Advisory Council on Employee Welfare and Pension Benefit Plans

Report to the Honorable Eugene Scalia, United States Secretary of Labor

Beyond Plan Audit Compliance: Improving the Financial Statement Audit Process

November 2019

NOTICE

This report was produced by the Advisory Council on Employee Welfare and Pension Benefit Plans, usually referred to as the ERISA Advisory Council (the "Council"). The Council was established under Section 512 of the Employee Retirement Income Security Act of 1974, as amended ("ERISA") to advise the Secretary of Labor on matters related to welfare and pension benefit plans. This report examines the role of the plan administrator in the financial statement audit process prescribed under Section 103 of ERISA to determine whether, through the provision of additional educational tools or guidance, improvements in the accuracy of financial statements and other indirect benefits – such as, enhancements in the safety of plan assets or in the operational compliance of the plan with its governing documents and applicable laws – could be achieved.

The contents of this report do not represent the position of the Department of Labor (the "Department").

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ABSTRACT

The 2019 ERISA Advisory Council examined the regulations and guidance implementing the independent qualified public accountant annual examination of financial statement requirements under Section 103 of ERISA to determine whether changes could enhance the safety of plan assets, the effectiveness of the plan's design, the efficiency of the plan's operations, and the compliance of the plan with ERISA, the Code, and other applicable laws. In particular, the Council focused its inquiry on the effectiveness of the current regulatory environment in terms of the promotion of legal compliance and the safeguarding of plan assets, and then sought out ways in which that environment might be improved.

Based upon testimony received during public hearings, supplemented by submissions of written material from the Department and interested stakeholders, the Council developed a recommendation for updating sub-regulatory guidance for plan administrators and plan service providers to improve their understanding of the value of the financial statement audits mandated under Section 103 of ERISA. Specifically, the Council recommends that the Department further develop its plan administrator education program to provide more information and better tools to help plan administrators more knowledgeably and more prudently participate in the financial statement audit process.

ACKNOWLEDGEMENTS

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I. RECOMMENDATION

Based on testimony and research and for the reasons stated herein, the Council recommends that the Department make available to plan administrators new educational resources and access to tools and data regarding the uses of financial statement audits, specifically:

a) Send notices to plan administrators advising them of their responsibilities regarding selecting, retaining, and interacting with the independent auditor of the plan's financial statements, and of the tools available to assist them in these responsibilities.

b) Publish a revised brochure regarding the selection, retention and interaction with an independent auditor of the plan's financial statements, including a best practice checklist. The Council has drafted a sample checklist, which is included in Appendix A to this report.

c) Publish a list of the most common deficiencies found in plan audits.

d) Make more information available to plan administrators and their advisors regarding auditors who perform financial statement audits for employee benefit plans, *e.g.*, add features to EFAST2 to allow for searches of filings by auditor.

e) Expand the Department's financial statement audit education programs to target plan advisory groups in the Department's outreach.

II. DISCUSSION

A. Council's Inquiry

The reporting and disclosure requirements of Title I of the Employee Retirement Income Security Act of 1974, as amended ("ERISA") play a central role in the achievement of the participant protection goals of ERISA, and an audited financial statement by an independent auditor is central to those requirements. The audited financial statement requirement is set forth in Section 103(a)(1)(B)(i) and Section 103(a)(3) of ERISA as follows:

(a) Publication and filing

(1)

. . .

(B) The annual report . . . shall also include—

(i) a financial statement and opinion, as required by paragraph (3) of this subsection

. . .

(3)

(A) Except as provided in subparagraph (C), the administrator of an employee benefit plan shall engage, on behalf of all

> plan participants, an independent qualified public accountant, who shall conduct such an examination of any financial statements of the plan, and of other books and records of the plan, as the accountant may deem necessary to enable the accountant to form an opinion as to whether the financial statements and schedules required to be included in the annual reports by subsection (b) of this section are presented fairly in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Such examination shall be conducted in accordance with generally accepted auditing standards, and shall involve such tests of the books and records of the plan as are considered necessary by the independent qualified public accountant. The independent qualified public accountant shall also offer his opinion as to whether the separate schedules specified in subsection (b)(3) of this section and the summary material required under section 1024(b)(3) of this title present fairly, and in all material respects the information contained therein when considered in conjunction with the financial statements taken as a whole. The opinion by the independent qualified public accountant shall be made a part of the annual report. . . .
>
> **(B)** In offering his opinion under this section the accountant may rely on the correctness of any actuarial matter certified to by an enrolled actuary, if he so states his reliance.
>
> **(C)** The opinion required by subparagraph (A) need not be expressed as to any statements required by subsection (b)(3)(G) prepared by a bank or similar institution or insurance carrier regulated and supervised and subject to periodic examination by a State or Federal agency if such statements are certified by the bank, similar institution, or insurance carrier as accurate and are made a part of the annual report.
>
> **(D)** For purposes of this subchapter, the term "qualified public accountant" means—
>
> **(i)** a person who is a certified public accountant, certified by a regulatory authority of a State;
>
> **(ii)** a person who is a licensed public accountant licensed by a regulatory authority of a State; or
>
> **(iii)** a person certified by the Secretary as a qualified public accountant in accordance with regulations published by him for a person who practices in States where there is no certification or licensing procedure for accountants.

As provided in the statutory text above, the Department's authority to regulate the independent auditor is limited by two factors. First, rather than delegating to the Department the power to set standards for an employee benefit plan financial statement audit, ERISA specifies that the accounting standards to be applied are the generally accepted accounting principles ("GAAP") examined utilizing generally accepted auditing standards ("GAAS"). Second, ERISA provides that the licensing requirements in the individual states would regulate the criteria by which an accountant could be certified to perform audits in accordance with GAAS. By and large as a result of these limitations, regulation of the accountants who perform employee benefit plan financial statement audits is provided by the accounting profession through the American Institute of Certified Public Accountants ("AICPA") and through the individual state boards of accountancy. Accordingly, the Department has very limited means to regulate the conduct or quality of a financial statement audit.

In 2010, the Council reported on the quality of plan audits and auditors. The 2010 Council recommended, among other things, that the Department coordinate efforts with the AICPA to develop higher quality standards and to provide better training to auditors. In keeping with this recommendation, the Department consulted with the AICPA in the development of the AICPA's Statement on Auditing Standards Number 136, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA.* The Department has now asked this 2019 Council to consider ways to improve the value and utilization of the plan financial statement audit by the plan administrator, who is the party responsible for securing the audit from an independent auditor.

Unlike its limited role in the regulation of the independent auditor, the Department does have authority to regulate plan administration and to control the contents of the plan's annual report. In its request that the 2019 Council review the plan administrator's conduct and responsibilities regarding the procurement of the plan's annual financial statement audit, the Department raised concerns about the "commoditization" of such audits, in that the plan administrator was not sufficiently availing itself of the financial statement audit process to reexamine the inputs provided to the auditor, to achieve the routine operational discipline that a proper annual audit process should encourage, or to learn about improvements in the plan's documentation, operations, policies, or procedures that could arise from a robust financial statement audit engagement.

