



Surviving an IRS Audit of Your 403(b) Plan



Part II



Tax Deferred Solutions | 6939 Sunrise Blvd, Suite 250 | Citrus Heights, CA 95610
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4/10/2012

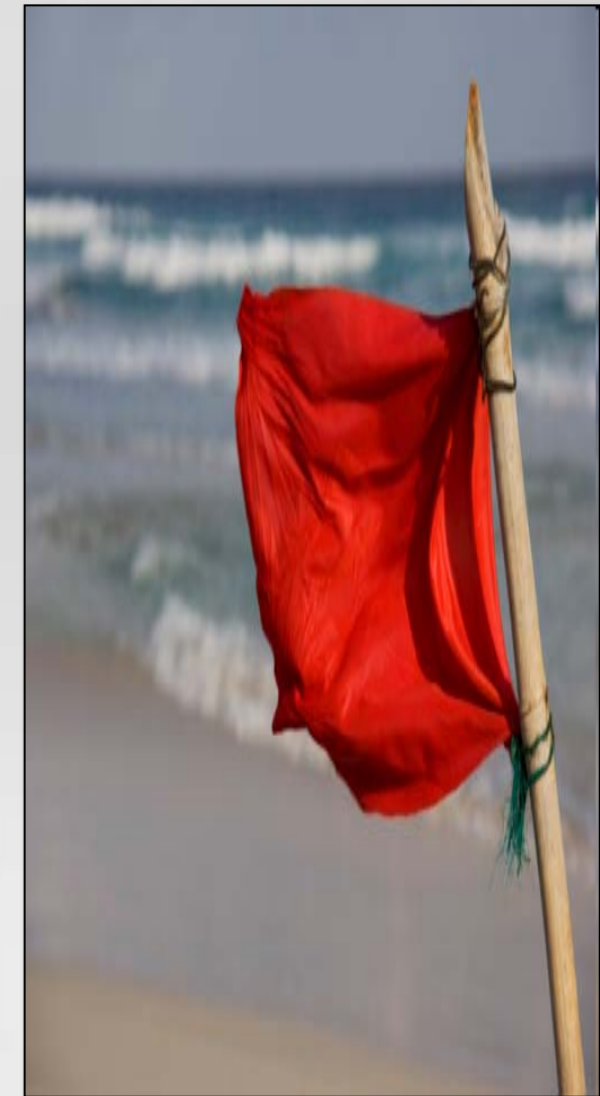
About TDS

- ❖ California's largest independent Third Party Administrator
- ❖ Our priority is education and compliance
- ❖ The only TPA recommended by CSBA



Who will be audited?

- A District that received a questionnaire from the IRS and did not respond.
- A District that received a questionnaire and sent responses that indicated compliance issues.
- W-2's reported by employee differ from employer.
- Completely random.
- **** New Data **** Districts and Offices of Education selected to meet the quota within that particular area.



80% of plans audited by the IRS FAILED!

IRS Audit Red Flags:

- Written Plan Document
- Excess Contributions
- Universal Availability
- Operational Failures

Are you confident that your plan
will meet IRS guidelines?



The Letter You Don't Want (but might receive)

- Only 2-weeks to prepare
- 8-page letter
- 38 individual items to provide

Internal Revenue Service
Tax Exempt and Government Entities Division
TEGE Employee Plans
9350 Flair Dr. 2nd Floor, El Monte, Ca. 91731

Date: 01/27/2012

Department of the Treasury
95-6000777

Name of Plan:
403(b) & 457 Plan
Plan Year(s) Ended:
12/31/2010
Date of Appointment:
Will call you to set up a date in March 2012.
Time of Appointment:
N/A
Place of Appointment:
Person to Contact/ID Number:
Ann Jitpalima/02-35904
Contact Telephone Number:
818-274-0799

Plan Year 2010!

2 weeks to prepare!

Dear Sir:

We are examining your Internal Revenue Code section 403(b) and 457 plan for the above year(s) and have arranged the appointment shown. The attachment lists documents and information needed to conduct our examination. To help make the examination as brief as possible, please have these items mailed to me by 02/17/2012.

If you would like someone else to represent the plan during this examination, you must submit a written power of attorney. Form 2848, *Power of Attorney and Declaration of Representative*, may be used for this purpose.

