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US DEPARTMENT OF LABOR ADVISORY COUNCIL

ON EMPLOYEE WELFARE AND PENSION BENEFIT PLANS

TOPIC: EMPLOYEE BENEFIT PLAN AUDITING AND FINANCIAL REPORTING MODELS

Good morning, my name is Susan Diehl, President of PenServ Plan Services, Inc. (“PenServ”).

PenServ is a retirement plan consulting company and currently services over 1000 financial institutions with IRA, SEP, SIMPLE, qualified plan, 457 and 403(b) documents, administrative forms and technical information. We are also a Mass Submitter of prototype documents with the IRS and make sure that our clients have the most current information with respect to these plans and the administrative forms needed to comply with all areas of qualification, withholding and taxation. PenServ also serves as the third party administrator (TPA) of over 3000 employee benefit plans ranging from the smallest plan (1 person) to large plans with thousands of participants. It is on behalf of these clients (both institutional and employers) that we are here today testifying with the following comments.

First we would like to commend the Advisory Council for identifying that there are issues on the audit side of ERISA 403(b) Plans and permitting comments on the methodology of audits to enhance participant protection. We appreciate the opportunity to comment on the issues listed below and to address the provisions that continue to complicate the administration and servicing of 403(b) plans.

I would like to begin by telling you a true story of a nonprofit company that is an organization committed to helping abused children. They are located in a number of cities nationwide (6 at this time) but only have a total of 110 employees. Most of the individuals who “work” are volunteers of the organization. They work hard to raise enough money to assist in their efforts to help the kids that need it most.

About 10 years ago they decided to establish a 403(b) plan to permit the employees to defer from income so that they could put some money away for their retirement. There were and still are no Highly Compensated Employees that work at this employer. From the inception of the Plan forward only about 35 employees decided to participate in the plan. Over the last 10 years it has been pretty consistent that the participant count is around 35. When the final 403(b) regulations were issued, they understood that they would need to adopt a plan and looked for help in providing a plan document and help in making sure that the plan in operation satisfied all of the 403(b) requirements. They understood that this would need to be a part of their budget going forward and estimated that the annual costs would be about $1,500 per year. They were satisfied that they could afford this amount.

A Third Party Administrator (TPA) was hired to start to collect the data from the investment companies and calculate the amounts that each participant had in each of the sources of monies under the Plan. Since there were no employer contributions, the only amounts that needed to be sorted were the principal amount of elective deferrals, earnings thereon, incoming rollovers into the plan and the earnings thereon, and breakdown of transferred amounts from other 403(b)s that had been consolidated. In this particular case the investment companies did not have this information, so the TPA received the historical data and then broke it down into sources.

And then…the FAB was issued. The retirement plan of this charity was turned upside down. First they were told that they now had to satisfy ERISA. What does that mean?

- A new plan document;
- Summary Plan Description;
- Form 5500 filings (retroactive to 2009); and
- Obtain an auditor and collect the information needed for the Audit requirements.

All of these at an additional cost to the Employer! The new costs they were told would be approximately…

- A new plan document - $500;
- Summary Plan Description - $250;
- Form 5500 filings (retroactive to 2009) - $850 per year ; and
- Obtain an auditor and collect the information needed for the Audit requirements – if limited scope audit is available the cost would be approximately $5,000, if a full scope audit is required then the cost would be between $10,000 and $15,000 (they were told that based on the auditing firm's experience so far the limited scope audit would probably not be available).

In fact, a limited scope audit was not an option since most of the investment companies that the employer was investing did not have a SAS 70 audit and could not produce the desired data and reports by the time of the audit.

The employer then decided that they could not afford these fees and they would need to terminate the plan. At which point they were told that was not an option …not yet, since the IRS and DOL were working on how a 403(b) plan could effectively terminate their plan, but the good news is that it should be "soon" when the guidance is issued to assist in terminating and distributing all of the assets within a reasonable time. And the employer could not "force" distributions under these plans as is the case under qualified plans.

Unfortunately this is a true story that has affected thousands of nonprofit organizations that have sponsored 403(b) plans over the last 40 years. The cost of now maintaining an ERISA plan is unrealistic when weighted against the mission of these charities.

