Crowe Horwath LLP
Independent Member Crowe Horwath International

330 East Jefferson Boulevard
Post Office Box 7
South Bend, Indiana 46624-0007
Tel +1 574 232 3992
Fax +1 574 236 8692
www.crowehorwath.com

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AICPA Auditing Standards Board
c/o: Ms. Sherry Hazel
American Institute of Certified Public Accountants
Audit and Attest Services
1211 Avenue of the Americas
New York, NY 10036-8775

Via email to Sherry.Hazel@aicpa-cima.com

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

Dear Auditing Standards Board members,

Crowe Horwath LLP appreciates the opportunity to comment on the AICPA Auditing Standards Board's (ASB or Board) Proposed Statement on Auditing Standards (SAS), *Forming An Opinion And Reporting On Financial Statements Of Employee Benefit Plans Subject to ERISA* (Proposal or Proposed SAS).

We support the Board's continued efforts to improve the communicative value and relevance of the auditor's report and the quality of employee benefit plan (EBP or Plan) audits by strengthening the associated standards.

Our observations are described below. Items have been segregated based on our views of significance.

SIGNIFICANT OBSERVATIONS

Certain Requirements for Audits of ERISA Plan Financial Statements (Paragraphs 15 and 16)

Paragraph 15 begins with "Irrespective of the risks of material misstatement," and then paragraphs 15 and 16 proceed to list a number of areas in which testing is required regardless of the assessed risk of material misstatement.

The use of the terminology of "irrespective of the risks of material misstatement" is concerning as it seems contradictory to the guidance within AU-C Section 315, and we believe the use of this terminology could have unintended consequences. AU-C Section 315.03 states that "the objective of the auditor is to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and relevant assertion levels through understanding the entity and its environment, including the entity's internal control, thereby providing a basis for designing and implementing responses to the assessed risk of material misstatement." By mandating that the auditor perform testing irrespective of the risks of material misstatement, auditors might conclude that it is not necessary to perform and/or document their assessment of risks of material misstatement and thus they may fail to test at an appropriate level. In May 2015, the U.S. Department of Labor (DOL) Employee Benefits Security Administration issued a report, *Assessing the Quality of Benefit Plan Audits* (DOL Study). One of the repeated deficiencies noted in the DOL Study was "lack of documentation of risk assessment procedures." Stating within the Proposed SAS the procedures that need to be performed irrespective of risk of material misstatement could potentially increase findings of this nature which would be detrimental to the overall quality of Plan audits.

Paragraph A15 of the Application and Other Explanatory Material states that the "auditor's risk assessment may reduce, but not eliminate, the audit procedures required by paragraphs 15-16." By including this language in the Application and Other Explanatory Material section, we believe there could be an unintended consequence of auditors performing less testing than is currently being performed. For example, an auditor might justify testing only one item within each of the prescribed areas. The ability to use the Proposed SAS to perform less testing than is currently being performed does not appear to align with the objective of the Proposed SAS.

Rather than the current wording of paragraph 15, we would recommend replacing "Irrespective of the risks of material misstatement, the auditor should perform substantive procedures for the following:" with language similar to "Even if the risk of material misstatement is assessed as low, the auditor should perform substantive procedures…" Within the application guidance, we believe there should simply be a reference to the guidance in AU-C 330.A65 as to how the items for testing should be selected (selecting all items, selecting specific items or audit sampling). This would appear to accomplish the desired outcome while tying the Proposal to existing guidance regarding risk assessments and substantive testing.

Currently, the list of items which are required to be tested within paragraphs 15 and 16 is very prescriptive. Including such a detailed list within the Proposed SAS presents concerns as it could lead audit teams to conclude that testing in other areas is not necessary as it is not specifically required by the standard. Also, listing the specific items to test within the Proposal will make adjustments cumbersome if new topics become areas of heightened concern from a regulatory and/or compliance perspective. The current list does not address some of the current areas where compliance issues are routinely identified including auto-enrollment, auto-escalation, and participant loan activity. We believe that the Proposed SAS should be modified to be less prescriptive and to indicate that there is an expectation that substantive testing procedures will be performed on all relevant areas of Plan and participant activity to ensure compliance with the applicable provisions within the Plan document. Within the application guidance, we believe examples could be given of the testing which should be considered similar to the audit guide examples.

