

Limited Scope Audits

of Employee Benefit Plans

The AICPA EBPAQC is a firm-based, volunteer membership center created with the goal of promoting quality employee benefit plan audits. Center members demonstrate their commitment to ERISA audit quality by joining and agreeing to adhere to the center's membership requirements. EBPAQC member firms receive valuable ERISA audit and firm best practice tools and resources that are not available from any other source.

Visit the center website (aicpa.org/EBPAQC) to see a list of EBPAQC member firms and find other valuable tools prepared for plan sponsors and other stakeholders. For more information, contact the EBPAQC at ebpaqc@aicpa.org.

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Introduction

The AICPA Employee Benefit Plan Audit Quality Center (EBPAQC) prepared this advisory to provide you, the plan sponsor, administrator or trustee, with an understanding of limited scope audits of employee benefit plans under the Employee Retirement Income Security Act of 1974 (ERISA).

Generally, ERISA requires employee benefit plans with 100 or more participants to have an audit as part of their obligation to file an annual return/report (Form 5500 Series). If your employee benefit plan is required to have an audit, in certain circumstances described in this advisory, you have the option to instruct the auditor not to perform any auditing procedures with respect to investment information. This option commonly is referred to as a “limited scope audit.”

This advisory describes the statutory and regulatory basis for the limited scope audit exemption, which institutions are qualified to issue a limited scope certification, what constitutes a proper certification from a qualified institution, the plan administrator’s responsibilities for determining the acceptability of a limited scope certification, the auditor’s responsibilities for determining whether a certification can be relied upon to limit the scope of the audit, the limited scope audit in the current environment, the effect of the limited scope audit exemption on the scope of the independent auditor’s testing and reporting, and common deficiencies in limited scope certifications. It also includes an example limited scope certification. The sponsor of the plan is the plan administrator under the law unless another individual or entity is specifically designated to assume this responsibility. The term plan administrator as used throughout this document refers to the party that is the plan administrator, including a plan sponsor, third-party administrator or trustee.

Statutory and Regulatory Basis

In 1974, Congress enacted ERISA to help protect retirement benefits for workers who participate in private pension plans. In addition to establishing minimum standards for benefit accrual, funding and vesting, ERISA section 103(a)(3) required an independent qualified public accountant to audit certain employee benefit plans. However, ERISA section 103(a)(3)(C) allows the plan administrator to instruct the auditor not to perform any auditing procedures with respect to investment information prepared and certified by a bank or similar institution or by an insurance carrier that is regulated, supervised, and subject to periodic examination by a state or federal agency, that acts as trustee or custodian (referred to as “qualified institutions”).

The U.S. Department of Labor (DOL) administers and enforces ERISA’s independent audit requirements. The DOL issued implementing regulations in 29 CFR 2520.103-8 — *Limitation on scope of accountant’s examination*, which established regulatory requirements to meet the limited scope audit exemption.

The U.S. Securities and Exchange Commission (SEC) does not permit limited scope audits to be included with Form 11-K filings with the SEC under the Securities Exchange Act of 1934.

Qualified Institutions

Only qualified institutions can certify investment information for the purpose of limiting the scope of an employee benefit plan audit. The DOL established requirements for qualifying institutions to certify information to the plan administrator in 29 CFR 2520.103–5 — *Transmittal and certification of information to plan administrator for annual reporting purposes*. Under DOL regulations, investments held by a bank, trust company, or similar institution or by an insurance company that is regulated and subject to periodic examination by a state or Federal agency, and related information do not have to be audited, provided the plan administrator instructs the plan’s independent auditor to perform a limited scope audit and the institution holding the assets certifies the required information.

