Employee Benefit Plan Audit Quality

By CariAnn J. Todd

Audit quality is of great concern to the CPA profession as well as the DOL. A recent EBSA study indicates that there is some significant room for improvement in the audits of employee benefit plans. This article discusses how CPAs are addressing audit quality as well as some of the challenges to the process.

As a CPA, I am fortunate to be in a profession that, with the exception of the Enron and Arthur Andersen debacles in 2001 and a recent award show envelope mix-up, rarely makes the national news. While it did not make the Today Show when the Employee Benefits Security Administration (EBSA) released its study of audit quality in 2015, it made headlines in many of the most popular business publications. As a long-time auditor of employee benefit plans, it felt like Matt Lauer was knocking on our door.

CariAnn J. Todd, CPA, is the Director of the Employee Benefit Plan Audit Group for BeachFleischman PC, one of Arizona's largest locally-owned CPA firms. As Director, she is responsible for the development and evolution of the firm's audit approach for employee benefit plans. She has spoken at conferences and conducted webcasts for ASPPA, WPBC, and NIPA on the topics of plan audits and nontraditional investments. She is a CPA licensed in Arizona and Texas, a member of the American Institute of Certified Public Accountants, and a graduate of Abilene Christian University in Abilene, Texas. She can be reached at: *ctodd@beachfleischman.com.*

The EBSA study revealed that 61 percent of audits complied with auditing standards or had minor deficiencies; however, 39 percent had one or more major deficiencies. While batting .610 would score us a 10-year, nine-figure contract in major league baseball, it is a number that is on the verge of embarrassing for our profession.

CPAs have long been self-governed and prided ourselves in doing a great job of keeping each other in line. The EBSA study revealed that in the area of auditing employee benefit plans, we have somehow missed the mark. The American Institute of Certified Public Accountants (AICPA) issued a six-point plan in May 2015 that addresses audit quality for all types of audits, not just employee benefit plans. The plan, which is available to the public on the AICPA website, starts in the prelicensure phase, then touches on all aspects of self-governance: education, peer review, monitoring, ethics enforcement, and clarified auditing standards.

The plan starts at the beginning, looking at how to attract talented students to accounting in high school, then moves on to the type of instruction and professor qualifications at the universities. Then there is the new CPA Exam launching this year that will try to better assess critical thinking skills and professional skepticism. With respect to peer review, there is an increased level of scrutiny in the area of employee benefit plan audits. Having just completed our peer review, I can vouch for the fact that our benefit plan audit practice experienced a higher level of scrutiny than any of the past peer review visits in my professional career. The additional scrutiny during peer review, along with the auditor inspection efforts of the DOL, together will help with the ethics enforcement objective of the six-point plan and attempt to identify and then discipline those firms who are doing deficient audit work in the area of employee benefit plans. The DOL and AICPA both refer known audit deficiencies and/or ethics violations to the CPA's or firm's state board of accountancy for further investigation.

Education is an area in which there is a lot of resources available; however, not all CPA firms have invested the time and money into it. The AICPA has an Employee Benefit Plan Audit Quality Center that is designed to offer its members a number of resources to educate themselves on many facets of auditing employee benefit plans. The AICPA also provides an annual conference with up to four days of continuing education in this topic area as well as a number of webcasts and self-study materials available online. At the state level, most states offer at least one course annually on auditing employee benefit plans. From my personal experience, I think a large resource for education that is largely untapped by CPAs is the education offered by ASPPA, NIPA, WPBC, and similar organizations, both at the national level and local levels. So while continuing to improve education is a focus area for the AICPA as part of its plan, there already exists a large supply of education available to practitioners.

Practice monitoring is something all firms that provide attest services are required to do. Most firms currently use an annual internal inspection process to self-evaluate the quality of work performed. There is, however, a trend towards on-going, almost real-time practice monitoring as an attempt to address quality concerns as they occur as opposed to as a historical exercise. While this may seem intuitive, movement to real-time monitoring is an extreme shift in thinking as well as in workflow and risk management.

