



# PROFESSIONAL ETHICS EXECUTIVE COMMITTEE

Open Meeting Agenda

**July 25 – 26, 2017**  
**Denver, Colorado**



**AICPA Professional Ethics Executive Committee  
Open Agenda  
July 25-26, 2017  
Denver**

July 25 <sup>th</sup>	<i>Open Meeting Begins</i>	
9:00 a.m. – 10:30 a.m.	<b>Leases</b> Mr. Wilson and Mr. Mercer will seek the Committee’s approval to expose a revised interpretation for comment.	<b>Agenda Item 1A Agenda Item 1B Agenda Item 1C Agenda Item 1D</b>
10:30 a.m. – 11:00 a.m.	<b>AM Break</b>	
11:00 a.m. - Noon	<b>Information Technology and Cloud Services</b> Ms. VanDyne and Ms. Gorla will seek the Committee’s feedback on the revised Information Systems Design, Implementation or Integration interpretation.	<b>Agenda Item 2A Agenda Item 2B</b>
Noon – 1:00 p.m.	<b>Lunch</b>	
1:00 p.m. – 2:30 p.m.	<b>Client</b> Mr. Mintzer and Ms. Ziembra will seek the Committee’s approval to adopt the proposals.	<b>Agenda Item 3A Agenda Item 3B Agenda Item 3C Agenda Item 3D</b>
2:30 p.m. – 2:45 p.m.	<b>IESBA Update</b> Ms. Snyder will update the Committee on the June and July meetings of the IESBA.	
2:45 p.m. – 3:00 p.m.	<b>State Tax Tribunals</b> Ms. Gorla will seek the Committee’s feedback on a new Frequently Asked Question.	<b>Agenda Item 4</b>
	<i>Open Meeting Concludes</i>	
Informational Purposes Only	<b>Outstanding Exposure Drafts</b> ❖ External Link - <a href="#">SLG Exposure Draft</a> ❖ External Link - <a href="#">Long Association Exposure Draft</a>	
Informational Purposes Only	<b>Minutes of the Professional Ethics Executive Committee Open Meeting</b> The Committee approved the minutes from the May 2017 meeting via email. ❖ External Link - <a href="#">May 2017 Minutes</a>	
Informational Purposes Only	<b>Committee Project Agenda</b> ❖ External Link - <a href="#">Project Agenda</a>	
	<b>Future Meeting Dates</b> • November 28-29, 2017 - Nashville • February 13-14, 2018 - TBD	

## **Leases Task Force**

### **Task Force Members**

Blake Wilson (Chair), Bill Mann, Alan Gittelson, David East, Nancy Miller, Chris Cahill  
Staff: Brandon Mercer

### **Task Force Charge**

Revise the independence guidance based upon the revised accounting standards on leases issued by the Financial Accounting Standards Board (FASB).

### **Reason for Agenda Item**

The Task Force held two conference calls in June 2017 to discuss feedback received from the May 2017 meeting PEEC and to prepare an updated proposal. The purpose of this agenda item is to update PEEC on the Task Force's discussions, obtain additional feedback, and present a proposed standard to PEEC for consideration and possible exposure to membership.

### **Summary of Issues**

#### Structure of the Proposal

The proposed standard can be viewed at **Agenda Item 1B**. The approach contemplated by the proposed standard is that when a covered member enters into a lease with an attest client during the period of professional engagement, independence will be impaired unless certain safeguards are met (paragraph .02). Once those safeguards are met, the proposal requires a conceptual framework approach to any other threats caused by the lease(s), which may require additional safeguards. Examples of factors for members to consider in the evaluation are included in the proposal in paragraph .03.

When a covered member and/or attest client entered into the lease outside the period of professional engagement, the proposal provides relief from the requirement that the lease be on market terms established at arm's length, and does not apply a materiality safeguard to such leases. Amounts must be paid in accordance with the lease terms and the terms may not change in any manner not provided for in the original lease. The premise for this is that the lease was entered at a time when the independence rule was not applicable or when either the covered member or attest client was not counterparty to the lease, thus mitigating the risk of entering the lease when independence is required. Such leases include:

- Leases entered into by either the covered member or the attest client prior to the lease being subject to the Independence rule (i.e. prior to the party being an attest client);
- Leases that exist and become subject to the independence rule due to an acquisition by/of the covered member or the attest client;
- Leases that a member and attest client enter into prior to the member becoming a covered member with respect to an attest client; and
- Leases that were permitted operating leases at the effective date of the proposed standard (transition provision).