In an Advisory Opinion to PaineWebber Inc. dated Aug. 3, 1993, the DOL clarified that an institution must be subjected to routine examinations by a state or Federal agency in order to be considered a qualifying institution for purposes of certifying investment information and, as such, an institution that is not regulated would not qualify:

“Inasmuch as securities brokerage firms are not regulated, supervised and subject to periodic examination by a state or Federal agency, it is the Department’s position that the term ‘similar institution,’ as used in 29 C.F.R. § 2520.103–8, does not extend to such entities.”

Although brokerage firms and investment companies generally would not meet the eligibility requirements for certifying information under the limited scope audit exemption, some of those institutions may have established separate trust companies that could meet the requirements to be a qualified institution.

Proper Certifications

To meet the requirements for the limited scope audit exemption, the qualified institution must certify both the completeness and accuracy of the required information, and the certification must be signed, manually or electronically, by a person authorized to represent the institution. 29 CFR 2520.103-5 provides the following sample certification language for the certifying institution:

The XYZ Bank (Insurance Carrier) hereby certifies that the foregoing statement furnished pursuant to 29 CFR 2520.103-5(c) is complete and accurate.

Certifications that only state the information is either accurate or complete, but not both, or are not signed by an authorized individual, do not meet the DOL requirements for a proper certification.

In situations where a limited scope audit is to be performed on a plan funded under a master trust arrangement or other similar vehicle, the plan administrator would need to obtain separate individual plan certifications from the trustee or the custodian for the allocation of the assets and the related income activity specific to the plan.

In some cases, the trustee or custodian may not certify all of the plan's investment information. For example, the trustee or custodian may exclude investments from the certification, or plan management may change trustees or custodians during the plan year so each trustee or custodian held the assets for part of the year, and only one of the trustees or custodians will certify investment information for part of the year.

The Plan Administrator's Responsibilities for Determining the Acceptability of a Limited Scope Certification

Only the plan administrator can request the plan auditor to limit the scope of the audit when all requirements are met. The plan administrator is responsible for determining that the conditions of the limited scope audit exemption have been met. The DOL reinforced this position in a letter addressed to the AICPA in 2002:

"Consistent with the obligation of employee benefit plan administrators to file complete and accurate annual reports, it is the responsibility of the administrator to determine whether the conditions for limiting the scope of an accountant's examination, as set forth in ERISA and the department's regulations, have been satisfied."

The plan administrator's responsibility for the plan's financial statements includes determining that the certification is from a qualified institution and signed by an authorized person, and that the investment information is certified as both complete and accurate.

Plan administrators should take steps to make sure they understand the nature and scope of the certification the institution has provided before concluding that the certified information may be used to satisfy the administrator's obligation to report the current value of the assets on the plan's annual report (Form 5500 Series) and in the plan's financial statements. The DOL observed that if there is a question as to whether a party providing a certification as an authorized representative of a financial institution holding plan assets is in fact authorized to represent the financial entity for this purpose, as may be the case where there is not an explicit statement of authority included as part of the certification, the plan administrator must take steps to resolve this question before authorizing limited scope reporting.

As part of its fiduciary duties, the plan administrator is responsible for determining whether the financial statements and note disclosures related to investment information are prepared in accordance with GAAP and in compliance with DOL rules and regulations. In situations where the plan administrator becomes aware that adequate year-end valuation procedures have not been performed, and, therefore, the financial statements may not be prepared in accordance with GAAP, the plan administrator may request the qualified certifying institution to recertify or amend the certification for such investments at their appropriate year-end values, or to exclude such investments from the certification. If the trustee or custodian amends the certification to exclude such investments from the certification, the plan administrator is responsible for determining the fair values of such investments as of the plan year-end and engaging the auditor to perform full-scope audit procedures on the investments excluded from the certification. If the certification is not amended, it is the plan administrator's responsibility to determine whether the financial statements and note disclosures related to such investment information are prepared in accordance with DOL rules and regulations and generally accepted accounting principles (GAAP).

