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Michael Santay, Chair, Auditing Standards Board  
Darrel Schubert, Chair, Employee Benefit Plan Reporting Task Force  
American Institute of Certified Public Accountants  
1211 Avenue of the Americas  
New York, NY 10036

Transmitted via email to [sherry.hazel@aicpa-cima.com](mailto:sherry.hazel@aicpa-cima.com)

Re: Proposed Statement on Auditing Standards (SAS), Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA

Dear Sirs:

We are pleased to provide feedback on the proposed Statement on Auditing Standards (SAS), Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA. We support the Board's objective to improve audit quality and enhance the communicative value and relevance of the auditor's report. We appreciate that the proposed SAS was developed in response to requests made by the Department of Labor to revisit the auditor reporting model for ERISA plan audits.

As CPAs, the partners of Lemke Chinen & Tanaka CPA, Inc. have provided accounting and auditing services to over seventy multiemployer plans for the past several decades. Our services include full scope audits, payroll agreed upon procedures, medical claims examinations, preparation of Form 5500's and 990's. Our clients are comprised of Taft-Hartley plans from the construction, hotel, trucking and other service industries. They range in size from under 100 to over 10,000 participants with net assets up to \$400,000,000. As stakeholders in the ERISA plan industry, we are writing on behalf of our firm and our clients to provide feedback on particular aspects of the proposed SAS, and to offer certain suggestions.

The following is our feedback on the issues on which the Board requested feedback:

Issue 1—Required Procedures When an ERISA-Permitted Audit Scope Limitation is Imposed

Respondents are asked to provide their views on whether

- the procedures and guidance will achieve the objectives of enhancing execution and consistency in these engagements and if not, why;

We believe that the specific procedures and guidance will increase consistency in those executing the requirements. In order for affected plans to benefit, the specific procedures and guidance need to enhance execution. We question whether the procedures enhance execution.

- and any procedures that should be required are missing, and if so, describe them.

20a. We suggest that this procedure or relaxed explanatory material include a step requiring the auditor to evaluate whether the certification itself is in compliance with the statutory regulation that allows the scope limitation. Key certification requirements are described in A7; however, we believe that the auditor should also ensure that the certification is signed by an authorized person of the certifying financial institution.

20b. We suggest that the auditor evaluate management's assertion that (and not assessment of whether) the entity issuing the certification is a qualified institution.

#### Issue 2—The Form and Content of the Auditor's Report on ERISA Plan Financial Statements with the ERISA-permitted Audit Scope Limitation

Respondents are asked to provide feedback on whether the form and content of the proposed auditor's report, including the form and proposed content of the new form of opinion

- provide improved transparency with respect to reporting on an audit of ERISA plan financial statements when an ERISA-permitted audit scope limitation exists, and if not, how could it be revised;

As further explained below, we believe that the form and content of the proposed auditors report will not improve transparency. A piecemeal opinion that only attests to a portion of financial statements does not give plan sponsors the needed level of assurance. The specific form of opinion will, in our opinion, confuse the reader as to the level of assurance obtained by the auditor.

- will improve the auditor's understanding of his or her responsibilities in a limited scope audit resulting in potential improvements in audit quality, and if not, why;

We believe that the procedures described in Paragraph 20 will achieve this objective.

- better describe management's responsibilities for the financial statements, and if not, why;

We believe that the proposed content better describes management's responsibilities for the limitation on the scope of the audit.

- provide sufficient clarity to users with respect to the auditor's responsibilities and matters reported, and if not, why.

We believe that the proposed content provides decreased clarity to users with respect to the auditor's responsibilities, in the following ways:

- The heading Auditor's Responsibility (Including Responsibility for the Certified Investment Information) is misleading. The auditor is not responsible for any part of the financial statements, including the certified investment information.