The Council set out to discover whether various professionals and stakeholders shared the Department's concern, and to learn about the efficacy of various tools that the Department could make available to plan administrators to enhance the value provided by an improved engagement in the plan's annual financial statement audit process.

B. Statutory and Regulatory History

In crafting the participant protection provisions in Title I of ERISA, Congress intended to enhance the disclosure requirements previously adopted under the Welfare and Pension Plan Disclosure Act of 1959, as amended in 1962 ("WPPDA"). The independent audit requirement was a chief method for achieving the goal of allowing "better assessment of the plan's financial soundness by administrators and participants alike." S. Rep. 93-127, 1974 U.S.C.C.A.N. 4,8383-64 (Aug. 18, 1973). This concern led to ERISA's requirement that the plan administrator "engage, on behalf of all plan participants, an independent qualified public accountant . . . [to] conduct an examination of [the plan's] financial statements. . ." ERISA § 103(a)(3)(A).

Significantly, Congress defined the "qualified public accountant" as "(i) a person who is a certified public accountant certified by a regulatory authority of a State; (ii) a person who is a licensed public accountant licensed by a regulatory authority of a State, or (iii) a person certified by [the Department] as a qualified public accountant in accordance with regulations published by [the Department] for a person who practices in States where there is no certification or licensing procedure for accountants." ERISA § 103(a)(3)(D). Further, Congress specified that the qualified public accountant's opinion as to the fair presentation of the employee benefit plan's financial statements and schedules is to be based on their "conformity with [GAAP] . . ." and that the conduct of the examination be "in accordance with [GAAS] . . ." *Id.*

Congress' specific definition of the audit principles and standards to be applied to employee benefit plan financial statements removed the ambiguity in the WPPDA, which described the audit as "comprehensive" and to be conducted in accordance with "accepted auditing standards," but provided no details as to the method by which comprehensiveness should be measured, or as to the source of accepted auditing standards. Further, Congress removed from earlier drafts of ERISA, the authority of the Department to establish higher standards than GAAP and GAAS provide. *See Employee Benefit Security Act*, 93d Cong., 2d sess., 1974, H.R. 2 (including in the definition of qualified public accountant the following proviso: "except that if [the Department] deems it necessary in the public interest, [it] may prescribe by regulation higher standards than those required by the regulatory authorities of the States, and a person shall be considered a qualified public accountant for purposes of [ERISA] only if he meets such standards"). Thus, in the context of employee benefit plans subject to ERISA, Congress did not provide the Department a substantive role either in setting the standards by which employee benefit plan financial statement audits are to be conducted, or, because all States have done so, in regulating the qualifications of qualified public accountants. This limitation in authority stands in contrast to the powers provided to the U.S. Securities and Exchange Commission ("SEC") in monitoring accountants performing audits of public companies under the Securities Exchange Act, s*ee* 15 U.S.C. § 78m(b)(1) (Commission may prescribe rules and regulations inconsistent with state law requirements to the extent it determines that the public interest or the protection of investors so requires), which was reinforced and strengthened by the Sarbanes-Oxley Act of 2002, *see* 15 U.S.C. § 7218(b) (Commission shall promulgate rules and regulations to carry out the new accounting standards as it deems necessary or appropriate in the public interest or for the protection of investors).

C. Department Compliance Investigations and Studies

The Department has long sought to assess and improve the quality of employee benefit plan financial statement audits. To that end, the Department has conducted several major studies of audit quality over the years.[1] Each of these studies revealed a significant number of deficient financial statement audits, raising serious concerns by the Department regarding the integrity of the financial statement audit process, and whether that process was sufficiently protecting the benefit security of plan participants and beneficiaries.

The most recent study issued in 2015, *Assessing the Quality of Employee Benefit Plan Audits* (the "2015 Study"), found that overall, 39 percent of audits reviewed for the 2011 filing year contained major deficiencies with respect to one or more GAAS requirements. By way of comparison, previous studies reported deficiency rates of 33 percent in 2004 and 19 percent in 1997. Thus, despite extensive guidance issued by the AICPA, the findings showed that the quality of employee benefit plan audits had deteriorated.

Among the 400 audits reviewed in the 2015 Study, the most frequently cited deficiencies (50 or more occurrences) were: failure to adequately test allocations to participant accounts, no/insufficient testing of payroll data, no/inadequate testing of participant investment options, inadequate footnote disclosures, no work performed in regard to administrative expenses, and failure to test timely remittance of employee contributions.[2]

The 2015 Study called attention to the fact that audit quality varied greatly by the size of a certified public accountant ("CPA") firm's employee benefit plan financial statement audit practice. Firms performing only one or two plan audits per year had a 76 percent deficiency rate, while firms performing at least 100 plan audits per year had a deficiency rate of 12 percent.[3]

Another notable observation in the 2015 Study was a correlation between financial statement audit deficiencies and limited-scope audits. As the number of limit-scope audits has increased

[1] **DOL Employee Benefit Plan Audit Quality Studies**	**Year Issued**	**Filing Year Studied**	**# Audits Studied**	**Deficiency Rate**
Assessing the Quality of Employee Benefit Plan Audits (https://www.dol.gov/sites/dolgov/files/EBSA/about-ebsa/our-activities/resource-center/publications/assessing-the-quality-of-employee-benefit-plan-audits-report.pdf)	2015	2011	400	39%
The details of this study were not made publicly available; summary data appear on page 8 in the 2015 report	Not reported	2004	Not reported	33%
Assessment of the Quality of Employee Benefit Plan Audits (https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/publications/assessment-of-the-quality-of-employee-benefit-plan-audits)	1997	1992	276	19%
Changes Are Needed in the ERISA Audit Process to Increase Protections for Employee Benefit Plan Participants (Report No. 09-09-001-12-001)	1989	1986	279	23%

[2] U.S. Department of Labor, Employee Benefits Security Administration, Office of the Chief Accountant, *Assessing the Quality of Employee Benefit Plan Audits* (May 2015), Appendix II.

[3] *Id.*, at p. 9.

over the years, so has the number of audit deficiencies. This correlation has led the Department to conclude that limited-scope audits may contribute to declining audit quality because, in the Department's view, CPA firms have less incentive to focus on relevant audit areas when they will not be rendering an opinion on the plan's financial statements.[4]

Overall, the four major Department studies show that there was no improvement in audit quality between 1986 and 2015, and that audit deficiency rates remained significant as of 2015.

D. Development of Industry-Regulatory and State Licensing Standards

The licensing authority and requirements for CPAs generally fall under the auspices of the Board of Accountancy for the state or jurisdiction in which a CPA practices. The federal government rarely sets, or oversees, accounting standards by statute.[5] Instead, the accounting standards that private entities follow in financial dealings, maintaining accounting systems and preparing financial statements are contained in GAAP. The standards by which those prepared financial statements are audited are set forth in GAAS. As self-reported, the AICPA plays a central role in setting ethical standards for the profession and U.S. auditing standards for private companies, nonprofit organizations, federal, state and local governments."[6] Members in the AICPA's Employee Benefit Plan Audit Quality Center ("EBPAQC") follow additional self-imposed policies and procedures with respect to auditing ERISA plans.[7] Although GAAS comprises numerous detailed specific standards, the outcome of any particular audit also depends upon the relevant training, knowledge, experience, and professional judgment of the auditor, for example, in assessing risk or determining materiality.

