



PROFESSIONAL ETHICS EXECUTIVE COMMITTEE

Open Meeting Agenda

November 28, 2017



**AICPA Professional Ethics Executive Committee
Open Agenda
November 28, 2017
Conference Call: 11:00 A.M. Eastern Time**

| Phone Access: 1-408-638-0968 or 1-646-876-9923 and Meeting ID: 9194024936 Web Access: https://aicpa.zoom.us/j/9194024936 | | |
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| November 28 th | <i>Open Meeting Begins</i> | |
| 11:00 a.m. – 11:15 a.m. | Welcome Mr. Burke will welcome the Committee members and discuss administrative matters. | |
| 11:15 a.m. – 12:30 p.m. | Information Technology and Cloud Services Ms. VanDyne and Ms. Gorla will seek the Committee's approval to expose a revised interpretation for comment. | Agenda Item 1A Agenda Item 1B |
| 12:30 p.m. – 12:45 p.m. | Break | |
| 12:45 p.m. – 2:00 p.m. | Long Association Ms. Dourdourekas and Ms. Ziemba will update the Committee on comment letters received to date. | Agenda Item 2A Agenda Item 2B Agenda Item 2C |
| 2:00 p.m. – 2:10 p.m. | IESBA Update Ms. Gorla will update the Committee on the September meeting of the IESBA. The Committee is asked to provide Staff with feedback on the Inducements Exposure for inclusion in the comment letter. ❖ External Link - Inducements Exposure Draft | |
| 2:10 p.m. – 2:25 p.m. | NOCLAR Mr. Denham will update the Committee on the Task Force's discussions. | |
| 2:25 p.m. – 2:30 p.m. | Minutes of the Professional Ethics Executive Committee Open Meeting The Committee is asked to approve the minutes from the July 2017 meeting. | Agenda Item 3 |
| | <i>Open Meeting Concludes For Day</i> | |
| Informational Purposes Only | Outstanding Exposure Drafts ❖ External Link - SLG Exposure Draft ❖ External Link - Long Association Exposure Draft ❖ External Link - Leases | |
| Informational Purposes Only | Committee Project Agenda ❖ External Link - Project Agenda | |
| | Future Meeting Dates <ul style="list-style-type: none"> • February 13-14, 2018 – Nashville • May 8-9, 2018 - TBD • August 8-9, 2018 - TBD • November 7-8, 2018 – Durham | |

Information Technology and Cloud Services

Task Force Members: Shelly VanDyne (Chair), Anna Dourdourekas, Mike Brand, Cathy Allen, Nancy Miller, Katie Jaeb, Dan O'Daly, John Ford. Staff: Ellen Gorla

Task Force Objective

Recommend to the Committee any changes necessary to the nonattest services subtopic considering current information technology (including cloud) service offerings by members.

Reason for Agenda

Approve the proposed revised *Information Systems Design, Implementation, or Integration* interpretation found in **Agenda Item 1B** for exposure.

Summary of Issues

The extant *Information Systems Design, Implementation, or Integration* interpretation has not had any substantive changes made to it since September 2003. The Task Force is recommending certain clarifications be made to keep up with the complex ever changing information systems environment.

Introduction

The Task Force continues to believe that when the services do not relate to a financial information system, that the member may be able to reduce threats to independence to an acceptable level by applying the safeguards outlined in the various interpretations of the Nonattest Services subtopic. While all the safeguards in the subtopic are critical, the Task Force recommends emphasizing that even if the services do not relate to a financial information system, that independence would be impaired when the services result in the attest client outsourcing a management responsibility to the member. This emphasis is made in paragraph .02.

The Task Force also continues to believe that when a member designs or develops an attest client's financial information system, that threats are so significant that no safeguards can be applied. Given the feedback received through the exposure process for the Hosting Services interpretation, the Task Force believes that members could question whether this would include situations where a member designs a spreadsheet or software product to assist the member in providing a discrete nonattest service such as depreciation or tax provision calculation. As such, the Task Force clarified in paragraph .03 that designing or developing a template such as this would not constitute designing or developing a financial information system.

Paragraphs .01 through .04 of **Agenda Item 1B** are the introduction paragraphs proposed by the Task Force.

Questions for the Committee

1. Is it clear that information systems services include services provided that relate to software and hardware such as networks? If not, should the phrase "including hardware and software products" be added to the end of paragraph .01?
2. Although the phrase "including that the attest client has not in essence outsourced a function, process or activity to the member" included in .02 does not appear elsewhere the Code, Staff believes the underlying theory is addressed in the Management Responsibilities interpretation. Does the Committee believe this phrase is clear enough

or does the phrase need to stipulate that the outsourced function, process or activity is something that would constitute a management responsibility?

3. Does the Committee believe it would be helpful to include the clarification that designing or developing a template would not constitute designing or developing a financial information system?

Terminology

There are several terms that the Task Force believes would be helpful to include in a terminology section. For the most part, the terms found in this section appear in various places throughout the revised interpretation. However, the term data mapping, appears only in paragraph .06. For readability purposes, the Task Force recommends this definition appear in the terminology section.

There are other terms and phrases that are defined throughout the interpretation that the Task Force does not recommend be included in the terminology section. Rather, recommends the definitions appear within the discussion that they relate so that the guidance can be easily read and understood.

Staff and Ms. VanDyne believe it would be helpful to include a definition of a financial information system. For discussion purposes, the definition added to item e, is consistent with the SEC's definition found in paragraph (c)(4)(ii)(B) "Designing or implementing a hardware or software system that aggregates source data underlying the financial statements or generates information that is significant to the audit client's financial statements or other financial information systems taken as a whole."

Paragraph .05 of **Agenda Item 1B** is the terminology paragraph proposed by the Task Force.

Questions for the Committee

1. Does the Committee believe that the phrase "an information system" in items b and c could be deleted without disrupting the definition since the terms "designing" and "developing" are used in a general sense in some places in the proposal?
2. Does the Committee have any suggested revisions to the definition of a financial information system?

COTS Financial Information System Software Solution

When a member provides certain implementation, services related to a COTS financial information system that the member has not designed or developed, the Task Force believes there can be situations where independence is impaired. As such, the Task Force proposes separate sections to address the broad categories of typical implementation services that members may be asked to provide. Each section starts off with an explanation of what these services would entail and then goes on to describe whether independence would be impaired.

Paragraphs .06 through .19 of **Agenda Item 1B** are the implementation paragraphs proposed by the Task Force.

System and Network Maintenance, Support and Monitoring Services

After an information system is implemented, there are several services that may need to be performed. The Task Force believes that for the most part, these “post-implementation” services will fall into one of the following three categories:

- Maintenance services
- Support services
- Monitoring services

The Task Force believes that when these services involve the member performing ongoing functions, processes or activities where the attest client has outsourced these to the member, independence would be impaired because the member would be performing management responsibilities. The Task Force believes this to be true even when the information system that the services relate to is a nonfinancial system.

Since the extant guidance did not include the qualifier that the examples listed not result in the member performing ongoing functions, processes or activities, the Task Force believes some members may need additional time to identify these services and terminate the contracts.

Paragraphs .20 through .21 of **Agenda Item 1B** are the maintenance, support and monitoring paragraphs proposed by the Task Force.

Questions for the Committee

1. Can the Committee think of any post-implementation services that would not fall into one of the three categories of maintenance, support or monitoring?
2. Does the Committee believe the guidance in paragraph .20 would be more restrictive than the SEC guidance since we are saying that independence would be impaired if a member were to perform the services even if they related to a nonfinancial system?
3. Are there any other examples that the Committee believes should be included in this section?

Effective Date

The Task Force recommends a one year delayed effective date is appropriate in the event the clarifications result in members having to terminate services that they previously thought would not impair independence.

Action Needed

The Task Force seeks the Committee’s approval to expose the proposal.

Communication Plan and Member Training Tools

The exposure draft will be published on the division’s website, the CPA Daily and incorporated into the division’s presentations.

Once the proposal is exposed for comment, the Task Force will review the nonattest services FAQs that relate to information technology and determine what changes are necessary and bring those recommendations to the Committee when it seeks approval to adopt.

Materials Presented

Agenda Item 1B Proposed Revised Information Systems Services Interpretation



1.295.145 Information Systems Services

- .01 Self-review and management participation threats to the covered member's compliance with the "Independence Rule" [1.200.001] may exist when a member provides services related to an attest client's information systems.
- .02 When performing services described in this interpretation for an attest client that are not related to a financial information system, threats to compliance with the "Independence Rule" would be at an acceptable level provided all the requirements of the [Nonattest Services](#) subtopic [1.295] of the Independence Rule [1.200.001] are met including that the attest client has not in essence outsourced a function, process or activity to the member.
- .03 When a member designs or develops an attest client's financial information system, threats to compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and could not be reduced to an acceptable level by the application of safeguards. Designing and developing a template that performs a discrete calculation such as a tax provision or depreciation calculation does not constitute designing or developing an information system and will not impair independence provided the member complies with all the requirements of the [Nonattest Services](#) subtopic [1.295] of the Independence Rule [1.200.001].
- .04 When performing services described in this interpretation for an attest client that relate to a financial information system that is a commercial off-the-shelf software (COTS) package that the member has not designed or developed, threats to compliance with the "Independence Rule" would be at an acceptable level provided the requirements of this interpretation are met.