The requirements of paragraph .04 address the leases listed above. These requirements are similar to the grandfathering provisions of the Loans and Leases with Lending Institutions Interpretation [1.260.020] (See **Agenda Item 1D**), in that leases entered prior to independence being required or prior to the member becoming a covered member are permitted. In addition, the permitted leases must be kept current and the terms cannot change.

Paragraph .05 addresses primary residences. The Task Force requests PEEC input on the breadth of the proposed primary residence exemption later in this agenda.

#### Immediate Family

At the May 2017 PEEC meeting, the Committee requested that a covered member's immediate family be included in the requirements of the proposal. The Task Force initially agreed, but it was later noted that the existing provisions of 1.270.010 would apply; those provisions stipulate that the Independence Rule applies to the covered member's immediate family except in certain interpretations in the Independence Rule. The leases standard is not an exception to the immediate family requirements, therefore immediate family would be subject to the proposed leases standard regardless of whether it is specifically mentioned. The Task Force's proposal does not include any reference to the covered member's immediate family for this reason. The resulting paragraph .02 is as follows:

*.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 – Application to Individuals

The PEEC previously voted in a straw poll to apply the materiality safeguard to firm and the attest client, concluding that a lease material to either party would impair independence (paragraph .02). However, the PEEC did not specifically vote or have substantive discussion on whether the materiality requirements should only apply to individuals on the engagement team and individuals in a position to influence the attest engagement. One member noted that materiality should generally not extend to individuals, and it was also noted that individuals can be isolated from the engagement as a safeguard. However, it was not clear to the Task Force that PEEC intended to allow material leases between the attest client and members of the engagement team or chain of command. The Task Force position is that a lease that is material to a member of the engagement team or an individual in a position to influence the attest engagement creates significant threats and impairs independence. Under this approach, staff members can be removed from the engagement team to meet the materiality safeguard, but it may be more challenging to isolate individuals in the chain of command from the ability to influence the engagement due to the authority of the role. The resulting proposed paragraph .02 is as follows:

*.02 Threats to compliance with the "Independence Rule" 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 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 the firm, an individual participating on the attest engagement team, or an individual in a position to influence the attest engagement; and*
- d. *The lease is not material to the attest client.*

A visual aid illustrating the impact of the materiality safeguard can be viewed at **Agenda Item 1C**.

**Does PEEC agree with the contents in paragraph .02, specifically the breadth and application of the materiality safeguard in .02c to certain individuals only (members of the engagement team and individuals in a position to influence the attest engagement)? If not, to which specific individuals does PEEC think the materiality safeguard should apply?**

#### Evaluation of Threats Paragraph

As noted above, if a lease is permitted by paragraph .02, the covered member should evaluate any other threats caused by the lease and apply safeguards if necessary. The Task Force reviewed the factors included in paragraph .03 regarding evaluation of other threats. After applying the revisions suggested by PEEC, the Task Force determined that some factors were no longer necessary, because the factors were already included in the safeguards of paragraph .02 in a way that the factor is no longer relevant for additional evaluation. For example, materiality to the attest client would not be evaluated under .03 because if the lease is material to the attest client, it would already impair independence under .02, and .03 would not be applicable. The Task Force requests that PEEC review the remaining factors and approve their inclusion in the proposal. The proposed paragraph .03 is 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.*

<b>Does PEEC agree with the contents of paragraph .03 and the factors for evaluation?</b>
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Permitted or "Grandfathered" Leases

*Permitted Leases other than Primary Residence Leases*

As previously mentioned, certain leases are permitted if they meet the requirements of paragraphs .04 - .05, which are similar to the grandfathering requirements for certain permitted loans (see **Agenda Item 1D**):

- The lease payments must be paid on accordance with the terms of the lease;
- The terms may not change in any manner not provided for in the original lease;
- The lease was entered into at a time when the Independence Rule was not applicable to the lease. For example, prior to the member becoming a covered member, prior to the attest client becoming the attest client, or prior to any acquisition or transaction involving the lessor/lessee that renders the lease relationship subject to the Independence Rule. The safeguards refer to the lessor/lessee as "counterparty" to the lease.

