

Power of Collaboration Among CPA Auditors to Improve Audit Quality

BY LISA GERMANO

In 2015, the Department of Labor (DOL) released its study of audit quality for employee benefit plans. This study was the third such study undertaken by the DOL. Since the last study, the certified public accountant (CPA) profession mobilized to provide additional resources, including a dedicated Employee Benefits Audit Quality Center and focused education on audit standards. Despite that focus and attention, the 2015 report shows that improvement has not been what was hoped for and anticipated. The profession responded with not just additional

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resources targeted to the noted deficient areas, and comprehensive learning opportunities, but the grassroots source of new resources began to take hold. In 2015, the Virginia Society of CPAs held a town hall to call employee benefit plans (EBP) auditors to collaborate, and the profession has responded in a profound way.

Background

On May 28, 2015, the DOL released its most recent study on audit quality for EBPs. More than 7,300 CPAs nationwide audited more than 81,000 employee benefit plans. (See Exhibit 1.)

Exhibit 1. The DOL's Statistical Sample of 400 Plan Audits

- 2011 Form 5500 filings
- 6 strata based on size of EBP practice
 - 1-2 plans
 - 3-5 plans
 - 6-24 plans
 - 25-99 plans
 - 100-749 plans
 - 750+ plans
- 1 audit in lowest 2 strata, 5 in all others

The Employee Benefit Security Administration's (EBSA) study of 400 plan audits found that, while 61 percent of audits substantially complied with professional auditing standards, 39 percent did not. Among the deficient audits are those performed by firms who have not identified as an EBP auditor. That means they likely have not been subject to peer review, which is a requirement to perform EBP audits. A firm not submitting to peer review is subject to state licensure enforcement action by the State Board of Accountancy (BOA) with jurisdiction over their firm's license to practice. The DOL study was based on 2011 Form 5500 filings, creating different strata by the number of audits performed by CPA firms. (See Exhibit 2.)

As a result of the study, the DOL, the licensing state BOA, the BOA national association, the National Association of State Boards of Accountancy (NASBA), as well as the CPA profession's national membership association, the American Institute of Certified Public Accountants (AICPA) and CPAs state membership

associations (State Society), have collaborated to seek solutions.

The Regulatory Response

Certain BOAs have collaborated with State Societies to offer education about roles and responsibilities for firms that perform EBP audits, state licensing requirements,

and the enforcement process. The AICPA also has enhanced its six points of Audit Quality focus, with additional resources at each point of reference, including a certificate program for EBP auditors and collaborative competency-based learning. (See Exhibit 3.)

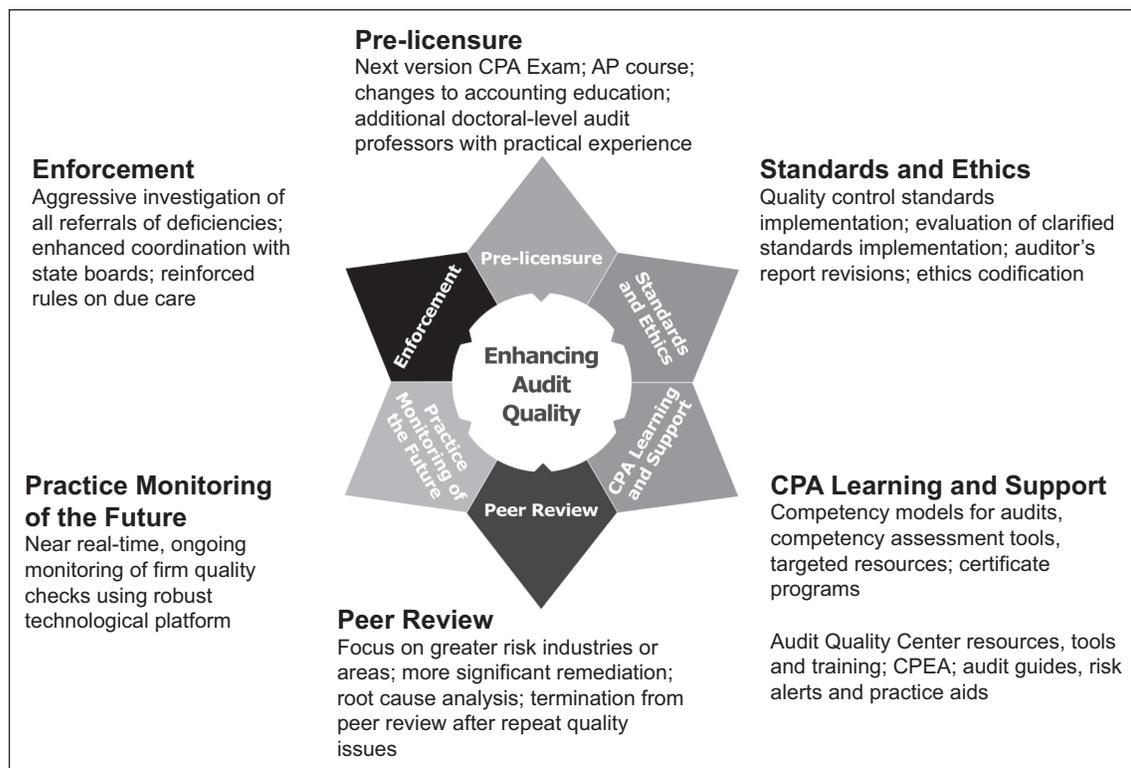
The 39 percent rate of audit deficiencies cited in the study raised significant concerns for the Virginia Board of Accountancy (VBOA). The mission of the VBOA is “to protect the citizens of the Commonwealth through a regulatory program of licensure and compliance of CPAs and CPA firms.” The VBOA has a responsibility to ensure that audits are being conducted in accordance with current and relevant technical standards as well as the Code of Professional Conduct.

