Agenda Item 4

Reports on ERISA Audits — Cover Letter and Issues Paper

Objective

To continue discussing the development of an auditor's report specific for employee benefit plans, in particular reporting on internal control over financial reporting and compliance with certain provisions of Department of Labor Rules and Regulations for Reporting and Disclosure under ERISA.

Task Force

The Employee Benefit Plan Reporting Task Force (the EBP task force) members are:

- Darrel Schubert (Chair)
- Josie Hammond
- Jerry Murray
- Scot Philips (TIC representative)
- Alice Wunderlich
- Michael Auerbach (DOL)

Agenda Items Presented

Item 4 – Cover Letter and Issues Paper

Item 4A – Comparison of AU-C 806 to Yellow Book

Item 4B – Concept for Possible SAS on Internal Control and Compliance

The members of the EBP task force will use Agenda Item 4 as a basis for discussion at the October ASB meeting. Agenda Item 4A is provided for informational purposes to contrast reporting as a by-product report versus the Yellow Book. Agenda Item 4B has been provided to illustrate the concepts discussed in this issue paper into one document.

The issues discussed in this issue paper are for the purpose of asking the ASB for direction in developing new requirements for employee benefit plan audits to include a report on internal control over financial reporting and compliance with certain provisions of DOL rules and regulations for reporting and disclosure. Therefore we ask that the ASB focus on the concepts of the document and not necessarily the wording.

Issues Paper

Background

In January 2015 a special task force of the ASB (EBP task force) was formed to consider a proposal to improve the quality of employee benefit plan (EBP) audits by strengthening the EBP auditor's report. The Employee Benefits Security Administration (EBSA) of the Department of Labor (DOL) asked us to rethink the EBP auditor's report to help auditors better understand their responsibilities and to provide users with more information about what auditors do, especially in the case of the limited scope audit, as permitted by the DOL's rules and regulations for reporting and disclosure under the Employee Retirement Income Security Act of 1974 (ERISA). The DOL provided specific suggestions on ways to improve auditor reporting for plans.

Summary of the ASB's discussion at the July 21, 2015 ASB Meeting

At the July 2015 ASB meeting, the ASB supported the development of a new auditing standard to address the form and content of the auditor's report for employee benefit plans. The ASB asked the EBP task force to also consider whether there is a need to revise the performance standards related to compliance aspects of employee benefit plan audits to help with audit quality. At the July meeting Mr. Schubert noted that the task force planned to discuss compliance reporting and bring the task force's views to the ASB at a future meeting. The highlights from the July 2015 ASB meeting summarize the ASB's discussions about the form and content of the standard auditor's report.

Task force Discussions

Since the July ASB meeting, the EBP Task Force focused on developing a model for employee benefit plan reporting to include a report on internal control over financial reporting and compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA. This agenda item is intended to discuss possible ways for an employee benefit plan to report on internal control and compliance as part of the reporting model being developed for employee benefit plans and to gain direction from the ASB. At a future ASB meeting, the task force plans to bring a proposed SAS for the complete reporting model for employee benefit plans (this includes a proposed standard report for both full scope and limited scope audits, and the reporting on internal control and compliance).

Issues for ASB discussion

New Reporting Section on Compliance

The DOL requested a new section be added to the auditor's report that would address the tests the auditor performs, in connection with the audit, of the plan's compliance with certain provisions of laws, regulations, plan documents, and other agreements.

The EBP task force believes that this form of reporting could be helpful to include in the auditor's report because there are many aspects of an ERISA audit that are compliance in nature. The task force recognizes however, that such form of reporting would require an identification of which compliance tests are considered within the scope of what is being reported on. The EBP task force does not believe that a broad reference to DOL rules and regulations would be appropriate, but rather there would need to be a determination of the significant compliance areas that may have a direct effect on the financial statements being audited. The EBP task force asked the DOL to provide a listing of the compliance tests that they believe are of most importance and which they would like to be covered by this compliance report. The EBP task force noted that creating a requirement to report on compliance could change the performance procedures for an ERISA audit.

At the April 9, 2015 AITF meeting, the EBP Task Force provided the AITF with an update of this project and asked for their initial feedback. The AITF expressed some concerns with reporting on compliance because of the lack of an existing compliance framework to audit. In addition, the AITF noted that the compliance tests subject to such reporting should be limited to those items that could have a direct effect on the financial statements and therefore should already be tested as part of the financial statement audit.