Some of the "luckier" smaller 501(c)(3) employers that have 3 – 10 employees have been able to terminate since the assets were readily identifiable, and have managed to terminate and distribute all assets. These employees will no longer have a retirement plan available to them. There is no other option for these small employers to offer their employees. We have heard many times that SIMPLE IRAs would work for these smaller employers, but remember there are required employer contributions and these employers can not afford to make an employer contribution.

We have been requested to address a series of questions today. After going through these questions we took into consideration the protection of participants and beneficiaries intended by Congress. Since the 2009 year is affected, we have concluded that there is only one remedy and that is to provide transitional relief to allow vendors, financial institutions, TPAs and auditors the time needed to address the inconsistencies and the collection of data for the audits. Here are the comments and antidotal information in support of this request.

1. Does the relief provided to 403(b) administrators by the DOL under FAB 2009-02 and 2010-01 adequately protect the interest of plan participants and beneficiaries in a manner that Congress intended when it imposed the audit requirement?

We understand and agree that the audit requirements are meant to protect the participants and beneficiaries in ERISA Plans. For ERISA plans where this is not a new requirement the audits serve a purpose of protection. For 403(b)s where this is new, statistics from the AICPA show that very few 5500s have been completed for ERISA 403(b)s since there has not been adequate time for auditors to review their own auditing procedures and to make adjustments to their own internal requirements to reflect the differences in the types of 403(b) plans and compare the these procedures with the procedures that have been in place for other ERISA plans. The

403(b) plans have in the past 40 plus years been treated as individual accounts, and the current audit guidelines and specifications and audit manuals place the responsibility on the CPA. Even though the FAB permits assets from a “deselected vendor” (those that accepted no contributions after 2008) to be ignored for 5500 purposes, the accounting procedures require that the auditor cannot just pick up these accounts from the first day of the plan year, rather they must go back to prior data to “protect” their credentials.

The following problems have been uncovered in the process of heading towards a Form 5500 filing and collecting the audit reports from the vendors under ERISA Plans:

A. Additional “vendors” are being uncovered during the data collecting process. This not only complicates the data collection process but delays the audit for the Form 5500. One example of this occurrence is when the “vendor” is a broker-dealer and the underlying investment company is identified during the data collection process.

B. Vendors were not required to maintain data. They do not currently and have not in the past maintained the source data for the past 40 plus years. Vendors, Recordkeepers, and TPAs are building the files but time is running out. Billions of dollars have been spent by the segments of this industry since 2007 and progress is being made, but most industries still need time to be able to produce accurate reports and data which will ensure that the audits will be accurate.

   Unfortunately we are not there yet.

C. We have heard from many employers, TPAs, CPAs, and financial institutions (vendors) that in order to avoid penalties something will be filed and later amended. But most of the reports will need to be filed late, resulting in additional cost to these employers in an attempt to provide a retirement benefit.

D. Due to many factors, another problem is the lack of understanding by some industry partners of 403(b) plans and related rules. Remember many of these employers were told in 2007 that documents needed to be prepared for the first time; vendors were required to share data (some of them are still working on that piece); and interaction with an auditor was necessary to share data that is merely beginning to be collected. The additional time will also serve to educate the employers, CPAs, TPAs, and investment companies about what the audit requirements are and the type of information that needs to be gathered for the audit and for the completion of the Form 5500.

E. From the DOL perspective the audits would protect the participants if there was some transitional relief. The fact of the matter is, there will be thousands of noncompliant 5500 forms being filed, or worse, those that will be filed late thereby imposing additional cost to employers. The end result will be the termination of these plans.

F. For 40 years, from the largest investment company to the smallest, the individual accounts were not controlled by ERISA. The investment companies are now building out their systems and procedures to capture this data back to 2008, or in some cases, to the inception of the plan.

G. Reports from the vendors do not reconcile, and the time frame to compose the revised data and prepare a new report is a minimum of 10 more days.

H. It is difficult to reach an individual in a large company that truly understands the audit process and the information that is necessary to provide the auditors.

I. There is no allocation of sufficient resources within the vendors themselves.

J. Large players in the 403(b) marketplace continue to stay in the market and offer products, although they have no current ability to track sources of funds and no ability to provide an audited program report. The TPA will receive from this vendor a series of Excel spreadsheets that do not balance, and reports that contain errors. The TPA then must go back to the Employer in an effort to balance the report, but find that the Vendor records are not correct. The reports must then be redone; all the while the various involved will vent their frustration on TPA and the auditor.