The VBOA is in the process of looking closely at CPA firms that have conducted audits of Virginia-based EBPs. The VBOA believes that efforts aimed at improving audit quality are good for the profession, good for the citizens of the Commonwealth, and a key component of its mission. The VBOA wanted to be a part of a collaboration effort that began with a small group of CPAs who perform EBP audits. These Collaborator Champions, as they have become known, are willing to work with other CPA EBP auditors to develop and perform a quality audit process and documentation. So, how do we find these firms that

**Exhibit 2. DOL Audit Quality Study
2011 Form 5500 Database
CPA Firms Performing
Plan Audits**

Number of Plans Audited	Number of CPA Firms	Number of Audits Performed
1-2	3,684	4,891
3-5	1,519	5,773
6-24	1,603	17,747
25-99	433	18,910
100-749	77	15,418
750+	14	18,423
Total	7,330	81,162

Exhibit 3. Six-Point Audit Quality Focus



perform five or fewer audits to offer them resources? In Virginia, it began with all the stakeholders at the highest level: the DOL, NASBA, VBOA, AICPA, and the VSCPA. These regulators, educators, and advocates of quality EBP audits came together by invitation only to those firms who perform EBP audits in Virginia. This town hall was the first of its kind, and was held in July 2015, two months following the issuance of the DOL Audit Quality Study. The town hall was the brainstorm of CPAs in Georgia, California, Texas, and Arizona, all EBP CPAs who work hard to keep quality in their EBP audit work.

Grassroots Collaboration

One resource that had not been offered in the past was this grassroots idea of CPAs being personal, live resources to firms that do not perform many EBP audits. Collaboration allows those CPAs who have a specialty area to offer that expertise to others who need help.

Sometimes the collaboration develops into a strategic partnership, other times an ongoing pre-issuance inspection or pre-audit review; sometimes, consulting. Personal, live interaction and problem solving is more fun and relevant to competency-based learning and is a great complement to the other AICPA and technical resources that are available, thanks to many AICPA member volunteers. Countless CPA volunteer hours have been dedicated since 2004 and the AICPA Employee Benefit Plan Audit Quality Center (EBPAQC) has grown substantially since its inception. Although most resources are only available to members, there is a public part of the EBPAQC where plan sponsors can access resources and tools.

In order to bring new and personal audit quality resources to CPAs performing these audits, the VBOA partnered (along with the DOL, NASBA, and the AICPA) with the Virginia Society of CPAs (VSCPA) in its efforts to work closely with the AICPA and other state and national accounting organizations on a profession-wide audit quality initiative. This partnership resulted in VSCPA-led EBP Audit Quality town halls at various locations in Virginia in 2015, and has spawned collaboration efforts by CPAs in other states as well. In Virginia, the collaborations have been free of charge. They have been led by EBP auditors and the VBOA, assisted by the AICPA and EBP peer reviewers. The DOL, NASBA, and the AICPA also kicked off the first town hall, which can be found on the VSCPA website and is a resource listed at the end of this article.