The Auditor's Responsibilities for Determining Whether a Certification Can Be Relied Upon to Limit the Scope of the Audit

The AICPA Audit and Accounting Guide, *Employee Benefit Plans* (Guide), establishes certain responsibilities the auditor has related to determining whether the certification can be relied upon to limit the scope of the audit as permitted by ERISA section 103(a)(3)(C), including obtaining and reading a copy of the certification from the plan administrator, and determining whether the entity issuing the certification is a qualifying institution under DOL regulations. The AICPA Audit Guide also notes that although the auditor has no responsibility to test the accuracy or completeness of the investment information certified by the qualifying institution, if the auditor becomes aware that the certified information is incomplete, inaccurate or otherwise unsatisfactory, further inquiry may be necessary, which might result in additional testing or modification to the auditor's report. In certain instances, a limited scope audit may no longer be appropriate. If, for example, the auditor becomes aware that adequate year-end valuation procedures have not been performed and, therefore, the financial statements may not be prepared in accordance with GAAP, it is important for the auditor to communicate those findings to the plan administrator.

The Effect on the Audit Scope and Testing

When the plan administrator instructs the auditor to perform a limited scope audit, the auditor has no responsibility to test the accuracy or completeness of the investment information certified by the plan's trustee or custodian, obtain an understanding of internal control maintained by the certifying institution over investments held and investment transactions executed for the plan, or assess control risk associated with assets held and transactions executed by the institution. As such, the auditor would not need to obtain or review a SOC 1 report from the plan's certifying trustee or custodian relating to the certified investments.

The limited scope exemption applies only to the investment information certified to by the qualified certifying institution and does not extend to:

- Participant data
- Contributions
- Benefit payments
- Required financial statement disclosures
- Other information, regardless of whether it is included in the certified information
- Plan investments held by the certifying institution or investment income information that are not specifically included in the certification
- Plan investments not held by a qualified institution, such as real estate, leases and mortgages
- Self-directed brokerage accounts or participant loans that are not held by the qualified institution


Plan investments not held by a qualified trustee or custodian and any other investment or investment information not covered by the certification, including investment elections and income allocations to participant accounts, should be subjected to appropriate audit procedures. This means that the independent auditor will perform audit testing — including understanding and documenting internal controls and assessing risks — on the non-investment activity of the plan, such as participant eligibility; employee and employer contributions; benefit payments; and plan administrative expenses. In addition, amounts the certifying institution reports as being received from, and disbursed at the direction of, plan management or other authorized parties are subject to audit procedures to evaluate whether such transactions have been properly determined in accordance with the terms of the plan and that the information included in the financial statements and supplemental schedules has been presented in compliance with the DOL's rules and regulations. The Guide describes the independent auditor's responsibilities in a limited scope audit.

Loans to participants in defined contribution plans (i.e., notes receivable from participants) are not considered investments for financial reporting purposes, but sometimes the limited scope certification extends to such loans. Because the Form 5500, *Annual Return/Report of Employee Benefit Plan* requires that loans to participants be presented as plan investments, the auditor may limit the scope of testing with regard to loans to participants the certification covers if they are held by a qualified institution. However, in such cases, the amounts received or distributed still would be subject to audit procedures to evaluate whether they were determined in accordance with the plan's provisions, as discussed above. A limited scope audit restricts testing of certified investment information, but audit procedures need to be performed on other non-investment information.

Limited Scope Audits in the Current Environment

When ERISA established the limited scope audit exemption in 1974, the majority of plan investments were held in common stocks, mutual funds, bonds and other instruments that were either directly held by the plan, or held in trust or custodial accounts at banks, insurance companies or similar institutions regulated by a Federal or state agency. Since ERISA was enacted, many plans have shifted their investments into more complex, hard-to-value investments, such as limited partnerships, private equity funds and hedge funds. In today's environment, such investments are not necessarily held directly but rather may be held in a multi-layered investment, such as a fund of funds, or as a piece of an original investment such as a derivative, thus making them more difficult to identify and value.