EBP Task Force Discussions

The EBP Task force discussed various frameworks in which to base employee benefit plan specific compliance reporting. The EBP task force considered (a) Yellow Book reporting on internal control and compliance, (b) by-product reporting under AU-C 806 *Reporting on Compliance with Aspects of Contractual Agreements or Regulatory Requirements in Connection with Audited Financial Statements*; and (c) compliance audits under AU-C 935 *Compliance Audits*. Overall the task force believes that compliance audits under AU-C 935 do not fit the particular circumstances of an EBP audit. The task force liked aspects of both the Yellow Book reporting and AU-C 806 and noted that the reporting was somewhat similar under both sets of requirements. See Agenda Item 4A- *Comparison of Reporting Under AU-C 806 Versus Yellow Book* to view a comparison of elements of an AU-C 806 report versus a yellow book report.

Task Force Recommendations

The EBP task force believes that the proposed auditor reporting standard being developed for employee benefit plans should include a requirement for the auditor to report on internal control over financial reporting and compliance with certain provisions of DOL rules and regulations for reporting and disclosure because such reporting will help users and auditors to better understand the audit work performed in an employee benefit plan audit. The EBP task force favored the Yellow Book approach to reporting on internal control and compliance, however the EBP task force had concerns with describing, in the report, all significant deficiencies, material weaknesses, and instances of noncompliance identified during the audit because the users of employee benefit plan financial statements differ from that of a government. The EBP task force used the Yellow Book as a base for developing a proposed standard, with modifications as the task force deemed appropriate to the circumstances.

The EBP task force proposes the following requirement be established for all plans:

Possible Requirements	***Possible Application Material***
.01 When providing an opinion on employee benefit plan financial statements, the auditor should also report on internal control over financial reporting and on compliance with certain provisions of the Department of Labor (DOL) rules and regulations for reporting and disclosure under the Employee Retirement Income Security Act of 1974 (ERISA). The auditor should report on internal control and compliance, regardless of whether or not the auditor identifies control deficiencies or instances of noncompliance.	.A1 It is the responsibility of management, with the oversight of those charged with governance, to ensure that the plan's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in a plan's financial statements.[1] .A2 The requirements in this section related to reporting on compliance are designed to assist the auditor in identifying instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA as part of the audit of the financial statements. The auditor is not responsible for preventing noncompliance with such provisions and cannot be expected to detect noncompliance with all laws and regulations.
.02 The report on internal control over financial reporting and compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA should be in writing and should be provided either in a separate report or in one or more paragraphs included in the auditor's report on the financial statements.	

[1]Paragraph .03 of AU-C 250 *Consideration of Laws and Regulations in an Audit of Financial Statements*.

Action Requested of the ASB

1. Does the ASB agree with the EBP task force that there is merit to developing a report on internal control over financial reporting and compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA, as part of the reporting model for employee benefit plans?

Issue 1: Procedures to Report on Compliance

The task force believes that as a start, there is a need for the proposed standard to identify the compliance procedures the auditor should perform, as part of an EBP audit in accordance with generally accepted auditing standards (GAAS), to enable the auditor to provide a report on compliance with certain provisions of DOL rules and regulations for reporting and disclosure.

The task force noted that the DOL rules and regulations for reporting and disclosure under ERISA creates a compliance framework, however there are aspects of such compliance requirements that do not affect the financial statements and therefore should not be included within the context of such reporting. The EBP task force discussed identifying the significant compliance areas that may have a direct effect on the financial statements being audited. Accordingly, the task force believes it is appropriate to develop required procedures to enable the auditor to report on compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA.

Task Force Recommendations

The EBP task force developed the following proposed requirement to set the framework for what the auditor will be reporting on.

Possible Requirements	***Possible Application Material***
.03 In order to report on compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA the auditor should perform the following procedures, if they have not already been performed as part of the financial statement audit.	
a. For defined contribution plans, determining whether the aggregate of the participants' accounts agree to the amount of net assets available for benefits	

b. For defined contribution plans, determining whether forfeitures were used in accordance with the plan document.	
c. For defined contribution plans, determining whether net earnings have been properly allocated to participants and beneficiaries (active and inactive or terminated)	
d. Testing whether identified prohibited transactions have been appropriately disclosed in the supplemental schedules	
e. Testing whether the plan has complied with vesting provisions in accordance with the plan document	
f. Testing whether the plan has complied with eligibility provisions in accordance with the plan document	
g. Testing whether benefit payments or claim payments have been made in accordance with the plan document	
h. Testing whether contributions have been made in accordance with the plan document, including that the use of compensation upon which contributions are based is consistent with the definition of compensation in the plan document	
i. For multiemployer plans, testing that the plan has allocated expenses in accordance with the feasibility study or as appropriate between the plans and the union	
j. Inquiring of management whether the plan has performed and passed, corrected, or plans to correct failures of relevant IRC compliance tests, within the time provided by the regulations.	.A3 To determine that a plan is operating within the specific guidelines established by the plan document in accordance with the IRC, certain nondiscrimination and other compliance tests are performed annually by plan management. Exhibit A—*Nondiscrimination and Other Operating Tests for Plan Qualification* includes a list of