In these meetings, participants were provided with tax and audit compliance resources for EBP auditors and honest dialog ensued at each. Each of these presentations was followed by a panel discussion of CPAs who are willing to be expert resources to firms that may not perform many EBP audits. This open conversation, in my opinion, is the key to future success—CPA-to-CPA collaboration in our quest to enhance competency. These forums also have provided all firms with information about enforcement by the BOA, as the vast majority of firms have never focused on that process. The participation also has opened the dialog to understanding roles and responsibilities.

So, how do you help EBP firms come to lunch, to hear about resources they think they have always had available to them, and to understand the value of collaboration? The answer: You ask the regulator to invite them. After all, they are all free of charge. In Virginia, the BOA has been in the forefront, seeking to educate first about the audit quality deficiencies, as well as the licensing and enforcement initiatives. The BOA will continue to be in the forefront to enforce quality as may be needed and will likely continue to educate along the way.

DOL Recommendations

In addition to increased outreach to CPAs and enforcement of audit standards by EBSA, the DOL report proposes legislative fixes. It recommends that Congress amend the Employee Retirement Income Security Act (ERISA) definition of “qualified public accountant” to include additional requirements and qualifications necessary to ensure the quality of plan audits.

The DOL report also urges Congress to repeal the ERISA limited scope audit exemption and give the DOL the authority to define when a limited scope audit would be an acceptable substitute for a full scope audit. As the limited scope audit exemption is commonly considered by CPAs to undermine and impose hindrances to a complete opinion, the CPA profession historically has been supportive of repealing the exemption. The DOL study mainly reviewed limited scope audits. (See Exhibit 4.)

Similar to their past audit quality studies, the DOL found a correlation between the size of a firm’s EBP practice and deficient audit work. Nearly 75 percent of plan audits were deficient in firms that audit one or two plans annually. Deficient audits in this stratum also had a greater number of deficiencies. It was also discovered that there was less EBP-specific training

Exhibit 4. DOL Sample by Type

- Type of Audit
 - 80% = Limited Scope
 - 19% = Full Scope
 - 1% = Other
- Plan Type
 - 89% = DC Pension Plan
 - 6% = DB Pension Plan
 - 5% = Welfare Plan
- Sponsor Type
 - 95% = Single Employer
 - 3% = Multi-Employer
 - 2% = Multiple Employer
- EBPAQC Member
 - 55% = Yes
 - 45% = No

by firms in that stratum. In response, the DOL has stepped up its public website to include educational materials about fiduciary responsibility for plan sponsors in hiring the auditor, the work of the auditor, and internal controls for plan administration and operation.

This deficient stratum is the “sweet spot” for Collaborator Champion efforts. It also is the place where it is hard to reach these firms; they do not understand the issue, since their audit was limited scope and they believed that the standards they used for the audit were in accordance with generally accepted audit standards. In other words, some CPA firms that audit so few EBPs do not know what they do not know, so do not diagnose themselves as being in need of assistance. The emphasis here is not the size of the firm, as large firms also can have offices that do few EBP audits. The deficiencies appear tied to firms that do not perform audits as a large part of their practice or perform few EBP audits.

DOL Plan Sponsor Outreach

The DOL also sent an email to each plan sponsor that hires an EBP auditor. The email was intended to remind them of their responsibility:

Employee benefit plan audits have unique audit and reporting requirements and are different from other financial audits. Care should be taken by the plan administrator

to select a CPA who possesses the requisite knowledge of plan audit requirements and expertise to perform the audit in accordance with professional auditing standards. To ascertain the qualifications of a CPA firm to perform your Plan's audit you might want to consider the following factors:

- The number of employee benefit plans the CPA audits each year, including the types of plans;
- The extent of specific annual training the CPA received in auditing plans;
- The status of the CPA's license with the applicable state board of accountancy;
- Whether the CPA has been the subject of any prior DOL findings or referrals, or has been referred to a state board of accountancy or the American Institute of CPAs for investigation; and
- Whether or not your CPA's employee benefit plan audit work has recently been reviewed by another CPA (this is called a “Peer Review”) and, if so whether such review resulted in negative findings.