As set forth above, Section 103 of ERISA requires that plans undergo a financial statement audit process annually. In an annual financial statement audit, a CPA applies GAAS and opines as to as to whether the financial statements are presented fairly, in all material respects, in accordance with GAAP.

Prior to 2015, auditors of employee benefit plans used the same GAAS applicable to all types of private entities; GAAS contained no auditing standards specific to employee benefit plans subject to ERISA.[8] In early 2015, a few months prior to the issuance of the Department's May 2015 report on audit quality described above in Section C, at the urging of the Department, a special task force at AICPA's Auditing Standards Board (ASB) was formed to consider a

[4] *Id.* at p. 8, 17.

[5] For publicly-traded entities, accounting and auditing standards are subject to regulation by the SEC. Currently, the SEC recognizes the Financial Accounting Standards Board (FASB) as the designated authority for establishing GAAP. SEC Accounting Series Release No. 150 (ASR 150), 1973.

[6] AICPA, "About the AICPA," http://www.aicpa.org/ABOUT/Pages/About.aspx

[7] Significantly, according to James G. Haubrock, Chair of the AICPA EBPAQC Executive Committee, those EBPAQC members perform over 85 percent of employee benefit plan audits nationwide.

[8] AICPA has issued guidance in the "AICPA Accounting and Audit Guide, Employee Benefit Plans," which the Department actively participated in drafting and revising periodically.

proposal to improve the quality of employee benefit plan financial statement audits. The Office of Chief Accountant ("OCA") of the Department's Employee Benefit Security Administration ("EBSA") actively participated in the process.[9]

Two years after that process began, in April 2017, the ASB issued a 133-page Exposure Draft of a proposed statement on auditing standards (SAS) specifically addressing financial statement audits of employee benefit plans: "*Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*" (the "Exposure Draft"). The Exposure Draft included new engagement acceptance requirements, new written management representations, and expanded descriptions of management's responsibilities; and it required new emphasis-of-matter paragraphs. The Exposure Draft also proposed an entirely new reporting model for financial statement audits of employee benefit plans performed pursuant to Section 103(a)(3)(C) of ERISA[10] that required auditors to test compliance with various specified plan provisions "irrespective of risks of material misstatement" (Exposure Draft A15-18), and required the audit to include a list of all of the resulting findings unless "clearly inconsequential" (Exposure Draft A120-123).

AICPA received over 100 comment letters, many of which raised similar objections to the new requirements: they were too costly and burdensome; they effectively undermined limited scope audits otherwise permissible under ERISA; they required testing and reporting without regard to risk or materiality, thus departing far from traditional risk-based audit concepts and going beyond ERISA requirements; and public reporting of immaterial operational errors would be disruptive to the financial statement audit process, misleading, and counterproductive.[11] Some observers specifically objected to the Department's perceived outsize role in the process.[12]

[9] Exposure Draft at 4 ("The [OCA] participated in the task force and ASB deliberations and provided the task force with insights and recommendations as to areas where the [Department] believes the auditor's report can be strengthened.")

[10] Section 103(a)(3)(C) of ERISA permits plan management to elect to exclude from the audit certain investment information held by and certified to by a qualified institution.

[11] *E.g.,* The American Benefits Council and the Committee on Investment of Employee Benefit Assets comments to the [ASB] on its Exposure Draft, August 18, 2017, ("[W]e have a general concern about the overall breadth of the changes, as AICPA has made no attempt to quantify what these changes mean to the cost of an audit. Second, we believe that requiring auditors to report operational errors, regardless of materiality, is a dangerous and ill-advised rule that would impose unnecessary burdens on plan sponsors while contributing little to the overall quality of audit reports. Third, although we welcome AICPA's efforts to improve the quality and the content of the limited scope audit, we are concerned that the changes proposed in the Exposure Draft will become part of a broader effort by the [Department] to undermine the use of the limited scope audit altogether.")

[12] *E.g.,* Howard B. Levy, CPA, "Has the DOL Pushed the ASB Too Far?" *The CPA Journal*, August 2017 ("For no apparent justifiable reason, it appears that the ASB is proposing to capitulate to the demands of the [Department] to satisfy its regulatory objectives (which appear to extend beyond its statutory purpose and authority under ERISA) by mandating procedures and reporting language, most of which have little or nothing to do with the sole purpose of a financial statement audit, which is providing financial statement users with assurance as to the absence of material misstatements therein.")

In December 2018, taking note of the comments, the ASB significantly revised and voted to publish a "Final Balloted Draft" of the standard, which removed many of the most controversial provisions, but remained specifically targeted at employee benefit plan financial statement audits. The Final Balloted Draft was subject to public meetings of the ASB. In July 2019, four years after the ASB taskforce began its deliberative process to address employee benefit plan audits, the ASB issued as a final standard: SAS No. 136, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA* ("SAS No. 136"). The final SAS No. 136 will be effective for audits of financial statements for periods ending on or after December 15, 2020.

SAS No. 136 includes new requirements in all phases of an employee benefit plan financial statement audit, including engagement acceptance, risk assessment and response, communication with those charged with governance, performance procedures, and reporting. In addition, SAS No. 136 requires: that the auditor's opinion identify the plan as an employee benefit plan subject to ERISA; that management's and the auditor's roles and responsibilities be specified; and that new content relating to the ERISA-required supplemental schedules to the Form 5500 be reported.[13] With respect to audits performed in accordance with Section 103(a)(3)(C) of ERISA ("Section 103(a)(3)(C) Audits," formerly referred to as "limited scope audits"), SAS No. 136 requires new procedures, new acknowledgements related to management's responsibilities as to the investment certification, and a new form of report intended to provide greater transparency about the scope and nature of the financial statement audit.

1. Engagement Acceptance[14]

Although most of the changes apply to the auditor, the new requirements for audit engagement, in particular, the required acknowledgements, effectively apply to plan management. SAS No. 136 requires plan management to agree that those responsible for plan governance (and not the auditor) are responsible, among other things, for maintaining a current plan document and all amendments, administering the plan and determining that the plan's transactions presented in the financial statements are in conformity with the plan's provisions, and for providing the auditor with a substantially complete draft Form 5500.

When management elects a Section 103(a)(3)(C) Audit, SAS No. 136 also requires new acknowledgements of management's responsibilities to determine that a Section 103(a)(3)(C) Audit is permissible under the circumstances, that the certifying institution is qualified,[15] and that the certification meets the regulatory requirements.[16] The auditor is required: to evaluate

[13] The Form 5500, Annual Return/Report for Employee Benefit Plan, was jointly developed by the Department, the Internal Revenue Service ("IRS"), and the Pension Benefit Guaranty Corporation ("PBGC") as part of an EBP's annual reporting requirements under Title I and Title IV of ERISA and the Code. ERISA requires that certain supplemental schedules accompany the ERISA plan financial statements and the Form 5500. The required schedules vary depending on the size and type of plan. *See generally* https://www.dol.gov/agencies/ebsa/employers-and-advisers/plan-administration-and-compliance/reporting-and-filing/form-5500.