Reporting on Specific Plan Provisions Relating to the Financial Statements (Paragraphs 119-124 and also impacting Paragraphs 17-19)

The additional reporting proposed in paragraphs 119-124 is intended to clarify and strengthen communication of significant findings and issues noted by the auditor during the performance of audit procedures. While well-intentioned, we believe that the proposed reporting will not achieve the desired goal and could have unintended consequences which would greatly outweigh any benefit which might come from this reporting. We recommend that this reporting requirement be eliminated from the Proposed SAS. The following paragraphs provide further context regarding our recommendation.

Under AU-C 260 and AU-C 265, management and those charged with governance are being provided with the information they need to oversee the Plan and to perform their responsibilities to the Plan. One of the objectives of AU-C 260, *The Auditor's Communication with Those Charged with Governance*, is to "provide those charged with governance with timely observations arising from the audit that are significant and relevant to their responsibility to oversee the financial reporting process." The objective of AU-C 265, *Communicating Internal Control Related Matters Identified in an Audit,* is for the auditor "to appropriately communicate to those charged with governance and management deficiencies in internal control that the auditor has identified during the audit and that, in the auditor's professional judgment, are of sufficient importance to merit their respective attentions." Under the guidance within AU-C 260 and AU-C 265, mechanisms already exist for ensuring that those individuals who are responsible for the Plan are aware of identified deficiencies in internal control and other significant observations. As the individuals who are communicated with under the existing standards are the ones who have the ability to solve the identified issues and who have fiduciary responsibility for the Plan, we believe that adding the proposed reporting requirements and making that reporting available to the general public would not improve plan compliance or audit quality. The general public and Plan participants do not have the ability to facilitate necessary corrections or improve Plan operations.

The proposal also includes a stipulation that the report need not include findings that are deemed "clearly inconsequential," which may cause further confusion and inconsistencies with the Proposal. According to AU-C 250.A26 "The auditor may reach agreement in advance with those charged with governance on the nature of matters that would be considered clearly inconsequential and thus, need not be communicated."

We believe this approach is problematic when reporting externally. The subjective nature of "clearly inconsequential" could lead to inconsistencies in reporting of similar findings among audit firms and management. An outside reader's comparison of publicly-available reports of a variety of Plans may lead to the erroneous conclusion that the absence of a particular finding in a report means that finding does not exist. Within Illustration 1 of the Proposal, the example wording in "Report on Specific Plan Provisions Relating to the Financial Statements" states:

> "We noted instances when vesting was not calculated in accordance with the plan instrument which resulted in the plan not paying the appropriate benefits."

The "Report on Specific Plan Provisions Relating to the Financial Statements" section of Illustration 3 within the Proposal contains the following language:

> "During our audit, we did not have any findings related to whether the plan and plan transactions are in accordance with the specific plan provisions."

Depending on how the auditor has defined "clearly inconsequential", it is possible that the testing results could have been the same for both audits associated with illustration 1 and illustration 3. For example, if the auditor had tested a sample of 20 and identified a single error, the auditor could have performed procedures to quantify the potential magnitude of the error and concluded that the dollar impact of the noted error was immaterial. Auditor "A" could conclude that the error constitutes a finding regardless of potential financial statement impact and include it within the report (Illustration 1), but Auditor "B" could conclude that the error was "clearly inconsequential" since it would not have a material financial statement impact and not mention it in the report (Illustration 3). Readers of Illustration 3 might assume that there were no issues identified in the testing performed; however, the same errors could have been identified in the participant level testing as were noted in Illustration 1 but the auditor interpreted clearly inconsequential differently.