- Although the auditor may perform limited procedures with respect to the certified investment information, procedures (a) and (b) relate mainly to the certification itself and not the underlying investment information. Procedure (c) was already included in existing content and procedure (d) would, in our opinion, be better conveyed in a paragraph regarding the form and content of the financial statements in compliance with the applicable reporting framework.
  - The proposed content makes clear that the auditor "did not assess the risks of material misstatement" nor "consider internal control" but omits information that the auditor performed no procedures to obtain reasonable assurance about whether the investment information is free from material misstatement.
  - The proposed content tells the user that "In our opinion, based on our audit and based on our use of the certification of the investment information..., the financial statements present fairly, in all material respects... "
- a. The certification, as described in paragraph A45, does not provide sufficient appropriate audit evidence on its own, and therefore, the auditors opining on the financial statements as a whole, without explaining the effect of the scope limitation, could be misleading to the user.
  - b. The possible effects on the financial statements of undetected misstatements in the area of investment information that was unaudited, could be both material and pervasive. Therefore, we believe that the disclaimer of opinion remains the appropriate modification to the auditor's report in the circumstances.

#### Issue 3—Modifications to the Opinion in the Independent Auditor's Report

Respondents are asked for their views about the proposed interaction of AU-C section 705 and the proposed SAS when the ERISA-permitted audit scope limitation is imposed by management including

- whether the guidance in paragraphs 31 and 34 of the proposed SAS (a) is clear with respect to the auditor's responsibilities for addressing the circumstances described previously, and (b) achieves the objective of providing transparent reporting to the users, and if not, suggested revisions.
- the form and content of the example reports (nos. 5-7) illustrating qualified and disclaimers of opinion regarding the application of the guidance in paragraphs 31 and 34.

This guidance includes the ERISA-permitted scope limitation as a basis for disclaimer of opinion, although such scope limitation on its own would not result in a disclaimer of opinion, under the form and content in other example reports. This conflicting guidance does not achieve the objective of either clear guidance or transparent reporting. We believe that, as previously stated, the disclaimer of opinion remains the appropriate modification to the auditor's report in the circumstances of an ERISA-permitted scope limitation.

#### Issue 4—Required Emphasis-of-Matter Paragraphs

Respondents are asked to consider whether the situations identified are appropriate for requiring the inclusion of emphasis-of-matters paragraphs in the auditor's report. Respondents are also asked to consider whether there are additional situations that should result in a required emphasis-of-matter paragraph.

Paragraph 116 requires the auditor to include an emphasis of matter paragraph when any of three specific situations exist. The guidance in this paragraph is too prescriptive to allow for the auditor's professional judgment regarding the need for an emphasis of matter paragraph.

We suggest that the guidance require the auditor to consider including an emphasis of matter paragraph when certain information in the financial statements should be emphasized, and that the identified situations be presented as examples specific to employee benefit plans.

Paragraph 116a describes the situation when there are significant plan amendments that affect net assets. Because plan amendments often affect only the benefit obligations disclosed in the notes, we suggest that the guidance be revised to "significant plan amendments that affect net assets and/or benefit obligations."

Paragraph 116c describes the situation where there are significant changes in the nature of the plan. The effects of a plan termination, partial termination or hard or soft freeze, would also warrant required consideration for an emphasis of matter paragraph.

Additional situations which may warrant required consideration for an emphasis of matter paragraph include the following:

- The plan is significantly underfunded and requires increased contributions and/or has implemented limitations on benefit increases and accruals. In the case of multiemployer plans, the funded status of the plan is critical, or critical and declining, within the meaning of the Pension Protection Act of 2006, and whether the plan is making progress on a Funding Improvement or Rehabilitation Plan, based on information provided by the actuary
- In the case of multiemployer plans, a mass withdrawal, withdrawal of a significant number of employers or withdrawal of a major contributing employer
- Plan assets include a significant percentage of alternative or hard-to-value investments whose fair values have been estimated in the absence of readily determinable fair values
- The plan has entered into nonroutine significant prohibited transactions that require correction

#### Issue 5—Reporting Internal Control Deficiencies

Respondents are asked to provide feedback on whether

- the current reporting of internal control deficiencies to those charged with governance is sufficient; and/or
- there are other reporting considerations the ASB should evaluate.

We believe that the current requirements to communicate with those charged with governance the internal control deficiencies identified during the audit are sufficient.

#### Issue 6—Certain Requirements for Audits of ERISA Plan Financial Statements and Related Required Report on Specific Plan Provisions Relating to the Financial Statements

Respondents are asked to provide feedback about the required procedures discussed in paragraphs 15-16, and the reporting of findings discussed in paragraphs 119-124 of the proposed SAS, including views regarding the following:

1. With respect to the required procedures in paragraphs 15-16

- a. Will these requirements enhance the consistency and quality of the audit work performed relating to matters that could have a direct effect on the financial statements, including related disclosures, and if not, why?
- b. Does the proposed SAS provide appropriate guidance on achieving these requirements, including i. which provisions of the plan instrument should be tested; and ii. to what extent testing should be performed?
- c. What procedures related to other plan provisions or specific areas of the financial statements should be included in the required testing to enhance the usefulness of the proposed reporting of the findings?