[14] SAS No. 136 ¶¶ 15-17 and A16-A17

[15] *See* 29 CFR 2520.103-8

[16] *See* 29 CFR 2520.103-5

management's assessment of whether the certifying institution is qualified; to obtain the certification from management and to read it as it relates to the investment information; to compare the certified investment information with the related information presented and disclosed in the financial statements and Form 5500; and to read the disclosures that relate to the certified investment information to assess whether they are in accordance with the presentation and disclosure requirements of GAAP. Ultimately, the auditor will be required to express an opinion as to whether the certified investment information reported in the financial statements and Form 5500 agrees to, or is derived from, in all material respects, the information prepared and certified by an institution that management determined satisfies the requirements of Section 103(a)(3)(C), and audit the non-certified investment information in the financial statements and ERISA-required schedules and express an opinion as to them.

2. Audit Risk Assessment and Response[17]and Communication with Management or Those Charged with Governance[18]

SAS No. 136 requires the auditor to obtain and to read the current plan document and effective amendments, and (a) to perform a risk assessment of plan provisions that affect the risk of material misstatement and (b) to perform audit procedures that test the risk – that is, to consider relevant plan provisions that affect the risk of material misstatement at the relevant assertion level for classes of transactions, account balances, and disclosures. Although not requiring the specified testing as proposed in the Exposure Draft, SAS No. 136 requires that if an auditor determines that it is not necessary to test any relevant plan provisions, the auditor should document the considerations in reaching that determination, and makes clear that at least some testing of plan provisions is expected except in rare cases.[19] SAS No. 136 includes an Appendix that lists examples of common plan provisions by audit area.[20]

Unlike the Exposure Draft, which required the financial statement audit itself to include a list of all findings unless "clearly inconsequential" (Exposure Draft ¶¶ A120-A123), the final standards require the auditor to evaluate whether noted instances of noncompliance amount to "reportable findings" (*i.e.*, noncompliance or suspected noncompliance with laws or regulations; significant and relevant to those charged with governance regarding their responsibility to oversee the financial reporting process; or deficiencies in internal control not communicated to management by other parties and that, in the auditor's professional judgment, are of sufficient importance to merit management's attention). The final standards require the auditor to communicate

[17] SAS No. 136 ¶¶ 18-26 and A18-A37

[18] SAS No. 136 ¶¶ 27-28 and A38-A46

[19] SAS No. 136 ¶ A27 ("Because of the nature of ERISA plan engagements, it would be rare for the auditor, based upon the assessed risks of material misstatement at the relevant assertion level, not to test any relevant plan provisions").

[20] SAS No. 136 Appendix A, ¶ A153

"reportable findings" to plan management,[21] in contrast with the Exposure Draft, which would have required public exposure of all findings not "clearly inconsequential."

With respect to prohibited transactions, the auditor should evaluate whether they have been appropriately reported in the ERISA-required supplemental schedules, and for prohibited transactions involving a party-in-interest which have not been properly reported, the auditor should discuss with management. And if not ultimately reported, and material, the auditor should modify the auditor's opinion accordingly. If not material, the auditor should consider including an "Other Matter" paragraph on ERISA-required supplemental schedules, describing the prohibited transaction.

3. Procedures for a Section 103(a)(3)(C) Audit[22]

The Section 103(a)(3)(C) Audit report not only should note it is a Section 103(a)(3)(C) Audit, but also describe the requirements and limitations applicable to such audits. The new standard makes clear that when management elects to rely upon certified investment information pursuant to Section 103(a)(3)(C) of ERISA, such an election will not be the basis for an audit opinion disclaimer, as had been the practice with "limited scope audits."

The auditor is required to audit the non-certified investment information in the financial statements and ERISA-required schedules and express an opinion as to them (excluding the certified investment information). With respect to the certified investment information, the auditor will be required to evaluate management's assessment as to whether a Section 103(a)(3)(C) Audit is permissible and management's assessment of whether the certifying entity is qualified. The auditor will also be required to express an opinion as to whether the amounts and disclosures in the financial statements and ERISA schedules agree to or are derived from the certified investment information provided by a qualified institution.

4. Auditor's Review of Form 5500[23]

SAS No. 136 requires the auditor to obtain and read a substantially complete draft of the Form 5500 before issuing an audit report. If the auditor finds a material inconsistency between the draft Form 5500 and the ERISA plan financial statements, the auditor should determine whether the financial statements or draft Form 5500 need to be revised. If needed revisions are not made, the auditor should take further appropriate steps, such as discussing with those charged with governance, modifying the opinion, withholding the opinion or even withdrawing from the

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[21] SAS No. 136 explanatory note A40, states "It is important for the plan administrator, as part of his or her fiduciary responsibilities, to be informed about reportable findings identified during the audit so that the plan administrator can decide whether to participate in the IRS or [the Department] correction programs, if applicable. The auditor may want to discuss his or her reportable findings with the plan administrator prior to the written communication so that the plan administrator can take corrective action in a timely manner."

[22] SAS No. 136 ¶¶ 29-46 and A47-A58

[23] SAS No. 136 ¶¶ 47-59 and A78-A85

engagement. Those additional steps are spelled out in detail in SAS No. 136 and depend on whether the revisions relate to the financial statements[24] or the draft Form 5500.[25]

5. Auditor's Report[26]

The final standards require the auditor's report to include a section on "Responsibilities of Management for the Financial Statements" including the description set forth above as well as a section on "Auditor's Responsibilities for the Audit of the Financial Statements." For a Section 103(a)(3)(C) Audit, the auditor's report should also state that the audit did not extend to the certified investment information, except for obtaining and reading the certification, comparing the certified investment information with the related information presented and disclosed in the financial statements, and reading the disclosures relating to the certified investment information to assess whether they are in accordance with the presentation and disclosure requirements of the applicable financial reporting framework. The audit report should also state that the objective of a Section 103(a)(3)(C) Audit is not to express an opinion about whether the financial statements as a whole are presented fairly in all material respects, in accordance with the applicable financial reporting framework.

6. ERISA-Required Supplemental Schedules[27]

The auditor is required to report whether the ERISA-required supplemental schedules to the Form 5500 are fairly stated, in all material respects, in relation to the financial statements as a whole and state that the schedules: contain information required by the Department's rules and regulations for reporting and disclosure; such information is the responsibility of management and was derived from and relates directly to the underlying records used to prepare the financial statements; that the information has been subjected to the auditing and other procedures; and that the auditor, in forming an opinion, evaluated whether the schedules are presented in conformity with the Department's rules and regulations for reporting and disclosure.

If the auditor concludes that information in the ERISA-required schedules is materially inconsistent with, or materially misstated in relation to the financial statements, the auditor should seek revisions and/or the auditor's opinion should be modified accordingly.