Because many plan custodians or trustees do not provide valuation services for their plan clients, the amounts the institution certifies may not represent the appropriate values of these hard-to-value investments for financial statement and Form 5500 reporting purposes. The contract with the trustee or custodian will indicate what information the plan sponsor receives. The typical custodial service trustees and custodians provide includes values that are based on the best information available to them at the time the statements are produced. If the plan is invested solely in assets with readily determinable fair values, such as exchange traded securities, the trustee or custodian typically obtains fair values from nationally recognized pricing services. However, in cases where the plan invests in other types of assets, and where the trustee or custodian may have been engaged only to provide custodial services, the values in the trust statement may be a pass-through of the values provided by the fund issuer or general partner, or by a boutique vendor or broker for nonmarketable securities. In those cases, the reported values are based on the best information available to the trustee and custodian at the time the trustee or custodial report is prepared, which may or may not be the appropriate values for financial statement and Form 5500 reporting purposes as of the plan's year end.



In addition to the increased complexity in plan investments, plan structures also have become much more complex. And as discussed in the “Proper Certifications” section on page 5, there are reasons why some assets may not be covered by a certification at all. As such, it is important that plan administrators evaluate whether these limited scope audit exemptions continue to make sense for their plan audits.

The Auditor’s Report

An independent auditor performing a limited scope audit generally would be unable to express an opinion on the financial statements and supplemental schedules taken as a whole due to the significant limitation on the scope of the audit. The Guide provides example auditor’s reports for limited scope audits where the auditor believes the plan administrator’s restriction on the auditor’s examination to be a significant limitation on the scope of the audit.

Common Deficiencies in Limited Scope Certifications

No Certification or Incomplete Certification

- The plan administrator instructs the auditor to perform a limited scope audit but does not obtain a certification from the qualified certifying institution.
- The plan changed custodians during the year, and neither entity certified the investment information. For example, the Plan used Entity X during the 20X5 plan year, but changed to Entity Y on 12/31/X5. Neither Entity X nor Entity Y certified to the assets; for administrative ease, the statements of Entity X showed the assets as liquidated and certified as a zero balance at 12/31/X5. Entity Y did not receive the assets until 1/9/X6, so appropriately could not certify as being held by Entity Y at 12/31/X5.
- The plan changed custodians during the year, and only received a certification from one of the custodians.

Omissions and Errors in the Certification

- The certification does not include the plan name.
- The certification is not attached to plan investment information, so it's not clear what information is certified.
- The qualified certifying institution certifies to either the completeness or accuracy of the investment information, but not both.
- The certification is not signed.
- The certification is signed by an individual who is not authorized to represent the qualified institution.
- The certification(s) do not cover the entire period under audit.
- The certification does not cover the stated period (for example, the plan was terminated during the year on 6/30/X6 but the certification states that it is as of and for the period ended 12/31/X6).
- The certification does not include all investments (for example, it covers separate account assets but does not cover general account assets).

- The certification is issued by an entity other than a qualified institution (for example, a record-keeper that is not a bank, trust company, or insurance company) or similar institution, and is not acting as an agent for a qualified institution (for example, brokerage arms of certain banks/providers or investment companies).
- Qualifying language that conflicts with the assertion that certified information is accurate and complete (for example, a certification containing the following disclaimer language may impair the usefulness of the certification: “Values reflected for publicly traded assets are from unaffiliated financial industry sources believed to be reliable. Values for non-publicly traded assets may be determined from other unaffiliated sources. Assets for which a current value is unavailable and may be reflected at the last reported price, at par, or may be shown as having nominal or no value. Reported values may not be the price at which an asset may be sold. Asset values are updated as pricing becomes available from external sources, and may be updated less frequently than statements are generated.”)

