

# The Towering Form 5500 Inferno

By Ary Rosenbaum, Esq.

One of the greatest disaster movies of all time is the 1974 classic “The Towering Inferno.” It took two studios (20th Century Fox and Warner Brothers) to make it. It starred Steve McQueen and Paul Newman who had the same billing and the same amount of lines. It also starred Faye Dunaway, William Holden, Fred Astaire, Robert Wagner, and O.J. Simpson. In terms of potential disaster, your retirement plan’s 5500 could make The Towering Inferno look like a small fire. This is all about the pitfalls of Form 5500.

## What is Form 5500?

Form 5500 is a tax return designed to satisfy the annual reporting requirements under ERISA (which stands for the Employee Retirement Income Security Act and the Internal Revenue Code). Form 5500 is the rate tax form where it’s under review by both the Internal Revenue Service (IRS) and the Department of Labor. By completing and filing the correct version of Form 5500 for their retirement plan, plan sponsors provide the Federal government with key details about their retirement plan’s financial condition, investments, and operations. The purpose of the tax return is to make sure that employee contributions and investments remain protected. Generally, any employer that sponsors a retirement plan must file a Form 5500 each year that the plan holds assets. However, plans with no employees don’t have to file a

Form 5500 until the plan hit \$250,000 in assets or more. Form 5500 must be completed seven months after the end of the month the plan year ends, with an option to extend the deadline for two and a half months. If you have a calendar year-end plan, for example, on December 31, audits must be completed by July 31 of the following year, with an option to extend the filing until October 15.

or 120 if the plan hasn’t been previously audited, and 100 every year after. The new participant counting methodology will count only participants with an account balance at the beginning of the plan year. Prior to this change, the participant count included eligible participants, even if not participating, or participants with an account balance. Most notably, eligible participants who have never participated, and/or do not have account balances due to any form of contributions will no longer need to be counted as participants. A Plan with fewer than 100 participants can use Form 5500-SF and will not require an audit. This participant counting change is effective immediately for plan years beginning on or after January 1, 2023. For Forms 5500 for plan years beginning prior to January 1, 2023, they must follow the old participant count methodology, which includes participants that are eligible but not participating. The audit must be conducted by a Certified Public Accounting (CPA) firm. The CPA must be independent of any other plan provider, and it would be a mistake to hire a firm that doesn’t have the background and expertise to audit a retirement plan. There are a few CPA firms that only

do retirement plan audits and it might be wise to hire a firm like that. The problem with filing a Form 5500 without a required audit is that the government treats it as if you never filed it at all. That brings up the



## The 5500 Audit

Generally, a retirement plan must be audited and the audit must be attached to Form 5500 when it has more than 100 participants on the first day of the plan year—

problem of late filings.

### Late filings

The costliest error is not filing Form 5500 on time. A lot of time, a plan sponsor isn't aware that they are late in filing until they receive a letter from IRS or DOL stating the plan sponsor didn't file one. It's normally a year after it was due and includes a substantial penalty. While there is a 3-year statute of limitations for a filed Form 5500, there is no statute of limitations for a Form 5500 that hasn't been filed. Late-filed returns are subject to penalties from both IRS and DOL, so it's very important to file on time. The IRS penalty for late filing of a 5500-series return is \$250 a day (up to a maximum of \$150,000). The DOL penalty for late filing can run up to

\$2,529 per day, with no maximum. Recently, I received a letter from a potential client where the DOL is demanding an \$86,000 penalty for a late 5500. If a plan sponsor has a late Form 5500 to file, one of the great things out there is the DOL's Delinquent Filer Voluntary Compliance Program (DFVCP). It gives the plan sponsor the opportunity to pay reduced civil penalties for voluntarily complying with the annual reporting requirements, instead of getting a six-digit penalty letter. To be eligible to reduce these potential penalties through the DFVCP, you will have to file the application as a plan sponsor. If the plan is under IRS or DOL audit or you get a penalty letter from either, you are going to find yourself no longer eligible for the DFVCP. Sometimes, your third-party administrator (TPA) is at fault for a late or missing 5500, but the problem is that you will foot the bill.

### The government does read Form 5500

Thanks to the mandatory electronic filing of Form 5500, it is easier for the IRS and DOL to manage the 5500 review process. By streamlining the process, the IRS and DOL can easily review Form 5500s (and attached audit if required) and focus on



some troublesome answers on the form. I believe that some answers on Form 5500 can target a plan sponsor to be audited. The purpose of an audit of Form 5500 is to make sure that plan sponsors voluntarily comply with the Internal Revenue Code and ERISA. Sometimes, an IRS or DOL audit is done randomly and you get the unlucky pick when you're chosen. However, a good deal of the time, it's because of an answer you made on Form 5500, a tax form where you answered under penalties of perjury. For example, if you admit to a serious plan issue such as committing a prohibited transaction or depositing 401(k) salary deferral late, don't be surprised if an IRS or DOL agent calls you to conduct an audit. If you admit on Form 5500 that your plan doesn't have an ERISA bond or not enough bond coverage, that might target you for an IRS or DOL audit. Mistakes by your TPA in the completion of Form 5500 can trigger an audit. For example, I had a plan sponsor client audited, simply because the employer contributions listed on Form 5500 were inconsistent with the tax deduction that the plan sponsor took for those employer contributions on their corporate tax return. If a plan requires a CPA audit attached to Form 5500, any problematic is-

ssues that the audit points out, may also trigger an IRS or DOL audit.

### Read Form 5500 before you file it

While plan sponsors just immediately file Form 5500 once their TPA sends it to them, you should take a look at it, before you file. As mentioned before, anyone filing Form 5500 is doing it under penalties of perjury, and the last time I checked that was still a crime. A plan sponsor who doesn't review their Form 5500 might be committing perjury because of something that was wrong on Form 5500. One should never make any claim under penalties of perjury unless they reviewed such claims. As stated before, major omissions on Form 5500 are just a

recipe for a plan audit. Claiming an insufficient ERISA bond amount on Form 5500 could get the red flag treatment from the Internal Revenue Service and/or Department of Labor for a targeted plan audit. I learned at an early age that you should read what you sign. The same should go for a plan sponsor who is e-filing Form 5500.

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