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Sherry Hazel
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American Institute of Certified Public Accountants, Inc.
1211 Avenue of the Americas
New York, NY 10036-8775

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

Dear Ms. Hazel and Auditing Standards Board Members,

The North Carolina Association of Certified Public Accountants (NCACPA), representing over 20,000 North Carolina CPAs in public practice, industry, government, and education, welcomes the opportunity to respond to the Proposed Statement on Auditing Standards, *Forming an Opinion and Reporting Financial Statements of Employee Benefit Plans Subject to ERISA.* The NCACPA Employee Benefit Plan Committee deliberated the exposure draft and submits the following responses:

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

Q-Do the procedures and guidance achieve the objectives of enhancing execution and consistency in these engagements and if not, why? Are any procedures missing that should be required?

A-The procedures and guidance do effectively achieve the objections of enhancing execution and consistency in limited scope engagements. However, paragraph A47 states "…the auditor <u>may</u> need to understand the types of investments held by the plan to evaluate whether the form and content of the ERISA plan's financial statement disclosures for those investments are in accordance with the applicable financial reporting framework." We often find that auditors do not obtain a sufficient understanding of plan investments in a limited scope audit. We think this sentence should be modified to say "should" instead of "may." This will cause auditors to investigate more thoroughly to ensure that they understand the types of investments being held so they can determine if they are being properly reported. This is a critical risk in the private middle market where typically auditors are also preparing the draft financial statements for their clients.

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

Q-Will the proposed auditor's report improve 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 can it be revised?

A-The proposed auditor's report will improve transparency of reporting for limited scope engagements. One of our main concerns with the new reporting relates to the *Report on Specific Plan Provisions Relating to the Financial Statements* and the reporting of findings, which we discuss in Issue 6.

Q-Will the proposed auditor's report improve the auditor's understanding of his responsibilities in a limited scope audit resulting in potential improvements in audit quality, and if not, why?

A-The proposed auditor's report will improve the auditor's understanding of his or her responsibilities in a limited scope audit. We question whether the auditor's report is the place for the auditor to be understanding his or her responsibility in a limited scope audit, and how beneficial it is to the user of the financial statements compared to the increased efforts and costs. We think overall audit quality would be improved if the AICPA and state societies were more consistent in policing and penalizing the firms that are not performing well rather than placing additional burdens on plan sponsors and quality auditors. Good firms tend to always find a way to exceed expectations regardless of where the bar moves. Poor quality firms tend to find loopholes, and would probably be more likely to weigh the cost benefit of performing plan audits if they knew what the penalties were for sub-standard engagements.

Q-Will the proposed auditor's report better describe management's responsibilities for the financial statements, and if not, why?

A-The proposed auditor's report does provide a better description of management's responsibilities with respect to the financial statements. We think management may need to consider retaining ERISA counsel to evaluate their risks, which is something that should be considered as potential cost and risk to the plan sponsor

Q-Will the proposed auditor's report provide sufficient clarity to users with respect to the auditor's responsibilities and matters reported, and if not, why?

A-The proposed auditor's report does provide additional clarity for knowledgeable users with respect to auditor's responsibilities and matters reported. As noted previously, see Issue 6 for our comments on *Report on Specific Plan Provisions Relating to the Financial Statements*.

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

Q-Is the guidance in paragraphs 31 and 34 of the proposed SAS (a) 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?

A-The guidance in paragraphs 31 and 34 is clear with respect to the auditor's responsibility, and achieves the objective of providing transparent reporting to the users. We suggest adding more clarity with respect to 403(b) engagements that do not have access to plan records prior to 2009 who have been following field assistance bulletins ("FAB") 2009-02 and 2010-01. An example auditor's report would be beneficial.

Q-Is 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 appropriate?

A-Yes, the examples will be useful to auditors drafting these types of modified audit reports. As noted above, an example for a 403(b) plan that is following the FABs would be helpful.

Issue 4-Required Emphasis of Matter Paragraphs (paragraph 116)

Q-Are the identified emphasis of matter paragraph situations appropriate? Are there additional situations that should be required?