Terminology

- .05 The following terms are defined solely for the purpose of applying this interpretation:
 - a. Commercial Off-the-Shelf ("COTS") means a software package developed, distributed, maintained and supported by a third-party vendor (vendor), sometimes simply referred to as an "off the shelf" package or solution. COTS solutions have generally referred to traditional on-premises software that runs on a customer's own computers or on a vendor's "cloud" infrastructure. COTS solutions range from software packages requiring only installation on a computer and are ready to run to large scale, complex enterprise applications.
 - b. Designing an information system means determining how a system or transaction will function, process data and produce results (for example, reports, journal vouchers and documents such as sales and purchase orders) to provide a blueprint or schematic for the development of software code (programs) and data structures.
 - c. Developing an information system entails creating software code, for individual or multiple modules, and testing such code to confirm it is functioning as designed.
 - d. Data mapping involves assisting the client in understanding and identifying how the fields in the legacy system relate to fields in the new system.
 - e. Financial information system is a system that aggregates source data underlying the financial statements or generates information that is significant to the financial statements or other financial information systems taken as a whole.

Implementation of a Commercial-Off-The-Shelf Financial Information System Software Solution

- .06 Implementation services involve activities related to an attest client's information systems after the design and development of the system. Implementation ceases when the system is available on a regular basis to the client for its intended use. For example, implementation services can include activities such as installing, configuring, interfacing, customizing, data translation and data mapping. Services that are performed post-implementation, such as the maintenance, support and monitoring of the system, are not considered to be implementation services.
- .07 Threats created by certain COTS implementation services related to the attest client's financial information system may be reduced to an acceptable level by the application of safeguards, while in other situations threats to compliance with the "Independence Rule" [1.200.001] would be significant and could not be reduced to an acceptable level by the application of safeguards.

Install a Commercial-Off-The Shelf Financial Information System Software Solution

- .08 To install a COTS financial information system software solution means the initial loading of software on a computer, normally onto a customer's server(s). Software configuration, development, integration and conversion activities may follow installation.
- .09 When a member installs a COTS financial information system software solution, threats to compliance with the "Independence Rule" would be at an acceptable level provided all the requirements of the [Nonattest Services](#) subtopic [1.295] of the Independence Rule [1.200.001] are met.

Configure a Commercial-Off-The Shelf Financial Information System Software Solution

- .10 To configure a COTS financial information system software solution means selecting the software features, functionality options, and settings that will determine how the software will perform certain transactions and process data. Configuration options may also include selecting the predefined format of certain data attributes and the inclusion or exclusion of such attributes. For purposes of this interpretation, configuring a COTS financial information system software solution does not generally involve developing new software code or features to modify or alter the functionality of the COTS software solution in ways not pre-defined by the vendor.
- .11 When a member configures a COTS financial information system software solution, threats to compliance with the "Independence Rule" would be at an acceptable level provided all the requirements of the [Nonattest Services](#) subtopic [1.295] of the Independence Rule [1.200.001] are met.

Customize of a Commercial-Off-The Shelf Financial Information System Software Solution

- .12 To customize a COTS financial information system software solution means altering or adding to the features and functions provided for by the vendor, which go beyond all options available when configuring the COTS software solution. For purposes of this interpretation, customizing can either involve modification or enhancements:
 - a. Modification involves altering the COTS software solution code to change or add to the functionality provided by the vendor, or

- b. Enhancements involve developing new code, external to the COTS software solution, and works in concert with the COTS software solution to provide altered or additional functionality.
- .13 If a member customizes an attest client's COTS financial information system software solution, threats to compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and could not be reduced to an acceptable level by the application of safeguards.

Interface a Commercial-Off-The Shelf Financial Information System Software Solution

- .14 Providing interface services for a COTS financial information system software solution means connecting two or more systems by designing and developing software code that passes data from one system to another. Interfaces may flow in one direction or be bidirectional. Interfaces may involve the performance of an end-to-end transaction or they may pass data from one system to another.
- .15 If a member provides interface services for a COTS financial information system software solution, threats to compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and could not be reduced to an acceptable level by the application of safeguards except as provided for in paragraph .16.
- .16 If a member uses an Application Program Interface (API) that is developed by a third party to interface one or more legacy or third-party COTS financial information system software solutions, threats to independence would be at an acceptable level provided the member will not be designing or developing code for the API to work and all the requirements of the [Nonattest Services](#) subtopic [1.295] of the Independence Rule [1.200.001] are met.

Data Translation Services Related to a Commercial-Off-The Shelf Financial Information System Software Solution

- .17 Performing data translation services for a COTS financial information system software solution involves designing and developing the rules or logic necessary to convert legacy system data to a format that is compatible with that of the new system.
- .18 If a member performs data translation services for a COTS financial information system software solution threats to compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and could not be reduced to an acceptable level by the application of safeguards expect as provided for in paragraph .19.
- .19 If a member uses an API that is developed by a third party to perform data translation services for a COTS financial information system software solution, threats to independence would be at an acceptable level provided the member will not be designing or developing code for the API to work and all the requirements of the [Nonattest Services](#) subtopic [1.295] of the Independence Rule [1.200.001] are met.

System and Network Maintenance, Support and Monitoring Services

- .20 Maintenance, support and monitoring services are activities that are provided after a financial or non-financial system or network is implemented. If post-implementation services involve ongoing functions, processes or activities where the *attest client* has in essence outsourced these functions, processes or activities to the *member*, compliance with the "Independence Rule" [1.200.001] would not be at an *acceptable level* and could not be reduced to an

acceptable level by the application of *safeguards*, and *independence* would be *impaired*. Examples of services that involve ongoing functions, processes or activities would include a service whereby the member directly or indirectly:

- a. operates the attest client's network
- b. supervises the operation of the attest client's information systems
- c. monitors the attest client's network on a routine or continual basis

.21 Independence will not be impaired provided all the requirements of the [Nonattest Services](#) subtopic [1.295] are met and where the maintenance, support and monitoring services are discrete nonrecurring engagements where the attest client has not in essence outsourced a function, process or activity to the member. Examples of such services may include being engaged for a discrete project to:

- a. analyze a network.
- b. apply virus protection solutions or updates that the member did not design or develop.
- c. apply certain updates and patches that the member did not design or develop.
- d. provide training or instruction on a new software solution.

Nonauthoritative questions and answers regarding information systems design, implementation, and integration services are available at www.aicpa.org/InterestAreas/ProfessionalEthics/Resources/Tools/DownloadableDocuments/NonattestServicesFAQs.pdf.

IFAC Convergence – Long Association**Task Force Members**

Anna Dourdourekas (Chair), Coalter Baker, Bob Denham, and Shelly Van Dyne. Staff: Shannon Ziemba. Observer: Ellen Gorla.

Task Force Charge

The Task Force is charged with reviewing the International Ethics Standards Board for Accountants' (IESBA) standard entitled, [Long Association of Personnel with an Audit or Assurance Client](#) (Long Association) and recommend to PEEC revisions to the AICPA Code for purposes of convergence.

Reason for Agenda Item

To review the IESBA's Long Association comment letters from the Exposure Draft and determine how to proceed.

Background Summary***Background***

The Public Interest Oversight Board (PIOB) approved the IESBA's Long Association standard on January 19, 2017. The standard addresses threats to independence that may be created by using the same personnel on an audit engagement or assurance engagement over a long period of time. The project commenced when a number of stakeholders raised concern on the continued robustness of the IESBA Code to address threats to independence arising from long association, particularly with respect to the audit of a client that is a public interest entity (PIE).

The concern expressed by the IESBA in their August 2014 exposure draft is that over a period of time, the audit team may become too familiar with the audit client, its personnel and their interests, including accounting and reporting issues, resulting in a loss of independence either of mind or in appearance.

The IESBA also noted that the cumulative knowledge and experience of an audit client's business, management and controls environment gained through familiarity with the audit client contributes positively to audit quality and evaluation and identification of audit risk areas.

The proposed changes broadly cover the following areas:

- Strengthening the general provisions that apply to all audits and assurance engagements with respect to the threats created by long association;
- Increased mandatory "cooling-off" period for the engagement partner and the partner responsible for the engagement quality control review on the audit of an entity that is a PIE;
- Strengthening the restrictions on the type of activities that can be undertaken with respect to the audit client and audit engagement by a former key audit partner (KAP) during the cooling off period; and
- Ensuring the concurrence of those charged with governance (TCWG) with respect to the application of extant paragraphs 290.150 and 290.152.

The final IESBA standard can be found in **Agenda Item 2B**.

Scope of Convergence

At the February 2017 meeting the Committee agreed that it should not consider the guidance applicable to PIEs since the SEC has more restrictive rules pertaining to partner rotation for PIEs located in the United States, rather should focus on just the general provisions of the IESBA Standard– paragraphs 290.148 – 290.152.

Exposure Draft

At the May 2017 PEEC meeting, PEEC approved the release of the Exposure Draft which would add a Long Association Interpretation to the Code.

The Exposure Draft was released July 14, 2017 and the comment period for the Exposure Draft closed on September 15, 2017.

The division received seven [comment letters on the exposure draft](#). The comment letters are summarized in **Agenda Item 2C**.

Two of the comment letters (Florida Institute of CPAs (CL1) & BDO (CL2)) supported the proposal. One comment letter (New York State Society of CPAs (CL3)) was in support of the proposal but requested the interpretation more closely align with the IESBA standard than what was exposed by PEEC. Four comment letters (PCPS Executive Committee (CL4), Piercy Bowler Taylor & Kern (CL5), Nevada State Board of Accountancy (CL6), and Garry Hutchison (CL7)) did not support of the proposal and believe it would be detrimental to the small to medium-sized firms who perform attest services to adopt this interpretation. These four commenters voiced concern that even though the proposal was a threat and safeguard approach that it will be viewed as best practice or requirement.

Comments Letters In Support of the Exposure Draft

Florida Institute of CPAs (CL1) was in support of the Exposure Draft and does not believe the effective date needs to be delayed. BDO (CL2) was in support of the Exposure Draft but does recommend delaying the effective date for three months in order to educate partners and staff on the matter. BDO recommends the following minor edit to ET 1.267.010.03: “...However, a **familiarity threat may be created when a member’s long-who is included** inclusion among senior personnel of the attest engagement teams **has a long association may create a familiarity threat** with any of the following:...”