If you have any questions, please contact me at the telephone number shown above.

Thank you for your cooperation.

Sincerely,



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CSBA Webinar Series

- **How to survive an audit of your 403(b) Plan – Part I**
- **How to survive an audit of your 403(b) Plan – Part II**
- **Three common ‘Universal Availability’ errors and how to fix them.**
- **Plan Participation – Why should you care? Because the IRS does.**
- **Red Flags regarding contribution amounts and limits.**

CSBA Webinar Series

Part I Review

Key Operational Errors

- **Universal Availability**
- **Contribution Limits**
- **Loans**



CSBA Webinar Series

4 More Key Operational Errors



Red Flag # 4

Hardships

Hardships

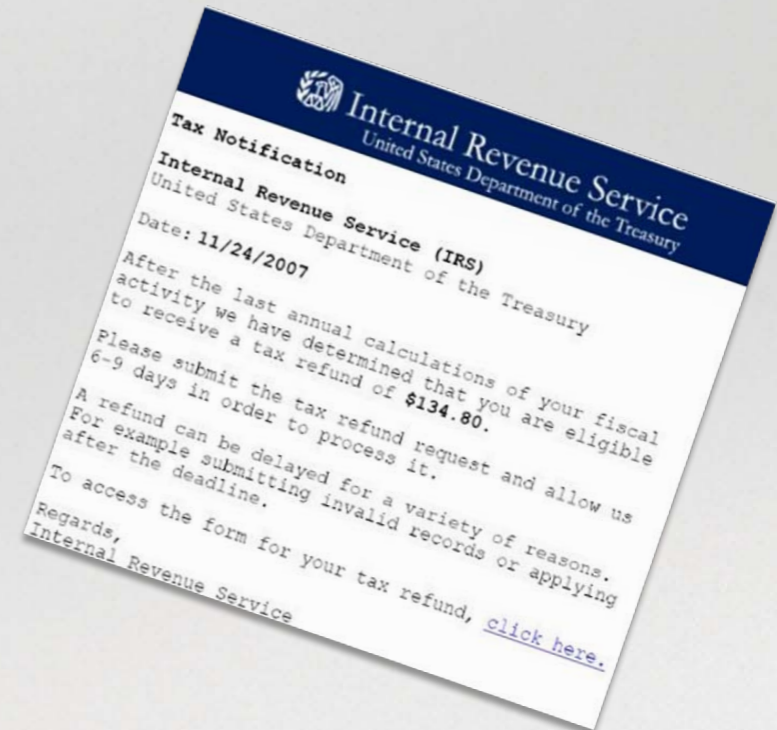
- Hardship must meet specific requirements, with supporting documentation
- 6 month suspension of contributions
- All transactions must be done in accordance with the Plan Document

Red Flag # 4

Hardships

Actual Audit Requests

- A list of all participants who received a hardship distribution
- Copies of the application form with supporting documents to verify eligibility
- Copies of the IRS Form 1099-R for distributions
- Salary deferral history for employees receiving hardship distributions for proof of 6-month suspension (IRS wants to see the system)
- If a Vendor is involved with approving hardships, copy of their procedures, distribution notices and forms



Red Flag # 5

Early Retirement Incentive

Quick Poll...

Does your District or County Office offer an
Early Retirement Incentive?

Yes or No?



Red Flag # 5

Early Retirement Incentive

**This has come up 100% of the time
in a 403(b) Plan audit.**



Red Flag # 5

Early Retirement Incentive

Two things the IRS is looking for:

1. Improper coding
2. Constructive Receipt

Red Flag #5

Early Retirement Incentive

Improper Coding

This happens when an employer contributes funds to a retiree's 403(b) and codes the contribution as income.

Red Flag #5

Early Retirement Incentive

Improper Coding Example

- John Smith retired in June, 2011.
- Part of his Early Retirement Incentive is for his employer to put \$10,000 per year into his 403(b) for the next three years.
- The employer “keeps John on payroll” because that is the only way their system can cut the check to send to John’s 403(b) account.
- It means the employer is paying an employee who is no longer active, and reporting it on the W2 versus sending employer contributions and issuing no W2.

Red Flag # 5

Early Retirement Incentive

Constructive Receipt

Question...

