



August 21, 2017

Ms. Sherry Hazel
Audit and Attest Standards
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

RE: Proposed Statement on Auditing Standards, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*

Dear Ms. Hazel:

We appreciate the opportunity to comment on the Proposed Statement on Auditing Standards, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA* (the "proposed SAS").

Audit quality is top of mind for PwC and the auditing profession. It is particularly important in relation to employee benefit plans ("EBPs") given the potential impact on stakeholders if audit quality is not brought to bear. The regulatory framework set in place for audits of financial statements subject to the Employee Retirement Income Security Act of 1974 ("ERISA plan audits") takes this into account as well, with multiple agencies working together to promote accountability and transparency. In light of the Employee Benefits Security Administration's ("EBSA") findings in its May 2015 report, we recognize the Department of Labor's ("DOL") call to action for auditors to enhance both the performance and reporting of ERISA plan audits.

Under ERISA, the DOL and the Internal Revenue Service ("IRS") are charged with the authority to issue regulations covering the reporting and disclosure requirements for EBPs. The Administrative Procedures Act and associated Executive Orders contain specific guidelines for how agencies issue regulations, including assessing the necessity, performing an analysis of costs and benefits, and allowing for public comment on new regulation.

Through the proposed SAS, we believe the Auditing Standards Board ("ASB") would be establishing compliance requirements for plan administrators that do not exist under ERISA or current DOL or IRS regulations. This proposal would impose these new compliance requirements for plan administrators as a precondition to obtaining an audit beyond what is needed to meet the existing reporting requirements of ERISA. In addition, the proposal would fundamentally change the nature of an ERISA plan audit, by moving away from the risk-based approach that underpins financial statement audits and expanding the auditor's responsibilities to include reporting on compliance. The ASB's role should be to establish guidelines for auditing and reporting in circumstances when regulations require such reporting, not to establish incremental compliance requirements. Actions by the ASB should complement other changes targeted at management, including plan administrators (such as enforcement of existing fiduciary standards, new regulations or changes to Form 5500), but should not set out compliance requirements in the absence of regulations from the DOL or IRS.

In particular, we believe it is important for the DOL, the ASB and audit firms themselves to understand the root causes of the deficiencies identified by the EBSA in the May 2015 report in order to determine how

PricewaterhouseCoopers LLP, 400 Campus Drive, Florham Park, NJ 07932
T: (973) 236 4000, F: (973) 236 5000, www.pwc.com



best to respond from an audit quality perspective, including when standard setting may be appropriate. For example:

- Clarity in the auditing standards about what is expected in performing ERISA plan audits could enhance auditor performance, by establishing appropriate principles and providing robust guidance about how those principles are to be applied.
- The Audit and Accounting Guide, *Employee Benefit Plans* (“EBP Guide”), which has been overhauled in recent years, sets out robust authoritative guidance to illustrate what is expected of auditors in a variety of circumstances, as the spectrum of plans under ERISA is wide. Firms should be using this guidance to supplement the auditing standards, which historically have not established specific requirements for EBPs.
- Continued efforts to monitor and hold those preparing ERISA plan financial statements and performing ERISA plan audits accountable for quality are necessary (e.g., remedial, corrective actions as a result of the peer review process). Changes to auditing standards may not be an effective means of dealing with firms that are performing deficient audits, and could impose an undue burden on plan sponsors and firms who are already performing quality audits.
- Changes to auditor reporting for ERISA plan audits could provide more transparency to users of those reports. However, we do not believe that stakeholders other than the DOL are calling for the explicit reporting of findings. We also do not support the proposal to move from the current form of opinion (i.e., a disclaimer of opinion with an other-matter paragraph) to a new format when the ERISA-permitted audit scope limitation exists, as this comes with a risk that users may misunderstand the limited extent of the auditor’s procedures on the certified investment information.
- Education, training and communication would reinforce the auditing standards and guidance to ensure that those performing these engagements are sufficiently competent and focused on appropriately applying the risk-based approach that underpins the auditing standards.

