-SSA not yet released, but should be soon
  - **Do not** attach to the Form 5500

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Annual review of plan by tax specialist should include

- Form 5500 accuracy
  - Compliance with changes implemented with 2009 return
- Annual non-discrimination testing
- Review plan document/amendments
- Employee contribution timing
- Unrelated business income tax
  - VEBA's — overfunded
  - Qualified plans — Types of investments?
- IRS determination letter/IRS exemption letter/filing cycle compliance

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Annual review of plan by tax specialist should include (cont.)

- Plan forfeitures, proper use of
- Plan loans, proper reporting
- Prohibited Transactions
- Plan termination/partial or full
- Financial Statements/tax status footnote
- Substantive testing — administrative error detection and proper and timely correction

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