Does your Early Retirement Incentive Contract let the employee choose how they want to receive their money?

Yes or No?

Red Flag # 5

Early Retirement Incentive

Constructive Receipt

- If it does, then...
- according to the IRS, that is non qualified money so it cannot be in the 403(b) Plan.

Red Flag # 5

Early Retirement Incentive

Constructive Receipt

- Constructive receipt refers to income that you do not have physical possession of but it has been made **available** to you **without restriction**.
- Per the IRS, you have constructive receipt of income when you have **control** over the such income.

Red Flag # 5

Early Retirement Incentive

Actual Audit Requests

- **Copies of Incentive Contracts**
- **“Constructive Receipt”**
 - Are employees able to select their incentive option
 - Non-qualified Funds in Plan
- **Contribution Coding**
 - Employee vs. Employer

Red Flag # 6

Proper separation of contributions on W-2

This point has come up 100% of the time during a
403(b) Plan audit



Red Flag # 6

Separation of contributions on the W-2

Box 12 Code E: 403(b) Box 12 Code G: 457(b)

a Control number		d Employee's social security number 999-99-9999		1 Wages, tips, other compensation 41,770.30		2 Federal income tax withheld 1,802.47			
c Employer's name, address, and ZIP code UNIV OF CALIFORNIA - BERKELEY BUSINESS SVCS. - PAYROLL #1104 BERKELEY, CA 94720-1104			b Employer identification number 94-6002123		3 Social security wages 42,391.57		4 Social security tax withheld 2,628.28		
				5 Medicare wages and tips 42,391.57		6 Medicare tax withheld 614.68			
				9 Advance EIC payment		10 Dependent care benefits			
e Employee's name, suffix BEAR, OSKI			f Employee's address and ZIP code 951 BEARS ROAD BERKELEY, CA 94720			12 See Instrs. for Box 12		14 Other	
				12a C 0.00		DCP-CAS 0.00			
				12b E 0.00		DCP-REG 914.29			
				12c G 0.00		INCLUDED IN BOX 01:			
				12d P 0.00		OTHER INC 0.00			
						INTEREST 0.00			
						FRINGES 0.00			
This information is being furnished to the Internal Revenue Service. OMB No. 1545-0008 Department of the Treasury-Internal Revenue Service				11 Nonqualified plans			Form W-2 Wage and Tax Statement 2010		
				13 Statutory Employee <input type="checkbox"/>			Retirement Plan <input checked="" type="checkbox"/>		
							Third-party sick pay <input type="checkbox"/>		
				Copy B. To Be Filed With Employee's FEDERAL Tax Return.					
15 State	Employer's state I.D. No.	16 State wages, tips, etc.	17 State income tax	18 Local wages, tips, etc.	19 Local income tax	20 Locality			
CA	935-0503-0	41,770.30	488.19						

Red Flag # 6

Separation of contributions on the W-2

Why is this an issue?

1. **It's a flag for an audit.**
2. **It allows the IRS to dig.**
 - a. They can expand their audit into other years and open the door to every participant.
3. **Potential sanction.**
 - a. The IRS will have to correct their records – that could translate into a fine.

Take Our Survey and Receive Our Free “IRS Audit Survival Guide”

Special Offer....

At the conclusion of this webinar you will receive a link to a brief survey. Please take a few minutes to tell us what you thought of today’s webinar.

As a way of saying thanks, everyone who completes the survey today will receive the “403(b) Audit Survival Guide” for free.



Red Flag # 7

Timeliness of contributions

What the IRS will review

- **Date the funds leave the District and go to the Common Remitter (if applicable).**
- **Compare that to the date the funds leave the Common Remitter to disburse to the specific Vendors.**
- **Even if the Common Remitter is the delay, the employer (in this case you) are held responsible.**

Red Flag # 7

Timeliness of contributions

Actual Audit Requests

- **Employer Processes**
 - From pay date, to remittal date, to posting date
- **“Administratively Reasonable”**
 - Facts and Circumstances

The End?

Nope...

In two weeks we will present Part 3 of this series and share

Three Common 'Universal Availability' Errors &
How to Correct Them

Mark your calendars for Tuesday, April 17th, 10am
Watch for e-mails from CSBA to register



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