	IRC requirements with which a plan is required to comply in order to maintain its tax exempt status. This list contains the compliance tests contemplated by paragraph 3(j) when reporting on compliance in this SAS. This list is not all inclusive, however, the auditor would not be required to report on compliance with other IRC compliance tests other than those listed in exhibit A.
k. For multiemployer plans, testing, as part of contribution testing, whether there are receivables from certain employers	
l. Obtain written representations from management	
1. that plan management has communicated to the auditor whether the plan has performed and passed or corrected failures of relevant IRC compliance tests. 2. that when the report on compliance is not presented with the audited financial statements, management will make the audited financial statements readily available to the intended users of the report on compliance no later than the date of issuance by the entity of the report on compliance and the auditor's report thereon.	

EXHIBIT A—NONDISCRIMINATION AND OTHER OPERATING TESTS FOR PLAN QUALIFICATION

This list contains the compliance tests contemplated by paragraph 3(j) when reporting on compliance in this SAS.

Type of Test	Applicable IRC reference
3. Minimum coverage test	IRC section 410(b) (retirement plans only)

4. Nondiscrimination test	IRC Section 401(a)(4) or 505 (retirement plans, and if funded through VEBA, welfare plans) (Collectively bargained (CB) plans are deemed to automatically satisfy this test.)
5. Average deferral and contribution percentage limits	IRC Section 401(k) and (m) (defined contribution plan only; however 403(b) plans with employer contributions are only subject to the contribution percentage test)
6. Top heavy test	IRC Section 416 (qualified retirement plans only; not 403(b) plans; plans with no key employees, and CB plans are deemed to automatically satisfy this test)
7. Benefit and contribution limits	IRC Section 415(b) (retirement plans only)
8. Employee deferral contribution limitations	IRC Section 402(g)- defined contribution plans only)
9. Minimum funding obligations	IRC Sections 412 or 430 (defined benefit plans and money purchase pension plans)
10. Diversification rules for ESOPs	IRC Section 401(a)(28)
11. Unrelated business income tax	IRC Sections 419A and 511 (retirement and health and welfare plans – if plans are invested in other than typical passive investments, such as hedge funds, partnerships, or real estate)

Action Requested of the ASB – Issue 1

2. Does the ASB support the EBP task force's approach to require specific compliance procedures to be performed by the auditor in order to report on compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA?

Issue 2 — Communication with Those Charged with Governance

Once the procedures for reporting on compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA were established (see issue 1), the task force discussed how and what to report on compliance in a separate report or in the auditor's report.

The task force considered three options for such reporting:

Option 1 (general statement of auditor's responsibilities relating to compliance)

This option would require the auditor to include standard language in the auditor's report (possible OM paragraph) that says that as part of the EBP audit, the auditor is required to perform procedures on the plan's compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA.

Option 2 *(Include a description of instances of noncompliance)*

Option 2 would require the auditor to report, in a separate report or in the auditor's report, a statement that the says that as part of the EBP audit, the auditor is required to perform procedures on the plan's compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA and include a description of the instances of noncompliance that were identified as part of audit of the financial statements. The EBP task force discussed a possible filter to determine which ones rose to the level to be reported.

Option 3 (Require communication with those charged with governance)

Option 3 creates a new communication requirement for the auditor to communicate to those charged with governance the items of noncompliance that were identified as part of the compliance procedures performed (as discussed in Issue 1). Such communication would be similar to the required communication in AU-C 265 *Communicating Internal Control Related Matters* and would serve as a basis for further reporting about instances of noncompliance.

The auditor would then be required to report, in a separate report or in the auditor's report, that GAAS requires the auditor to communicate to those charged with governance instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA that have been identified during the audit of the financial statements. Such report would also include whether or not the auditor identified instances of noncompliance that have been communicated to those charged with governance. Under this option, the auditor would be permitted, but not required, to include a description of those instances of noncompliance that were identified in the report on compliance. (See Issue 3)

EBP Task Force Recommendations

The EBP task force supports option 3 because they believe it will provide more transparency to the compliance aspect of the audit and help to drive better audit quality by requiring the auditor to communicate their findings to those charged with governance.

The EBP task force noted that option 1 does not provide transparency into the audit and will not provide much enhancement to the auditor's report.

The EBP task force discussed the Yellow Book framework for reporting on compliance and noted that the Yellow Book requires the report to describe the instances of noncompliance that were identified as part of the audit. Certain members of the EBP task force expressed concerns with option 2 and felt that describing the identified instances of noncompliance in the report could hinder communications with management and those charged with governance.