K. Audits have never been required for 403(b) plans in the past so you have an industry that has never been exposed to this process. The only experience they have is with 401(k)s, if they also offer qualified plans.

2. What protections, if any, do disclaimed opinions, furnished in response to such relief provide to participants and beneficiaries?

Even though Department of Labor officials have indicated that it is not their intent to reject filings of 403(b) Form 5500s where a modified audit report is attached due to the difficulty of obtaining the pre-2009 contract and account information. The difficulty, as outlined above however, goes well beyond the determination of the beginning balances.

Unlike the governmental 403(b) area where trade associations in every state, and an international association that provides education to its members and has so every since the 403(b) regulations were finalized, non profit organizations have been harder to reach out to even by the IRS. For this reason, there are still 403(b) plans (whether they are considering themselves to be ERISA or NonERISA) that are just now learning:

- New plans documents are required;
- The definition of “participant” includes all those that are eligible to defer not merely the number contributing to the plan;
- Audit requirements must be met if the plan has more than 100 “participants” that are eligible;
- Vendors are learning what an “audit report” must contain of only when the employer receives a copy of the auditor’s list of items.

Those that have followed the issuance of the FAB and wish to maintain their ERISA exemption now need to enter into new agreements with the vendors under their plan and put their entire trust in the vendors to run the plan compliantly. If any one of the vendors at this late date decides they cannot work with any other vendors, then the plan once again runs the risk of becoming subject to ERISA. Without the availability of hiring a third party to collect data and make sure the plan satisfies the requirements of

403(b)s, the Employer is at the mercy of the vendors and their representatives. Under qualified plans, whether the plan is subject to ERISA or not there is a general consensus among and suggestions by investment companies that the employer should hire a third party administrator. Yet under a 403(b) the "new" suggestion is to fire your TPA and put your plan in the hands of the investment providers/vendors who may or may not be qualified to administer the Plan.

3. Should alternative procedures (other than or in addition to audits) be required for 403(b) plans, such as an Agreed Upon Procedures reporting model? How could such procedures be implemented?

We believe that there are only a few viable solutions to the current disarray of ERISA plans. Our suggested solutions are as follows:

A. Transitional Relief

- Audits are due in 45 days! It is our opinion that the only option that will work at this late date is a transitional rule or relief which would provide additional time for a new procedure and for the Department of Labor to gather information from the industry to come up with a viable solution that will ensure the protection of participants and beneficiaries. If any such relief is to be released, some type of announcement needs to be issued very soon in order to avoid the additional costs that are being charged to the Employers.

- Transitional relief would also assure that the data reported would be accurate and would not unnecessarily put these employers in a penalty situation.
- Transitional relief would permit the vendors to finish implementing their data sharing elements, and by continue to address their internal programs for sharing of data and understanding what the auditing firms need from them in an "Audit Report".
- Multiple industry education could continue through the efforts of AICPA, the EBSA for the Employers, Vendors, CPAs and TPAs. This educational outreach should include material aimed at vendors to make them aware of their responsibility and the type of reporting required of them. Many vendors are not familiar with a SAS 70 audit and most did not have procedures in place on 1/1/2009 to have a SAS-70 audit of their internal procedures. Our experience to date with the top 10 vendors in the 403(b) industry is that only half of them have been able to provide the documentation required to file an adequate form 5500.
- Faced with having to deal with a 40 year old industry standard, every day more vendors are falling by the wayside.

B. Small Plan ERISA Exemption

- We continue to believe that there should be relief for the small 501(c)(3) Employers who cannot afford the new world of 403(b)s. Some of them have considered moving in the direction of a single vendor, but then realize that would potential subject them to ERISA.

- As stated before, it seems that the result of the new requirements for small employers will be plan termination which was not the intent of the new regulations and the FAB, but nonetheless will be necessary in order for the small non-profits and charities to survive.

In conclusion, transitional relief at this late date is the only answer. The auditors are doing their job but if they perform a valid ERISA audit, they must capture pre-2009 data in order to satisfy their “best practices”. Some are going back to 2004 to determine who the “grandfathered” vendors are to dismiss for the future years.

I thank you for the opportunity to present our views and recommendations. We would be happy to address any questions you may have and also be prepared to participate in any additional committees or assist in any way we can with input, training and educational materials, and/or assistance in developing alternative reporting models.