
Making Your Plan More Cost-Effective Through a Dependent Audit



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How closely are you monitoring dependent enrollments? Are you at all? Most employers offer benefits and often allow employees to name qualified persons as dependents for at least some of those benefits, which makes a plan more expensive. Making sure that the non-employees your plan covers are eligible can be in your financial interest. One way to do that is through a dependent audit.

A comprehensive dependent audit is a study by which an employer or plan administrator can validate that: (1) an employee has properly entered dependents in plan documents; and (2) an employee's claimed dependents meet the employer's eligibility criteria.

Such examinations can be useful for both private- and public-sector employers. Both may find that a dependent audit makes it possible to save money on a benefit plan and reduce the claims made under it by cutting the number of dependents its plan covers. A dependent audit can help an employer, whether private- or public-sector, to manage its financial resources more responsibly by:

- making its benefit plan more cost-effective;
- helping it to exercise fiduciary duty responsibly; and
- rooting out and preventing fraud.

But their motivations also can differ. While a private-sector employer may see an audit as a way to help the bottom line, a public-sector employer could better serve the public interest through the audit — since it is funded through tax dollars, it could save money on behalf of the public by verifying that claimed dependents are valid. Public-sector employers at the federal and state level have an additional reason to consider holding their own dependent audits — the possibility of a watchdog government agency conducting an investigation.

What Does a Dependent Audit Entail?

Dependent audits are a multi-stage process, entailing setting a plan and having it reviewed, corresponding with employees, defining eligibility rules, establishing an amnesty period and deciding whether to require employees to submit documentation. They can include the following steps:

- 1) Set a plan with the parties involved in conducting the audit, and have legal counsel review it.
- 2) Send a letter to employees outlining the business case concerning benefits and applicable rules and responsibilities under ERISA.
- 3) Define the eligibility rules under which employees may cover dependents through the company plan.
- 4) Identify the party that will conduct the audit.
- 5) Send a letter to employees that:

- outlines the criteria by which the dependents will be evaluated;
 - identifies the procedures that will be followed; and
 - encourages employees to participate in the audit, which can use a carrot-and-stick approach.
- 6) Send employees another letter, containing the following:
- eligibility rules;
 - names of individuals they have entered as dependents;
 - demographic information;
 - information concerning how employees can respond — for instance, on paper, online or both;
 - information about any amnesty period during which employees may voluntarily remove employees who are not eligible for coverage, without penalty; this information can have wording similar to the fraud language used on benefit request forms.
- 7) After two-thirds to three-fourths of the amnesty period has elapsed, contact employees who have not responded and remind them that they, and their dependents, may be dropped from the plan if they don't respond by the specified date.
- 8) If employees are to be required to submit copies of formal, government-issued documents during or after the amnesty period, allow employees additional time since it will take them longer to gather such materials. Send employees a reminder letter about such a requirement, if there is one.

Communication is critical

Effective communication is key to an audit, and can heighten participation — which, in turn, makes the dependent audit a more worthwhile use of time and resources. But simply providing information is not enough — the message, and how it is conveyed, also matters. For instance, an employer may find it helpful to stress that the audit is not a sign that it distrusts employees, but rather a way to better exercise its fiduciary responsibility.

If an employer contracts with a third party to conduct an audit, that third party can also provide services that may enhance communication, such as providing a call center and an online component. This gives employees a means to obtain information and better enables the contractor to gather information, develop reports and report to the employer regarding which dependents are eligible for coverage and which ones are not.

Who Conducts Dependent Audits?

Some companies conduct these investigations themselves; others hire third parties to do so.

Self-audits

Employers may decide to conduct a dependent audit in-house to spare themselves the fees they would have to pay an outside party to do so. They also may do so to help protect the privacy and confidentiality of employees and their dependents and to handle sensitive and unique situations.

Audits by third parties

Other employers turn to specialized third parties to conduct dependent audits. Third-party auditors will provide the following services:

- contacting employees in print and/or electronically;
- establishing a call center employees can contact;
- informing employees about the audit; and
- providing recommended documentation the employer should consider requiring employees to provide when they seek to enroll dependents in the benefit plan

A third party can help an employer that lacks the resources, such as human capital and time, to perform that function. In addition, calls concerning the audit and the changes that result from it can go to the third party, with only appeals of those changes going to the employer.

A third party also may lend a stronger sense that the process is objective and make it seem less intrusive. In addition, having a third party conduct the audit is to put distance between it and the process, which can make it easier for an employer to handle difficult situations.

Timing

There are different schools of thought regarding when to conduct a dependent audit. Some believe it's best to conduct a dependent audit within the calendar year, since an audit that is retrospective can raise unwelcome tax issues. Some employers conduct them before open enrollment; others do so while open enrollment is going on. Still others who conduct dependent audits argue that there is no good time, and that an employer should simply make sure it hold one every year.

Cost

A dependent audit will cost something whether it is conducted by in-house personnel or by a third party with which the employer has contracted. The cost may be somewhat harder to quantify if it is done in-house, since the primary costs will be employees' time and whatever material resources belonging to the company are required to conduct the audit.

The cost of a dependent audit is easier to quantify if it is conducted by a third party. The fee a third party will charge for a dependent audit depends on the services the third party offers.

One employer that has 2,325 eligible employees with covered dependents was told by a third party it interviewed that it would cost \$44 per employee per employee to conduct the audit, meaning the audit would cost the employer more than \$100,000.

That's on the high end, according to Dan Priga, principal and national business leader for Mercer Health & Benefits LLC's Performance Audit Group in Pittsburgh. He says that the cost to hire a third party varies from as little as \$14 to as much as \$35 per dependent.

Changes That Result

A dependent audit certainly can have short-term effects if it reveals dependents that should not be covered. Whether an audit has longer-term effects is up to the employer.

Short-term effects

An audit often results in fewer dependents being covered under an employer's benefit plan. That can save an employer substantial amounts of money, since it can cost an employer thousands of dollars to cover each dependent enrolled in a benefit plan. A dependent audit also can translate to fewer claims under the plan.

Long-term effects

A dependent audit can have lasting effects beyond cleaning up the rolls of whom the plan covers — the findings could lead an employer to change its policies and procedures.

After a dependent audit many employers require documentation from employees up front at enrollment. Such documentation can be a way to verify that claimed dependents meet age criteria. This can include copies of birth certificates, driver's licenses, or other government-issued documents that show year and date of birth.

Some employers request that employees who claim dependents older than age 19 submit signed statements, sometimes notarized, concerning the level of financial support the employee provides the dependent and the number of nights the dependent stays with the employee. Another form of proof some employers require to verify spouses is a copy of the top portion of an employee's tax return, but with information concerning income covered up.

Employers may be wise to decide in advance what they will do if ineligible dependents are discovered through the audit. Doing so will help the employer to implement new policies quickly and make changes efficiently.