E. Department's Efforts in Providing Guidance and Promoting Compliance

In order to aid plan administrators in complying with the relevant ERISA reporting and compliance requirements, the Department has established a specific section on its website. (See: www.dol.gov and go to the EBSA tab, as follows: EBSA > Employers and Advisers > Plan Administration and Compliance > Fiduciary Responsibilities > Fiduciary Education Campaign - Getting It Right - Know Your Fiduciary Responsibilities.) Included is the publication *Selecting an Auditor for Your Employee Benefit Plan* that was last issued in September 2018. In addition

[24] SAS No. 136 ¶ 51

[25] SAS No. 136 ¶ 53

[26] SAS No. 136 ¶¶ 60-76, 98-126, A86-121 and A137

[27] SAS No. 136 ¶¶ 120-121, 127-135 and A146-A152

to this and other helpful publications, the website includes sections for related seminars (previously held in over 50 locations throughout the United States) and webinars, tools (such as "The ERISA Fiduciary Advisor and the 401(k) Plan Fee Disclosure Form"), and references to the Department's employee benefit plan-focused correction programs.

Following the release of the 2015 Study, OCA issued a notice entitled "*Tips for Selecting and Monitoring a Plan Auditor*." This notice was sent electronically to sponsors of plans that are subject to the ERISA financial statement audit requirement as a part of the Department's ongoing outreach efforts with respect to audit quality. The notice also referenced the Department's publication, discussed above.

The notice encouraged, but did not require, plan administrators to consider the following factors in selecting an auditor:

- The number of employee benefit plans the CPA audits each year, including the types of plans;
- The extent of specific annual training the CPA receives in auditing plans;
- The status of the CPA's license with the applicable state board of accountancy;
- Whether the CPA has been cited for deficiencies in prior Department studies, or has been referred to a state board of accountancy or the AICPA for investigation; and
- Whether the CPA's employee benefit plan financial statement audit work has recently been peer reviewed by another CPA and, if so, whether the review resulted in negative findings.

Although the notice did not direct the plan administrator to take any action, the Council understands that many administrators forwarded the notice to their auditor requesting a response.

F. Available Non-Governmental Educational Resources

The Council heard from several witnesses regarding audit-related educational materials that are available to plan sponsors and others involved with the plan. James Haubrock, AICPA EBPAQC Executive Committee Chair, provided a number of educational materials published by the EBPAQC, summarized in Appendix B, that range from the hiring of a quality auditor, through understanding the financial statement audit process and the underlying financial statements. These materials can be located online and through the following: https://www.aicpa.org/.

Dennis Mahoney, Director of the Certified Employee Benefit Specialist Program ("CEBS"), a professional education course of study co-sponsored by the Wharton School of the University of Pennsylvania and the International Foundation of Employee Benefit Plans ("IFEBP"), described to the Council the CEBS course topics specifically addressing the financial statement audit of an employee benefit plan. Mr. Mahoney described one of the Strategic Benefits Management modules titled "Overseeing and managing plan audits." He explained that the learning objectives of this required module are to explain modern accounting concepts and the relevant regulatory framework, and to enable students to be able to describe the major types of information that must be included in the annual financial statements. In addition, the course is designed to help students understand the importance of high-quality financial statement auditing, as well as to describe the compliance-related communications that auditors must obtain and must issue related to various topics, including internal control matters, and to summarize the conditions that are conducive to fraud.

Will Hansen and Nevin Adams for the American Retirement Association ("ARA") described for the Council a newly created certification program sponsored by the Plan Sponsor Council of America. The Certified Plan Sponsor Professional ("CPSP") educational credential is designed to provide "practical, retirement plan administration focused training" for plan sponsors on topics such as choosing, building, and running a plan, understanding investment concepts, and fiduciary obligations for plan sponsors, as well as "Plan Audits and Compliance," a course that focuses plan sponsors on the financial statement audit process.

G. Analysis of Impact of Enhanced Focus on Financial Statement Audits

The Department raised concerns that plan administrators over-emphasized cost in procuring a plan's annual financial statement audit and, in effect, commoditized the process. The Department also believed that plan administrators were not sufficiently availing themselves of the benefits of a robust financial statement audit engagement. The Council gained a better understanding of the Department's concerns from the testimony of Ian Dingwall, retired head of the OCA. The Council also solicited testimony from various professionals, ranging from industry group representatives, attorneys, and consultants who specialize in the employee benefits area, gauging their reaction to the Department's concerns regarding the employee benefit plan financial statement audit process.

Stephen L. Dobrow, testifying on behalf of the National Association of Plan Advisors, shared the Department's concern that the audit requirement is more of a distraction than a benefit for many plan administrators. Mr. Dobrow testified that plan administrators are too busy trying to run their businesses to pay attention to employee benefit plan financial statement audits, but they do understand the risk of receiving an inadequate audit. Mr. Dobrow stated that despite this risk, plan administrators are not incentivized to embrace a proactive audit process. Mr. Dobrow shares the Department's concern that price is the sole determinant in the selection of an employee benefit plan financial statement auditor.

Mr. Hansen, for the ARA, disagreed with Mr. Dobrow not only with respect to the view that plan administrators hired auditors based solely on price, but that they even prioritize price. Moreover, Mr. Hansen doubted that price correlated with financial statement audit quality. Mr. Hansen testified that cost should play a role in the selection of an auditor, just as the auditor's qualifications should. To act in the best interests of participants, a plan administrator should include price in the factors to be considered as a part of the Request for Proposal ("RFP") process to procure the best quality financial statement auditor. Mr. Hansen testified that he had never seen a single study that supports the Department's concerns regarding the financial audit process.

Mr. Adams shared some statistics from informal, nonscientific polling from constituents in the National Association of Plan Advisors ("NAPA") and the Plan Sponsor Council of America ("PSCA"), whom he represents. From a sample size of 110 plan advisors, 57 percent responded that they thought plan administrators chose their benefit plan auditors on price and cost. The

PSCA asked the same question of administrators of both large and small plans, and, of 92 responses, only 17 percent of the administrators indicated that price/cost was the primary consideration when selecting an auditor. When isolating the responses to the smallest plans, price/cost was the primary consideration 31.3 percent of the time.

The Council also heard testimony indicating that even where price and cost was a primary consideration for selection of a financial statement auditor, price and cost are not determinative of audit deficiencies. As Mr. Haubrock observed regarding OCA's audit quality findings, ". . . there is no correlation to fees whatsoever. In fact, if anything, I think … fees weren't necessarily the driver of quality." Rather Mr. Haubrock stated that "it was more the number of plan audits that [the auditors] did that drove quality over the pricing."

Mr. Haubrock testified that, in recent years, the AICPA has increased its oversight of employee benefit plan audits through internal examinations, enhanced peer review processes, and internal monitoring of employee benefit plan auditors. And Mr. Haubrock noted that the number of employee benefit plan auditors has decreased from over 7,500 down to 5,000, and, significantly, that the approximately 2,500 auditor members of EBPAQC perform 85 percent of the total number of audits. Mr. Haubrock told the Council that many auditors have stopped performing employee benefit plan audits because they have decided that the cost of compliance, the continuing professional education ("CPE") requirements, and the risk of performing a deficient audit outweigh the benefit of performing a few employee benefit plan audits per year. With increased standards under the new SAS No. 136, Mr. Haubrock predicted that most accounting firms would not increase their pricing of employee benefit plan financial statement audits, but that those firms currently charging lower fees probably would bring their prices up for financial statement audits.