Another challenge with the proposed reporting requirements and the "clearly inconsequential" classification is the employee benefit Plan auditor has been engaged to perform a financial statement audit rather than a compliance audit. The new proposed reporting is focused on specific Plan provisions relating to ERISA Plan financial statements. While it is highly unlikely that any individual findings which result from testing specific participant activity would be material to the Plan overall, the intent of the new reporting appears to be focused on compliance matters. Without additional guidance to implement "clearly inconsequential", there is the potential that those charged with governance could unduly influence this reporting and that there will be widespread inconsistencies in practice.

We are aware that the ASB is in the process of considering an approach similar to the Public Company Accounting Oversight Board's (PCAOB) recently approved new auditing standard which requires the reporting of critical audit matters (CAMs). Within the PCAOB standard, a CAM is defined as "matters communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements; and (2) involved especially challenging, subjective, or complex auditor judgement." As stated previously, we recommend eliminating reporting significant findings in the auditor's report, however, in light of the ASB project to consider CAMS, we believe it would be preferable to defer reporting of any specific findings for EBP audits until the ASB decides how they intend to address CAMs. Should the ASB ultimately conclude that project by including requirements similar to CAMs to be reported, it may provide the DOL and other users with sufficient knowledge to meet their objectives.

As it relates to the costs associated with this aspect of the Proposal, we believe that the addition of the reporting requirements within the Proposed SAS would lead to an increase in time and cost incurred in performing EBP audits with minimal, if any, improvement of audit quality. We anticipate that a great deal of time and effort could be devoted to interpreting audit findings to determine if they warrant reporting and carefully drafting the findings for public consumption. The time spent on these reports could detract from time which could be spent performing procedures which could improve audit quality.

Auditor's Report on ERISA Plan Financial Statements When Management Limits the Scope of the Audit as Permitted by ERISA (Paragraphs 98-106)

While we believe changes to the wording of the auditor's report could help achieve the stated objectives, we have concerns with the proposed wording noted in paragraph 106. We have significant concerns with the proposed wording in paragraph 106 and as presented in Illustration 3 within the Proposal. The wording of the "Auditor's Opinion With the ERISA-Permitted Audit Scope Limitation on the Financial Statements" is presented in Illustration 3 below:

> "In our opinion, based on our audit and based on our use of the certification of the investment information that we were instructed not to audit, the financial statements referred to above present fairly, in all material respects, the net assets available for benefits of ABC 401(k) plan as of December 31, 20X2 and 20X1, and the changes in net assets available for benefits for the year ended December 31, 20X2, in accordance with accounting principles generally accepted in the United States of America."

We believe the proposed wording implies a greater level of assurance than appropriate for the information which was certified. The proposed wording could be construed to provide the same level of assurance to the certified investment information as is obtained through the audit procedures which were performed on the information which is not covered by the limited scope certification. As a result, we believe the proposed wording could be misleading to users thereby increasing the expectation gap between users and the auditors.

We would recommend changing paragraph 106 to state that "the auditor's report should include a statement that in the auditor's opinion, except for the certified investment information that the auditor was instructed not to audit and did not audit, the financial statements present fairly, in all material respects, the […] in accordance with [the applicable financial reporting framework.]"

The wording in Illustration 3 would be revised to the following to clearly identify the scope limitation:

> In our opinion, except for the certified investment information that we were instructed not to audit and did not audit, the financial statements referred to above present fairly, in all material respects, the net assets available for benefits of ABC 401(k) plan as of December 31, 20X2 and 20X1, and the changes in net assets available for benefits for the year ended December 31, 20X2, in accordance with accounting principles generally accepted in the United States of America.

Paragraphs .95-.97 have significantly expanded the description of management's responsibilities within the auditor's report. We suggest that guidance be added to the proposed paragraphs to address circumstances where management does not perform all of the items listed in these paragraphs covering management's responsibility section. The guidance might refer to further scope limitations if these responsibilities were not performed by management.

