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NTSAA

February 17, 2011

Ms. Phyllis C. Borzi
Assistant Secretary/EBSA
US Department of Labor
200 Constitution Avenue, NW, Ste. S-2524
Washington, DC 20210

Re: Audits of 403(b) Plans for Form 5500s

Dear Ms. Borzi,

As you know, certain 403(b) plans were required for the first time to include an independent audit as part of the plan's 2009 plan year annual return ("Form 5500"). Unfortunately, numerous sponsors of 403(b) arrangements have had significant difficulties in filing compliant Form 5500s for the 2009 plan year. The American Society of Pension Professionals and Actuaries ("ASPPA") and the National Tax Sheltered Accounts Association ("NTSAA") have previously raised our concerns in a letter sent to the Department of Labor ("Department") on October 8, 2010 (the "October 8th letter"), a copy of which is attached for your convenience. Although for many plans the deadline to file has come and gone, our experience with this process and our suggestions for transitional relief are still relevant and needed as our members anticipate similar difficulties with future filings. This letter is intended to provide additional feedback on the subject as well as further recommendations for transitional relief.

ASPPA is a national organization of more than 7,500 members who provide consulting and administrative services for retirement plans covering millions of American workers. ASPPA's membership includes the members of the NTSAA, a nonprofit organization that recently became part of ASPPA in order to expand both organizations' strengths in serving the §403(b) marketplace. ASPPA and NTSAA members are retirement professionals of all disciplines, including consultants, investment professionals, administrators, actuaries, accountants and attorneys. Our large and broad-based membership gives ASPPA a unique insight into current practical applications of ERISA and qualified retirement plans, with a particular focus on the issues faced by small- to medium-sized employers. ASPPA's membership is diverse but united by a common dedication to the employer-sponsored retirement plan system.

Independent Audits

In our October 8th letter, we listed a number of problems that our members were experiencing with respect to the collection of the data necessary to complete 2009 Form 5500s. These data collection problems made preparation of the plan's financial statements more difficult. This resulted in much higher costs, particularly for those plans subject to an independent audit requirement. Our members have reported that 403(b) audits for the 2009 plan year cost

significantly more (as much as ten times more in some cases) than the cost to conduct an audit for a 401(k) plan of similar size. In a significant number of cases, the 2009 audit fees for 403(b) plans ranged upwards of $50,000, with reports that some plans were charged nearly $100,000.

The employers sponsoring these arrangements cannot sustain these costs. Money to cover expenses of this magnitude simply does not exist for most 403(b) plan sponsors who are tax-exempt charitable organizations. The economic downturn has resulted in reductions in donations and other funding sources to many of these organizations. Efforts to avoid layoffs and continue healthcare benefits have exhausted most personnel budgets, despite a strong desire to provide a tax-qualified retirement savings program.

Although there are some steps a plan sponsor can take to attempt to reduce these auditing costs, most are either impractical or ineffective. For example, a specific investment provider might be unable to provide the appropriate certification to qualify for the limited scope audit provisions of ERISA Regulation §2520.103-8. The plan sponsor might try to reduce future auditing costs by eliminating or reducing the providers who are unable to provide the necessary certification to qualify for a limited scope audit. In the 403(b) market, however, this is not practical. For example, many investment providers issue individual contracts to participants in 403(b) plans where, under state law, all contractual rights are exercisable only by the participant. In other words, under the terms of the contracts, the plan fiduciary has no authority to direct the participant to transfer the funds to another provider, or to otherwise surrender the contract. In effect, the plan is "stuck" with the contract unless the participant takes action. Although the relief provided by the Department in 2009 and 2010 was intended to address these problems, unfortunately it has not been embraced by the majority of auditors who still seek confirmation with respect to assets that could otherwise be excluded under the transitional relief. As a result, 403(b) plan audit costs have skyrocketed.

Request for Additional Transitional Relief and Alternative Reporting

The new enhanced 2009 reporting obligations for 403(b) plans have presented challenges similar to those faced by plan sponsors when ERISA was enacted. At that time, the Department recognized the problems plan sponsors would have in determining opening balances for the initial independent audit. The Department provided relief using its authority under ERISA § 110. In particular, the Department issued ERISA Regulation § 2520.103-7, which relieved plans for their initial reporting year from the obligation to:

- Display at current value, the statement of assets and liabilities of the plan, as of the end of the previous year;

- Engage an independent qualified public accountant to conduct an examination of the plan's financial statements for the plan year or trust year covered by the initial annual report; and

- Include with the initial annual report, the opinion of an independent qualified public accountant as to whether the financial statements for the close of the initial plan year are presented on a basis consistent with that of the preceding year.