The safeguards in paragraph .04 are intended to address situations where the lease may have been entered into prior to the Independence Rule being applicable to the lease. PEEC has previously indicated that a significant risk of a lease is the entry into the lease. The approach is that if the lease is entered into outside the period of professional engagement, the lease inception would not have been subject to the Independence rule, thus relief is granted from the requirement that terms be established at arm's length or on market terms, unless the terms change during the period of professional engagement. If the terms change during the period of professional engagement, the lease is subject to the same requirements as any newly entered lease, including materiality and markets terms established at arm's length.

The paragraph also explains that automatic renewals provided for in the original lease agreement are not considered changes in lease terms for purposes of the paragraph. Automatic renewals include, for example, lease provisions that require no action on the part of the lessee or lessor in order for the lease to renew at a previously determined rate or term. The resulting paragraph .04 is as follows:

*.04 Threats to compliance with the "Independence Rule" would be at an acceptable level and independence would not be impaired provided that, 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 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 [the effective date of this interpretation] 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.*

<b>Does PEEC agree with the contents and approach of paragraph .04?</b>
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*Primary Residence Leases Exception*

At the July 2017 PEEC meeting, the Committee agreed by straw vote of 15-0-3 to address primary residences in a separate paragraph and apply requirements similar to those for home mortgages in the Loans and Leases Interpretation [1.260.020]. Under the home mortgage provisions, loans must have been entered under normal procedures and requirements of the lending institution, must be kept current at all times, and generally must have been entered at a certain time prior to the member becoming a covered member or independence being required. Covered members are not permitted to obtain a new home mortgage from a lending institution attest client during the period of professional engagement. The home mortgage provisions can be viewed at **Agenda Item 1D**.

Concerns raised by Task Force members and staff regarding the home mortgage requirements included the following:

- Under the extant Code, most newly entered primary residence leases are permissible as they qualify as operating leases. Mirroring the requirements of the home mortgage provisions in the Code would be more restrictive going forward with regard to primary residence leases, and may disallow leases that would be permissible under the extant Code as operating leases.
- Some expressed concern that failing to apply the home mortgage safeguards would allow certain newly entered leasing agreements that may carry appearance concerns, such as a newly entered material primary residence lease between an engagement partner or individual in a position to influence the engagement and an attest client.
- Some thought that the only requirement that should be applied to primary residence leases is that they be kept current at all times during the period of professional engagement.

- Some questioned the need for paragraph .05 if new primary residence leases are not permitted, as the requirements would be the same as other leases.

If PEEC does not wish to continue the current typical treatment of primary residence operating leases, and treat such leases similar to a home mortgage, the grandfathering provisions of paragraph .04 reflect the similar safeguards for those types of leases, and could be referenced in paragraph .05 as shown below. Note that these requirements would generally be more restrictive on primary residence leases going forward by prohibiting leases that are currently permitted, as discussed above. Materiality would not be a required safeguard for primary residence leases:

*.05 Threats to compliance with the "Independence Rule" would be at an acceptable level and independence would not be impaired, if a covered member leases the covered member's primary residence from a lessor attest client, provided [the safeguards in paragraph .04 are met].*

Alternatively, if PEEC agrees with this approach, PEEC could remove paragraph .05 altogether as it does not present any additional safeguards or threats, and primary residence leases would already be addressed by paragraphs .01-.04.