Overall, we believe that the objective of improving consistency and audit quality in a robust way will not be met by codifying required procedures into the final SAS. These procedures are already familiar to practitioners who perform quality audits and have been included in the industry's Audit Guide for many years. For practitioners who do not perform quality audits, the desired effect may only be realized on a limited scale, which is unlikely to improve the quality of audits. The DOL's concern was to improve the quality of audits. To reshuffle the scope of opinion without assurance of improved audit quality could increase costs to a plan without a corresponding benefit.

Specific feedback related to Paragraphs 15 and 16 is as follows:

- Paragraph 15 requires the auditor to perform substantive procedures regarding various plan provisions, irrespective of the risk of material misstatement.

The auditor's objective is to obtain sufficient appropriate evidential matter to provide a reasonable basis for forming an opinion on the financial statements as a whole. The nature of most evidence derives, in part, from the concept of selective testing of the data being audited, which involves judgment regarding both the areas to be tested and the nature, timing, and extent of the tests to be performed. The requirement to perform procedures irrespective of the risk of material misstatement eliminates this essential auditor judgment.

We suggest that the requirements of paragraph 15 direct the auditor to consider the areas to be tested, with examples provided in Paragraphs 15a-i, and to determine the nature, timing, and extent of such tests, in order to establish whether there were instances of noncompliance with key provisions set forth in the plan document and/or with applicable laws and regulations, that would have a direct and material effect on the financial statements.

- Paragraph 15a-d —These procedures relate to the auditor performing procedures as to whether various provisions are administered in accordance with the plan instrument. The determination of whether a plan is being operated in compliance with applicable laws and regulations (which include a requirement to comply with the provisions of the plan instrument) is primarily a legal determination made in conjunction with plan management and legal counsel. Because we understand that the auditor will not be forming a conclusion based on the procedures performed in Paragraphs 15a-d, we believe that such procedures should only be required as part of the auditor's overall objective of forming an opinion on the financial statements as a whole.

Furthermore, the provisions being tested as to whether they are in accordance with the plan instrument ignores the legal and regulatory environment in which the plan operates. For example, the plan instrument may provide for eligibility, vesting or benefit provisions that are

out of step with current regulations. Health plans especially are subject to an array of laws regarding eligibility and the provision and payment of benefits. This creates the potential risk that an auditor may follow the requirements in the new SAS and only test to the plan instrument, failing to protect the participants covered under the plan.

- Paragraph 15d — We suggest that the procedures additionally describe contributions that are calculated actuarially or that arise from collective bargaining agreements, as is the case with multiemployer plans.
- Paragraph 15e — We suggest that the auditor also determine whether the prohibited transaction is properly disclosed in the notes to the financial statement and whether it has been or will be corrected by management.
- Paragraph 15f — We suggest that the auditor consider the reasonableness and permissibility of plan expenses as well as their allocation. Payment of improper expenses from a qualified plan is a breach of fiduciary duties and may be considered a nonexempt transaction. Plan management considers whether plan assets are being expended to defray reasonable expenses of administering the plan, solely in the interest of participants and beneficiaries. Multiemployer plans experience unique challenges in structuring and monitoring compensation and service arrangements in order to meet the conditions allowing exemption from prohibition.
- Paragraph 16a —The guidance provides a "must-audit" with a limited list of Internal Revenue Code compliance tests in Exhibit B, which does not take into account numerous other compliance requirements for other agencies. For example, health plans are obliged to comply with a myriad of requirements introduced by the Affordable Care Act regarding plan changes, participant disclosures and notices, and mandated fees, as well as Department of Health and Human Services requirements for HIPAA, PHI, breach notifications, notices of creditable coverage and Medicare subsidies. Other requirements are enforced jointly by the Internal Revenue Service and the DOL, such as required notices to separated participants with deferred vested benefits, notices related to funding status, benefit suspensions or reduction in future accruals, just to name a few. It is unclear how far the auditor must extend his/her procedures to test compliance with laws and regulations, and how to "pick and choose" which compliance requirement to test.
- Paragraph 16b —This guidance seems to duplicate the procedures in 15i, or can be incorporated into 15i.

