Employee Benefit Plans Audit Expectations

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PURPOSE OF THE AUDIT

The Employee Retirement Security Act of 1974 (ERISA) generally requires employee benefit plans with 100 or more participants to have an independent financial statement audit as part of the plan sponsor's obligation to file a Form 5500.

Financial statement audits provide an independent, third-party opinion to participants, plan management, the DOL and other interested parties that the plan's financial statements provide reliable information to assess the plan's present and future ability to pay benefits. A financial statement audit helps protect the financial integrity of the employee benefit plan, which helps users determine whether the necessary funds will be available to pay retirement, health and other promised benefits to participants. The audit may also help plan management improve and streamline plan operations by evaluating the strength of the plan's internal control over financial reporting and identifying control weaknesses or plan operational errors. And the audit helps the plan sponsor carry out its legal responsibility to file a complete and accurate Form 5500 for the plan with the Department of Labor (DOL) and Internal Revenue Service (IRS).

The overall objectives of the plan auditor under professional standards are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error and to report on the financial statements in accordance with his or her findings. In addition, the DOL requires the independent auditor to offer an opinion on whether the DOL-required supplemental schedules attached to the Form 5500 are presented fairly in all material respects, in relation to the financial statements as a whole.

To accomplish these objectives, the auditor plans and performs the audit to obtain reasonable assurance that material misstatements, whether caused by error or fraud, are detected. The auditor assesses the reliability, fairness and appropriateness of the plan's financial information as reported by plan management. The auditor tests evidence supporting the amounts and disclosures in the plan's financial statements and DOL-required supplemental schedules; assesses the accounting principles used and significant accounting estimates made by management; and evaluates the overall financial statement presentation to form an opinion on whether the financial statements as a whole are free of material misstatement.

In conducting a plan audit, the auditor has a responsibility to perform procedures with respect to the provisions of ERISA and DOL and IRS regulations that have a direct effect on the determination of material amounts and disclosures in the financial statements. For employee benefit plans, this would include party in interest transactions that may be prohibited by ERISA. When the auditor becomes aware of information concerning a possible prohibited party in interest transaction or other noncompliance with laws and regulations, the auditor obtains an understanding of the nature of the transaction, the circumstances in which it occurred and sufficient other information to evaluate the effect on the financial statements. As part the auditor's consideration of the plan's compliance with laws and regulations, the auditor is required to make certain inquiries and review correspondence with the DOL and IRS. The auditor also considers the effect of the transaction on the financial statements.

AUDIT AREAS

The financial statement audit for employee benefit plans typically cover employee and employer contributions; benefit payments; plan investments and investment income (full scope audits); participant data; participant allocations; liabilities and plan obligations; loans to participants; and administrative expenses. In addition, the auditor considers other matters that may affect the financial statements, as discussed below.

Contributions — The auditor tests contributions from the employee and employer to determine whether the amounts received by or due to the plan are properly determined and recorded and disclosed in the financial statements, and whether any appropriate allowances have been made for uncollectable amounts.

Benefits and Benefit Payments — Benefits are tested to determine whether the payments are in accordance with plan provisions and related documents, whether payments are made to or on behalf of the persons entitled to them and only to such persons, and whether transactions are properly recorded in the proper account, amount and period.

Liabilities and Plan Obligations — The auditor performs tests to determine whether all plan liabilities are reported in the financial statements. In a defined benefit plan, the auditor will test plan obligations to determine that they are properly estimated and reported in the financial statements. Testing plan obligations typically will include using the work of an actuary.

Participant Data and Allocations — The auditor applies procedures to relevant participant data, such as demographic data (e.g., sex, marital status, birth date and period of service); payroll data relevant to determining contributions and benefit payments (e.g., wage rate, hours worked, earnings and contributions to the plan); participant elections (e.g., investment elections and elected deferral rates); and benefit data (e.g., benefit levels and options selected) to determine whether all covered employees have been properly included and whether accurate participant data were supplied to plan management and the plan actuary, if applicable. This work often is done in conjunction with other audit areas such as contributions or benefits testing. The auditor also tests whether investment income has been properly allocated to individual participant accounts.

Investments and Investment Income — In a full scope audit, the auditor applies procedures to determine whether investments are properly recorded, owned by the plan, properly valued as of the financial statement date (generally at fair value), properly presented in the financial statements and the appropriate related disclosures are made, and that investment transactions are made in accordance with the plan's established investment policies. The auditor also tests whether the income from the plan's investments has been properly recorded. In a limited scope audit, the auditor does not audit the certified investment information (investments typically are the most significant plan assets); however, he or she still tests the allocation of investment income to individual participant accounts and evaluates whether investments are properly presented in the financial statements and the appropriate related disclosures are made.

Loans to Participants — Loans to participants and the related interest are tested to determine whether the amounts due the plan have been properly identified, valued, recorded and disclosed in the financial statements.

Administrative Expenses — Expenses may be tested to determine if they are in accordance with agreements, are properly classified and are recorded in appropriate amounts in the proper period.

Other Auditing Considerations — Parties in Interest and Prohibited Transactions. Professional standards require that the auditor be aware of the possible existence of party in interest and material related party transactions that could affect the financial statements or for which DOL reporting regulations require disclosure and be aware of the possibility that noncompliance with laws and/or regulations (including party in interest transactions that may be prohibited by ERISA) may have occurred. They also require that the auditor perform procedures to identify instances of noncompliance with those laws and regulations related to party in interest and prohibited transactions that may have a material effect on the financial statements. Late deposits are a typical example of a prohibited transaction.

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