If PEEC wishes to continue to permit primary residence leases that otherwise qualify as operating leases (or short term leases under the FASB update), the PEEC could limit the required safeguards for primary residence leases to market terms established at arm's length and payments made in accordance with the lease terms. Unless PEEC wishes to avoid any reference to operating leases as it has throughout the proposed standard, PEEC could make an exception to the non-GAAP approach for primary residence leases, and permit primary residence leases that meet the criteria of an operating lease or a short term lease under GAAP (see text in [ ] below). This approach would essentially continue the current treatment of most primary residence leases, and would not contain a materiality safeguard. Such guidance could be drafted as follows:

*.05 Threats to compliance with the "Independence Rule" would be at an acceptable level and independence would not be impaired, if a covered member leases the covered member's primary residence from a lessor attest client, provided the lease is entered into on market terms established at arm's length (if entered into during the period of professional engagement), all amounts are paid in accordance with the lease terms and provisions during the period of professional engagement, [and the lease meets the criteria of an operating lease or a short term lease as defined by GAAP].*

**Does PEEC continue to agree with treating primary residence leases similar to home loans, and if so, are the safeguards in paragraph .04 appropriate? If so, does PEEC wish to remove paragraph .05? If not, does PEEC prefer to continue the extant treatment of primary residence leases, and with or without reference to GAAP categorization?**

**Effective Date**

The FASB Update is effective for fiscal years beginning after December 15, 2018 for public companies and December 15, 2019 for private companies. The Task Force sees no reason to deviate from the private company effective date, with early adoption permitted.

**Action Needed**

The Task Force requests that PEEC determine its positions regarding the issues in this agenda and revise the proposal accordingly. If PEEC is satisfied with the approach and revisions, the Task Force requests exposure of the proposal to membership for comment, specifically requesting comments on the issues noted in this agenda.

**Communications Plan**

If approved for exposure, the Exposure Draft will be distributed through normal distribution channels.

**Materials Presented**

**Agenda Item 1B** Proposed Revisions to the AICPA Code

**Agenda Item 1C** Visual Aid – Breadth of Materiality Safeguard

**Agenda Item 1D** Home Mortgages Provisions in AICPA Code

**Leases Task Force  
Proposed Revisions to the AICPA Code**

Final Version (“Clean” version)

**1.260.040 Leases**

**.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.

**.02** Threats to compliance with the “Independence Rule” 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 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 the firm, an individual participating on the attest engagement team, or an individual in a position to influence the attest engagement; and
- d. The lease is not material to the attest client.

**.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.

**.04** Threats to compliance with the "Independence Rule" would be at an acceptable level and independence would not be impaired provided that, 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 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 [the effective date of this interpretation] 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.

**.05** Threats to compliance with the "Independence Rule" would be at an acceptable level and independence would not be impaired, if a covered member leases the covered member's primary residence from a lessor attest client, provided [the 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), all amounts are paid in accordance with the lease terms and provisions during the period of professional engagement, [and the lease meets the criteria of an operating lease or a short term lease as defined by GAAP]]

**.06** This interpretation excludes leases addressed by [paragraph .04](#) of the "Loans and Leases with Lending Institutions" interpretation [1.260.020] of the "Independence Rule" [1.200.001].

**.07** Paragraphs .01 - .06 are effective **MONTH DAY, YEAR**, with early implementation allowed.

Markup Version (from extant Code)

Deletions are struck through, additions are **bold underlined**.

## **1.260.040 Leases**

**.01 When** ~~If a covered member enters into a leasing agreement (as described in GAAP) with an attest client during the period of the professional engagement, the self-interest, familiarity, and undue influence threats to the covered member's compliance with the "Independence Rule" [1.200.001] may exist.~~ would be at an acceptable level and independence would not be impaired if all the following safeguards are met:

- ~~a. The lease meets the criteria of an operating lease (as described in GAAP).~~
- ~~b. The terms and conditions set forth in the lease agreement are comparable with other leases of a similar nature.~~
- ~~c. All amounts are paid in accordance with the lease terms or provisions.~~

**.02 Threats to compliance with the "Independence Rule" 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 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 the firm, an individual participating on the attest engagement team, or an individual in a position to influence the attest engagement; and**
- d. The lease is not material to the attest client.**

**.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.

.04 Threats to compliance with the "Independence Rule" would be at an acceptable level and independence would not be impaired provided that, 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 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 [the effective date of this interpretation] 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.