2. With respect to reporting on the findings resulting from performing procedures related to the areas in paragraphs 119-124, whether there are opportunities to enhance the proposed requirements and guidance including whether:

- a. Including the list of individual areas tested is appropriate and if so whether there are other items that should also be included (if not, why not).

We suggest the following revisions to the report on findings included in the new reporting model:

"...are required to perform certain procedures to test whether the plan was operated in accordance with key plan provisions and applicable regulations."

- b. The requirement to exclude findings that are "clearly inconsequential" is appropriate, and if so is there guidance the ASB can consider to drive consistency in application in practice?

- c. The findings should also include any matters identified by management or the plan administrator? [Note: As currently drafted, the proposed SAS requires the auditor to include findings that were noted as part of the auditor's work performed in relation to paragraphs 15-16.]
- d. The reporting illustrations included in the Exhibits to the proposed SAS specific to reporting the findings are clear and result in sufficient information to the user of the report?

We believe that the Report on Findings resulting from procedures performed to determine the plan's compliance with its provisions is problematic, for reasons outlined in our feedback in #1 as well as the following:

- The auditor is performing the procedures in Paragraphs 15 and 16 not to form a conclusion or opinion, and not pursuant to an assessment of risk or materiality, but merely to report that they were performed and to report on any findings that resulted. Therefore, in practice the report may hide vast inconsistencies in audit quality, and foster an overreliance on the auditor's ability to detect and report noncompliance findings.
  - The user will have difficulty determining the potential effect of the findings on the plan's operations, qualification or financial position. For example, under the proposed reporting model, the auditor is not required to quantify the findings or provide more than general information. Furthermore, the user has no way of assessing whether the finding was a result of numerous errors, one error that was not significant (but not clearly inconsequential), or the size of the sample being tested. For example, one reported finding when the auditor tested 100 transactions is less serious than one reported finding when the auditor tested 10 transactions.
  - The user will have difficulty determining whether the findings of noncompliance have been remediated. The auditor is not required to repeat findings from prior years if not remediated.
  - The reporting model does not allow the audit of to present findings in a way that characterizes their severity or magnitude, either individually or in the aggregate, so that the user can differentiate between those findings the auditor may consider to be insignificant and those considered to be more serious.
- e. There may be unintended consequences from including the findings in the auditor's report, and if so, what those unintended consequences may be and how might they be mitigated?

Because the auditor's report is attached to the plan's Form 5500 filing, which is posted online and publicly available, the readers include not only the plan participants but anyone in the general public. A few unintended consequences may ensue, such as:

- Plan participants may become unduly alarmed regarding findings included in the report, even though the findings could be only routine operating errors, perhaps even already corrected. They may reduce or withdraw their participation in the plan, which could harm their ability to save for retirement—the very reason the plan was established.
- Plan sponsors may need to provide additional communications to participants to explain the findings, and seek assistance from professionals to do so, taking away from their ability to carry out other responsibilities and/or increasing costs without a corresponding benefit.

- Plan sponsors may avoid the reputational risk involved in having findings reported publicly and seek lower quality auditors who agree not to report findings, thwarting the very objective that this proposed SAS set to achieve. Quality auditors are likely to continue to perform quality work and would report findings in accordance with the requirements of the proposed SAS.
  - Findings of noncompliance may lead to actual or potential litigation, providing an incentive for the plan sponsor to discontinue the operation of the plan or change the nature of the plan so that an audit is not required, and in effect, to eliminate the protections that ERISA provides to participants.
  - Plan sponsors of multiemployer plans, who are an equal representation of labor union and management individuals, may be especially sensitive to findings which are susceptible to unintended interpretations being publicly available, for concern that their magnitude will be potentially inflated or misrepresented. Relations between labor and management, and between labor union officers and their rank-and-file members, are at times contentious, and the findings could be used for political agendas.
- f. There are alternatives to reporting the findings in the auditor's report that would achieve the objectives related to enhancing audit quality?

We believe that findings of noncompliance should be communicated with plan management and, if appropriate, plan governance. The auditor should evaluate the effect of such noncompliance on the financial statements, in accordance with the provisions of AU-C 250.

