

11th Capacity Building Seminar on Retirement Benefits (11th CBRB) Gurgaon 31 January 2025

Working effectively with auditors (US Pension Plans)

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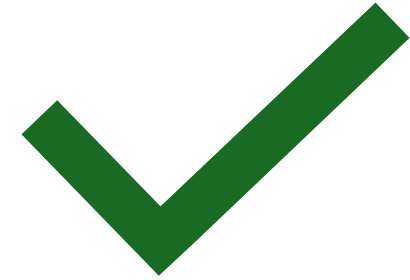
Background

- **Increased Auditor Scrutiny:** Auditors are applying greater skepticism during financial statement audits, with a focus on assumptions, interim events, and methodologies related to actuarial valuations of employee benefit
- **Skilled Audit Teams:** The Big Four audit firms (Deloitte, EY, KPMG, and PwC) are deploying staff with the requisite skills, knowledge, and experience to audit employee benefit plan measurements and disclosures, aiming to identify potential material misstatements and inconsistencies
- **Actuarial Preparedness:** Actuaries must adopt additional measures when preparing year-end disclosures and reports to minimize auditor queries, reduce the likelihood of revising measurements, and ensure a smoother audit process

Objectives of today's session



Understand key audit procedures



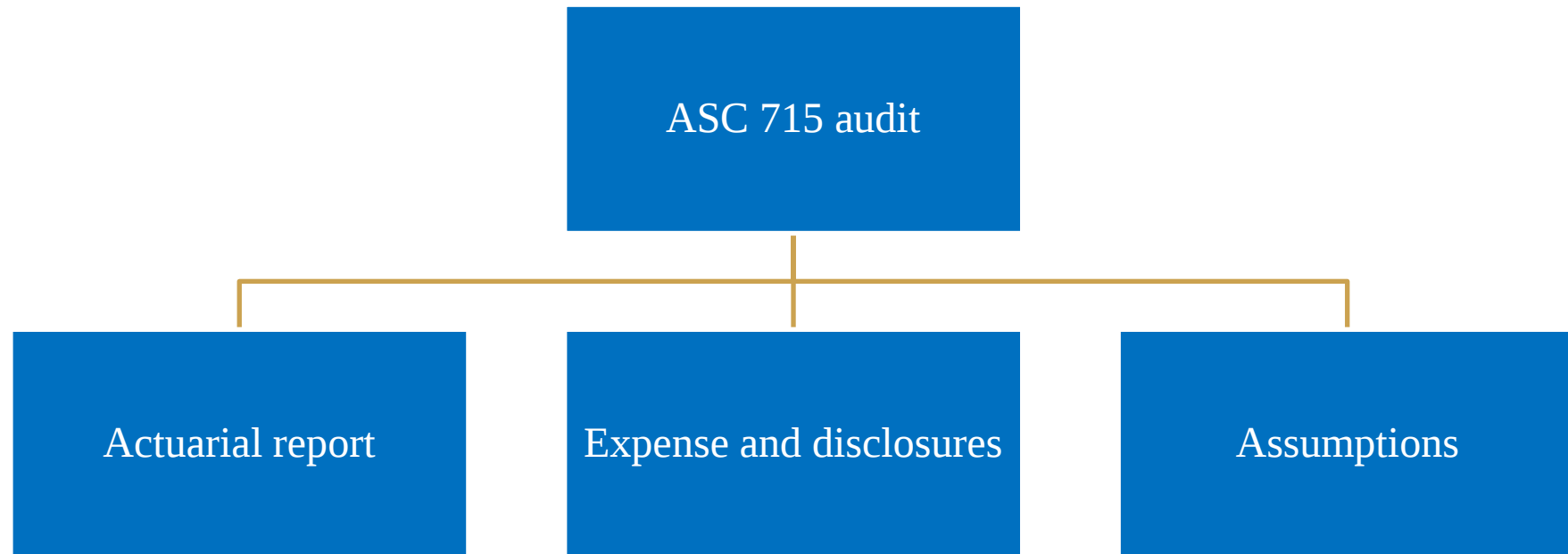
Best practices for preparing actuaries

Knowledge Check 1

Which accounting standard governs the valuation of pension plans in the United States?

- a) IAS 19R
- b) ASC 715
- c) IND AS 19
- d) IFRS 16

Understanding key audit procedures associated with ASC 715



Knowledge Check 2



What is the primary purpose of the actuarial report in the context of auditing employee benefit plans?

- a) To provide a summary of employee benefits
- b) To serve as a Statement of Actuarial Opinion and Actuarial Communication
- c) To outline the company's financial performance
- d) To detail the company's investment strategies

Actuarial Report



As a part of the audit procedures, the completeness and appropriateness of the Actuarial Report for its stated purpose are assessed. The actuarial reports are considered to be a Statement of Actuarial Opinion and an Actuarial Communication by the auditors. In particular, the following areas in the report are assessed.