The EBP task force supported option 3 because they believe that GAAS should provide a framework for the auditor to first communicate their findings to those charged with governance about instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA. Such communication can then provide the auditor with a basis for further reporting about such compliance. In addition, the DOL has the ability to request from the plan sponsor, such communications. Therefore, if the report on compliance contains information about whether the auditor identified and communicated instances of noncompliance to those charged with governance, then the DOL may have access to that information if they choose to request it.

The EBP task force developed the following proposed requirement to require the auditor to communicate with those charged with governance as discussed in option 3:

Possible Requirements	***Possible Application Material***
Communication to Management and Those Charged with Governance of Instances of Noncompliance With Certain Provisions of the DOL Rules and Regulations for Reporting and Disclosure Under ERISA	*Communication to Management and Those Charged with Governance of Instances of Noncompliance With Certain Provisions of the DOL Rules and Regulations for Reporting and Disclosure Under ERISA*
.04 The auditor should communicate in writing to those charged with governance on a timely basis instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA that have been identified by the auditor as a result of the procedures performed in accordance with paragraph .03 (see issue 1).	
.05 The auditor also should communicate to management at an appropriate level of responsibility, on a timely basis, in writing, identified instances of noncompliance that the	

auditor has communicated or intends to communicate to those charged with governance, unless it would be inappropriate to communicate directly to management in the circumstances.	
.06 The communications referred to in paragraphs .04-.05 should be made timely, but no later than 60 days after the report release date.	
.07 The auditor should include in the auditor's written communication to those charged with governance a description of identified instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA	.A4 Exhibit B—*Illustrative Auditor's Written Communication* includes an illustrative communication indicating that there were instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA that were reported to those charged with governance.
a. A description of the instances of noncompliance that have been identified as a result of the procedures performed in paragraph .03 and an explanation of their potential effects	
b. Sufficient information to enable those charged with governance and management to understand the context of the communication. In particular, the auditor should include in the communication the following elements that explain that	
1. In planning and performing the audit of the financial statements, the auditor performed tests of compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA as part of obtaining reasonable assurance about whether the financial statements are free from material misstatement. Providing an opinion on such compliance with those provisions was not the objective of the audit.	
2. The auditor is not expressing an opinion on compliance with those provisions	
3. Management is responsible to ensure that the Plan's operations are conducted in	

accordance with the provisions of applicable laws and regulations, including compliance with the provisions of applicable laws and regulations that determine the reported amounts and disclosures in the Plan's financial statements. The auditor is not responsible for preventing noncompliance with such provisions and cannot be expected to detect noncompliance with all laws and regulations.	
4. The auditor's consideration of compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA was not designed to identify all instances of noncompliance with such provisions and therefore instances of noncompliance with such provisions may exist that were not identified.	
	.A5 Management may wish to prepare a written response to the auditor's communication regarding such items of noncompliance identified during the audit. Such management communications may include a description of corrective actions taken by the plan, its plans to correct the instances of noncompliance, or a statement indicating that management believes the cost of correcting the instances of noncompliance would exceed the benefits to be derived from doing so. If such a written response is included in a document containing the auditor's written communication to management and those charged with governance concerning the instances of noncompliance with certain provisions of the DOL Rules and Regulations for Reporting and Disclosure under ERISA, the auditor may add a paragraph to the written communication disclaiming an opinion on such information. The following is an example of such a paragraph: *ABC 401(k) plan's written response to the instances of noncompliance with certain provisions of the DOL rules and*

	regulations for reporting and disclosure under ERISA identified in our audit was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.
c. An appropriate alert, in accordance with section 905, *Alert That Restricts the Use of the Auditor's Written Communication*	
.08 When the auditor issues a written communication stating that no instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA were identified during the audit, the communication should include the matters in paragraph. .07b and .07c.	

EXHIBIT B—ILLUSTRATIVE AUDITOR'S WRITTEN COMMUNICATION

The following is an illustrative auditor's written communication encompassing the requirements in paragraph .07.

To Management and [*identify the body or individuals charged with governance, such as the entity's Board of Directors*] of ABC 401(k) Plan

In planning and performing our audit of the financial statements of ABC 401(k) Plan (the "Plan") as of and for the year ended December 31, 20XX, in accordance with auditing standards generally accepted in the United States of America, we performed tests of the Plan's compliance with certain provisions of the Department of Labor Rules and Regulations for Reporting and Disclosure under ERISA as part of obtaining reasonable assurance about whether the Plan's financial statements are free from material misstatement. However, providing an opinion on compliance with those provisions is not an objective of our audit, and accordingly, we do not express such an opinion.

Management is responsible to ensure that the Plan's operations are conducted in accordance with the provisions of applicable laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in the Plan's financial statements. The auditor is not responsible for preventing noncompliance with such provisions and cannot be expected to detect noncompliance with all laws and regulations.