The New York State Society of CPAs (NYSSCPA) (CL3) recommends that senior personnel should include any level of staff from the in-charge accountant upwards which is the same as the IESBA interpretation. NYSSPCA believes the in-charge (senior or manager level) would have regular contact with the client and make decisions on sufficiency or appropriateness of evidence obtained and the extent of further testing required to address any issues found in the audit so they need to be included in this interpretation. NYSSCPA agrees that the partner or partner equivalent is ultimately in-charge but may not be aware of the decisions that were made during the engagement that could affect the outcome of the engagement. NYSSCPA recommends the guidance include examples of situations what would constitute long association and impair independence. NYSSCPA also recommends the interpretation include guidance on the appropriateness of a rotation period. NYSSCPA believes the only acceptable rotation period is permanent rotation since if they rotate back on then they familiarity threat would remain at the same unacceptable level. NYSSCPA believes that the self-interest threat should be included in the interpretation and recommends that the effective date be delayed at least three months. Although the NYSSCPA acknowledges that sole or small-sized firms will probably not be able to rotate senior personnel, that medium sized firms might have issues

convincing clients to rotate partners and that it will be difficult to get a client to pay increased fees necessitated by an additional layer of engagement review, these challenges should not prevent the standard from being adopted.

Concerns Expressed in the Comment Letters Not in Support of the Exposure Draft

The Comment Letter from the Technical Issues Committee (TIC) of PCPS Executive Committee (CL4) believes that for long association to actually be a threat to independence there would also need to be a failure of integrity and/or objectivity. TIC believes this failure is already addressed in the principles of the Code (i.e., [ET 0.300](#)). TIC also believes that if PEEC adopts this interpretation, there will be unintended consequences such as:

- Unfairly taint the majority of long associations by members with attest clients. TIC believes there is no risk to independence because the member conducts themselves with integrity, objectivity and professionalism.
- The addition of a partner rotation requirement as a safeguard then it could unintentionally create a “best practice” to address a perceived risk which does not actually exist. If partner rotation is perceived to be required, then it may negatively affect small practitioners who may not have other partners in which to rotate.
- The inclusion of an EQCR as a possible safeguard could once again result in a best practice when a familiarity threat does not exist, and the nature and complexity of the engagement does not warrant an EQCR.
- The additional documentation associated with long association would not add to the quality of the audit.

TIC believes if the PEEC needs to address the specific issues related to long standing senior personnel than it should be done in an existing interpretation and does not need to create a new interpretation with additional documentation requirements.

The Comment Letter from Piercy Bowler Taylor & Kern (PBTK) (CL5) believes that the sole motivator for this exposure draft is the adoption on the subject by the IESBA. PBTK does not believe this is sufficient justification. PBTK believe this interpretation will likely cause serious adverse consequences such as:

- Introducing a strong bias that will likely cause practitioners to engage in a great deal of unnecessary, unproductive and costly analysis and documentation for safeguards to rationalize away what is essentially an “imaginary threat”.
- PBTK does not believe the mere duration of the association that potentially poses a familiarity threat to independence; rather is the nature of the association and the member subsequent behavior.
- PBTK believes that saying the long association alone could impair auditor independence that it would be based on an inappropriate rebuttable presumption that “auditors are more like weak-willed used car salesman rather the professionals that are who have dedicated their lifelong career to high principles such as integrity, objectivity and public service”.
- PBTK believes this interpretation would present a biased, negative view of its own members without presenting the far more persuasive mitigating benefits of such associations which tend to enhance audit quality.
- PBTK states that most small practice units build their practices through relationships. It takes time to build these relationships and PBTK believes this interpretation would discourage the cultivating of these relationships. Some small firms might be forced to eliminate attest services entirely because they are not able to establish adequate safeguards to mitigate an imaginary independence threat and still maintain audit quality.

- PBTK also believes that this interpretation would provide “valuable ammunition” to potential litigants and other adversaries to challenge their judgment of auditors based on the length of the association.
- PBTK notes that the large majority of audit failures occur in the first two years of an audit engagement and believe that as the association continues the auditor’s knowledge of the attest client’s business and industry increase the audit quality.
- PBTK believe that partner or firm rotation has virtually nothing to do with auditor independence and can only impair, not improve, audit quality, and is unaware of any evidence to the contrary.

The Comment Letter from the Nevada State Board of Accountancy (CL6) supports PBTK’s position. Nevada State Board brought up that there has been no disciplinary case brought based on the duration of a client relationship. Cases related to familiarity threat have not been related to long association but related to highly inappropriate personal relationships. Nevada State Board is concerned that members will be spending a lot of time and energy justifying relationships that pose no threat, will drive some rotation that could sacrifice audit quality and will discourage others unnecessarily from continuing such relationships. Nevada State Board is also concerned that pressures will be put on firms by peer reviewers, litigants, regulators and other adversaries if this interpretation is adopted. Nevada State Board is also concerned that this interpretation will push smaller practices out of the attest business.

The Comment Letter from Garry Hutchison (CL7) does not support the interpretation. Mr. Hutchison stated that this interpretation might be necessary for larger firms but that the interpretation is not productive and would be a barrier to smaller firms in the audit arena. Mr. Hutchison realizes this interpretation does not require partner rotation but might imply a requirement.

Extant Conceptual Framework for Independence Long Association Addressed in the AICPA Code

The AICPA Code addresses long association in Conceptual Framework for Members in Public Practice (1.000.010) as follows:

.12 Familiarity Threat. The threat that, due to a long or close relationship with a client, a member will become too sympathetic to the client’s interests or too accepting of the client’s work or product. Examples of familiarity threats include the following:

- a. A member’s immediate family or close relative is employed by the client.*
- b. A member’s close friend is employed by the client.*
- c. A former partner or professional employee joins the client in a key position and has knowledge of the firm’s policies and practices for the professional services engagement.*
- d. Senior personnel have a long association with a client.*
- e. A member has a significant close business relationship with an officer, a director, or a 10 percent shareholder of a client.*

.23 The following are examples of safeguards implemented by the firm:

- r. Rotation of senior personnel who are part of the engagement team.*

Options for the Committee

Based on the comment letters received, the Task Force believes the following options are available:

1. Adopt the *Long Association* interpretation either as exposed or with revisions.

2. Not adopt the *Long Association* interpretation. If this option is selected, then the Committee could:
 - Decide if additional safeguards should be incorporated into the *Conceptual Framework for Independence* or other interpretation(s) to provide further insight into the long association threat.
 - Consider if a non-authoritative document (e.g., FAQs, toolkit) could be used to provide members with additional insights when evaluating the long association threat. A few possibilities include:
 - Develop a FAQ that seeks input on whether independence would be impaired when long association occurs. The answer could point the reader to the Conceptual Framework Conceptual Framework Toolkits and offer up some important items from the proposal as items to consider.
 - Revise the [Conceptual Framework Toolkit for Independence](#) (or Members in Public Practice or Business) to incorporate the guidance contained in the exposure draft that the Task Force believes is important to consider.

If option 2 is pursued, then a basis should be developed for how the Committee believes it has or has not converged in substance with the IESBA standard.

It should be noted that this exposed interpretation, if adopted, would be the first one, excluding the Conceptual Frameworks, that is exclusively a threats and safeguard approach interpretation.

The Task Force reviewed the above options and is looking for the Committee's input on how the Task Force should proceed. The Task Force is researching the criteria for convergence with the IESBA.

Action Needed:

What option does the Committee believe is the best choice for the members?

Next Steps:

The Task Force will take the feedback from the Committee and make a recommendation to the Committee at the next meeting regarding Long Association.

Materials Presented

Agenda Item 2B – Final IESBA Long Association Standard

Agenda Item 2C – Comment Letter Summary

Close-Off Document
[January 2017]

*International Ethics Standards Board for
Accountants®*

**Changes to the Code
Addressing the Long
Association of Personnel with
an Audit or Assurance Client**

IESBA

International
Ethics Standards
Board for Accountants®

This document was developed and approved by the International Ethics Standards Board for Accountants® (IESBA®).

The IESBA is an independent standard-setting board that develops and issues high-quality ethical standards and other pronouncements for professional accountants worldwide. Through its activities, the IESBA develops the *Code of Ethics for Professional Accountants™*, which establishes ethical requirements for professional accountants.

The objective of the IESBA is to serve the public interest by setting high-quality ethical standards for professional accountants and by facilitating the convergence of international and national ethical standards, including auditor independence requirements, through the development of a robust, internationally appropriate code of ethics.

This close-off document has received the approval of the Public Interest Oversight Board (PIOB), which concluded that due process was followed in the development of the document and that proper regard was paid to the public interest.

The structures and processes that support the operations of the IESBA are facilitated by the International Federation of Accountants® (IFAC®).

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CHANGES TO THE CODE ADDRESSING THE LONG ASSOCIATION OF PERSONNEL WITH AN AUDIT OR ASSURANCE CLIENT

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SECTION 290
INDEPENDENCE—AUDIT AND REVIEW ENGAGEMENTS
(CLEAN)

Long Association of Personnel (Including Partner Rotation) with an Audit Client

General Provisions

290.148 Familiarity and self-interest threats, which may impact an individual's objectivity and professional skepticism, may be created and may increase in significance when an individual is involved in an audit engagement over a long period of time.

Although an understanding of an audit client and its environment is fundamental to audit quality, a familiarity threat may be created as a result of an individual's long association as a member of the audit team with:

- The audit client and its operations;
- The audit client's senior management; or
- The financial statements on which the firm will express an opinion or the financial information which forms the basis of the financial statements.

A self-interest threat may be created as a result of an individual's concern about losing a longstanding client or an interest in maintaining a close personal relationship with a member of senior management or those charged with governance, and which may inappropriately influence the individual's judgment.

290.149 The significance of the threats will depend on factors, individually or in combination, relating to both the individual and the audit client.