.05 Threats to compliance with the "Independence Rule" would be at an acceptable level and independence would not be impaired, if a covered member leases the covered member's primary residence from a lessor attest client, provided [the 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), all amounts are paid in accordance with the lease terms and provisions during the period of professional engagement, [and the lease meets the criteria of an operating lease or a short term lease as defined by GAAP]]**

**.06** This **interpretation** paragraph excludes leases addressed by [paragraph .04](#) of the "Loans and Leases with Lending Institutions" interpretation [1.260.020] of the "Independence Rule" [1.200.001].

**.07 Paragraphs .01 - .06 are effective MONTH DAY, YEAR, with early implementation allowed.**

~~.02 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*, and *independence* would be *impaired*, if a *covered member* has a lease that meets the criteria of a capital lease (as described in GAAP). Accordingly, *independence* would be *impaired* because the lease would be considered to be a *loan* with an *attest client*. This paragraph excludes a lease that is in compliance with the "[Loans and Leases with Lending Institutions](#)" interpretation [1.260.020] of the "Independence Rule." [Prior reference: paragraphs .182-.183 of ET section 191]~~

**Leases Task Force**
**Breadth of Materiality Safeguard (paragraph .02)**

<b>Lessee is Attest Client and Lessor Is Covered Member or Entity Controlled by Covered Member</b>		
<b>Lessor</b>	<b>Lease Material to Lessee Attest Client [Paragraph .02d]</b>	<b>Lease Is Material to Lessor CM [Paragraph .02c]</b>
Firm	Impaired	Impaired
Attest engagement team member	Impaired	Impaired
Partner or partner equivalent in the office with engagement partner	Impaired	Evaluate under .03
Partner, partner equivalent or manager providing 10 hours of nonattest services to attest client in a fiscal year	Impaired	Evaluate under .03
Entity controlled by a covered member	Impaired	Evaluate under .03
Individual who evaluates the performance or recommends the compensation of the attest engagement partner.	Impaired	Impaired
Individual who directly supervises or manages the attest engagement partner, including all successively senior levels above that individual through the firm's chief executive.	Impaired	Impaired
Individual who consults with the attest engagement team regarding technical or industry-related issues specific to the attest engagement.	Impaired	Impaired
Individual who participates in or oversees, at all successively senior levels, quality control activities, including internal monitoring, with respect to the specific attest engagement.	Impaired	Impaired

<b>Lessor is Attest Client and Lessee is Covered Member or Entity Controlled by Covered Member</b>		
<b>Lessee</b>	<b>Lease Is Material to Lessee CM [Paragraph .02c]</b>	<b>Lease Material to Lessor Attest Client [Paragraph .02d]</b>
Firm	Impaired	Impaired
Attest engagement team member	Impaired	Impaired
Partner or partner equivalent in the office with engagement partner	Evaluate under .03	Impaired
Partner, partner equivalent or manager providing 10 hours of nonattest services to attest client in a fiscal year	Evaluate under .03	Impaired
Entity controlled by a covered member	Evaluate under .03	Impaired
Individual who evaluates the performance or recommends the compensation of the attest engagement partner.	Impaired unless only attest service is an AUP under the SSAES.	Impaired
Individual who directly supervises or manages the attest engagement partner, including all successively senior levels above that individual through the firm's chief executive.	Impaired	Impaired
Individual who consults with the attest engagement team regarding technical or industry-related issues specific to the attest engagement.	Impaired	Impaired
Individual who participates in or oversees, at all successively senior levels, quality control activities, including internal monitoring, with respect to the specific attest engagement.	Impaired unless only attest service is an AUP under the SSAES	Impaired

## Leases Task Force

## Home Mortgage Provisions in the AICPA Code

**1.260.020 Loans and Leases With Lending Institutions**

.01 The “Loans” interpretation [1.260.010] of the “Independence Rule” [1.200.001] provides that a self-interest *threat* would not be at an *acceptable level* and *independence* would be *impaired* if a *covered member* had a *loan* to or from an *attest client*, any officer or director of the *attest client*, or any individual owning 10 percent or more of the *attest client’s* outstanding equity securities or other ownership interests, except as provided for in this interpretation.