Our consideration of compliance with certain provisions of the Department of Labor Rules and Regulations for Reporting and Disclosure under ERISA was for the limited purpose described in the first paragraph and was not designed to identify all instances of noncompliance with those provisions and therefore, instances of noncompliance with those provisions may exist that were not identified. However, as discussed below, we identified certain instances of noncompliance. [*or* –

"Given these limitations, during our audit we did not identify instances of noncompliance with certain provisions of the Department of Labor Rules and Regulations for Reporting and Disclosure under ERISA"]

The following instances of noncompliance with certain provisions of the Department of Labor Rules and Regulations for Reporting and Disclosure under ERISA were identified:

[*Describe the instances of noncompliance that were identified and an explanation of their potential effects]*

This communication is intended solely for the information and use of management, [*identify the body or individuals charged with governance*], others within the organization, and [*identify any governmental authorities to which the auditor is required to report*] and is not intended to be, and should not be, used by anyone other than these specified parties.

[*Auditor's signature*]

[*Auditor's city and state*]

[*Date*]

Action Requested of the ASB – Issue 2

3. Does the ASB have a preference between options 1, 2, or 3?

4. Does the ASB support the EBP task force's recommendation to develop a new requirement for the auditor to communicate with those charged with governance instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA based upon the procedures established as part of Issue 1?

Issue 3 — Reporting on Compliance

As discussed in Issue 2 (option 3), the EBP task force recommends the auditor be required to report, in a separate report or in the auditor's report, that GAAS requires the auditor to communicate to those charged with governance instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA that have been identified during the audit of the financial statements. Such report would also include whether or not the auditor identified instances of noncompliance that have been communicated to those charged with governance. The auditor would be permitted, but not required, to include a description of those instances of noncompliance that were identified in the report on compliance.

The requirement to communicate in writing to those charged with governance instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA, forms the basis for reporting whether instances of noncompliance with such provisions are communicated in the report, when instances of noncompliance with such provisions are identified during the audit.

The EBP task force developed the following proposed requirement to require the auditor to report on compliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA.

Possible Requirements	***Possible Application Material***
Reporting on Compliance in a Separate Report or in the Auditor's Report	*Reporting on Compliance in a Separate Report or in the Auditor's Report*
.12 When reporting on compliance with certain provisions of the DOL Rules and Regulations for reporting and disclosure under ERISA the auditor should communicate, based on the work performed as part of the audit of the financial statements and the procedures performed in paragraph .03, whether the auditor identified instances of noncompliance with such provisions that were communicated to those charged with governance as required by paragraph .04.	
.13 The requirements in paragraphs .04-.08 to communicate in writing to those charged with governance instances of noncompliance with certain provisions of the DOL Rules and Regulations for reporting and disclosure under ERISA, forms the basis for reporting whether instances of noncompliance with such provisions are communicated in the report in this section, when instances of noncompliance with such provisions are identified during the audit.	
.14 When reporting on compliance with certain provisions of the DOL Rules and Regulations for reporting and disclosure under ERISA the auditor is permitted, but not required, to include in the report, a description of certain instances of noncompliance with such provisions based on the work performed as part of the audit of the financial statements. **.15** When the auditor chooses to include instances of noncompliance that were identified based on the work performed as part of the audit of the financial statements, as	.A7 After identifying instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA, the auditor may decide to communicate in the report on compliance certain instances of noncompliance. When making the determination which items to include in the report the auditor may want to consider management's plans to correct the

permitted by paragraph .14, management may wish to prepare a written response to the auditor's report regarding the instances of noncompliance with certain provisions of the DOL rules and regulations for reporting and disclosure under ERISA that were identified during the audit. When the auditor receives written comments from management, the auditor should include management's written comments in the report on compliance. In such situations the auditor should add a paragraph to the report disclaiming an opinion on such information.	noncompliance and include in the report those items that the auditor considers significant in the circumstances or those items that are not likely to be corrected in a reasonable period of time. When making this assessment the auditor may want to perform the following procedures: a. obtain information about management's plans that are intended to correct the noncompliance b. Assess whether it is likely that the noncompliance would be corrected by management's plans within a reasonable period of time c. Perform procedures to obtain audit evidence about management's plans to correct the noncompliance d. Assess whether it is likely that such corrections can be effectively implemented within a reasonable period of time .A8 Such management communications may include a description of corrective actions taken by the plan, its plans to correct the instances of noncompliance, or a statement indicating that management believes the cost of correcting the instances of noncompliance would exceed the benefits to be derived from doing so.

Action Requested of the ASB – Issue 3

5. Does the ASB support the EBP Task force's recommendation to develop a new requirement for the auditor to report on whether the auditor identified instances of noncompliance that were communicated to those charged with governance?

6. Does the ASB agree with allowing the auditor an option to include a description of certain instances of noncompliance in the report on compliance?