(a) Factors relating to the individual include:

- The overall length of the individual's relationship with the client, including if such relationship existed while the individual was at a prior firm.
- How long the individual has been a member of the engagement team, and the nature of the roles performed.
- The extent to which the work of the individual is directed, reviewed and supervised by more senior personnel.
- The extent to which the individual, due to the individual's seniority, has the ability to influence the outcome of the audit, for example, by making key decisions or directing the work of other members of the engagement team.
- The closeness of the individual's personal relationship with senior management or those charged with governance.
- The nature, frequency and extent of the interaction between the individual and senior management or those charged with governance.

(b) Factors relating to the audit client include:

- The nature or complexity of the client's accounting and financial reporting issues and whether they have changed.
- Whether there have been any recent changes in senior management or those charged with governance.
- Whether there have been any structural changes in the client's organization which impact the nature, frequency and extent of interactions the individual may have with senior management or those charged with governance.

290.150 The combination of two or more factors may increase or reduce the significance of the threats. For example, familiarity threats created over time by the increasingly close relationship between an individual and a member of the client's senior management would be reduced by the departure of that member of the client's senior management and the start of a new relationship.

290.151 The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Rotating the individual off the audit team.
- Changing the role of the individual on the audit team or the nature and extent of the tasks the individual performs.
- Having a professional accountant who was not a member of the audit team review the work of the individual.
- Performing regular independent internal or external quality reviews of the engagement.
- Performing an engagement quality control review.

290.152 If a firm decides that the threats are so significant that rotation of an individual is a necessary safeguard, the firm shall determine an appropriate period during which the individual shall not be a member of the engagement team or provide quality control for the audit engagement or exert direct influence on the outcome of the audit engagement. The period shall be of sufficient duration to allow the familiarity and self-interest threats to independence to be eliminated or reduced to an acceptable level. In the case of a public interest entity, paragraphs 290.153 to 290.168 also apply.

Audits of Public Interest Entities

290.153 In respect of an audit of a public interest entity, an individual shall not act in any of the following roles, or a combination of such roles, for a period of more than seven cumulative years (the "time-on" period):

- (a) The engagement partner;
- (b) The individual appointed as responsible for the engagement quality control review; or
- (c) Any other key audit partner role.

After the time-on period, the individual shall serve a "cooling-off" period in accordance with the provisions in paragraphs 290.155 – 290.163.

290.154 In calculating the time-on period, the count of years cannot be restarted unless the individual ceases to act in any one of the above roles for a consecutive period equal to at least the cooling-off period determined in accordance with paragraphs 290.155 to 290.157 as applicable to the role in which the individual served in the year immediately before ceasing such involvement. For example, an individual who served as engagement partner for four years followed by three years off can only act thereafter as a key audit partner on the same audit engagement for three further years (making a total of seven cumulative years). Thereafter, that individual is required to cool off in accordance with paragraph 290.158.

Cooling-off Period

290.155 If the individual acted as the engagement partner for seven cumulative years, the cooling-off period shall be five consecutive years.

290.156 Where the individual has been appointed as responsible for the engagement quality control review and has acted in that capacity for seven cumulative years, the cooling-off period shall be three consecutive years.

290.157 If the individual has acted in any other capacity as a key audit partner for seven cumulative years, the cooling-off period shall be two consecutive years.

Service in a combination of key audit partner roles

290.158 If the individual acted in a combination of key audit partner roles and served as the engagement partner for four or more cumulative years, the cooling-off period shall be five consecutive years.

290.159 If the individual acted in a combination of key audit partner roles and served as the key audit partner responsible for the engagement quality control review for four or more cumulative years, the cooling-off period shall, subject to paragraph 290.160(a), be three consecutive years.

290.160 If an individual has acted in a combination of engagement partner and engagement quality control review roles for four or more cumulative years during the time-on period, the cooling-off period shall be:

- (a) Five consecutive years where the individual has been the engagement partner for three or more years; or
- (b) Three consecutive years in the case of any other combination.

290.161 If the individual acted in any other combination of key audit partner roles, the cooling-off period shall be two consecutive years.

Service at a Prior Firm

290.162 In determining the number of years that an individual has been a key audit partner under paragraphs 290.153 to 290.154, the length of the relationship shall, where relevant, include time while the individual was a key audit partner on that engagement at a prior firm.

Position where Shorter Cooling-off Period is Established by Law or Regulation

290.163 Where a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) has established a cooling-off period for an engagement partner of less than five consecutive years, the higher of that period or three years may be substituted

for the cooling-off period of five consecutive years specified in paragraphs 290.155, 290.158 and 290.160(a) provided that the applicable time-on period does not exceed seven years.

Restrictions on Activities During the Cooling-off Period

- 290.164 For the duration of the relevant cooling-off period, the individual shall not:
- (a) Be a member of the engagement team or provide quality control for the audit engagement;
 - (b) Consult with the engagement team or the client regarding technical or industry-specific issues, transactions or events affecting the audit engagement (other than discussions with the engagement team limited to work undertaken or conclusions reached in the last year of the individual's time-on period where this remains relevant to the audit);
 - (c) Be responsible for leading or coordinating the firm's professional services to the audit client or overseeing the firm's relationship with the audit client; or
 - (d) Undertake any other role or activity not referred to above with respect to the audit client, including the provision of non-assurance services, that would result in the individual:
 - (i) Having significant or frequent interaction with senior management or those charged with governance; or
 - (ii) Exerting direct influence on the outcome of the audit engagement.

The provisions of this paragraph are not intended to prevent the individual from assuming a leadership role in the firm, such as that of the Senior or Managing Partner.

Other Matters

- 290.165 There may be situations where a firm, based on an evaluation of threats in accordance with the general provisions above, concludes that it is not appropriate for an individual who is a key audit partner to continue in that role even though the length of time served as a key audit partner is less than seven years. In evaluating the threats, particular consideration shall be given to the roles undertaken and the length of the individual's association with the audit engagement prior to an individual becoming a key audit partner.
- 290.166 Despite paragraphs 290.153 – 290.161, key audit partners whose continuity is especially important to audit quality may, in rare cases due to unforeseen circumstances outside the firm's control, and with the concurrence of those charged with governance, be permitted to serve an additional year as a key audit partner as long as the threat to independence can be eliminated or reduced to an acceptable level by applying safeguards. For example, a key audit partner may remain in that role on the audit team for up to one additional year in circumstances where, due to unforeseen events, a required rotation was not possible, as might be the case due to serious illness of the intended engagement partner. The firm shall discuss with those charged with governance the reasons why the planned rotation cannot take place and the need for any safeguards to reduce any threat created.
- 290.167 When an audit client becomes a public interest entity, the length of time the individual has served the audit client as a key audit partner before the client becomes a public interest entity shall be taken into account in determining the timing of the rotation. If the individual has served the audit client as a key audit partner for a period of five cumulative years or less when the

client becomes a public interest entity, the number of years the individual may continue to serve the client in that capacity before rotating off the engagement is seven years less the number of years already served. If the individual has served the audit client as a key audit partner for a period of six or more cumulative years when the client becomes a public interest entity, the partner may continue to serve in that capacity with the concurrence of those charged with governance for a maximum of two additional years before rotating off the engagement.

290.168 When a firm has only a few people with the necessary knowledge and experience to serve as a key audit partner on the audit of a public interest entity, rotation of key audit partners may not be an available safeguard. If an independent regulator in the relevant jurisdiction has provided an exemption from partner rotation in such circumstances, an individual may remain a key audit partner for more than seven years, in accordance with such regulation, provided that the independent regulator has specified other requirements which are to be applied, such as the length of time that the key audit partner may be exempted from rotation or a regular independent external review.

SECTION 291 INDEPENDENCE—OTHER ASSURANCE ENGAGEMENTS (CLEAN)

Long Association of Personnel with an Assurance Client

291.137 Familiarity and self-interest threats, which may impact an individual's objectivity and professional skepticism, may be created and may increase in significance when an individual is involved on an assurance engagement of a recurring nature over a long period of time.

A familiarity threat may be created as a result of an individual's long association with:

- The assurance client; or
- The subject matter and subject matter information of the assurance engagement.

A self-interest threat may be created as a result of an individual's concern about losing a longstanding assurance client or an interest in maintaining a close personal relationship with the assurance client or a member of senior management and which may inappropriately influence the individual's judgment.

291.138 The significance of the threats will depend on factors, considered individually or in combination, such as:

- The nature of the assurance engagement.
- How long the individual has been a member of the assurance team, the individual's seniority on the team, and the nature of the roles performed, including if such a relationship existed while the individual was at a prior firm.
- The extent to which the work of the individual is directed, reviewed and supervised by more senior personnel.
- The extent to which the individual, due to the individual's seniority, has the ability to influence the outcome of the assurance engagement, for example, by making key decisions or directing the work of other members of the engagement team.
- The closeness of the individual's personal relationship with the assurance client or, if relevant, senior management.
- The nature, frequency and extent of interaction between the individual and the assurance client.
- Whether the nature or complexity of the subject matter or subject matter information has changed.
- Whether there have been any recent changes in the individual or individuals who are the responsible party or, if relevant, senior management.

291.139 The combination of two or more factors may increase or reduce the significance of the threats. For example, familiarity threats created over time by the increasingly close relationship between an individual and the assurance client would be reduced by the departure of the person who is the responsible party and the start of a new relationship.

291.140 The significance of any threats shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards in relation to a specific engagement include:

- Rotating the individual off the assurance team.
- Changing the role of the individual on the assurance team or the nature and extent of the tasks the individual performs.
- Having a professional accountant who is not a member of the assurance team review the work of the individual.
- Performing regular independent internal or external quality reviews of the engagement.
- Performing an engagement quality control review.