.02 *Home mortgages, secured loans, and immaterial unsecured loans.* However, *threats* would be at an *acceptable level* and *independence* would not be *impaired* if a *covered member* or his or her *immediate family* has an unsecured *loan* that is not material to the *covered member’s* net worth (that is, immaterial unsecured *loan*), a home mortgage, or a secured *loan* from a *lending institution attest client*, if all the following *safeguards* are met:

- a. The home mortgage, secured *loan*, or immaterial unsecured *loan* was obtained under the *lending institution’s* normal lending procedures, terms, and requirements. In determining when the home mortgage, secured *loan*, or immaterial unsecured *loan* was obtained, the date a commitment or line of credit is granted must be used, rather than the date a transaction closes or funds are obtained.
- b. The home mortgage, secured *loan*, or immaterial unsecured *loan* was obtained
  - i. from the *lending institution* prior to its becoming an *attest client*;
  - ii. from a *lending institution* for which *independence* was not required and was later sold to an *attest client*;
  - iii. after May 31, 2002, from a *lending institution attest client* by a borrower prior to his or her becoming a *covered member* with respect to that *attest client*, or
  - iv. prior to May 31, 2002 and the requirements of the loan transition provision in [www.aicpa.org/interestareas/professionaethics/community/downloadabledocuments/transistion%20periods.pdf](http://www.aicpa.org/interestareas/professionaethics/community/downloadabledocuments/transistion%20periods.pdf) are met.
- c. After becoming a *covered member*, any home mortgage, secured *loan*, or immaterial unsecured *loan* must be kept current regarding all terms at all

times, and the terms may not change in any manner not provided for in the original agreement. Examples of changed terms are a new or extended maturity date, a new interest rate or formula, revised collateral, and revised or waived covenants.

- d. The estimated fair value of the collateral for a home mortgage or other secured *loan* must equal or exceed the outstanding balance during the term of the home mortgage or other secured *loan*. If the estimated fair value of the collateral is less than the outstanding balance of the home mortgage or other secured *loan*, the portion that exceeds the estimated fair value of the collateral may not be material to the covered member's net worth.

**Information Technology and Cloud Services**

**Task Force Members:** Shelly VanDyne (Chair), Cathy Allen, Wendy Davis, Katie Jaeb, Anna Dourkourekas, Dan O'Daly John Ford, Mike Brand. 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**

Discuss revisions to the proposed revised Information Systems Services Interpretation and determine if a cloud services FAQ should be issued.

**Summary of Issues***Cloud Services*

At the May 2016 meeting, the Committee decided not to expose for comment the following addition to the Scope and Applicability of Nonattest Services" interpretation:

**.09 Activities Provided Through a Cloud Based Solution.** 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. When providing nonattest services [1.295] through a cloud-based solution, members are reminded to comply with all the requirements for the Nonattest Services subtopic including the "Hosting Services" interpretation [1.295.143]

Instead, once the Hosting Services interpretation is adopted, the Committee requested the Task Force discuss if guidance in the form of a FAQ would be helpful. 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 the FAQ be issued only if it necessary. The Task Force also requested Staff solicit feedback from the PCPS Technical Issues Committee on this recommendation and Staff will update the Committee on their feedback.

**Question:** Would threats to independence be considered significant solely because a member provides a permissible nonattest service through a cloud-based solution?

**Answer:** No, however, when providing nonattest services [1.295] through a cloud-based solution members are reminded to comply with all the requirements for the Nonattest Services subtopic including the "Hosting Services" interpretation [1.295.143].