Issue 4 — Reporting on Internal Control Over Financial Reporting

The DOL requested a new section be added to the auditor's report that would provide the DOL with information the auditor gathered from AU-C section 265 Communicating Internal Control Related Matters Identified in an Audit *including items identified as a material weakness and those identified as a significant deficiency.*

The EBP task force believes that the GAAS requirement to communicate in writing significant deficiencies and material weaknesses in accordance with AU-C section 265 could form the basis for reporting on internal control over financial reporting in the report.

The task force considered three options for such reporting:

Option 1 (general statement of auditor's responsibilities related to reporting on internal control)

Option 1 would require the auditor to include standard language in the auditor's report that says the audit included consideration of internal control over financial reporting in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of internal control. Such report would also include the definitions of material weakness and significant deficiency and state that generally accepted auditing standards requires the auditor to communicate to those charged with governance significant deficiencies and material weaknesses identified during the audit.

Option 2 *(Include a description of the significant deficiencies and material weaknesses identified during the audit)*

Option 2 would require the auditor to report, in a separate report or in the auditor's report, based on the work performed as part of the audit of the financial statements, a statement that the auditor is required to communicate significant deficiencies and material weaknesses identified during the audit to those charged with governance, include the definitions for significant deficiencies and material weaknesses, and include a description of the instances of noncompliance that were identified as part of audit of the financial statements.

Option 3 (Require communication about whether significant deficiencies and material weaknesses were communicated to those charged with governance)

Option 3 would require the auditor to report, in a separate report or in the auditor's report, that GAAS requires the auditor to communicate to those charged with governance significant deficiencies and material weaknesses identified during the audit. Such report would also include definitions of significant deficiencies and material weaknesses, and state whether or not the auditor identified any significant deficiencies or material weaknesses that have been communicated to those charged with governance. Under this option, the auditor would be permitted, but not required, to include a description of the significant deficiencies and material weaknesses that were communicated to those charged with governance.

EBP Task Force Recommendations

The EBP task force supports option 3 because they believe it will provide transparency to the audit and provide information about whether or not significant deficiencies and material weaknesses were communicated to those charged with governance without requiring the auditor to describe those deficiencies in the auditor's report. However some members of the task force expressed concerns with reporting on internal control in the auditor's report.

The EBP task force noted that option 1 does not provide transparency into the audit and will not provide much enhancement to the auditor's report.

The EBP task force discussed the Yellow Book framework for reporting on internal control over financial reporting and noted that the Yellow Book requires the report to include a description of the significant deficiencies and material weaknesses that were communicated to those charged with governance. Certain members of the EBP task force expressed concerns with describing the significant deficiencies and materials weaknesses in the report and believe that providing such information in the auditor's report could hinder the two way communication with those charged with governance.

The EBP task force supported option 3 because they believe that the GAAS requirement to communicate significant deficiencies and material weaknesses provides a good basis for what should be reported. In addition, the DOL has the ability to request from the plan sponsor, such communications. Therefore, if the report on internal control over financial reporting contains information that the auditor identified and communicated significant deficiencies and material weaknesses to those charged with governance, then the DOL may have access to that information if they choose to request it.

The EBP task force developed the following proposed requirement to require the auditor to communicate deficiencies in internal control over financial reporting:

Possible Requirements	***Possible Application Material***
Reporting on Internal Control Over Financial Reporting in a Separate Report or in the Auditor's Report	*Reporting on Internal Control Over Financial Reporting*
.09 When reporting on internal control over financial reporting the auditor should communicate, based on the work performed as part of the audit of the financial statements, whether the auditor identified deficiencies in internal control that were considered to be significant	

deficiencies or material weaknesses that were communicated to management and those charged with governance. The GAAS requirement to communicate in writing significant deficiencies and material weaknesses in accordance with AU-C section 265 *Communicating Internal Control Related Matters Identified in an Audit*, forms the basis for reporting whether significant deficiencies and material weaknesses were communicated in the report in this section, when deficiencies are identified during the audit.	
.10 When reporting on internal control over financial reporting the auditor is permitted, but not required, to include in the report, a description of the significant deficiencies and material weaknesses in internal control that were identified based on the work performed as part of the audit of the financial statements. **.11** When the auditor chooses to include the significant deficiencies and material weaknesses in internal control that were identified based on the work performed as part of the audit of the financial statements, as permitted by paragraph .10, management may wish to prepare a written response to the auditor's report regarding significant deficiencies or material weaknesses identified during the audit. When the auditor receives written comments from management, the auditor should include management's written comments in the report on internal control. In such situations the auditor should add a paragraph to the report disclaiming an opinion on such information.	.A6 Such management communications may include a description of corrective actions taken by the plan, its plans to implement new controls, or a statement indicating that management believes the cost of correcting a significant deficiency or material weakness would exceed the benefits to be derived from doing so.