291.141 If a firm decides that the threats are so significant that rotation of an individual is a necessary safeguard, the firm shall determine an appropriate period during which the individual shall not be a member of the engagement team or provide quality control for the assurance engagement or exert direct influence on the outcome of the assurance engagement. The period shall be of sufficient duration to allow the familiarity and self-interest threats to be eliminated or reduced to an acceptable level.

Effective Date

Subject to the transitional provision below, paragraphs 290.148 to 290.168 are effective for audits of financial statements for periods beginning on or after December 15, 2018. Paragraphs 291.137 to 291.141 are effective as of December 15, 2018. Early adoption is permitted.

Paragraph 290.163 shall have effect only for audits of financial statements for periods beginning prior to December 15, 2023. This will facilitate the transition to the required cooling-off period of five consecutive years for engagement partners in those jurisdictions where the legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) has specified a cooling-off period of less than five consecutive years.

SECTION 290
INDEPENDENCE—AUDIT AND REVIEW ENGAGEMENTS
(MARK-UP FROM RE-EXPOSURE DRAFT)¹

Long Association of Personnel (Including Partner Rotation) with an Audit Client

General Provisions

290.148A Familiarity and self-interest threats, which may impact an individual's objectivity and professional skepticism, may be created and may increase in significance when an individual is involved in an audit engagement over a long period of time.

Although an understanding of an audit client and its environment is fundamental to audit quality, a familiarity threat may be created as a result of an individual's long association as a member of the audit team with:

- The audit client and its operations;
- The audit client's senior management; or
- The financial statements on which the firm will express an opinion or the financial information which forms the basis of the financial statements.

A self-interest threat may be created as a result of an individual's concern about losing a longstanding client or an interest in maintaining a close personal relationship with a member of senior management or those charged with governance, and which may inappropriately influence the individual's judgment.

290.1498B The significance of the threats will depend on factors, individually or in combination, relating to both the individual and the audit client.

(a) Factors relating to the individual include:

- The overall length of the individual's relationship with the client, including if such relationship existed while the individual was at a prior firm.
- How long the individual has been a member of the engagement team, and the nature of the roles performed.
- The extent to which the work of the individual is directed, reviewed and supervised by more senior personnel.
- The extent to which the individual, due to the individual's seniority, has the ability to influence the outcome of the audit, for example, by making key decisions or directing the work of other members of the engagement team.
- The closeness of the individual's personal relationship with senior management or those charged with governance.
- The nature, frequency and extent of the interaction between the individual and senior management or those charged with governance.

¹ February 2016 re-Exposure Draft, [Limited Re-Exposure of Proposed Changes to the Code Addressing the Long Association of Personnel with an Audit Client](#)

(b) Factors relating to the audit client include:

- The nature or complexity of the client's accounting and financial reporting issues and whether they have changed.
- Whether there have been any recent changes in senior management or those charged with governance.
- Whether there have been any structural changes in the client's organization which impact the nature, frequency and extent of interactions the individual may have with senior management or those charged with governance.

290.15048C The combination of two or more factors may increase or reduce the significance of the threats. For example, familiarity threats created over time by the increasingly close relationship between an individual and a member of the client's senior management would be reduced by the departure of that member of the client's senior management and the start of a new relationship.

290.15149A The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include:

- Rotating the individual off the audit team.
- Changing the role of the individual on the audit team or the nature and extent of the tasks the individual performs.
- Having a professional accountant who was not a member of the audit team review the work of the individual.
- Performing regular independent internal or external quality reviews of the engagement.
- Performing an engagement quality control review.

290.15249B If a firm decides that the threats are so significant that rotation of an individual is a necessary safeguard, the firm shall determine an appropriate period during which the individual shall not be a member of the engagement team, or provide quality control for the audit engagement, or exert direct influence on the outcome of the audit engagement. The period shall be of sufficient duration to allow the familiarity and self-interest threats to independence to be eliminated or reduced to an acceptable level. In the case of a public interest entity, paragraphs 290.1530A to 290.16853 also apply.

~~Audit Clients That Are Listed Entities~~ Audits of Public Interest Entities

290.1530A In respect of an audit of a ~~listed~~ public interest entity, an individual shall not act in any of the following roles, or a combination of such roles, not be a key audit partner for a period of more than seven cumulative years (the "time-on" period);

- (a) The engagement partner;
- (b) The individual appointed as responsible for the engagement quality control review; or
- (c) Any other key audit partner role.

a ~~After which the time-on period,~~ the individual shall serve a "cooling-off" period in accordance with the provisions in paragraphs 290.155 – 290.163.

~~Subject to paragraph 290.150D the cooling-off period shall be:~~

~~Five consecutive years for a key audit partner who during the time-on period acted as the engagement partner or the individual responsible for the engagement quality control review, in either capacity or a combination of these roles, for either (a) four or more years or (b) at least two out of the last three years.~~

~~Two consecutive years for a key audit partner who acted in any other combination of key audit partner roles during the time-on period.~~

290.154 In calculating the time-on period, the count of years cannot be restarted unless the individual ceases to act in any one of the above roles for a consecutive period equal to at least the cooling-off period determined in accordance with paragraphs 290.155 to 290.157 as applicable to the role in which the individual served in the year immediately before ceasing such involvement. For example, an individual who served as engagement partner for four years followed by three years off can only act thereafter as a key audit partner on the same audit engagement for three further years (making a total of seven cumulative years). Thereafter, that individual is required to cool off in accordance with paragraph 290.158.

Cooling-off Period

290.155 If the individual acted as the engagement partner for seven cumulative years, the cooling-off period shall be five consecutive years.

290.156 Where the individual has been appointed as responsible for the engagement quality control review and has acted in that capacity for seven cumulative years, the cooling-off period shall be three consecutive years.

290.157 If the individual has acted in any other capacity as a key audit partner for seven cumulative years, the cooling-off period shall be two consecutive years.

Service in a combination of key audit partner roles

290.158 If the individual acted in a combination of key audit partner roles and served as the engagement partner for four or more cumulative years, the cooling-off period shall be five consecutive years.

290.159 If the individual acted in a combination of key audit partner roles and served as the key audit partner responsible for the engagement quality control review for four or more cumulative years, the cooling-off period shall, subject to paragraph 290.160(a), be three consecutive years.

290.160 If an individual has acted in a combination of engagement partner and engagement quality control review roles for four or more cumulative years during the time-on period, the cooling-off period shall be:

(a) Five consecutive years where the individual has been the engagement partner for three or more years; or

(b) Three consecutive years in the case of any other combination.

290.161 If the individual acted in any other combination of key audit partner roles, the cooling-off period shall be two consecutive years.

~~*Audit Clients that are Public Interest Entities other than Listed Entities*~~

~~290.150B~~ In respect of an audit of a public interest entity that is not a listed entity, an individual shall not be a key audit partner for more than seven years (“the time-on period”), after which the individual shall serve a cooling-off period.

~~Subject to paragraph 290.150D, the cooling-off period shall be:~~

- ~~• Five consecutive years for a key audit partner who during the time-on period acted as the engagement partner for either (a) four or more years or (b) at least two out of the last three years.~~
- ~~• Three consecutive years for a key audit partner who during the time-on period was responsible for the engagement quality control review for either:
 - ~~(a) Four or more years; or~~
 - ~~(b) At least two out of the last three years; or~~
 - ~~(c) Who acted in a combination of engagement partner and engagement quality control review roles for four years or more or at least two out of the last three years.~~~~
- ~~• Two consecutive years for a key audit partner who acted in any other combination of key audit partner roles during the time-on period.~~

~~*Audit Clients that are Public Interest Entities*~~

Service at a Prior Firm

~~290.16250C~~ In determining the number of years that an individual has been a key audit partner under paragraphs 290.153 to 290.154, the length of the relationship shall, where relevant, include time while the individual was a key audit partner on that engagement at a prior firm.

Position where Shorter Cooling-off Period is Established by Law or Regulation

~~290.16350D~~ An independent standard setter, regulator or Where a legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) may have evaluated the familiarity and self-interest threats to independence that arise from long association with an audit client and determined that a different set or combination of safeguards to those required in this Code are appropriate to reduce the threats to an acceptable level. In such circumstances, has established a cooling-off period for an engagement partner of less than five consecutive years, the higher of that period or three years may be substituted for the cooling-off periods of five consecutive years specified in paragraphs 290.150A and 290.150B 290.155, 290.158 and 290.160(a) provided that the applicable time-on period does not exceed seven years. ~~may be reduced to three consecutive years if an independent standard setter, regulator or legislative body has:~~

- ~~(a) Implemented an independent regulatory inspection regime; and~~
- ~~(b) Established requirements for either:
 - ~~(i) A time-on period shorter than seven years during which an individual is permitted to be the engagement partner or the individual responsible for the engagement quality control review; or~~~~

- ~~(ii) Mandatory firm rotation or mandatory re-tendering of the audit appointment at least every ten years.~~

Restrictions on Activities During the Cooling-off Period

290.16450E For the duration of the relevant cooling-off period, the individual shall not:

- (a) Be a member of the engagement team or provide quality control for the audit engagement;
- (b) Consult with the engagement team or the client regarding technical or industry-specific issues, transactions or events affecting the audit engagement (other than discussions with the engagement team limited to work undertaken or conclusions reached in the last year of the individual's time-on period where this remains relevant to the audit); ~~However, if an individual who has acted as the engagement partner or the individual responsible for the engagement quality control review is also, or becomes, an individual whose primary responsibility is to be consulted within a firm on a technical or industry-specific issue, the individual may provide such technical consultation to the engagement team provided:~~
 - ~~(i) Two years have elapsed since the individual was a member of the engagement team or the individual responsible for the engagement quality control review;~~
 - ~~(ii) There is no other partner within the firm expressing the audit opinion with the expertise to provide the advice; and~~
 - ~~(iii) Such consultation is in respect of an issue, transaction or event that was not previously considered by that individual in the course of acting as engagement partner or the individual responsible for the engagement quality control review;~~
- (c) Be responsible for leading or coordinating the firm's professional services to the audit client or overseeing the firm's relationship with the audit client; or
- (d) Undertake any other role or activity not referred to above with respect to the audit client, including the provision of non-assurance services, that would result in the individual:
 - (i) Having significant or frequent interaction with senior management or those charged with governance; or
 - (ii) Exerting direct influence on the outcome of the audit engagement.