If the EBP Guide is not being used as intended, it makes sense that the ASB might seek to establish specific performance requirements for EBPs based on concerns from the DOL about the quality of these engagements, in part by elevating some of the material in the EBP Guide into the proposed SAS. However, the approach taken in the proposed SAS implies that, by requiring reporting on certain areas, auditor performance will be enhanced. While this may be true, we think it is important the ASB first sets out a view on where performance needs to be enhanced and how best to do so, and then considers where additional transparency through the changes to the auditor’s report could be meaningful to users of the auditor’s report. We are not convinced that the ASB has demonstrated a need for incremental reporting on compliance, nor do we understand the rationale for why certain elements have been selected for reporting, but other compliance matters that may be significant have not been addressed (e.g., requirements related to auto-enrollment or auto-escalation).

An audit in accordance with generally accepted auditing standards (“GAAS”) is not designed to identify all instances when the plan and plan transactions are not in accordance with specific plan provisions, but focuses on the risk that the financial statements of the plan may be materially misstated. Prescribing specific procedures irrespective of the risks of material misstatement, in our view, undermines the auditing standards and may have unintended consequences unless more guidance is included as to what is expected in carrying out those procedures. For example, auditors may move towards a more compliance-



based approach given the focus in the proposed SAS on reporting on certain required elements, and may not be attuned to more important drivers of the risk of material misstatement in an individual plan or other potential compliance matters that could have a material and direct financial statement impact but are not specifically addressed in the proposed SAS.

Though difficult to quantify, we also expect costs to increase given the need to perform substantive procedures in areas that may be assessed as lower risk or that, in the auditor's judgment, could be more appropriately tested through a controls-based approach. These incremental costs will likely be borne by plan participants, who may not find value in the proposed changes.

We understand why the ASB and DOL are focused on enhancing ERISA plan audits. However, we believe the proposed SAS would need significant revision before it could be effectively implemented and achieve its intended objective. We urge the ASB and DOL to form a view as to the root causes of the deficiencies that have been identified and first evaluate whether these deficiencies are indicative of a failure to apply existing GAAS or the EBP Guide, in particular in relation to the risk assessment standards. We believe incremental requirements in a proposed SAS should then focus on any areas not currently addressed in the auditing standards or the EBP Guide where substantial deficiencies have been noted from a performance perspective. In our view, the matters that gave rise to quality findings in recent inspections are not necessarily the matters on which auditors would be required to report under the proposed SAS.

We suggest the following questions and principles for the ASB to consider in moving forward in order to determine whether standard setting or other actions may be most appropriate:

- What are the most significant risks to audit quality that are unique to EBPs that need to be emphasized in the proposed SAS? For example, we are of the view that the proposed SAS does not sufficiently address the prevalent circumstance in which the control environment is outsourced and the EBP plan auditor relies on the work of a service auditor/SOC 1 report. It is not clear how this circumstance has been considered, especially when those matters on which the auditor will now be required to report in accordance with the proposed SAS are covered by a service auditor.
- Are there elements of the EBP Guide that could be made prominent in the proposed SAS to hone auditor focus during risk assessment and other key phases of an EBP audit, for example by elevating some of the material to requirements in the proposed SAS? Could new requirements or enhanced guidance better illustrate how auditors are expected to respond to both common and unique drivers of risk (i.e., to build upon the principles in AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, by focusing on EBP considerations)?
- Is there a greater role for others to play to improve audit quality? For example, the AICPA could undertake further outreach to industry groups or State Societies through the Employee Benefit Plan Audit Quality Center ("EBPAQC"), in order to promote a focus on quality and potentially increase membership in the EBPAQC. Could further activities promulgated by the EBPAQC be beneficial to raise the bar of its members, including making sure firms are sufficiently aware of the EBP Guide and other publications and tools? Should training requirements promulgated by the EBPAQC for partners and managers be more widely applicable?
- Could the AICPA's peer review process be further leveraged to improve audit quality at firms that continue to perform poor quality EBP audits or fail to use the available tools and guidance in the way in which they were intended? Should the EBPAQC also have a role in monitoring activities, for



example to set out greater expectations of its members or engage directly with firms that have received findings from the peer review process?