In addition, under the authority of ERISA Regulation § 2520.104–44, the Department provided relief specific to 403(b) plan sponsors, excusing them from most reporting requirements related to the Form 5500, including the obligation to include a financial statement with the opinion of a qualified independent auditor.

We believe the transitional problems faced by 403(b) plan sponsors in complying with the new reporting rules are every bit as daunting as those present when ERISA was enacted. Consistent with the relief provided at that time, we request that the Department exercise its authority under ERISA § 110 in two ways.

Opening Balance Relief **- ASPPA and NTSAA recommend** that a rule be developed under which the auditor of the financial statements of a 403(b) plan can rely upon an employer's documented good faith effort, whether successful or not, to identify and compile an opening balance for the 2009 and 2010 plan years, and that an auditor's opinion will only be required for financial activity for the current year assuming a correct opening balance.

Disclaimed Audit Relief. All of a 403(b) ERISA plan's assets (except for electing church plans) are required to be held in regulated financial institutions. These institutions are eligible to certify to the accuracy of the data they provide under ERISA Regulation § 2520.103-8. Because of the extent of such certification, auditors are often unable to issue an opinion as to the financial statement as a whole. This results in the plan paying unreasonable costs for an opinion which states that no opinion can be given. This, in turn, provides fiduciaries, the Department and plan participants with little or no useful information with which to fulfill important ERISA obligations or enforce rights. A real life example reported by one of our members involved a plan with 2,000 participants where there were two active vendors in the plan and five deselected vendors. One of the deselected vendors, which held the contributions for only 5 of the 2,000 participants, received a single contribution in January of 2009, which resulted in the contributions held by the deselected vendor having to be included the 2009 Form 5500 financial statements. Since this deselected vendor would not sign a certification, the entire plan was subject to a full-scope audit. Until the 5 participants move from those investments, this plan will unfortunately continue to be subject to the requirement of a full scope audit.

Similarly, auditors will often attempt to conduct full scope audits because of their lack of familiarity with 403(b), and some investment vendors will not offer the limited scope certification. Because of the highly regulated nature of the institutions holding 403(b) funds, little is accomplished by these expensive attempts at a full scope audit, even where there is no certification. These efforts are of little use, as the controls of such institutions are well outside of the employer's control and the potential for sponsor abuse is virtually non-existent.

ASPPA and NTSAA recommend that a rule be developed to ensure that the audit will provide useful information to the fiduciaries, Department and participants, while substantially reducing expenses. We propose that, where an auditor will not be able to issue an opinion because of the application of the limited scope exemption, or where a limited scope cannot be formed because of the lack of a vendor certification, that the plan, in the alternative, can engage the auditor to opine on the business controls of the plan sponsor in handling the assets or other financial matters of the plan within the control of the sponsor.

Assist in the Development of an Auditing Checklist for 403(b) Plans

The current relief offered under Field Assistance Bulletins ("FABs") 2009-02 and 2010-01 is not providing the benefits anticipated because the auditing community has generally not accepted the information on which the 2009 plan year starting account balances were established. As a result, we believe that standards of practice for auditing 403(b) plans need to be developed by the Department.

ASPPA and NTSAA recommend that a committee of industry experts be established to suggest, review and modify the existing audit guidelines for 403(b) plans. The committee should specifically consider:

- The differences between group annuities, individual contracts, and individual custodial agreements and the potential for different audit requirements for each;

- The need for relief and clarification that beginning balances as of January 1, 2009, are absolute for all purposes under applicable auditing standards, and that auditors may modify their standard procedures and accept data provided as of January 1, 2010;

- Creation of a model "Audit Checklist" for 403(b) plans that is specific to 403(b)s and does not contain qualified plan requirements; and

- Better coordination between the Department's rules and the Internal Revenue Service compliance rules by creating educational communications and training materials specifically focusing on 403(b) plans for employers, vendors, auditors and administrators.