Information Improperly Certified

- Plan investments are certified by two custodians when only one of them held the assets.
- The incorrect entity certifies the plan’s investment information. This can happen when plans change custodians/trustees or merge with another plan. For example, Plan A merged into Plan B on 1/5/X6, and the transfer of Plan A’s assets occurred on 1/15/X6. Prior to the merger, Entity A was custodian for Plan A, and Entity B was custodian for Plan B; Entity B is the custodian for the merged Plan B. Entity B “backdated” the merger transaction to 12/31/X5 for a smooth transition on record-keeping and certified all investment information, even though the processing and actual receipt of Plan A’s assets had not yet occurred, and Entity A still held those assets.
- The certified statements include assets that are held by a separate custodian.

Incorrect/Improper Information Certified

- The entity certifies current year ESOP units and activity, but the shares are certified at prior year values.
- Plan investments are improperly categorized in the certification (for example, the plan invests in a hedge fund that is listed in the certification as mutual funds).
- The certification includes investments purchased after year-end. For example, the certifying entity bought investments on 12/31/X5 related to payroll deferrals that were made and transmitted on 1/1/X6, before they received the cash, and included them in the 12/31/X5 certification.
- The certified statements list the incorrect asset value due to errors in cutoff. For example, a plan purchases assets on 12/30/X5 (trade date) but the entity certifies the asset value is zero assuming the transaction will take two (2) days to settle, but the actual settlement date was 12/31/X5.
- The certified trust statements include contribution and investment activity from the next period, indicating poor cutoff.

Example Limited Scope Certification

Limited Scope Certification	
Example limited scope certification that complies with the requirements of 29CFR 2520.103-5c.	
What to look for ...	
✓	Prepared by a qualified institution (or authorized agent)
✓	Specifies the plan name
✓	Attached to (or included with) the plan investment information being certified
✓	Covers the entire period under audit
✓	The institution certifies to <i>both</i> the completeness and accuracy of the investment information (no caveats or other qualifying language)
✓	Signed by an authorized representative of the qualified institution

ABC Institution [letterhead]

Re: XYZ Profit Sharing and 401(k) Plan And Trust

Enclosed are the certified Trust Statements for the above referenced Plan(s) for the following periods:

- Certified Trust Statement covering the annual period through 10/31/X5 and
- Certified Trust Statement beginning 11/01/X5 through the end of the reporting period

ABC National Bank hereby certifies that the information furnished pursuant to 29CFR2520.103-5c is complete and accurate.

Please contact your Plan Manager if you have questions.

Sincerely,

Jane Doe

Jane Doe
Vice President, ABC National Bank

Additional Resources

EBPAQC Plan Sponsor Resource Center

The EBPAQC has compiled helpful tools and resources for plan sponsors, administrators and trustees at aicpa.org/EBPAQC.

DOL Resources

29 CFR 2520.103–8 – Limitation on Scope of Accountant’s Examination, provides ERISA guidance on the limited scope audit exemption.

DOL [*Advisory Opinion to Mr. Richard Bentley, Paine Webber Inc.*](#), dated Aug. 3, 1993, clarifies definition of an institution qualified to issue a certification.

DOL [Information Letter](#), dated May 17, 2002, clarifies the application of the limited scope audit provisions of section 103(a)(3)(C) of the Employee Retirement Income Security Act of 1974, as amended (ERISA).

[U.S. Department of Labor Employee Benefits Security Administration Fiduciary Education Campaign website](#). The Fiduciary Education Campaign includes nationwide educational seminars and webcasts to help plan sponsors understand rules and meet their responsibilities to workers and retirees. The campaign also includes educational materials on topics such selecting an auditor.

[Meeting Your Fiduciary Responsibilities](#)

To meet their responsibilities as plan sponsors, employers need to understand some basic rules, specifically ERISA. ERISA sets standards of conduct for those who manage an employee benefit plan and its assets (called fiduciaries). This publication provides an overview of the basic fiduciary responsibilities applicable to retirement plans under the law.

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