A-The three identified emphasis of matter paragraph examples appear appropriate. There should be a more clear connection to AU-C 706, Exhibit B, which lists other considerations when adding an emphasis of matter paragraph.

Issue 5-Reporting Internal Control Deficiencies

Q-Is the current reporting model of reporting internal control deficiencies to those charged with governance sufficient? Are there other reporting considerations that should be evaluated?

A-Yes, we agree with the Auditing Standards Board ("ASB") that the current reporting model of reporting internal control deficiencies to those charged with governance is sufficient. It would be detrimental and have unforeseen consequences to report significant deficiencies and material weaknesses to the general public. It also does not seem appropriate to report internal control findings in a report that states that we are not forming an opinion on internal control. It might be helpful if there are tools developed to assist auditors with determining what to consider when assessing compliance issues noted during an audit and how to classify them as a tool to improve audit quality.

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

Q-Will the required audit procedures enhance the consistency and quality of the audit work performed? Does the proposed SAS provide appropriate guidance on achieving the above requirements? In the Plan provisions reporting, is including the list of individual areas tested appropriate and if so whether there are other items that should also be include (if not, why not)?

A -Yes, the required audit procedures may enhance the consistency of the audit work performed. The guidance provided by the SAS appears appropriate to achieve the stated requirements. We think it is helpful to include the list of individual areas to be tested. It was noted in paragraph 14 that paragraphs 15 and 16 do not include all requirements, which is important. We expect there will be many questions and decisions that need to be made with respect to sampling approaches and what will be sufficient for audit purposes. We also think that these are just describing procedures that have been part of the design of quality audits already. We do question the requirement to perform procedures "irrespective of the assessed risks of material misstatement." Auditors use materiality and ERISA knowledge to assess the risk areas to the plan when designing our procedures. Once we take away auditor's judgement, it aligns more with an agreed upon procedure than an audit. It appears to be an unreasonable penalty to knowledgeable auditors in order to try to educate uninformed auditors, and will come at a cost. As it stands, many plan sponsors question audit fees, and try to understand the value of our efforts. We somehow have to capture the DOL goals of ensuring participants are protected, and our goal of improving audit quality, and ensure that the additional cost is beneficial to participants.

Q-What procedures related to other plan provisions or specific areas should be included in the required testing?

A–Other procedures related to compliance with the plan document may include compliance with the participant loan policy.

Q-In the Plan provisions reporting, is the requirement to exclude findings that are "clearly inconsequential" appropriate, and if so is there guidance the ASB can consider to drive consistency in application in practice?

A–We strongly disagree with including any type of findings in the auditor's report. The use of the term "clearly inconsequential" is not specific enough to provide uniform reporting amongst accounting firms. In addition, most plans have some types of operational issues during the year. This reporting of findings penalizes smaller plans, which typically have smaller plan assets, lower materiality by a significant amount than larger plans, and therefore there will be more of a likelihood that findings will need to be reported than with the larger plans. In most cases, those findings are corrected as soon as they are found, but once reported, it leaves a bad impression of the Plan sponsor and the plan, which may be unwarranted. If it is decided that findings need to be reported, we think it is more appropriate to report only material findings. If material findings are corrected or included as receivables in the financial statements by the report date, that fact should also be included to give the reader (plan participants) an understanding of the full picture. However, we think it is more appropriate to report findings to those charged with governance and plan management.

Q-In the Plan provisions reporting, should the findings also include any matters identified by management or the plan administrator?

A–No, as noted above, we strongly disagree with reporting findings in the auditor's report. We think it would be an unnecessary penalty to a plan sponsor to report matters that they discovered by their own controls, matters that are immaterial to the financial statements, and matters that have been corrected by making participants whole.

Q-Are 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?

A–See above response. We do not agree with reporting findings in the auditor's report.

Q-There may be unintended consequences from including the Plan provisions findings in the auditor's report, and if so, what may those unintended consequences be, and how might they be mitigated?

A–See above response.

Q-Will the required additional procedures and reporting of findings 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?