Mr. Hansen of the ARA testified that he would hesitate to endorse additional efforts in this arena that add any additional burden for plan administrators, because: (1) more time should be allowed to assess the impact of SAS No. 136's effect before burdening administrators with additional tasks; (2) additional guidance is not needed; (3) the premise that plan sponsors are not availing themselves of the financial statement audit process is misplaced and unsupported and therefore adding complexity in the rules is unwarranted; (4) there are already existing resources for plan administrators regarding audit procedures that are available through the Department as well as the private sector; and (5) any additional requirements placed upon plan sponsors would further discourage small employers from sponsoring retirement plans.

Finally, Chantel Sheaks of the U.S. Chamber of Commerce observed that previous Advisory Councils have noted that part of the audit requirement was for participants to be able to understand the financial statements. Ms. Sheaks doubted that enhanced reporting requirements would improve the understanding of financial statements by either the administrator or the participants, but she feared that it would increase costs.

H. The Council's Observations

1. The statute limits the purpose and use of a plan financial statement audit; it only assures the reader of the financial statements that there are no material misstatements in those statements and of the fairness of the financial statements in all material respects. Accordingly, the Council finds that, to the extent that the Department seeks to enhance the safety of plan assets and

improve the plan's compliance with the structural and fiduciary requirements of title I of ERISA, increasing the awareness of plan administrators of the tools afforded to them through the financial statement audit process could help, but the Department has not been provided with the authority to change the scope of the financial statement audit or the standards by which it is conducted.

Accordingly, the Council considered, but does not recommend, that the Department establish financial statement audit standards that are not required under GAAS. Further, given that the implementation of SAS No. 136 is just commencing, the Council did not find an additional review of the financial statement audit standards to be warranted at this time even if the Department had the authority to do so.

2. Most of the Department's observed deficiencies in financial statement audits, regardless of their importance, appear to be technical and procedural errors made by the auditor. This observation was underscored by the results of the 2015 OCA Study, which demonstrated that audit quality correlated closely with the experience of the auditor. Firms performing only one or two plan audits per year had a 76 percent deficiency rate, while firms performing at least 100 audits per year had a deficiency rate of 12 percent. The correlation suggests to the Council that there is little that is within the control of the plan administrator – other than educating them to select more experienced auditors – that could effect a reduction of financial statement audit deficiencies.

3. Improvement in audit quality will result in more accurate financial statements, but it is not clear whether improved audit quality would result in (i) greater compliance with design or operational rules found in Title I of ERISA or the tax qualification or exemption rules of the Code, or (ii) of greater protection from fraud and theft. Although Mr. Dingwall, Mr. Haubrock, Mr. Dobrow, and Jewell Lim Esposito of Fischer Broyles LLP told the Council that they believed greater involvement in the financial statement audit process would lead to improvement in both of these areas, the Council received no evidence of this effect. Tellingly, Serena Simons of The Segal Group explained to the Council that the process that her firm uses to conduct compliance audits asks few questions about, and certainly does not focus in any way on, the plan's financial statement audit process. This suggested to the Council not only that there may not be significant compliance gains made by focusing plan administrators more pointedly on the financial statement audit process itself, but also that the role of financial statement audits in overall plan compliance and safety issues, although relevant and necessary, could be overestimated by plan administrators, as the financial statement audit alone should not be relied upon to assure the safety of plan assets or the plan's operational compliance with its governing documents or with the requirements of ERISA and the Code.

The Council did learn through its review of SAS No. 136 that one area where financial statement audits performed under the new standards might improve the overall compliance of the plan's operations is with respect to the newly stated standard that, except in rare circumstances, the auditor should test a plan's operational compliance to the extent that those plan operations pose a material risk of misstatement in the financial statements. This improvement would not be dependent, however, on the plan administrator's greater involvement in the financial statement audit process.

4. Nonetheless, the Council finds that more and better education of plan administrators in the financial statement audit process would be desirable. The Council heard testimony that administrators do not understand the value of accurate financial statement audits. Ms. Esposito, Mr. Dobrow, and Mr. Haubrock shared Mr. Dingwall's view that the level of understanding of the financial statement audit process is low among a large number of plan administrators. Each of these witnesses encouraged additional educational outreach by the Department to plan administrators.

Further, there is evidence that plan administrators would welcome the additional educational outreach. Mr. Adams presented informal survey results that indicated that a large majority of plan administrators would find enhanced communications and greater outreach by the Department to the plan administrator community helpful.

The Council finds that in order to shrink the "expectations gap," a key aspect of the education that needs to be disseminated to plan administrators by the Department regards the limited scope and purpose of a financial statement audit. For example, administrators need to know that even though a financial statement audit might help a plan administrator detect some cases of fraud or theft, the audit is not expressly designed to do so. Similarly, administrators need to know that even though a financial statement audit might help a plan administrator detect design or operational compliance errors, the financial statement audit is not expressly designed to do so.

Ms. Esposito testified that plan administrators often assume that a clean financial statement audit means there are no compliance issues with the plan, and many are shocked to later experience compliance issues that went undetected in the financial statement audit process, which she calls "ERISA bombs." Ms. Esposito explained that plan administrators often need to be reminded that, while some compliance testing is a necessary part of the financial statement audit process, the financial statement audit process is no substitute for rigorous internal financial procedures and controls or certainly for an overall internal ERISA compliance review.

The contrast between a financial statement audit and a compliance audit – and the frequency as to which plan administrators do not make the distinction – was made evident by Ms. Esposito's testimony and the testimony the Council heard about the robust market for compliance review services offered by various types of plan providers, including accountants (outside the financial statement audit process), lawyers, consultants, and various other plan providers. Ms. Simons described her firm's compliance review process, which involves a checklist of approximately 75 specific compliance items and may take from 100 to 150 hours to complete. As noted above, questions about the annual financial statement audit comprise only a minor segment of the review. Ms. Simons testified that the characteristics of a successful compliance review process include having sufficient time to complete the review, voluntary participation by the administrator, a focus on internal correction, and an interactive interview process. The Council observed that these characteristics appear to be the converse of the characteristics of the financial statement audit process, which is performed on an involuntary basis, must be finalized during the window between the end of the fiscal year and the Form 5500 filing deadline, and must be publicly disclosed. Thus, the Council concluded that the plan administrators should be educated on the limits of the financial statement audit process.

Finally, the Council observed that the Department should review the models of robust education programs regarding the financial statement audit process that exist in the employee benefit plan professional community. Two industry groups have responded to the educational needs of the employee benefits community by adding an audit component to their certification programs: The IFEBP includes a module in its CEBS strategic benefits management course that focuses on overseeing/managing plan audits; and PSCA introduced a new plan administrator education credential, the CPSP, with one if its nine key areas of focus being plan audits and compliance. These courses could inform any new sub-regulatory guidance that the Department issues regarding the financial statement audit process.

5. Development of additional requirements or incentives are either not justified or would be ineffective, or both. Other than the testimony of Mr. Dingwall and Mr. Dobrow, the witnesses that testified before the Council did not support additional guidance that would be viewed as new requirements by the plan administrators. For example, these witnesses opposed guidance being issued in field assistance bulletins or included in Form 5500 instructions, arguing that the current process of selecting auditors was sufficient, that the deficiencies found in the Department reviews over the last decade resulted from audit errors rather than plan administrator actions, and that changes to guidance would result in an increased burden on plan administrators.