- Signing Actuary's credentials and reputation
- Actuarial cost method and Asset method
- Measurement Date
- Date of Census Data

Expense and Disclosures

The auditors assess the reasonableness of the following expense components by performing independent calculations. The actuarial report is expected to contain all necessary information to assist auditors in these calculations.



- Service Cost
- Interest Cost
- Expected Return on Assets
- Amortization of Prior Service Costs
- Amortization of Gains/Losses for the current fiscal year

Additional Evaluations:

- Reasonableness of gain/loss in benefit obligation reconciliation
- Reconciliation of Accumulated Other Comprehensive Income (AOCI) components from prior to current year Measurement Date
- Current and noncurrent amounts of benefit asset or liability
- Schedule of expected benefit payments
- Accounting treatment for interim measurements, plan amendments and special events such as curtailment, settlement, etc., if any

Knowledge Check 3



Which of the following is a key area of assessment for auditors?

- a) Employee job satisfaction
- b) Economic and demographic assumptions
- c) Company's marketing strategies
- d) Employee training programs

Assumptions

Another significant area of assessment is assumptions. Both economic and demographic assumptions used to determine the net periodic benefit expense as well as the year-end benefit obligation are tested. Some of the key assumptions include –

- Discount rate
- Long-term rate of return on plan assets
- Salary Increase
- Mortality
- Turnover
- Retirement
- Cash Balance Interest Crediting Rate (applicable for cash balance plans only)
- Lump Sum Conversion (applicable where a plan allows accrued benefit payable as an annuity to be converted into a lump sum)

Knowledge Check 4

What should actuaries provide to auditors to support the discount rate assumption?

- a) Employee satisfaction surveys
- b) Projected benefit cash flows and spot rates
- c) Company's investment portfolio
- d) Historical financial statements

Knowledge Check 5



Which of the following is NOT a key assumption tested by auditors in the actuarial valuation of employee benefit plans?

- a) Discount rate
- b) Long-term rate of return on plan assets
- c) Employee satisfaction rate
- d) Mortality

Audit procedures associated with IAS 19 (Revised 2011) and IND AS 19 measurements



IAS 19 (Revised 2011)

The audit procedures for ASC 715 also apply to IAS 19 (Revised 2011) with specific modifications –

1. **Limit on Net Defined Benefit Asset:** Auditors ensure that any Net Defined Benefit Asset is limited to the present value of economic benefits available as refunds from the plan or reductions in future contributions
2. **Expense Components:** Current Service Cost and Net Interest Cost are computed independently, unlike ASC 715 which uses service cost and interest cost
3. **Non-Applicable Components:**
 1. Expected Return on Plan Assets
 2. Amortization of Prior Service Costs
 3. Amortization of Gains/Losses
 4. Reconciliation of AOCI
 5. Schedule of Expected Benefit Payments
4. **Return on Plan Assets:** Calculated using a discount rate instead of a long-term rate of return on assets

IND AS 19 No significant differences from IAS 19, thus the same audit procedures apply.

Knowledge Check 6

What is one of the key differences between ASC 715 and IAS 19 (Revised 2011) regarding the calculation of return on plan assets?

- a) ASC 715 uses a discount rate
- b) IAS 19 uses a long-term rate of return on assets
- c) IAS 19 uses a discount rate
- d) ASC 715 does not calculate return on plan assets

Knowledge Check 7

Which of the following is a good practice for actuaries to ensure a smoother audit process?

- a) Avoiding communication with auditors
- b) Providing high-quality data in an organized format
- c) Keeping known issues hidden from auditors
- d) Ignoring interim events

Best practices for actuaries



1. Communication is key

- ☐ **Advance notice of future events**
- ☐ **Discussions throughout year**
 - Impact of interim events
 - Curtailments
 - Settlements
 - Merger / spin-off
 - Amendments
 - Asset re-allocation
- ☐ **Timely resolution of issues and questions**

2. Data quality

- ☐ sending data in an organized and a usable format which ties to items in request list
- ☐ provide explanation if it doesn't tie to prior year/quarter
- ☐ identify items that might not be obvious like manual adjustments

Best practices for actuaries



3. Be open about known issues with auditors from the beginning

- ☐ Builds credibility
- ☐ Increases efficiency and quality of testing

4. Effective documentation

- ☐ Reflects processes as of valuation date
- ☐ Include details regarding assumptions used, claims development patterns, etc.
- ☐ Communicate report revisions/updates
- ☐ Provide calculation details if needed

5. Teamwork

- ☐ Essential for Accuracy, Compliance, and Risk Management
- ☐ Fosters Collaborative Environment
 - Leverages each team's strength
 - Leads to better organizational outcomes
- ☐ Best Practices: Regular meetings, clear roles, open communication, joint training, and integrated reporting significantly enhance the effectiveness of this collaboration

Thank you!