The provisions of this paragraph are not intended to prevent the individual from assuming a leadership role in the firm, such as that of the Senior or Managing Partner.

Other Matters

290.1650F There may be situations where a firm, based on an evaluation of threats in accordance with the general provisions above, concludes that it is not appropriate for an individual who is a key audit partner to continue in that role even though the length of time served as a key audit partner is less than seven years. In evaluating the threats, particular consideration shall be given to the roles undertaken and the length of the individual's association with the audit engagement prior to an individual becoming a key audit partner.

290.16654 Despite paragraphs ~~290.150A and 290.150B~~ 290.153 – 290.161, key audit partners whose continuity is especially important to audit quality may, in rare cases due to unforeseen

circumstances outside the firm's control, and with the concurrence of those charged with governance, be permitted to serve an additional year as a key audit partner as long as the threat to independence can be eliminated or reduced to an acceptable level by applying safeguards. For example, a key audit partner may remain in that role on the audit team for up to one additional year in circumstances where, due to unforeseen events, a required rotation was not possible, as might be the case due to serious illness of the intended engagement partner. The firm shall discuss with those charged with governance the reasons why the planned rotation cannot take place and the need for any safeguards to reduce any threat created.

- 290.16752 When an audit client becomes a public interest entity, the length of time the individual has served the audit client as a key audit partner before the client becomes a public interest entity shall be taken into account in determining the timing of the rotation. If the individual has served the audit client as a key audit partner for a period of five cumulative years or less when the client becomes a public interest entity, the number of years the individual may continue to serve the client in that capacity before rotating off the engagement is seven years less the number of years already served. If the individual has served the audit client as a key audit partner for a period of six or more cumulative years when the client becomes a public interest entity, the partner may continue to serve in that capacity with the concurrence of those charged with governance for a maximum of two additional years before rotating off the engagement.
- 290.16853 When a firm has only a few people with the necessary knowledge and experience to serve as a key audit partner on the audit of a public interest entity, rotation of key audit partners may not be an available safeguard. If an independent regulator in the relevant jurisdiction has provided an exemption from partner rotation in such circumstances, an individual may remain a key audit partner for more than seven years, in accordance with such regulation, provided that the independent regulator has specified ~~alternative safeguards~~ other requirements which are to be applied, such as the length of time that the key audit partner may be exempted from rotation or a regular independent external review.

SECTION 291
INDEPENDENCE—OTHER ASSURANCE ENGAGEMENTS
(MARK-UP FROM RE-EXPOSURE DRAFT)

Long Association of Personnel with an Assurance Client

291.137A Familiarity and self-interest threats, which may impact an individual's objectivity and professional skepticism, may be created and may increase in significance when an individual is involved on an assurance engagement of a recurring nature over a long period of time.

A familiarity threat may be created as a result of an individual's long association with:

- The assurance client; or
- The subject matter and subject matter information of the assurance engagement.

A self-interest threat may be created as a result of an individual's concern about losing a longstanding assurance client or an interest in maintaining a close personal relationship with the assurance client or a member of senior management and which may inappropriately influence the individual's judgment.

291.138~~7B~~ The significance of the threats will depend on factors, considered individually or in combination, such as:

- The nature of the assurance engagement.
- How long the individual has been a member of the assurance team, the individual's seniority on the team, and the nature of the roles performed, including if such a relationship existed while the individual was at a prior firm.
- The extent to which the work of the individual is directed, reviewed and supervised by more senior personnel.
- The extent to which the individual, due to the individual's seniority, has the ability to influence the outcome of the assurance engagement, for example, by making key decisions or directing the work of other members of the engagement team.
- The closeness of the individual's personal relationship with the assurance client or, if relevant, senior management.
- The nature, frequency and extent of interaction between the individual and the assurance client.
- Whether the nature or complexity of the subject matter or subject matter information has changed.
- Whether there have been any recent changes in the individual or individuals who are the responsible party or, if relevant, senior management.

291.139~~7C~~ The combination of two or more factors may increase or reduce the significance of the threats. For example, familiarity threats created over time by the increasingly close relationship between an individual and the assurance client would be reduced by the departure of the person who is the responsible party and the start of a new relationship.

291.14037D The significance of any threats shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards in relation to a specific engagement include:

- Rotating the individual off the assurance team.
- Changing the role of the individual on the assurance team or the nature and extent of the tasks the individual performs.
- Having a professional accountant who is not a member of the assurance team review the work of the individual.
- Performing regular independent internal or external quality reviews of the engagement.
- Performing an engagement quality control review.

291.14137E If a firm decides that the threats are so significant that rotation of an individual is a necessary safeguard, the firm shall determine an appropriate period during which the individual shall not be a member of the engagement team, or provide quality control for the assurance engagement, or exert direct influence on the outcome of the assurance engagement. The period shall be of sufficient duration to allow the familiarity and self-interest threats to be eliminated or reduced to an acceptable level.

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**International
Ethics Standards
Board for Accountants®**

529 Fifth Avenue, New York, NY 10017
T + 1 (212) 286-9344 F +1 (212) 286-9570
www.ethicsboard.org

COMMENT SUMMARY
PROPOSED Interpretation of “Long Association of Senior Personnel With an Attest Client”

| Comment Letter | Feedback Highlights |
|---|---|
| CL 1 FICPA Accounting Principles & Auditing Standards Committee Support | <ul style="list-style-type: none"> The Committee agrees that a self-interest threat does not need to be included in this interpretation and that the effective date does not need to be extended. |
| CL 2 BDO Support with recommendations | <ul style="list-style-type: none"> BDO agrees that a self-interest threat does not need to be included in this interpretation. <p>Recommendations:</p> <ul style="list-style-type: none"> Recommends delay the effective to three months after the issuance in the Journal of Accountancy in order to educate partners and staff on the matter. Recommends the following edits to ET 1.267.010.03: “...However, a familiarity threat may be created when a member’s long-who is included inclusion among senior personnel of the attest engagement teams has a long association may create a familiarity threat with any of the following:...” |
| CL 3 New York State Society of CPAs (NYSSCPA) Support with recommendations | <ul style="list-style-type: none"> NYSSCPA supports PEEC’s efforts to provide specific guidance regarding the implementation of appropriate safeguards to reduce the threat to independence that may result from senior personnel having a long-term relationship with an attest client. <p>Recommendations:</p> <ul style="list-style-type: none"> ET 1.267.010.01 – NYSSCPA wants to expand the definition of senior personnel. NYSSCPA believes that any level of staff from the in-charge accountant upwards could meet that definition. NYSSCPA believes that since in-charge (senior or manager level) would have regular contact with the client and make decisions on sufficiency or appropriateness of evidence obtained, the extent of further testing required to address any issues that they need to be included in this interpretation. The partner or partner equivalent is ultimately in-charge but may not be aware of the decisions that were made during the engagement that could affect the outcome of the engagement. NYSSCPA recommends mirroring the approach of the IESBA ET 1.267.010 – NYSSCPA believes it would be helpful for the interpretation to provide specific examples regarding what constitutes a long association with an attest client that would cause an independence threat. |

| Comment Letter | Feedback Highlights |
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| | <ul style="list-style-type: none"> • ET 1.267.010.06e – NYSSCPA is looking for guidance regarding the appropriate length of the rotation period, the ability to rotate back onto the engagement, etc. NYSSCPA believes the only effective rotation would be a permanent rotation off the client. NYSSCPA believes if senior personnel rotates back onto the client then the familiarity threat would remain at the same unacceptable level. • ET 1.267.010.06a – NYSSCPA does not believe an adequate safeguard would be change the role of the senior personnel. NYSSCPA believes the only acceptable alternative role is relationship partner which would not be considered part of the engagement team. NYSSCPA recommends reconsidering the effectiveness of this safeguard. • Documentation – NYSSCPA proposes that the final interpretation include a requirement to document any identified threats resulting from a long association of senior personnel and documenting any safeguards implemented to do reduce that threat to an acceptable level. • Response to Question 1 – NYSSCPA believes that IESBA position should be maintained and thus include the self-interest threat in this interpretation. • Response to Question 2 – NYSSCPA recommends the effective date be delayed at least three months after being published in the Journal of Accountancy. NYSSCPA believes that sole or small-sized firms probably are not able to rotate senior personnel and medium sized firms might have issues convincing clients to rotate partners. NYSSCPA might also believe that it would be difficult to get a client to pay increased fees necessitated by an additional layer of engagement review. |
| <p>CL 4 AICPA Private Companies Practice Section (PCPS) through the Technical Issues Committee (TIC) <i>Does not Support</i></p> | <ul style="list-style-type: none"> • TIC believes that 0.300 already addresses the threats related to long association which would be a failure of the integrity and/or objectivity. • TIC also believes there are negative unintended consequences if this interpretation is issued: <ul style="list-style-type: none"> ○ TIC believes that there is an over-whelming majority of long associations is not a risk to independence since members conducts themselves and the engagement with integrity, objectivity, and professionalism. ○ TIC believes this interpretation would imply that partner rotation is best practice and would create a perceived risk is created when an actual risk does |