- Is it sufficiently clear how the auditor would be able to comply with the expanded performance and reporting requirements in relation to certain elements? Further guidance is likely needed in the proposed SAS to reflect how auditors approach EBP audits today (i.e., reliance on and testing of controls vs. substantive testing), with consideration given as to the scope of testing that is necessary to report on the elements in paragraphs 15-16 of the proposed SAS and the implications of reporting based on limited testing.
- Is it appropriate to require compliance reporting absent changes to regulations being promulgated by the DOL or IRS? If so, have the right matters been selected and will reporting on these matters continue to be relevant as new provisions are incorporated in EBPs? Will users of the auditor's report understand the findings that are being reported? Is there a risk that users will assume this list includes all aspects of compliance that would be relevant to a particular plan (e.g., compliance with ERISA investment guidelines is not included)? Is there a need to reconsider the position of reporting on all findings other than those that are clearly inconsequential? There is a lack of clarity about how materiality impacts the obligation to report findings, particularly in light of the current compliance programs (e.g., DOL and IRS) that allow for plans to correct errors. We believe further consideration should be given to explaining how auditor judgment may influence the decision to report findings, and the definition of findings reconsidered to include a materiality component.
- Finally, can the ASB satisfy itself that the implementation of the proposed SAS will have a measured effect on audit quality, at a cost that is not perceived as outweighing the benefits, and result in an auditor's report that is understood by – and not misleading to – users?

Our detailed comments in response to the issues posed in the exposure draft are included in the Appendix and have been developed with these principles in mind. Where possible, we have sought to suggest alternatives that could achieve the intended outcome.

* * * *

We appreciate the opportunity to express our views and would be pleased to discuss our comments or answer any questions you may have. Please contact Leonard L. Combs at (973) 236-5265 or Michele Weldon at (617) 530-7334 regarding our submission.

Sincerely,

Pricewaterhousecoopers LLP



APPENDIX

Issues for consideration

Issue 1—Required procedures when an ERISA-permitted audit scope limitation is imposed

We believe the procedures and guidance will achieve the objectives of enhancing execution and consistency in these engagements. We have not identified any additional procedures that should be required.

Issue 2—The form and content of the auditor’s report on ERISA plan financial statements with the ERISA-permitted audit scope limitation

We support clarifying management’s responsibilities for determining whether the ERISA-permitted audit scope limitation is permissible, as well as the fact that such limitation does not relieve management of its responsibility for determining whether the certified investment information is appropriately measured, presented and disclosed in accordance with generally accepted accounting principles (“GAAP”). However, we believe it would be helpful for the DOL to clarify certain aspects of management’s responsibilities by defining terms in the regulations such as “sufficient” with respect to maintaining records or “hold” with respect to certifying entities.

However, we do not support the proposal to move from the current form of opinion (i.e., a disclaimer of opinion with an other-matter paragraph) to a new format when the ERISA-permitted audit scope limitation exists for the following reasons:

- We do not agree with the DOL’s view that changing the form of opinion will reinforce the auditor’s responsibilities with respect to the certified investment information. We believe the focus of the proposed SAS should first be on application of the relevant auditing standards to ERISA plan audits, together with the material in the EBP Guide. As noted in our response to Issue 1, we support required procedures on this information to increase consistent application in practice.
- The increased transparency in the *Management’s Responsibility for the Financial Statements* and *Auditor’s Responsibility* paragraphs in the auditor’s report as proposed comes with a risk that users may misunderstand the limited extent of the auditor’s procedures on what is likely to be the most significant component of the financial statements, since the *Opinion* paragraph refers to the fact that “the financial statements present fairly...” The previous use of a disclaimer of opinion in this circumstance acknowledged that the auditor was not able to obtain sufficient appropriate audit evidence about a material amount in the financial statements.