3. Whether the required additional procedures and reporting of findings will result in additional costs, and if so, views as to the extent of those costs and whether they outweigh the potential benefits of enhanced audit quality?
- We believe that the additional procedures and reporting of findings will obviously increase the cost of performing an audit, undoubtedly in the first year of implementation and ongoing.

The consideration of what will be reported as a finding of noncompliance with plan provisions will ultimately be a matter of legal determination, causing plan management to increasingly seek legal counsel as a part of developing the report on findings and any management responses, driving up costs even more.

The cost that is harder to quantify is the "human cost" that may arise out of the unintended consequences described above. If participants are ultimately harmed by an overreliance on the auditor's ability to detect noncompliance, an overreaction to findings reported, or the failure of this proposed SAS to improve audit quality, their ability to obtain needed benefits could be jeopardized.

#### Issue 7—Required Procedures Relating to the Form 5500

Respondents are asked for their views about whether the proposed procedures in paragraphs 36-48 of the proposed SAS would achieve the objective of increased consistency with respect to identifying information in the Form 5500 that may be relevant to the audit of ERISA plan financial statements, and if not, why?



We agree that the proposed guidance in paragraphs 36-48 is needed to increase consistency and execution of procedures performed with respect the plan's Form 5500 filing; provided that in situations where a matter involves other professional disciplines, the auditor's responsibility is to coordinate a response.

#### Issue 8—Proposed New Reporting Standard and Amendments to Other AU-C Sections

Respondents are asked whether

- the proposed approach of creating a new reporting model for reporting on ERISA plan audits (AU-C section 703) will better describe management's and the auditor's responsibilities in these engagements;

The new reporting model which better describes management's responsibilities related to ERISA-permitted scope limitations, is likely to result in a longer audit report and more costs to the plan without a corresponding benefit. Provisions that shift responsibility do not necessarily improve audit quality.

We suggest the following revisions to other descriptions of management's responsibilities included in the new reporting model:

Management is also responsible for maintaining a current plan instrument including all plan amendments, for administering the plan in accordance with plan provisions and in compliance with applicable laws and regulations, and consistent with the applicable ERISA prudence requirements for maintaining sufficient records with respect to each of the participants, in accordance with applicable sections of ERISA, to determine the benefits due or which may become due to such participants.

- the proposed amendments to the other AU-C sections are appropriate; and

The proposed amendments to other AU-C sections appear appropriate.

- whether there are other sections of AICPA Professional Standards that might need to reflect the provisions of this proposed SAS.

There may need to be revisions to AU-C 250, Consideration of Laws and Regulations in an Audit of Financial Statements, if in the final SAS, the auditor is required to include findings of noncompliance with laws and regulation in the audit report.

#### Issue 9—Proposed Effective Date

The proposed effective date for the proposed SAS is for ERISA plan audits of financial statements for periods ending on or after December 15, 2018. Respondents are asked whether the proposed effective date provides sufficient time for preparers, auditors, and others to adopt the new standard and related conforming amendments.

We believe that the proposed effective date does not allow enough time to implement the changes in practice that the proposed SAS would bring about, as well the necessary outreach to clients, service providers, legal counsel and users who would all be affected by the revisions in practice and reporting.

The partners of Lemke Chinen & Tanaka CPA, Inc. take seriously the responsibility we have to the public interest, especially in the arena of employee benefit plans. We are constantly engaged in the task of assessing whether our work meets the expectations of those users as well as the standards of our profession and the scrutiny of government regulators.

We welcome proposals that improve the quality of employee benefit plan audits, but are not as hopeful that this objective can be materially achieved through revisions to the audit reporting model. Initiatives to strengthen continuing professional education through a mandated number of minimum required hours each year, and to enhance oversight through peer review, are more likely, in our opinion, to strengthen and improve quality.

Lemke Chinen & Tanaka CPA, Inc. appreciates the Board's consideration of these comments and recommendations. Please feel free to contact Lemke Chinen & Tanaka CPA, Inc. if you have any questions.

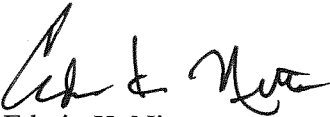
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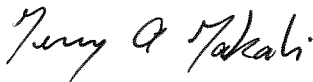
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