To a plan sponsor reading this, there are some things that should be clarified. The number of plans an auditor completes is relevant, but there are two things to consider in that statement:

1. If the auditor completes only 24 audits, it will appear at first blush that the auditor will have one strike against it based on the DOL study. However, if the business for that auditor is health and welfare and/or pension audits, these 24 audits could constitute his or her entire business. As a result, this firm, which practices entirely in the EBP area and performs excellent auditing work, may by the raw numbers appear to be part of the less-qualified stratum.
2. If the firm completes 1,500 audits, the true issue for audit quality may be the question of who within the firm reviews the audits. There could be pockets of low number offices in a larger firm, with the result that, notwithstanding the size of the firm's overall EBP practice, the offices that do little EBP work may be experiencing a significant number of deficiencies.

Remember, it is not the size of the audit firm that is an indicator of quality; it is the number of EBP audits performed and the quality of the EBP practice in the firm that matters. The DOL has actively reviewed those Forms 5500 with audited financial

statements, trying to determine deficiencies and participate in education efforts. Also, please note that for some plans inspected as part of the 2015 Audit Quality Study, the DOL discovered deficiencies in EBP plan audits that had been subjected to peer reviews; therefore, having a clean peer review may not be a totally reliable indication of an EBP plan audit that would not be found deficient by the DOL.

The Profession's Response

In addition to augmenting the Six Points for Enhancing Audit Quality, the AICPA created competency-based testing and certificate programs. The heart of the matter and thought to be part of the solution, truly, is to get 100 percent of EBP firms to be members of the EBPAQC. There are specific EBP-related education and firm practice requirements for audit firms to become members in EBPAQC, and the DOL study showed that EBPAQC members performed better with fewer deficiencies than nonmembers. Membership in the EBPAQC is cited as a number one resource by all Collaborator Champions. The requirements are many, but the CPE provided and its vast audit and technical resources more than pays for its dues.

In addition to these tools, the AICPA is revamping its EBP peer review process and taking a harder look at competency and specialization for peer reviewers. As a CPA, peer review is the heart of professional practice and, just as with EBP auditors, peer reviewers have the same challenges of tax code and ERISA competency in addition to accounting standards when performing these audits.

Plan Sponsor Response

There are two excellent resources available to plan sponsors that want to perform due diligence on their plans' auditor:

1. "Selecting an Auditor for your Employee Benefit Plan," a publication from the DOL, <https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/publications/selectinganauditor.pdf>
2. "Obtaining Quality Employee Benefit Plan Audit Services: The Request for Proposal and Auditor Evaluation Process," a publication from the AICPA, https://www.aicpa.org/InterestAreas/EmployeeBenefitPlanAuditQuality/Resources/PlanSponsorResourceCenter/DownloadableDocuments/Plan_Sponsor_Guidelines_preparing_RFP.pdf

Plan sponsors should also attend an EBP conference at least once every two years to keep in touch with

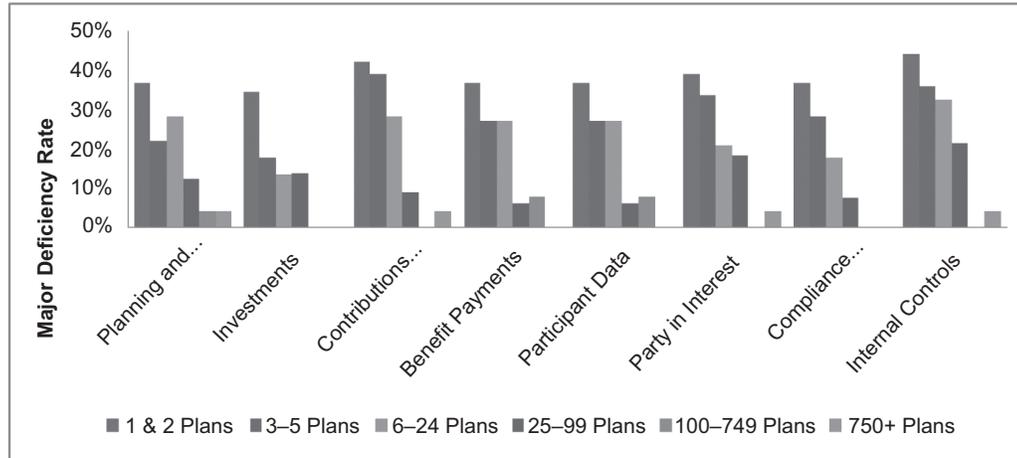
changing regulatory, audit, and tax environments. Each May, the AICPA hosts a national conference dedicated to audit and tax quality in the EBP area. Being in an observing space for this Audit Quality Study, with many years working with EBP auditors, I know how hard most EBP auditors work to keep their competence level up and also how difficult it is at times to make a professional judgment when there are so many areas in EBP law that lack definitive answers. And, I do not believe that professional judgment can be regulated.