ASPPA and NTSAA further recommend that the Department use its regulatory authority to establish specific auditing standards under ERISA for 403(b) plans that:

- Consider the existing regulatory requirements of the issuers of 403(b) annuity and custodial account products;

- Audit the plan at the employer level rather than at the financial institution level, taking into account the internal controls of the employer in lieu of the financial institutions; and

- Establish an absolute starting date for contracts/accounts to be included under the plan for ERISA enforcement purposes and direct auditors to disregard balances and transactions that predate the specified date.

Any such standard must take into account the differences between group annuities, individual annuities and custodial accounts. For individual contracts, for example, the employer has no legal control or authority over such contracts. The contracts are subject to other substantial state and federal laws protecting both the plan and the participants. There is minimal need for protection from employer malfeasance as the employer has no ability to access, control or otherwise interfere with the individual contracts under these laws. Only the participant or beneficiary has direct enforcement rights under the contract and under state and federal laws.

These comments were prepared by the ASPPA/NTSAA Task Force on 403(b) Audits chaired by Susan Diehl with input from Tax-Exempt/Governmental Plans Subcommittee of the ASPPA Government Affairs Committee. We welcome the opportunity to discuss these issues with you. If you have any questions regarding the matters discussed herein, please contact Craig Hoffman, General Counsel and Director of Regulatory Affairs at (703) 516-9300.

Thank you for your consideration.

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Comment Letter Submitted by ASPPA and NTSAA
to the Department of Labor on October 8, 2010

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NTSAA

October 8, 2010

Mr. John J. Canary
Deputy Director of Regulations and Interpretations
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Re: Relief for 403(b) arrangements

Dear Joe,

ASPPA appreciated the opportunity to speak with you and your staff this week to follow-up on our earlier discussions regarding potential transitional relief for certain 403(b) arrangements that may have inadvertently become subject to ERISA coverage. In addition, thank you for allowing us to raise the current challenges being faced by ERISA plans attempting to file compliant Form 5500s on a timely basis. This letter is intended to provide further input relevant to both of these topics.

ASPPA is a national organization of more than 7,300 members who provide consulting and administrative services for retirement plans covering millions of American workers. ASPPA's membership includes the members of the National Tax Sheltered Accounts Association ("NTSAA"), a nonprofit organization that recently became part of ASPPA in order to expand both organizations' strengths in serving the §403(b) marketplace. ASPPA and NTSAA members are retirement professionals of all disciplines, including consultants, investment professionals, administrators, actuaries, accountants and attorneys. Our large and broad-based membership gives ASPPA a unique insight into current practical applications of ERISA and qualified retirement plans, with a particular focus on the issues faced by small- to medium-sized employers. ASPPA's membership is diverse but united by a common dedication to the employer-sponsored retirement plan system.

<u>Form 5500s and Audits</u>

The most time sensitive topic on which we would like to provide further input relates to the problems we are seeing with respect to the filing of 2009 5500 Forms and the associated independent audits that are required for large plans. Our members are reporting that a number of problems have been uncovered as the data collection process has unfolded. The problems relate to the following:

A. Additional investment providers (vendors) are being uncovered that were not anticipated as the process began. This not only complicates data collection but delays the completion of the associated independent audit. One example of this occurrence is when the "vendor" is a broker-dealer and an underlying investment company is identified during the data collection process that previously was undisclosed.
B. Vendors were not required to maintain extensive data that could be easily correlated prior to the final 403(b) regulations being issued. Some do not currently, and have not in the past, maintained the source data which in some cases goes back 40 years or more. Vendors, recordkeepers, and administrators are building the files to accommodate the tracking and delivery of this data, but time is running out. Since 2007, many providers in this industry have spent billions of dollars to address these issues, and some progress has been made, but most still need time to be able to produce accurate reports and data which will ensure that the audits will be accurate.
C. We have heard from many plan sponsors and their advisors that in order to avoid penalties "something" will be filed and later amended. But most of the reports will need to be filed late, resulting in additional cost to these employers.
D. Due to many factors, another problem is the lack of understanding by various service providers of how 403(b) plans differ markedly from 401(k) plans. In 2007, many plan sponsors first realized that plan documents were needed; vendors were required to share data; and interaction with an auditor was necessary.
E. Reports from the vendors do not reconcile, and the time frame to compose the revised data and prepare a new report is a minimum of 10 or more days.
F. It is difficult to reach a responsible individual in a large company that truly understands the audit process and the information needed to conduct an audit.
G. In many cases, these problems were not anticipated and there is insufficient allocation of resources within the vendors themselves to meet the filing deadline.