Action Requested of the ASB – Issue 4

7. Does the ASB have a preference between options 1, 2, or 3?

8. Does the ASB support the EBP Task force's recommendation to develop a new requirement for the auditor to report on whether the auditor identified any significant deficiencies or material weaknesses that were communicated to those charged with governance?

9. Does the ASB agree with allowing the auditor an option to include a description of such deficiencies?

Issue 5 — Layout and Wording of Separate Report on Internal Control and Compliance

The EBP task force discussed a possible layout and wording for a separate report on internal control and compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA.

The following are proposed elements to be included in the separate report on compliance and internal control. See also Agenda Item 4B for a complete version of the proposed SAS that has been discussed in this issue paper.

Separate Report on Internal Control Over Financial Reporting and Compliance with Certain Provisions of DOL Rules and Regulations for Reporting and Disclosure Under ERISA Based on an Audit of EBP Financial Statements Performed in Accordance with GAAS	**Separate Report on Internal Control Over Financial Reporting and Compliance with Certain Provisions of DOL Rules and Regulations for Reporting and Disclosure Under ERISA Based on an Audit of EBP Financial Statements Performed in Accordance with GAAS**
.16 When the auditor reports on internal control over financial reporting and compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA in a separate report, the report should include the following:	.A7 Exhibit C— *Illustrative Separate Report on Internal Control Over Financial Reporting and on Compliance with Certain Provisions of DOL Rules and Regulations for Reporting and Disclosure Under ERISA Based on an Audit of EBP Financial Statements Performed in Accordance with GAAS* includes an illustrative report on internal control over financial reporting and compliance with certain provisions of DOL rules and regulations for reporting and disclosure in an EBP audit.
a. A title that includes the word *independent* to clearly indicate that it is the report of an independent auditor.	
b. An appropriate addressee.	
c. A paragraph that states that the financial statements were audited in accordance with generally accepted auditing standards and an identification of the United States of America as the country of origin of those standards (for example, auditing standards generally accepted in the United States of America or U.S. generally accepted	

auditing standards) and the date of the auditor's report on those financial statements.	
d. The report should include a section with the heading "Internal Control Over Financial Reporting." This section of the report should describe: 1. the scope of the auditor's testing of internal control over financial reporting, including that the purpose of the audit was for the auditor to express an opinion on the financial statements 2. the audit included consideration of internal control over financial reporting in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of internal control 3. the auditor is not expressing an opinion on the effectiveness of internal control 4. the definition of the terms *material weakness* and *significant deficiency* 5. GAAS requires the auditor to communicate to those charged with governance significant deficiencies and material weaknesses identified during the audit. 6. the auditor's consideration of internal control was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and that significant deficiencies or material weaknesses may exist that have not been identified 7. When significant deficiencies or material weaknesses have been identified and communicated to those charged with governance in accordance with AU-C 265, a statement that the auditor identified certain deficiencies in internal control that were considered significant deficiencies or material weaknesses that were communicated to those charged with governance.	[Expand this section to include how to include the optional description of significant deficiencies or material weaknesses]
8. When no material weaknesses have been identified as part of the audit, a statement that given the limitations expressed previously,	

the auditor did not identify any material weaknesses to be communicated to those charged with governance. 9. The auditor should not issue a written communication stating that no significant deficiencies were identified during the audit.	
e. The report should include a section with the heading "Compliance with Certain Provisions of DOL Rules and Regulations for Reporting and Disclosure Under ERISA." This section of the report should describe:	
1. the scope of the auditor's testing of compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA, including that the purpose of the audit was for the auditor to express an opinion on the financial statements 2. the auditor performed tests of the plan's compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA as required by GAAS, but not for the purpose of expressing an opinion on such compliance. 3. the auditor is not expressing an opinion on the compliance with such provisions. 4. GAAS requires the auditor to communicate to those charged with governance instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA that have been identified as part of the audit of the financial statements.	
f. When no instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA have been identified, a statement that given the limitations listed	

previously, no instances of noncompliance with such provisions were identified to be reported to those charged with governance.	
g. When instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA have been identified and communicated to those charged with governance as required by paragraph .04, a statement that the auditor did identify certain instances of noncompliance with DOL rules and regulations for reporting an disclosure under ERISA that were communicated to those charged with governance.	[Expand this section to include how to include the optional description of such instances of noncompliance]
h. A paragraph that includes an appropriate alert in accordance with AU-C 905, *Alert That Restricts the Use of the Auditor's Written Communication*.	

