SAG·AFTRA HEALTH PLAN | SAG·Producers PENSION PLAN

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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

Dear Sirs:

The purpose of this letter is to provide our thoughts and comments on the proposed Statement on Auditing Standards, Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA. We recognize that the failure rate in employee benefit plan audits has been unacceptable to both the AICPA and the Department of Labor (DOL) and that maintenance of the status quo in employee benefit plan auditing has become unacceptable. Actions must be taken to improve the overall quality of employee benefit plan audits and, therefore, we offer our comments to the proposed changes to the auditing standards.

SAG-AFTRA Health Plan is primarily a self-insured multiemployer plan covering actors who have performed services in television and theatrical motion pictures, television commercials or other entertainment related areas, such as new media, for an employer under a collective bargaining agreement with SAG-AFTRA that specifically requires contributions to the Plan. There are 27,271 participants covered and 4,677 contributing employers. Total assets available for 2016 were $299 million. As stakeholders in the ERISA plan industry we are writing on behalf of our participants to provide feedback on particular aspects of the proposed SAS, and to offer certain suggestions.

SAG-Producers Pension Plan is a multiemployer defined benefit pension plan covering actors who have performed services in television and theatrical motion pictures, television commercials or other entertainment related areas, such as new media, for an employer under a collective bargaining agreement with SAG-AFTRA that specifically requires contributions to the Plan. There are 59,359 participants covered and 4,677 contributing employers. Total assets available for 2016 were $3.3 billion. As stakeholders in the ERISA plan industry we are writing on behalf of our participants to provide feedback on particular aspects of the proposed SAS, and to offer certain suggestions.

Overall, we believe that there are many high-quality audit firms that serve the employee benefit plan industry. We also believe that there are many audit firms that do not perform quality audits and do not adhere to the existing auditing standards. Our understanding of the DOL's most recent audit quality initiative is that a significant portion of the audit findings were found in audits performed by firms that only perform a few plan audits. In this scenario, we do not believe that increasing audit and reporting requirements as proposed in this SAS will have a significant impact on enhancing audit quality. We believe the failure rate in employee benefit plan audits is an education and a performance problem and solutions should be created that address both. Deficient employee benefit plan audits result from auditors not performing audit procedures already required by existing auditing standards. We do not believe most of the provisions of the proposal will achieve higher quality audits. Simply adding more procedures does not remedy this situation when auditors are not complying with the existing standards.

Significantly increasing educational requirements as a condition to issuing an audit report on an employee benefit plan would provide meaningful change to audit quality. Further, improving the quality of the peer review process and insisting that firms conducting employee benefit plan audits use the services of a peer review team with knowledge and experience in auditing employee benefit plans will bring positive change to improving audit quality.

The following are our comments regarding the specific issues identified by the Board:

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; and**

- **Any procedures that should be required and are missing, and if so, describe them**

We do not instruct our auditors to perform an ERISA-permitted limited scope audit. We feel a full-scope audit is more appropriate to ensure the protection of all plan assets, especially over the largest assets held by retirement plans and most other plans as well. Accordingly, we have no comments on this Issue.

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;**

- **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;**

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

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

We do not instruct our auditors to perform an ERISA-permitted limited scope audit. We feel a full-scope audit is more appropriate to ensure the protection of all plan assets, especially over the largest assets held by retirement plans and most other plans as well. Accordingly, we have no comments on this Issue.

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.**

We do not instruct our auditors to perform an ERISA-permitted limited scope audit. We feel a full-scope audit is more appropriate to ensure the protection of all plan assets, especially over the largest assets held by retirement plans and most other plans as well.. Accordingly, we have no comments on this Issue.

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.

The proposed SAS requires the auditor to include an emphasis-of-matter paragraph when specific situations exist. This requirement is too rigid in that it eliminates auditor's judgement in these situations. Any of these specific situations could be considered immaterial and insignificant to the financial statements, as a whole, and an emphasis-of-matter paragraph may actually be misleading. Insisting that these specific situations be included in the auditor's report could actually decrease transparency as a result.

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 the internal control deficiencies identified during the audit with those charged with governance are sufficient. Requiring an auditor to include these comments in the auditor's opinion is duplicative at best and, for multiemployer plans especially, will create significant conflicts between plan auditors, boards of trustees and plan legal counsel. The current communication requirements between auditors and those charged with governance is sufficient to ensure that significant deficiencies and material weaknesses in internal control are presented to those responsible for the plan so that corrective action can be made. Any public reporting of internal control deficiencies is inappropriate and counter-productive to plan management.