A–The additional procedures and the additional reporting will result in a significant amount of time upfront modifying audit forms and programs, training auditors, and educating plan sponsors. These up front costs are acceptable. In addition, there will be some extra time spent during fieldwork. The amount of additional time spent will depend on the accounting firm, but will increase to some degree in most firms. The bulk of the additional time will be spent discussing the contents of the findings reported in the auditor's report. We foresee that this will cause a large amount of time at the back-end of the engagement. Typically in the middle market, there is someone from human resources (and possibly accounting) who is involved for the majority of the engagement. The chief financial officer or others charged with governance may not be too heavily involved with the engagement until they review the financial statements. Any reporting of findings will cause major efforts by the auditor, the plan sponsor, may involve their attorney, and will impact the relationship, all to report findings that are "clearly not inconsequential." This does not seem to achieve the goal of this standard, nor is it beneficial to either the plan sponsor or the auditor. In fact, it may cause turnover in audit firms to auditors who may not be as detailed, as an unintended consequence. Overall, we agree with the aspects of the standard related to paragraphs 15-16, but we strongly disagree with reporting findings in the report. We think the cost as described above clearly outweigh any benefit to audit quality, and penalizes specialized benefit plan audit practices and smaller plan sponsors, and smaller size plans to a degree that it may cause some private sponsors to eliminate their plans or to push more of their costs to the plan participants.

Issue 7- Required Procedures Relating to the Form 5500 (paragraphs 36-48)

Q-Do the required procedures related to the Form 5500 increase consistency with respect to identifying information in the Form 5500 that may be relevant to the audit?

A-We agree that the procedures noted in paragraphs 36-48 appear reasonable and appropriate to perform on a Form 5500 with respect to a benefit plan audit engagement. However, some of the challenges with consistency also relate to reporting of plan investments. There is still a lack of understanding of investments, for example insurance products, by auditors and third party administrators ("TPAs"). This, combined with outdated investment lines on the Form 5500 (until proposed 5500 changes go into effect, if at all) often lead to auditors misreporting investments in the financial statements. It seems that there is a risk that auditors may therefore improperly report variances on the auditor's report. Reporting material variances on the auditor's report may have unintended consequences and present more legal issues and risk to plan sponsors and auditors alike if the root issue of plan auditors, plan sponsors, and TPAs not understanding plan investments is not first addressed.

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

Q-Does the proposed approach of creating a new reporting model for reporting on ERISA plan audits better describe management's and the auditor's responsibilities in these engagements?

A-Yes, the proposed approach for the new reporting model does better describe management's and the auditor's responsibilities than the current model. However, we are not currently in favor of the reporting model as it stands for the reasons outlined in Issue 6. We think that this is not addressing the root cause of the audit quality issues, and for all the cost and pain to all audit firms and sponsors alike, it will not improve audit quality, which we understand to be the main goal.

Q-Are the proposed amendments to the other AU-C sections appropriate? Are there other sections of AICPA Professional Standards that might need to reflect the provisions of this proposed SAS?

A–Yes, the proposed amendments to the other AU-C sections seem appropriate. We have not noted other sections that might need to reflect provisions of this proposed SAS.

Issue 9-Proposed Effective Date

Q-Does the proposed effective date provide sufficient time for adoption?

A-We recommend that the effective date begin for years beginning no sooner than twelve months subsequent to the issuance of the final standard. This will provide firms with sufficient time to discuss with and educate plan sponsors, provide plan sponsors time to determine the impact to them, develop, offer, and perform detailed training for CPAs, and for firms to update their forms and programs.

Thank you so much for the opportunity to provide feedback on this proposed standard. If you would like additional discussion with respect to the above comments, please contact Monique Elliott, Chair of the NCACPA Employee Benefit Plan Committee, at 704-654-6967. This response was approved for release by the North Carolina Association of CPAs on September 29, 2017.

Sincerely,

Monique E. Elliott, CPA

Monique Eve Elliott, Chair
NCACPA Employee Benefit Plan Committee

cc: Rollin J. Groseclose, CPA, CGMA, Chair, NCACPA Board of Directors
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