Should this new format be retained, in our view, the language in the auditor’s report would need to be enhanced to give appropriate context to the opinion, and make explicitly clear the limited procedures the auditor has performed. For example, the auditor’s report could specifically note “with respect to the certified investment information that management instructed us not to audit, the auditor did not assess the risks of material misstatement nor did the auditor consider internal control over the certified investment information, or perform procedures to test the completeness, accuracy or valuation of this information.” The auditor’s report could then continue to describe the limited procedures that were performed.



Issue 3—Modifications to the opinion in the independent auditor’s report

We support clarifying the proposed interaction with AU-C section 705, *Modifications to the Opinion in the Independent Auditor’s Report*, when the ERISA-permitted scope limitation is imposed by management. While our response to Issue 2 flags our overall concern with respect to the changes to the opinion, we find the example reports to be clear in highlighting the intent of the requirement. However, the language in paragraph 34 could be improved to better articulate the requirements to apply AU-C section 705 in the circumstances. We view paragraph 34 as applying regardless of whether an ERISA-permitted scope limitation has been imposed; however, this paragraph is also seeking to explain how the requirements for reporting when such limitation has been imposed would need to be modified. We also believe paragraph 34 would be better placed as a separate section after paragraph 71 to give sufficient prominence to modified opinions, which would be consistent with the treatment in other standards.

Issue 4—Required Emphasis-of-Matter Paragraphs

We are unsure why the ASB considers it necessary to require the auditor to include an emphasis-of-matter paragraph in these situations, as auditors today have the ability to do so in accordance with AU-C section 706, *Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor’s Report*, if they believe such a matter would be fundamental to users’ understanding of the financial statements. It may be helpful to remind auditors that, when such circumstances have occurred and the disclosure in the financial statements is inadequate or omitted, there may be implications for the auditor’s report that cannot be resolved by merely including an emphasis-of-matter paragraph.

We have not identified additional situations that would always result in the need for an emphasis-of-matter paragraph.

Issue 5—Reporting internal control deficiencies

Absent a legal or regulatory requirement to do so, we agree with the ASB’s position that it would be inappropriate to require auditors to publicly report internal control deficiencies. Under GAAS, auditors have flexibility in terms of the nature, timing and extent of testing controls to obtain sufficient appropriate audit evidence as a basis for their audit opinion. An absence of communication about significant deficiencies or material weaknesses could inadvertently be viewed as a positive indication about an entity’s controls, when the auditor may not have used a controls reliance strategy in performing the audit.

We recognize the potential benefit of transparency about significant deficiencies and material weaknesses but, if this disclosure is considered necessary, we are of the view that management should be required to provide it. We suggest the DOL continue to consider whether to establish requirements for reporting of these circumstances, for example on Form 5500 or through some other method.

Issue 6—Certain requirements for audits of ERISA plan financial statements and related required report on specific plan provisions relating to the financial statements

Absent a legal or regulatory requirement to do so, we do not agree with the ASB’s proposal to require auditor reporting on compliance with the specific plan provisions in the proposed SAS, and are concerned with the precedent and unintended consequences of doing so. We have specific concerns with the following aspects of the proposal:



- Currently, audits are designed and performed based on an assessment of the risk of material misstatement of a plan's financial statements, also taking into account AU-C section 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*. Efforts to explicitly report on compliance with the areas outlined in the proposal are likely to be incremental to what would be considered necessary to opine on the financial statements of the plan as a whole, especially if the audit approach relies on controls that are appropriately designed and operating effectively or if the instances of noncompliance were otherwise determined to be immaterial. In addition, some of the matters on which the auditor may be required to report may relate more to compliance with regulations rather to specific plan provisions, which may not be appropriate if considered to be outside of the auditor's expertise.
- The proposed SAS includes certain compliance provisions relating to a plan but not all provisions when an error could have a material impact (e.g., participant loans, investments, required notices). Auditors could therefore confuse the requirements and ignore aspects of compliance in risk assessment that could have a material impact. Also, under the new reporting, only those compliance errors relating to the provisions specifically included in the proposed SAS would be included in the report. Thus, compliance errors relating to other areas not listed in the proposed SAS would not be included, which is likely to cause confusion to users.
- The proposed SAS does not provide sufficient guidance on the nature and extent of effort that would be necessary in these areas to facilitate transparent and useful communication to users of the auditor's report. Said differently, compliance reporting as a byproduct of ERISA plan audits is difficult to achieve if there are not objective criteria against which compliance can be measured. The proposed SAS is also not clear whether every aspect of a plan provision must be tested in order to enable the auditor to report in accordance with the requirements in the proposed SAS.
- The proposed SAS does not consider whether the plan has corrected issues under existing regulatory reporting mechanisms, including those offered by the Employee Plans Compliance Resolution System of the IRS (i.e., Self-Correction Program, Voluntary Correction Program, and Closing Agreement Program). In addition, the DOL has its Voluntary Fiduciary Correction Program for certain errors relating to fiduciary aspects of plans. Errors corrected under these programs do not currently require any form of public reporting.
- We envisage a potentially unwieldy process whereby the auditor, plan administrator and others may debate how the findings are to be presented in the auditor's report, in particular given a lack of consideration of the materiality of individual findings.
- Users of the auditor's report may misinterpret the findings. Individual plan participants may request confirmation from the plan administrator that their particular accounts were not among those listed as exceptions.
- We question whether plan administrators would see value in this additional testing given existing compliance requirements, including potential changes to Form 5500, and the fact that this proposal would impose these new compliance requirements on plan administrators as a precondition of obtaining the audit beyond what is needed to meet the existing reporting requirements of ERISA.



Alternatives

We believe the ASB and DOL should first focus on determining how the performance obligations for auditors could be strengthened in key areas noted by the DOL or through the AICPA inspection and peer review processes. We believe the ASB's primary role is to set GAAS and provide guidance necessary to support quality audits. Actions that may be beneficial include enhanced performance requirements in the proposed SAS or reinforcement of material included in the EBP Guide. Understanding and applying this authoritative guide is an important aspect of quality in ERISA plan audits, so further promotion and training on the intent of key aspects of the EBP Guide may be necessary. For example, the ASB could establish more specific requirements in the proposed SAS for the auditor to obtain sufficient appropriate audit evidence about certain common aspects of ERISA plan audits, and focus the auditor's risk assessment and response on these areas. Doing so would strengthen the focus while not overriding the judgments permitted today about the nature, timing and extent of both substantive procedures and tests of controls necessary to obtain sufficient appropriate audit evidence.

To address calls for additional transparency – which we view as a separate question to be solved - the ASB and DOL could also consider when the communication of “key audit matters” in the auditor's report for ERISA plan audits may be an alternative means of highlighting the most significant matters the auditor addressed during the audit. We believe this would have more informational value to plan participants, rather than the reporting of exceptions (or lack thereof) based on potentially limited testing. Such an approach would also address our concern that the DOL or IRS, rather than the ASB, should be the drivers in changing compliance reporting requirements. In addition, any enhanced reporting should first focus on whether plan administrators should be required to publicly report on compliance matters as a precondition to requiring auditor reporting on such matters. For example, we recognize the potential benefit of transparency about significant deficiencies and material weaknesses but, if this disclosure is considered necessary, we are of the view that management should be required to provide it. We suggest the DOL continue to consider whether reporting of these circumstances on Form 5500 would be appropriate.