I have seen the difficult questions with no answers. On the other side, I do not understand why essential documentation was not provided when necessary to perform a quality audit under generally accepted audit standards. Collaboration can help both these challenges. Finally, there is much confusion today—and plan sponsors are guilty here—about what should be done by an auditor in a limited scope audit. Even if you understood EBP audit standards, limited scope audits are a unique animal. It is not easy balancing what you need to do, pricing its time, and ensuring all the nuances are covered when tax code compliance is embedded in the audit standards, unlike with a standard financial audit. Regulations and a myriad of alternative investments cropping up to further confuse a sometimes too complex fair value standard makes EBP audits a very specialized area.

Plan sponsors bear some responsibility for audit quality (or lack thereof) by not taking the time to sit with auditors prior to the engagement and at the beginning of the audit to help gather and understand the data necessary for the auditor to do his/her work, and to value the work done by the auditor. Audits are often internally viewed as a "hassle," instead of a valuable delivery of good oversight to the plan operation. Often a plan sponsor will ask the same firm that does their financial statement audit to do the EBP audit, never considering the specialized nature of the EBP audit. It is more than just auditing standards. It is a completely different technical knowledge base. It is an ERISA fiduciary function to hire an EBP auditor—a standard that does not apply to a corporate financial statement audit.

With this collaboration, as part of this collaboration conversation, the CFO and controllers who have received these DOL emails should open the door to have a conversation with their auditors. It is part of the due diligence oversight that plan sponsors must have over all their service providers. This

Exhibit 5. Audit Areas With Most Deficiencies



is particularly true if the audit is highly specialized within the EBP area, such as when the plan is an employee stock ownership plan. Some plan sponsors put pressure on their audit firms to complete the EBP audit, even when a complex plan situation is involved, as part of the corporate audit because it is “just a limited scope audit.” The perception that an EBP audit is a throw-away (which is implied to some by the phrase “limited scope”) is not acceptable, never has been, and is one of the root causes for poor quality EBP audits. In short, some aspects of an EBP audit that are shown to be deficient are highly specialized fields of knowledge, each one of them requiring an expertise that goes beyond professional audit standards. Further, it is the decision of the plan administrator to elect a limited scope audit; the plan administrator can choose to engage a firm for a full scope audit. (See Exhibit 5.)

In working with the CPAs who have become Collaborator Champions, sharing knowledge and checklists, the limited scope audit seems to be a wild hair that has disrupted the auditor approach to auditing defined contribution plans. It has been misunderstood on all levels at the same time as these plans have been growing at exponential rates. Limited scope audits account for the majority of the deficient audit work. This is likely due to the lack of understanding by the auditor of the work that needs to be done, coupled with the industry-wide demand for lower fees. There is now a growing amount of resources to understand the behavior behind the deficient work, and clear choices in how to perform better audits. Getting the word out may be the only barrier to success. (See Exhibit 6.)

Exhibit 6. Additional Resources

- <http://www.dol.gov/ebsa/>
- <http://www.dol.gov/ebsa/pdf/2014AuditReport.pdf>
- <http://www.vscpa.com/DOLReport>
- <http://www.vscpa.com/DOLTownHallVideos>
- <http://tinyurl.com/EBPAQC>

Collaborator Champion Conversations

So, what is next for the collaboration conversation? In Virginia, Georgia, and California, where the grassroots of the collaborative conversations began in 2015, we expect lots of extra study and engagement opportunity. We also expect to see lots of personal resources and consulting services by CPAs who make EBP audits their primary or even exclusive area of practice. And, with an enhanced peer review program and additional competency-based learning by the AICPA, the profession is positioned to become stronger through individual professional confidence. Because these EBP auditors collaborated with their peers, the group is stronger as an EBP audit profession and likely the individuals can go the distance and demonstrate audit quality competence at an increased rate in 2017 and seek excellence together.

Statistical perfection for the next DOL inspection or audit quality study is a great goal, but professional judgment will always leave room for a difference of opinion on the minor interpretations that

an audit quality review may discover. What matters now is that the conversation has begun, we cannot look back, and we will use history as a guide only for what needs to be done moving into a new

collaboration space. As trusted advisors, CPAs will answer this call to action and will join together to renew and revise our commitment to audit quality with enthusiasm. ■