Notwithstanding the negative view of many witnesses, the Council did consider whether plan administrators could be incentivized to take a more proactive role in the financial statement audit process. In this regard the Council contemplated whether a checklist added to a schedule to the Form 5500 – which in exchange for its voluntary completion by the plan administrator would result in the waiver of any civil penalties under Section 502(c)(2) of ERISA for an inadequate audit – could be a useful tool in promoting greater attention and care paid to the financial statement audit process. The concept was rejected by the Council, however, because the Department's regulations under Section 2560.502c-2(b)(3) already provides the plan administrator with a 45-day cure period for a rejected Form 5500 due to a deficient financial statement audit. The existing availability of a cure period would be inconsistent with the contemplated waiver.

6. SAS No. 136 should improve the quality of financial statement audits; coordinating the Department's education programs with the implementation of the new standard should produce a wider and more attentive audience. Although the new SAS No. 136 standards are not yet in effect, in the Council's view, it is predictable that the new standards will improve the financial statement audit process for auditors and plans and provide more transparency and assurance for participants and beneficiaries, especially with respect to Section 103(a)(3)(C) Audits.

It appears to the Council that auditors are likely to heed the specific provisions for employee benefit plan financial statement audits and recognize that employee benefit plan audits are complex and different from other financial statement audits, and that even for experienced employee benefit plan auditors the new procedures could lead to increased vigilance and plan provision compliance testing. Further, the Council is optimistic that the requirement in the new standards – that plan administrators be expressly reminded it is the responsibility of the administrator, and not that of the auditor, to maintain a current plan document and to administer the plan and to produce financial statements that fairly and accurately represent the plan's financial condition – will result in greater attention being paid not only to the financial statement audit process, but to overall compliance with ERISA and the Code by the plan administrator.

Finally, the Council views the new procedures for a Section 103(a)(3)(C) Audit – requiring auditors to inquire as to the certifications, to compare the reported information to the certified information, and to provide an opinion with respect to the non-certified investments and other amounts and disclosures in the financial statements and the Form 5500 supplemental schedules – as an important development in increasing the accuracy of the plan financial statements because the administrator would be responsible for gathering the certifications and certified financial information but would be assisted by inquiry by the auditor in that regard, and because the auditor would test and provide an opinion as to the non-certified information in the financial statements and Form 5500 and related schedules. Accordingly, it appears to the Council that all of these changes incorporated into SAS No. 136 should, over time, help to reduce audit error and improve the accuracy of the plan financial statements.

7. Targeting the related professional community would be an efficient method of spreading the education. Messrs. Hansen, Dobrow, and Adams testified that plan administrator education could best be achieved through outreach to the financial advisor community – specifically targeting advisors who specialize in employer-sponsored retirement plans.[28] The Council's sense was that, for small and mid-sized plans, this approach could have a greater impact than trying to reach plan administrators directly. Their testimony was supported by recent survey data that indicate that plan administrators are increasingly reliant on advisors for fiduciary education and guidance, [29] suggesting that advisors who specialize in employee benefit plans figure prominently in the fiduciary governance of those plans. Yet, the majority of employee benefit plan advisors appear to be largely unaware of the Department's concerns around financial statement audits. As a result, relatively few have been proactive in educating or guiding their plan sponsor clients on the fiduciary considerations associated with audits. Only 37 percent of the 110 plan advisor respondents in an informal August 2019 NAPA survey had been directly involved in any aspect of a financial statement audit in the past two years and, at least in some cases, only from the perspective of helping round up information. When asked if they knew that the Department had a guide titled "Selecting an Auditor for Your Employee Benefit Plan," a clear plurality (48 percent) did not, and another 15 percent said they did "remember a publication, though not that specific one."

III. BASIS FOR RECOMMENDATION

Based on the observations described above, the Council recommends that the Department update and enhance the subregulatory guidance and educational tools made available to administrators who are charged with procuring an annual financial statement audit on behalf of the plan. The recommendation has five specific elements each of which, in the view of the Council, should increase the plan administrator's understanding of the value of the financial statement audit and

[28] Hansen, Dobrow, and Adams testimony. Mr. Adams also noted that roughly 4,000 advisors are retirement plan specialists that hold the NAPA certified plan fiduciary advisor ("CPFA") credential.

[29] Harris Insights and Analytics, *2019 Plan Sponsor Attitudes Study*. Respondents included 1,252 plan sponsors. All plans in the survey had at least 25 participants and at least $3 million in assets; The Callan Institute, *2019 Defined Contribution Trends*. Respondents included 106 plan sponsors. More than 90% of plans in the survey had over $100 million in assets; 62.2% had more than $1 billion in assets; Plan Sponsor of America (PSCA), *61st Annual Survey of Profit Sharing and 401k Plans*. The survey was published in December 2018 and reflects the experience of 605 plans.

the value of the plan administrator's proactive participation in the financial statement audit process. The five elements are as follows:

A. **Send notices to plan administrators advising them of their responsibilities regarding selecting, retaining, and interacting with the independent auditor of the plan's financial statements, and of the tools available to assist them in these responsibilities**.

The Council recommends that the Department repeat its 2015 initiative by sending a notice from the Department to each plan administrator identified as likely to be subject to a required financial statement audit for the upcoming plan year informing the administrator of (a) its obligations under Section 103 of ERISA (and the civil penalties under Section 502(c)(2) of ERISA that could be triggered by noncompliance), (b) the new SAS No. 136, (c) the Department's educational materials available on the Department's website, and (d) the availability of other educational materials from professional associations such as AICPA, PSCA, and CEBS. Anecdotal evidence suggests that the previous initiative at least increased the awareness by plan administrators of the financial statement audit process. Given the attention that the new SAS No. 136 is likely to generate, a renewed letter from the Department should draw even greater attention and appropriate responses from the plan administrators than it did in 2015. Direct outreach such as this notice will tie together each of the other elements of the Council's recommendation. Accordingly, the Council encourages the Department to obtain the necessary budgetary resources to fund the production and distribution of this notice to the broad population of relevant plan administrators.

B. Publish a revised brochure regarding the selection, retention and interaction with an independent auditor of the plan's financial statements, including a best practice checklist. The Council has drafted a sample checklist, which is included in Appendix A to this report.

The Council recommends that the Department reissue an updated and expanded version of its existing brochure now titled "*Selecting an Auditor for Your Employee Benefit Plan*" to more explicitly cover plan administrator responsibilities beyond merely the selection of the financial statement auditor but to cover the plan administrator's responsibilities with respect to retaining and communicating with the financial statement auditor as well. A revised brochure would be timely, given the attention that SAS No. 136 is likely to receive, and it would provide an opportunity for the Department to explain to the plan administrator the value that a financial statement audit provides and the limits on the reliance the administrator should place on the financial statement audit in terms of ensuring the safety of plan assets and the compliance of the plan with the requirements of ERISA and the Code. The Council further recommends that the revised brochure include a checklist of best practices for plan administrators to consult whenever they are engaging an auditor of the plan's financial statements. At Appendix A, the Council has attached a sample checklist for the Department's consideration. In the Council's view, a checklist is the most direct, accessible, and convenient way to facilitate the plan administrator's understanding of its roles and responsibilities in the financial statement audit process.