| Comment Letter | Feedback Highlights |
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| | <p>not exist. TIC believes this interpretation may negatively impact small practitioners who may not have other partners to rotate engagements while larger firms have multiple partners.</p> <ul style="list-style-type: none"> ○ TIC believe the inclusion of an Engagement Quality Control Review (EQCR) as a possible safeguard could result in a best practice even when the familiarity threat does not exist and the engagement does not warrant an EQCR. ○ TIC believes this interpretation could lead to additional documentation requirement surrounding the length of the association with the client which would not add to the quality of the engagement. <ul style="list-style-type: none"> ● TIC recommends that if PEEC believes that long associations with senior personnel needs to be addressed in the standards then additional consideration under the existing ethic sections on integrity and objectivity as not introduce any additional unintended documentation requirements. ● TIC believes that PEEC should consider the significant additional costs likely will be incurred as a result of this proposed interpretation and reconsidered if it is necessary. ● Response to Question 1 – TIC does not support this interpretation. TIC believes these threats are already included in the extant Code ● Response to Question 2 – TIC does not support this interpretation. If the interpretation is passed, TIC believes that the effective date should be delayed giving firms time to update their internal policies and procedures and understand the consequences of this interpretation. |
| <p>CL 5 Piercy Bowler Taylor & Kern (PBTk) <i>Does Not Support</i></p> | <ul style="list-style-type: none"> ● PTBK believes this interpretation is not necessary because long association is already addressed in the Conceptual Framework for Independence (1.210.010.14). ● PTBK does not believe the duration of the association that potentially poses a familiarity or any other threat to independence, rather the nature of the association and the behavior. <ul style="list-style-type: none"> ○ Egregious, inappropriate behavior such as that of a romantic relationship would clearly represent “a failure of integrity and/or objectivity” as mentioned in the TIC comment letter ○ Prof. Dennis Beresford, former Chair of FASB wrote regarding mandatory firm rotation that “little will be gained in the way of independence, objectivity, and skepticism with a good chance of a |

| Comment Letter | Feedback Highlights |
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| | <p>loss in quality.”</p> <ul style="list-style-type: none"> ○ The two SEC enforcement actions related “close personal relationship” were related to personal interactions not business related and close personal and romantic relationship between engagement partner and attest client’s CFO. This would require stronger quality control standards and not related to long association. ● PBTK believes that appropriately maintained long associations at a business/professional level actually enhances audit quality. ● PBTK concerned this interpretation could provide “ammunition to potential litigants and other adversaries to challenge the judgment of auditors regarding the efficacy of safeguards.” ● PTBK is concerned that in the future PEEC will adopt a mandatory partner or firm rotation requirement. ● PBTK says that the large majority of audit failures occur in the first 2 years of an audit engagement. PBTK believes that an auditor’s intuitiveness and effectiveness is inherently less in the early years of a client relationship and improves measurably and significantly, along with audit quality, with each successive year on any particular engagement. ● PBTK does not believe there is any evidence that partner or firm rotation would enhance an auditor’s independence. <ul style="list-style-type: none"> ○ PBTK referenced a study published by the American Accounting Association journal. The study concluded that “mandatory audit firm rotation could actually inhibit rather than encourage professional skepticism ‘to the detriment of audit effort and financial reporting quality.’” |
| <p>CL 6 Nevada State Board of Accountancy <i>Does Not Support</i></p> | <ul style="list-style-type: none"> ● Share the same concerns as PBTK and recommends total and permanent withdrawal of the proposed interpretation. ● Exposure draft proposal deeply grounded in several false premises and biases: <ul style="list-style-type: none"> ○ Long association viewed as a familiarity threat without regard to nature of the relationship and the behavior associated with it ○ CPA cannot be trusted to have strength of character to avoid over long periods of time inappropriate behavior that crosses the line between legitimate business/professional and a close person relationship ○ “fresh look” by rotating partners or firms would contribute to audit quality than the accumulation over time of intimate knowledge and |

| Comment Letter | Feedback Highlights |
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| | <p>understanding of client’s business and industry, the risks associated with it and the open communications based on years of trust with management and auditor.</p> <ul style="list-style-type: none"> • The interpretation will cause member to expend much time and energy justifying relationships that pose no threat. • Nevada State Board believes that rotation as a “safeguard” would sacrifice audit quality. • Nevada State Board believes that peer reviewers, litigants, regulators or other adversaries will put pressure on firms to challenge their good faith judgments regarding long association. • Nevada State Board concerned that this interpretation will push many smaller practice units out of the attest business. • Nevada State Board believes this interpretation would diminish audit quality and increase audit failure which occur mostly in the first two years of an audit engagement. • Nevada State Board believes that most audit failures are not a result of inadequate professional skepticism due to the familiarity threat but rather such things as undue fee or deadline pressure or disputes over accounting issue that lead to opinion shopping. |
| <p>CL 7 Garry Hutchison <i>Does Not Support</i></p> | <ul style="list-style-type: none"> • Garry Hutchison believes this might be a good rule for larger firms but it would not be productive to smaller firms and may be a barrier to smaller firms in the audit world. |

**AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS
 DIVISION OF PROFESSIONAL ETHICS
 PROFESSIONAL ETHICS EXECUTIVE COMMITTEE
 OPEN MEETING MINUTES
 JULY 25, 2017
 DENVER**

The Professional Ethics Executive Committee (Committee) held a duly called meeting on July 25, 2017. The meeting convened 9:00 a.m. and concluded at 2:41 p.m. on July 25th.

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| <p><u>Attendance:</u> Samuel L. Burke, Chair Coalter Baker Carlos Barrera Stanley Berman Chris Cahill Tom Campbell Robert E. Denham Anna Dourdourekas Janice Gray Greg Guin Brian S. Lynch</p> | <p>William Darrol Mann William McKeown Andrew Mintzer* Jarold Mittleider Steven Reed James Smolinski Laurie Tish Shelly Van Dyne Blake Wilson Lisa Snyder</p> <p><u>Not In Attendance:</u> Michael Brand</p> |
| <p><u>Staff:</u> James Brackens, VP - Ethics & Practice Quality Ellen Gorla, Sr. Manager Independence & Special Projects* Shelley Truman, Coordinator</p> | <p>Michael Jones, Assistant General Counsel Brandon Mercer, Technical Manager* April Sherman, Technical Manager* Shannon Ziemba, Technical Manager* James West, Technical Manager* Michele Craig, Technical Manager* Liese Faircloth, Technical Manager*</p> |
| <p><u>Guests:</u> Jeff Lewis, Chair, Independence/Behavioral Standards Subcommittee Ian Benjamin, Chair, Technical Standards Subcommittee Kelly Hnatt, Outside Counsel Nancy Miller, KPMG Dan Dustin, VP State Board Relations, NASBA Catherine Allen, Audit Conduct* George Dietz, PwC*</p> <p style="text-align: center;">*Via Phone</p> | |

1. Leases

Mr. Wilson presented this agenda item to the Committee. Mr. Wilson began by explaining that PEEC had made some suggestions at the previous meeting and came to some conclusions regarding materiality and the treatment of primary residence leases, but that the Task Force

discussed the conclusions and required clarification from PEEC on those issues. In addition, Mr. Wilson explained that the Task Force prepared a proposed revision at Agenda Item 1B for the PEEC's review. The Task Force requested that PEEC review the proposal, clarify its position on materiality and primary residences, and expose the resulting proposal to membership for comment.

Immediate Family

Mr. Wilson noted that at the previous meeting, PEEC requested that immediate family be included in the proposed standard. The Task Force discussed this request and noted that immediate family are included in the standard without reference, as a separate interpretation in the Code provides the specific exceptions to immediate family, and leases are not one of the exceptions. Thus, there is no reference to immediate family in paragraph .01, shown below. There was no further discussion on the topic, and the paragraph was not edited further:

.01 When a covered member enters into a lease with an attest client, self-interest, familiarity, and undue influence threats to the covered member's compliance with the "Independence Rule" [1.200.001] may exist.

Materiality

Mr. Wilson explained that at the previous meeting, there was a straw vote to apply the materiality safeguard to the firm and the attest client, but it was not clear to the Task Force what PEEC's view was on the breadth of the materiality safeguard in relation to individuals. The Task Force previously discussed the matter and agreed that individuals on the attest engagement and individuals in a position to influence the engagement created significant threats to independence, thus the Task Force's proposal prohibits leases that are material to an individual on the engagement team or an individual in a position to influence the attest engagement.

Mrs. Gorla noted that the drafted language is not clear that the individual on the attest engagement or in a position to influence has to be a party to the lease in order for the requirements to apply. PEEC edited the proposal to add clarity in this regard in .02c.

Mr. Wilson asked PEEC if they agreed with the Task Force approach to materiality, and PEEC members indicated that they agreed with the approach noted by Mr. Wilson, but made some clarification edits to the Task Force's proposal. The resulting paragraph .02 was approved as shown below; edits are changes to the Task Force proposal:

.02 ***If a covered member enters into a lease with an attest client during the period of the professional engagement, t***hreats to compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and could not be reduced to an acceptable level by the application of safeguards and independence would be impaired, unless all of the following safeguards are met during ***the that*** period of ~~the professional engagement:~~

- a. The lease is entered into on market terms and established at arm's length;
- b. All amounts are paid in accordance with the lease terms or provisions;
- c. The lease is not material to ***any of the following parties to the lease:***
 - i. the firm
 - ii. ***an*** individual participating on the attest engagement team
 - iii. ***an*** individual in a position to influence the attest engagement
 - iv. ***the attest client.***

Evaluation of Other Threats to Independence

Mr. Wilson presented paragraph .03 of the proposal to PEEC, which requires all leases to be further evaluated for any threats to independence that are not addressed by paragraph .02. Mr. Wilson requested that PEEC review the list of factors to consider in the paragraph and provide feedback or edits. Members noted that factor “e” regarding use of a third party to negotiate the lease really does not impact the threat to independence, and did not believe it added or removed anything from the proposal, so the Committee agreed to delete factor e and ask a question in the exposure draft regarding any other factors that should be included. The changes to the Task Force’s proposal are as follows:

- .03 If the covered member meets the safeguards in paragraph .02 above, as applicable, the covered member should evaluate the significance of any other *threats* to determine if the *threats* are at an *acceptable level*. If the covered member determines that *threats* are not at an *acceptable level*, he or she should apply additional safeguards to eliminate or reduce the threats to an acceptable level. If no safeguards are available to eliminate or reduce threats to an acceptable level, independence would be impaired. The significance of the threats will depend on factors such as the following:
 - a. The role of the covered member on the attest engagement and/or with the firm;
 - b. Materiality of the lease to the covered member other than those covered members identified in paragraph .02 above;
 - c. Whether multiple leases are entered into with the attest client, and if so, the aggregate materiality of those leases to the covered member and/or the attest client;
 - d. The extent to which the lease will be subject to attest procedures or financial statements disclosures; and
 - e. ~~The extents to which the covered member and/or attest client utilize third party service providers to conduct leasing activities on the covered member’s or attest client’s own behalf.~~

Permitted or Grandfathered Leases

Mr. Wilson presented paragraph .04 of the proposal, which permitted certain leases that were entered prior to independence being required or prior to a transaction such as an acquisition subjecting the lease to the Independence rule. Under the Task Force’s proposal, the lease would also not be required to be entered into on market terms at arm’s length, as the lease was entered into prior to independence being required. The Task Force acknowledged that this was inconsistent with loans in that loans entered into prior to independence being required are required to be on normal terms and conditions, but that the Task Force did not necessarily agree that leases would be able to be renegotiated at arm’s length at the time it is needed for independence purposes. A majority of PEEC members did not agree with the inconsistency with the loans provisions, and the PEEC added the requirement that the lease be entered into on market terms at arm’s length even if entered into prior to independence being required. Additionally, to be clear that materiality is not part of the conditions at paragraph .04, the proposal was revised to explicitly state that the conditions are irrespective of materiality. Some members had concerns that leases material to the attest client may not be addressed in paragraph .04. It was noted that materiality is only part of the loans provisions as it relates to collateral and that if materiality is a condition, there may be no use of paragraph .04 as the requirements would be the same for any lease. PEEC instructed staff to include a question in

the exposure draft for membership pointing out any other differences between paragraph .04 and the loans provisions and asking whether the differences are appropriate, and if there are any other situations that may need similar treatment. The Committee made edits to the proposal resulting in the following paragraph:

Grandfathered Leases

- .04 **Irrespective of materiality,** t Threats to compliance with the “Independence Rule” would be at an acceptable level and independence would not be impaired provided that, **the lease is entered into on market terms and established at arm’s length and** during the period of professional engagement, all amounts are paid in accordance with the lease terms and provisions, the terms do not change in any manner not provided for in the original lease, and any of the following **conditions safeguards** are met:
- a. The covered member entered into the lease with the attest client prior to becoming a covered member with respect to the attest client;
 - b. The covered member entered into the lease with a counterparty for which independence was not required, and that counterparty to the lease later becomes, acquires, or is acquired by an attest client;
 - c. The attest client entered into the lease with a counterparty which was not required to be independent of the attest client, and that counterparty to the lease later acquires or is acquired by the covered member.
 - d. The lease existed prior to **December 15, 2019** and the lease was permitted under the preexisting requirements of the Independence rule and its interpretations.

Automatic renewals provided for in the original lease are not considered changes in terms for purposes of this interpretation.

Primary Residence Leases

Mr. Wilson noted that the Task Force included options in the agenda for paragraph .05 regarding primary residence leases. The Task Force was in favor of the conditions in the proposal but requested that PEEC finalize its position and select the best option for addressing primary residence leases. After brief discussion, the Committee determined that the requirements for primary residence leases should be similar to those in paragraph .04, which are also similar to the home mortgage grandfathering provisions. It was pointed out that if the conditions for primary residences are the same as those for permitted leases addressed by paragraph .04, there may not be a need to have paragraph .05. However, PEEC members indicated that primary residence leases needed to be addressed in the proposal, as members and the public may not otherwise realize that primary residence leases are subject to the interpretation. Further, PEEC agreed that the paragraph should explicitly indicate that materiality is not a condition for those leases if they meet the other requirements contained in paragraph .04. To close the discussion, Mrs. Gorla made edits to the proposal which were approved by the PEEC below:

Covered Member Leases Primary Residence from Attest Client

- .05 **Irrespective of materiality,** if a covered member leases **his or her** ~~the covered member’s~~ primary residence from a lessor attest client, threats to compliance with the “Independence Rule” would be at an acceptable level and independence would

not be impaired, provided ***the member complies with the provisions in paragraph .04.:***

- a. ~~the ***conditions*** safeguards in paragraph .04 are met, ***OR*** [the lease is entered into on market terms established at arm's length (if entered into during the period of professional engagement),~~
- b. ~~all amounts are paid in accordance with the lease terms and provisions during the period of professional engagement,~~
- c. ~~[and the lease meets the criteria of an operating lease or a short term lease as defined by GAAP]~~

Effective Date

Mr. Wilson noted that the Task Force was not against an effective date that was concurrent with the FASB Update, but PEEC members noted concern that there may be additional tracking systems or procedures to be implemented by firms to comply with this proposal as well as the FASB Update. The Committee agreed to recommend an effective date similar to the FASB Update (periods beginning after December 15, 2019), but requested that staff include a question in the exposure draft regarding whether the effective date is allows time for implementing systems and procedures to track data and comply with the proposal.

After making edits to the proposal during the discussion, it was moved, seconded, and unanimously passed to expose the proposal as edited to membership for comment. The comment period should be sixty days and should include the questions for membership requested by PEEC above.

2. Information Technology and Cloud Services

Hosting Services

Ms. VanDyne explained that at the May 2016 meeting, the Committee decided not to expose for comment an addition to the Scope and Applicability of Nonattest Services” interpretation that would explain that threats to independence would not be considered significant solely because a member provides a nonattest service that does not impair independence through a cloud-based solution. Instead, the Committee recommended that the Task Force discuss if additional guidance was necessary once the Hosting Services interpretation is adopted.

Ms. VanDyne explained that the Task Force believes that the [Hosting Services](#) interpretation provides sufficient guidance (in the form of examples of activities that are not considered hosting services) for members to conclude that providing nonattest services through a cloud based solution does not by itself impair independence. As such, the Task Force recommends that the issue be monitored and a FAQ be issued only if it necessary. The Committee was supportive of this recommendation.

Information Systems Services

Ms. VanDyne went on to explain that at the last meeting there was some confusion with how the interpretation was organized and what could be done with a system developed by the firm as opposed to a commercial off the shelf system. She explained that the Task Force re-organized the introduction of the interpretation in an effort to help clarify.

Ms. VanDyne explained that the [Information Systems Design, Implementation, or Integration](#) interpretation concludes that independence would be impaired when a member makes other than insignificant modifications to source code underlying an attest client’s existing financial

information system. However, the Task Force members don't believe their firms use the provision except when evaluating the impact to independence when the firm inadvertently modifies source code. Ms. VanDyne explained that Staff reached out to the PCPS Technical Issues Committee (TIC) to see if their firms use the provision and if not, do they believe that the guidance in the [Breach of an Independence Interpretation](#) would provide enough guidance. Overall the feedback received from TIC members was that they wouldn't touch the source code. The PEEC agreed they would not be concerned eliminating the insignificant modifications provision.

3. **Client**

Mr. Mintzer provided the Committee with an overview of the comment letters received from the Client and Attest Client Exposure Draft. He explained that one significant issue raised related to whether distinguishing the engaging entity from the subject entity in the definition of client could result in challenges to members who are retained to provide litigation services by an attorney for their client. An example given was a member who was hired directly by an attorney to perform services for the attorney's client. The attorney engages the member versus the attorney's underlying client in order to extend the attorney's work product privilege to the work to be performed by the member. Currently a member would have the attorney sign the engagement letter and the subject entity signs the same engagement letter acknowledging that the both parties are aware and agree to the engagement. The concern raised was if the client definition is changed as exposed, the member may need to have separate engagement letters and the terms of the engagement with each client would be different due to the differences in privilege.

Mr Mintzer explained to the Committee that the Task Force discussed this issue at length and the intention was to clarify that if the engaging entity and the subject entity are different then you are two separate clients and not one "super client". Based on the feedback received, the Task Force recommended added the phrase "while there is only one engagement" to the client definition. The Task Force believed the addition of this phrase would alleviate the concerns regarding separate clients but still only one engagement, so members can continue to have one engagement letter. The Committee agreed after some discussion that adding the phrase "while there is only one engagement" would alleviate the issue raised by commenters to the Exposure Draft especially related to privilege.

Mr. Mintzer explained that there was a comment related to the attest client definition and editing the following wording "*need not be independent of the engaging entity except as may be required by the "Client Affiliate" interpretation [1.224.010]*". The commenter believed that there should be an affirmative statement and did not like the phrase "need not be independent". The Committee agreed with this comment but requested some further edits from the Task Force recommendation, and after some discussion decided on the following phrase "*should refer to the "Client Affiliate" interpretation [1.224.010] to determine if the engaging entity is an affiliate for which the member should be independent.*"

Mr. Mintzer explained a few other clarifying edits based on comments received from the Exposure Draft. The Committee agreed to all the clarifying edits.

It was moved, seconded and agreed to adopt the proposals as revised by a vote of 15 to 1 against with 2 abstentions, effective the last day of the month the changes are published in the Journal of Accountancy.

4. **IESBA Update**

Ms. Snyder provided an update of the IESBA's current projects.

5. **State Tax Tribunals**

The Committee agreed the incorporation of Staff's frequently asked question and answer would provide helpful guidance to members.

6. **Committee Project Agenda**

This item was on the agenda for informational purposes only.

7. **Minutes of the Professional Ethics Executive Committee Open Meeting**

It was moved, seconded and unanimously agreed to adopt the minutes from the May 2017 open meeting.