EXHIBIT C—ILLUSTRATIVE SEPARATE REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE WITH CERTAIN PROVISIONS OF DOL RULES AND REGULATIONS FOR REPORTING AND DISCLOSURE UNDER ERISA BASED ON AN AUDIT OF EBP FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GAAS

Circumstances include the following:

- This type of reporting would apply for both limited scope and full scope audits
- The auditor's report on the financial statements would include the following:
  - OM paragraph on supplemental schedules (IRT) and form and content opinion
  - Other Reporting Requirement – the following paragraph is added to the auditor's report on the financial statements

  In accordance with GAAS, we have also issued our report dated [date of report] on our consideration of ABC 401(K) Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of the Department of Labor rules and regulations for reporting and disclosure under the Employee Retirement Income Security Act of 1974. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an employee benefit plan audit performed in accordance with generally accepted auditing standards in considering ABC 401(K) Plan's internal control over financial reporting and compliance with certain provisions of the Department of Labor rules and regulations for reporting and disclosure under the Employee Retirement Income Security Act of 1974.

Separate Report on Internal Control Over Financial Reporting and on Compliance with Certain Provisions of DOL Rules and Regulations for Reporting and Disclosure Based on an Audit of EBP Financial Statements Performed in Accordance with GAAS

Independent Auditor's Report

[*Appropriate Addressee*]

We have audited, in accordance with auditing standards generally accepted in the United States of America, the financial statements of ABC 401(k) Plan, which comprise the statements of net assets available for benefits as of December 31, 20X2 and 20X1, and the related statement of changes in net assets available for benefits for the year ended December 31, 20X2, and the related notes to the financial statements, and have issued our report thereon dated October 15, 20X3.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered ABC 401(k) Plan's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of ABC 401(k) Plan's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of ABC 401(k) Plan's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Generally accepted auditing standards requires us to communicate to those charged with governance significant deficiencies and material weaknesses identified during the audit.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses.

[*Possible ways to report*]

1. [No material weaknesses have been identified]

Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

2. [Significant deficiencies were identified; no material weaknesses identified]

Given these limitations, we did not identify any material weaknesses, however during our audit we did identify certain deficiencies in internal control that we consider to be significant deficiencies that we communicated to those charged with governance.

3. [Material weaknesses were identified, no significant deficiencies identified]

Given these limitations, during our audit we identified certain deficiencies in internal control that we consider to be material weaknesses that we communicated to those charged with governance.

4. [Both significant deficiencies and material weaknesses were identified]

Given these limitations, during our audit we identified certain deficiencies in internal control that we consider to be significant deficiencies or material weaknesses that we communicated to those charged with governance.

5. [Optional reporting: When significant deficiencies or material weaknesses are communicated to those charged with governance and the auditor decides to include those items in the report on internal control.]

Given these limitations, during our audit we identified the following deficiencies in internal control that we consider to be significant deficiencies or material weaknesses that we communicated to those charged with governance

[Describe deficiencies]

Compliance With Certain Provisions of DOL Rules and Regulations for Reporting and Disclosure

As part of obtaining reasonable assurance about whether ABC 401(k) Plan's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of DOL Rules and Regulations for Reporting and Disclosure under ERISA as set forth in AU-C section XXX. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

Generally accepted auditing standards requires us to communicate with management and those charged with governance instances of noncompliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA that have been identified during the audit of the financial statements.

[*Possible ways to report*]

1. [No instances of noncompliance were identified]

Given the limitations in the first paragraph, during our audit we did not identify instances of noncompliance with certain provisions of the Department of Labor Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. However, instances of noncompliance may exist that have not been identified.

2. [Instances of noncompliance have been identified]

Given the limitations in the first paragraph, during our audit we identified certain instances of noncompliance with certain provisions of the Department of Labor rules and regulations for reporting and disclosure under the Employee Retirement Income Security Act of 1974 that we communicated to those charged with governance.

3. [Optional Reporting: when instances of noncompliance have been identified and the auditor decides to include some of those items of noncompliance in the report]

Given the limitations in the first paragraph, during our audit we identified certain instances of noncompliance with certain provisions of the Department of Labor rules and regulations for reporting and disclosure under the Employee Retirement Income Security Act of 1974 that we communicated to those charged with governance. The following are certain instances of noncompliance with certain provisions of Department of Labor rules and regulations for reporting and disclosure under the Employee Retirement Income Security Act of 1974 that, in the auditor's professional judgment, were of importance to include in the auditor's report.

[Describe identified items of Noncompliance]

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance with certain provisions of the Department of Labor Rules and Regulations for Reporting and Disclosure Under the Employee Retirement Income Security Act of 1974, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an employee benefit plan audit performed in accordance with generally accepted auditing standards in considering the plan's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

[*Auditor's signature*

[*Auditor's city and state*]

[*Date of the auditor's report*]

Action Requested of the ASB – Issue 5

10. Does the ASB conceptually support the layout of the proposed separate report on internal control over financial reporting and compliance with certain provisions of DOL rules and regulations for reporting and disclosure under ERISA for employee benefit plan audits?