C. Publish a list of the most common deficiencies found in plan audits.

The Council recommends that the Department publish on its website a list of the most common deficiencies found in financial statement audits. The informal survey data provided to the Council indicates that plan administrators and their advisors strongly favor the publication of such a list. In the Council's view, plan administrators would use the most common deficiencies list as a tool by which to monitor the plan's financial statement auditor's performance; that is, the administrator will refer to the list in asking the auditor what reasonable steps the auditor has taken to avoid those deficiencies in the audit being performed on behalf the administrator's plan. The Council has reviewed the Department's previous studies, which appear to contain sufficient information from which such a list could be collated, categorized, and contextualized so that the list would be understandable by the plan administrator and informative to the plan auditor.

D. Make more information available to plan administrators and their advisors regarding independent auditors who perform financial statement audits for employee benefit plans, *e.g.*, add features to EFAST2 to allow for searches of filings by auditor.

Because a key responsibility of the plan administrator with respect to the financial statement audit is the selection of a qualified auditor, having a tool that could help the plan administrator make this assessment would be valuable. For this reason, the Council recommends that the Department make available a searchable list of auditors which have performed financial statement audits. The obvious way of producing such a tool would be to add features to the EFAST2 system to permit searches of plan auditors. By making this data searchable, plan administrators could identify the auditor's previous experience performing employee benefit plan audits. Given the correlation between the deficiencies found by the Department and the relative inexperience of the auditors in a predominant number of such incidences, a plan administrator could be helped in evaluating a financial statement auditor just by being able to identify the volume of relevant work that the auditor had previously performed. Not surprisingly, the development of this tool was viewed favorably by the vast majority of plan administrators and their advisors who responded to the informal surveys provided to the Council.

E. Expand the Department's financial statement audit education programs to target plan advisory groups in the Department's outreach.

The Council recommends that the Department specifically address its educational outreach programs on the plan administrator's role and responsibilities in the financial statement audit process to the professional plan advisor community. Based on the evidence received by the Council, it appears that (a) plan administrators rely to a great extent on their advisors to explain to them their responsibilities, and (b) the professional advisor community was insufficiently informed about the Department's concerns about the relative inattention that the Department perceived many administrators were paying with respect to the financial statement audit process. Targeting the plan advisor community as the audience for the Department's educational outreach regarding the plan administrator's role and responsibilities in the financial statement audit process should be the most efficient way to spread the Department's message.

IV. APPENDICES

A. Sample Plan Administrator's Checklist Regarding Financial Statement Audits

For certain plans, especially large, funded plans (see DOL Instructions for Form 5500, *Section 1: Who Must File* and *Section 4: What To File*), the plan sponsor is required to engage an independent qualified public accountant to perform an audit of the plan's financial statements.

The following checklist, while not exhaustive, is intended to highlight certain plan sponsor responsibilities as they relate to the plan's financial statement audit and a sample of resources that are available to educate and assist the plan sponsor.

____ 1. Determine whether the plan requires a financial statement audit

- See DOL Instructions for Form 5500, *Annual Return/Report of Employee Benefit Plan*, *Section 1: Who Must File*

____ 2. Consider an auditor's relevant experience before retaining an independent qualified public accountant – the plan auditor

- See DOL publication *Selecting an Auditor for Your Employee Benefit Plan*
- See also the AICPA EBPAQC Plan Advisory: *The importance of hiring a quality auditor to perform your employee benefit plan financial statement audit*

____ 3. Determine whether a full scope audit or Section 103(a)(3)(C) Audit (formerly "limited scope audit") is required

- See DOL publication *Selecting an Auditor for Your Employee Benefit Plan*
- See also the AICPA EBPAQC Plan Advisories: *Employee benefits plans — financial statement audits;* and *Limited Scope Audits of employee benefit plans*

____ 4. Review the auditor's letter of engagement (an engagement letter) carefully to make sure that you understand the stated responsibilities of the plan administrator and the auditor respectively (you may wish to engage counsel with expertise in employee benefits to assist you in this regard)

- See DOL publication *Selecting an Auditor for Your Employee Benefit Plan*
- Schedule a meeting with the auditor (and appropriate other plan service providers) to discuss the plan and to develop and communicate the audit process

____ 5. Prepare and assemble the items that the auditor will require in order to perform a quality audit of the plan's financial statements, and note the deadlines for each item's production to the auditor

- Determine the appropriate individual(s) and/or service providers to fulfill the requests and establish relevant timing
- See also the AICPA EBPAQC Plan Advisory: *Effective monitoring of outsourced plan recordkeeping and reporting functions*

____ 6. Establish a schedule for regular communication with the auditor, and other service providers – as appropriate, in order to monitor the progress of the audit process and to address any potential recommendations, concerns or issues

____ 7. Review and discuss the required communications from the auditor and respond, as necessary

- See DOL publication *Selecting an Auditor for Your Employee Benefit Plan*
- See also the AICPA EBPAQC Plan Advisory: *Understanding auditor communications*

____ 8. Review and discuss the draft audited financial statements and the attached report of the auditor, the draft of Form 5500, including all required schedules and attachments, and compare to the audited financial statements

B. AICPA Employee Benefit Plan Audit Quality Center Resources

The AICPA Employee Benefit Plan Audit Quality Center prepares Plan Advisories for plan sponsors, administrators, and trustees. These comprehensive documents contain information to assist them in understanding their fiduciary and other responsibilities with respect to various aspects of their plans.

Limited Scope Audits of Employee Benefit Plans
If your employee benefit plan is required to have a financial statement audit, in certain circumstances described in this advisory, you have the option to instruct the auditor not to perform any auditing procedures with respect to investment information. This advisory helps you understand these limited scope audits. This Advisory will be redone for the new financial statement audit standard but not before the end of 2019.

The Importance of Hiring a Quality Auditor to Perform Your Employee Benefit Plan Audit
When hiring a plan auditor, plan administrators should use the same care and prudence in hiring a plan auditor that they use when hiring any individual or entity that provides services to the plan.

Employee Benefit Plans—Financial statement audits
Understand the independent audit of the financial statements of an employee benefit plan.

Understanding Auditor Communications
Plan Sponsors and others receive various communications from their plan auditors throughout the year.

Effective Monitoring of Outsourced Plan Recordkeeping and Reporting Functions
Hiring a service organization to perform plan administration services is a fiduciary function and, as such, plan administrators are required to periodically monitor their service organizations to ensure they are performing the agreed-upon services.

The Importance of Internal Controls in Financial Reporting and Safeguarding Plan Assets
Effective controls reduce the risk of asset loss and help ensure that plan information is complete and accurate, financial statements are reliable, and laws and regulations are complied with.

Valuing and Reporting Plan Investments
Investments are the most significant asset in a benefit plan, and plan management is responsible for ensuring proper valuation and reporting of those assets. Each different investment has unique valuation and disclosure considerations.