Transition Guidance

Paragraphs 49-108 of the Proposed SAS contain revisions to the auditor's report on ERISA plan financial statements when there is no ERISA-permitted audit scope limitation and the auditor's report on ERISA plan financial statements when management limits the scope of the audit as permitted by ERISA. EBPs are required to present comparative statements of net assets available for benefits. As comparative financial statements are required, we believe the Proposal needs to include transition guidance which addresses how these changes in the auditor's report should be presented in the year of adoption. We would recommend that the transition guidance include example wording of an auditor's report on ERISA plan financial statements when there is no ERISA-permitted audit scope limitation and an auditor's report on ERISA plan financial statements when management limits the scope of the audit as permitted by ERISA for the year in which the new reporting is presented.

OTHER OBSERVATIONS

In addition to the items discussed above, we have provided other comments and observations below for your consideration.

Paragraph 20(b)

Paragraph 20(b) states that the auditor "should evaluate management's assessment of whether the entity issuing the certification is a qualified institution under DOL rules and regulations." Given the subjective nature of the term "evaluate", we would recommend adding application guidance to paragraph 20(b) similar to the application guidance provided for paragraph 20(d) in A48.

Emphasis-of-Matter Paragraphs (Paragraph 116)

We believe that the requirement to include emphasis-of-matter paragraphs in the auditor's report including considerations for matters to be included is sufficiently addressed by the existing guidance in AU-C section 706: Emphasis-of-Matter Paragraph and Other-Matter Paragraphs in the Independent Auditor's Report (AU-C 706), and therefore additional specific requirements for EBPs in this proposed SAS are unnecessary. We do not believe that paragraph 116 would lead to improved audit quality or improved reporting. By listing within the Proposed SAS specific items which require an emphasis-of-matter paragraph, we believe there is a risk that auditors will only consider these items and could overlook other items which are worthy of inclusion in the auditor's report as an emphasis-of-matter or that are required by other standards.

Paragraphs 12(c), 22(b), 54(b) and 96(d)

Throughout the Proposal, there are references to management's responsibility to maintain "sufficient records with respect to each of the participants in accordance with ERISA sections 107 and 209 to determine the benefits due or which may become due to such participants". Paragraph 12(c) requires management to acknowledge this as a responsibility in the engagement letter, and Paragraph 22(b) requires management to provide representation of this in the management representation letter. AU-C 580.04 states "although written representations provide necessary audit evidence, they complement other auditing procedures and do not provide sufficient appropriate audit evidence on their own about any of the matters with which they deal." As the Plan auditor, our responsibility is to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. As the auditor has not been engaged to opine on ERISA compliance, the requirements of paragraphs 12(c), 22(b), 54(b) and 96(d) could cause others to conclude that audit procedures were performed specifically to test for compliance with ERISA section 107 and 209. We believe reference to sections 107 and 209 should be removed throughout the Proposal.

Paragraph 118(g)

Paragraph 118(g) would have the auditor report on whether the form and content of the supplementary information is presented in conformity with the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. While AU-C 725.07(b) requires the auditor to perform procedures related to form and content, AU-C 725.09 does not indicate that reporting on form and content is required. We do not believe the reporting requirements on supplemental schedules for a Plan should differ from the reporting requirements for supplemental schedules for other types of entities; therefore, we would recommend removing Paragraph 118(g) from this standard to be consistent with AU-C 725.09.

Effective date

We believe that at least a two (2) year transition period will be necessary between when the Proposal is finalized and the effective date. This transition period will allow for education of auditors and Plan sponsors regarding the new requirements.

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Crowe Horwath LLP supports the Board's continued efforts to improve the quality of EBP audits for the benefit of all stakeholders. We are grateful for the opportunity to comment on this proposed statement on auditing standards and would be pleased to respond to any questions regarding our comments and observations. Should you have any questions, please contact Jennifer Allen at (614) 280-5263 or Mike Yates at (574) 236-7644.

Sincerely,

Crowe Horwath LLP

Crowe Horwath LLP