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, the objective of enhancing the consistency and quality of audit work will not be achieved by adopting these proposed auditing procedures. The current auditing standards contain sufficient audit procedures to enable the auditor to express an opinion on the financial statements. Those procedures are supplemented by an industry Audit Guide and an industry focused membership center.

   We oppose all of the procedures required in paragraphs 15 and 16. Instead, we recommend that these steps be provided as areas of consideration. Specific examples could be offered to assist the auditor in designing their tests. Auditing standards permit auditors to use their judgement in determining the nature, timing, and extent of procedures to perform in order to render their opinion on the financial statements. The proposed procedures remove the use of auditor judgement and change the nature of the engagement from a financial statement audit to a plan compliance audit.

   We feel that it is inappropriate to use the financial statement audit process in order to perform DOL enforcement of operational compliance. It seems to us that the proposal is shifting the responsibility for monitoring ERISA enforcement from the DOL to the plan auditor, and therefore shifting the costs of enforcement to the Plan and its participants. Furthermore, the cost of enforcement must be born on an annual basis, without regard to plan operation or compliance history. What is the benefit of the additional cost? Adding procedures that focus on immaterial areas is not useful in rendering that opinion and will result in higher costs for the plan. This is not a good conclusion for our plan participants. Further, this doesn't improve audit quality. In fact, it could have the opposite effect, since these procedures may widen the cost differential between quality audits and non-quality audits. This may drive plan sponsors to less expensive and lower quality practitioners that ignore existing auditing standards and will likely ignore additional auditing standards.

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).**

   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 do not believe a Report on Findings should be included as part of the financial statements.

   The procedures in paragraphs 15 and 16 require performance and reporting on results. They are not performed in connection with the auditor's opinion on the fair presentation of the financial statements. Their inclusion in the auditor's report is inappropriate.

   - 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 auditor 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.

   - At a minimum, we suggest that the terminology "clearly inconsequential" be defined in quantitative terms.

   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 sponsors of multiemployer plans, where there is an equal representation of labor union and management individuals, may be especially sensitive to findings being publicly available and their magnitude potentially inflated. Relations between labor and management, and between labor union officers and their rank-and-file members, are at times contentious, and the findings could become political fodder.

- The statement of findings would likely have severe legal consequences for multiemployer plans. The findings of noncompliance could lead to actual or potential litigation.
- 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 and resources to carry out other responsibilities.
- 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.
- The additional review of the proposed statement of findings by plan management and legal counsel could cause additional time constraints to finalizing the audit.

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 any 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 current auditing standards.

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 over immaterial and/or insignificant areas and the related reporting of findings will increase the cost of performing an audit without providing an improvement in audit quality.

The consideration of what will be reported as a finding of noncompliance with plan provisions will ultimately be a matter of legal determination, causing plans 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 is 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?

The purpose of a financial statement audit is to enable the independent auditor to render an opinion on the fairness of the financial statements. In proposed paragraphs 36-48 the auditor is charged with responsibility for the Form 5500, which the auditor may or may not prepare. The requirements in paragraph 36 to 48 extend the auditor's responsibility too far and will cause delays in the issuance of the audited financial statements and filing of the Form 5500 and ultimately increase costs to the plan.

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

Respondents are asked whether

- ***a.*** **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;**
- ***b.*** **The proposed amendments to the other AU-C sections are appropriate; and**
- ***c.*** **Whether there are other sections of AICPA Professional Standards that might need to reflect the provisions of this proposed SAS.**

We have no comment to this Issue.

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 audit function that the proposed SAS would require.

Conclusion

As a recipient of audit services, SAG-AFTRA Health Plan and SAG-Producers Pension Plan applauds the Auditing Standards Board's focus on improving the audit quality of employee benefit plans. We do not believe that this proposed auditing standard is an effective means to that end. As previously mentioned, we believe that significantly increasing educational requirements as a condition to issuing an audit report on an employee benefit plan would provide meaningful change to audit quality. We also believe it would be helpful for plans to be able identify those auditors who have been found to perform sub-standard work. Perhaps a list could be available on the DOL website. Quality firms shouldn't be so hard to separate from the rest of the crowd. We also believe that the DOL could provide greater guidance to plans in the selection process for choosing an audit firm. We undertook a rigorous and detailed process when our Plans changed audit firms but we suspect that many plans may consider price and convenience over industry expertise, experience and commitment to quality when selecting a new auditor.

We hope that our comments and recommendations are worthy of consideration. If you need further information please contact Odéle Kohlstrand at 818-973-4420.

Very truly yours,

Odéle Kohlstrand, CFO
SAG-AFTRA Health Plan | SAG-Producers Pension Plan