Should the ASB decide to continue to require an approach aimed at reporting findings, we believe the Board will need to:

- Reconsider the definition of findings by introducing a materiality threshold to address practical considerations arising from documenting all findings and reporting all findings other than those that are clearly inconsequential (but which may not necessarily be material). For example, the Board could consider requiring auditors to only report findings that will not be corrected under existing programs.
- Better explain how auditor judgment may influence how findings are documented and reported. Users of the auditor's report may not understand the findings, leading to questions to plan administrators about which plans and participants are affected.

It could be feasible that compliance reporting be done akin to an agreed-upon procedures engagement, the findings of which could be restricted to the plan administrator and the DOL, rather than being made publicly available. This approach would enable the DOL to more clearly articulate their expectations on testing and reporting, taking into account changes being pursued to Form 5500 that may better place responsibilities for reporting on compliance first with management. While such an approach would likely



require a regulatory change, following current DOL and IRS processes for contemplating such changes would enable wider feedback from affected stakeholders beyond those who would comment specifically on the proposed SAS.

Issue 7—Required Procedures Relating to the Form 5500

It is unclear whether the EBSA’s review had significant findings related to the Form 5500, although we are aware that differences between Form 5500 and the audited financial statements were noted. We therefore agree it may be helpful to clarify auditor expectations with respect to the Form 5500 and the practical challenges that may arise, given the ERISA requirement to disclose in the financial statements any differences between the information contained in the financial statements and amounts reported on the Form 5500 Schedule H. We believe the framework in AU-C section 720 could serve as a useful basis for the auditor if greater consistency of performance is sought with respect to this information.

The ASB is currently reconsidering its approach to other information, including describing the auditor’s responsibilities for other information more explicitly in a separate section of the auditor’s report. It may be necessary to consider whether further changes may be needed to the proposed SAS in light of the direction of the AU-C section 720 revision project.

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

As noted in response to Issue 6, absent a legal or regulatory requirement to do so, we do not agree with the ASB’s proposal to require auditors to report on compliance in the auditor’s report. We also expressed concerns related to the form of opinion for the ERISA-permitted audit scope limitation in our response to Issue 2. We therefore question whether it is necessary to create a new reporting model for reporting on ERISA plan audits. Rather, we believe the ASB could explain how the required elements set out in AU-C section 700, *Forming an Opinion and Reporting on Financial Statements*, may need to be tailored in an audit of an EBP, including when an ERISA-permitted scope limitation exists.

We encourage the ASB to continue to consider whether changes to auditor reporting that are being contemplated more broadly may result in the need to further refine the proposed SAS before it is finalized, or could potentially result in making conforming changes, including to illustrative examples, shortly after this proposed SAS is finalized. This may in turn have an impact on the proposed effective date.

Issue 9—Proposed Effective Date

We believe the proposed SAS would need significant revision before it could be effectively implemented and achieve its intended objective, in particular given our concerns with requiring auditor reporting on compliance matters in the absence of a legal or regulatory requirement to do so. We believe the ASB should be working together with the DOL and ERISA to determine whether additional changes to the regulatory oversight responsibilities and related requirements for ERISA plan audits are needed to achieve the DOL and ASB’s objectives. We do not believe implementation of a new auditing standard should precede implementation of other changes as a result of regulatory reform.

As noted in our responses to Issues 7 and 8, more time may also be needed to consider whether further changes are necessary to the proposed SAS as a result of the ASB’s Auditor Reporting and Other Information projects, for which proposals are expected to be issued in the fourth quarter of this year. Corresponding changes would also be needed to the EBP Guide, which we believe should be made in



advance of a new auditing standard becoming effective. There may also be impacts on plan administrators, plan sponsors and service providers that would require a significant lead time.

For these reasons, we do not support the proposed SAS becoming effective for ERISA plan audits of financial statements for periods ending on or after December 15, 2018. The ASB should reconsider the effective date as its discussions progress on this and other projects, and should align the effective date with any future regulatory reform, rather than moving ahead with auditor reporting changes in isolation.