ASPPA recommends the following potential options to serve as transitional relief to ameliorate the current audit situation for the short term as well as the long term:

1. In the short term, Form 5500s and the associated audits are due in one week. It is our opinion that the only option that will work at this late date is a transitional rule that would provide additional time for new procedures to be instituted. The additional time will also serve to educate plan sponsors, administrators, auditors, and investment companies about the unique audit requirements for 403(b) plans and the type of information that needs to be gathered for the audit and completion of the Form 5500. The Department of Labor can use this delay to gather information to come up with a viable solution that will ensure the protection of participants and beneficiaries. We believe that a one (1) year transitional relief period should be enough time to prepare an alternative audit methodology. The Department should also consider some kind of modified criteria (to be determined by a committee of industry experts as described in #4 below) for the collection of

the data needed since many vendors do not presently have the data readily available that is required for audits.

2. An alternative (in lieu of a blanket extension) would be to permit the incomplete filings to occur and grant waivers of any late or incomplete filing penalties for plans that have made a "good faith effort" to collect data. The 5500 help line is suggesting plan sponsors file in this way, but only those plan sponsors that have actually called the help line are aware of this suggestion.

3. On a long term basis, the definition of "active participant" for 403(b) plans should be changed to "eligible employees that make or receive a contribution during the plan year," rather the 401(k) definition currently in use. This would recognize the significant effect the "universal availability" requirement (that only applies to 403(b) plans) has on the independent audit requirement under ERISA. Many more 403(b) plans would qualify for the small plan exception from audits than under current rules. This would help to alleviate many concerns.

4. Also in the long term, we believe a committee of industry experts should be set up to suggest, review and modify the existing audit guidelines for 403(b)s taking the following into consideration:

    a. The differences between group annuities, individual contracts, and individual custodial agreement and potentially set up different audit requirements for each;
    b. Specific clarification that beginning balances as of 1/1/2009 are absolute for all purposes, and relief to auditors so that they may modify their standard procedures and accept data provided as of 1/1/2010;
    c. Produce a model "Audit Checklist" for 403(b) Plans that is specific to 403(b)s and does not contain qualified plan requirements;
    d. Coordinate the DOL rules with the IRS compliance rules by creating educational communications and training materials specifically focusing on 403(b) plans for employers, vendors, auditors and administrators.

5. Finally, if any relief is to be provided for 2009 plan year filings, an announcement needs to be issued as soon as possible in order to avoid unnecessary expenses caused by the difficulties we have described.

<u>ERISA Exemption-Transitional Relief</u>

We understand and respect the challenges that the Department faces in offering additional guidance and relief beyond that provided by the previously issued Field Assistance Bulletins (FABs). However, we respectfully request that the Department consider our previous comments issued in this regard. We continue to believe that there should be relief for the small 501(c)(3) employers who cannot afford to maintain ERISA 403(b) arrangements if subjected to regulation under ERISA.

The presence of other marketplace legacy issues complicate the availability of the "safe harbor" exemption from ERISA coverage found in ERISA Regulation §2510.3-2(f). Some employers have considered moving in the direction of a single vendor so as to avoid the tax code compliance problems associated with multiple vendors, but then realize that it could subject them to ERISA coverage. Others have tried to meet their compliance responsibilities by utilizing services of a third party administrator only to be advised that under the "clarification" of FAB 2010-01, a similar result occurs.

403(b) plans were originally intended to be simple, payroll based savings plans for public schools and certain non-profit organizations exempt from the expense associated with burdensome regulation. As we stated in our previous letters and testimony to the ERISA Advisory Council, we believe the unintended result for small employers will be plan terminations. Unfortunately, this will be necessary in order for smaller non-profits and charities to survive in these challenging economic conditions.

We would be happy to address any questions you may have and also be prepared to participate in any additional committees or assist in any way we can with input, training and educational materials, and/or assistance in developing alternative reporting models.

These comments were prepared by ASPPA's Tax Exempt and Governmental Plans Sub-committee of the Government Affairs Committee, Robert Toth, APM Chair. Please contact Craig Hoffman, General Counsel and Director of Regulatory Affairs at ASPPA, at (703) 516-9300 ext. 128, if you have any comments or questions regarding the matters discussed above. Thank you for your consideration of this request.

Sincerely,

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