The last item in the AICPA's six-point plan is the clarification of the auditing standards. In the United States, auditing standards are issued by the AICPA Auditing Standards Board (ASB). The ASB recently completed a process whereby the standards were rewritten so that auditors could better understand and apply them to their practice. In my opinion, this is the hardest part of the plan for the profession to implement. Auditing standards are very general in nature. To help alleviate some of the generalities, the AICPA provides an 852-page Audit & Accounting Guide for Employee Benefit Plans. It would seem logical that with 852 pages of guidance on how to audit an employee benefit plan it would be simple to implement the auditing standards, right? The best analogy for why it is not so simple is to take a look at the DOL's regulation for timeliness of remittances of participant contributions. You probably know it by heart, so I will just quote my favorite part:

> …on the earliest date that they can reasonably be segregated from the employer's general assets, but in no event later than (i) for pension plans, the 15th business day of the month following the month in which the participant contributions are withheld or received by the employer …

For a large plan, the DOL has made it clear that the 15th business day of the month is by no means a safe harbor, the intent is on as soon as contributions reasonably can be segregated. But what does that mean to a particular employer? Is it one day? Three days? Seven days? Our experience with various DOL audits has been: it depends.

This is essentially how it works with auditing standards. Our audit approach, the level of testing, the time it takes, how much it costs… they all depend on the plan. The factors that contribute to how an audit is performed are: number of eligible participants, number of participants with account balances, experience in past audits, cleanliness of participant and payroll records, type of investments held, complexity of plan requirements, number and type of benefit payments, and how fees are paid by the plan. The use of service providers by a plan can sometimes decrease or increase the level of procedures required for the audit.

In addition to the plan characteristics that impact how an audit is performed, the auditing standards allow for auditor judgment in the application of how the auditing standards are met. This means that our firm can have a sampling and testing methodology for eligibility that is completely different from firm X down the street, and both of us could be considered "right" in terms of whether the auditing standards were met.

Finally, there is the issue that no one wants to talk about (or admit as an influential factor)…fee pressure. In a typical corporate audit scenario, the audit is being required by a third party from whom the corporation receives something they need: a loan, a guarantee, financial investment, a license, bonding, *etc*. The corporate entity is more than willing to obtain and pay for a quality audit in order to maintain the relationship with that third party. Unfortunately, the audit requirement set forth in ERISA does not come with a mutually beneficial relationship from the perspective of the plan sponsor. Up until recently, I would say that fee pressure was most prevalent in the under-500-participant strata. However, we recently proposed on a plan audit with a participant count in excess of 10,000 and fees were one of the top concerns of the plan sponsor.

We have worked hard in our practice to develop an audit approach that we can apply to our client base that meets the auditing standards in the most efficient manner. However, in our daily practice we regularly come across situations where we just have to do more work in order to do it right, and if we have to choose, quality versus profit, quality wins. We know what a quality audit looks like and sometimes we take lumps internally when the cost of quality exceeds what we are able to bill and collect. Many firms like us (trying to do it right) are seeing a trend toward commoditization, which focuses on cost above all else. We believe this market emphasis on cost is a major contributing factor to the results of the EBSA's study that found 39 percent of audits had one or more major deficiencies.

So how does the market balance cost and quality? The AICPA's efforts on improving audit quality via the six-point plan will help. The DOL's inspection program and enforcement activities will help. In my opinion, educating plan sponsors as to why audit quality matters is the greatest challenge. I have been on phone calls with prospective clients whose participant count just topped 120 and witnessed the pregnant pause or the not-so-silent gasp when we got to the topic of fees. It is challenging to perform a quality audit on the smallest of plans, with our best audit team, and realize standard rates due to the market fee pressure. We are appreciative that the AICPA and the DOL are aware of the quality issues in the marketplace and are hopeful that their programs and efforts will bring positive change to audits of employee benefit plans. Ultimately, it is plan sponsors and plan participants who will benefit the most. ■