**Question for The Committee**

1. Does the Committee believe the [Hosting Services](#) interpretation provides adequate guidance at this time?

*Design and Develop Information System That Is Unrelated to the Financial Statements or Accounting Records*

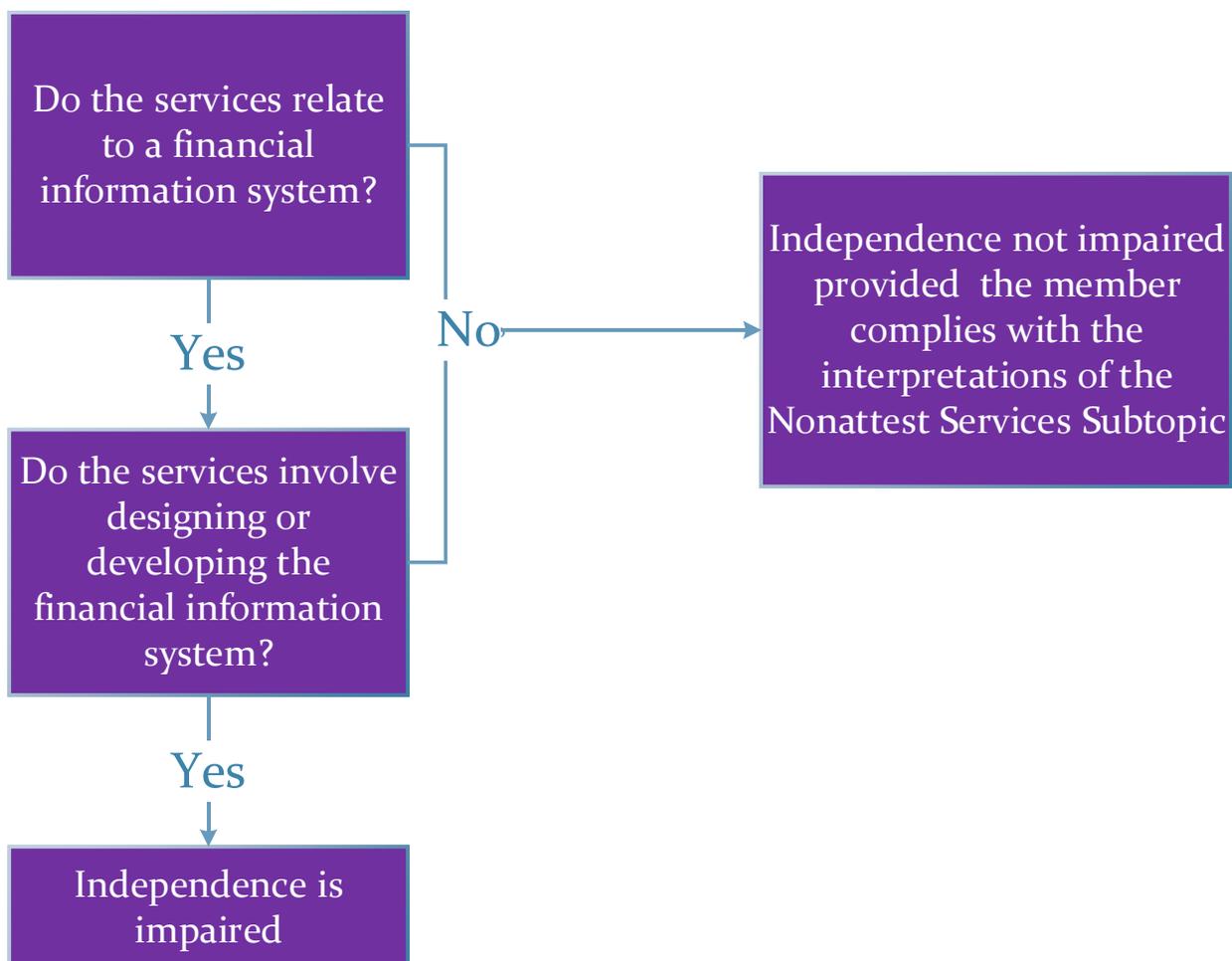
At the May 2017 meeting, the Committee noted that since a member can design and develop an information system that is unrelated to the attest client's financial statements or accounting

records when safeguards are applied, at a minimum, members should be able to install such non-COTs systems. Accordingly, the Task Force was asked to discuss whether there are other types of implementation services related to non-COTs software solutions that members could provide that do not impair independence.

The Task Force believes there are two critical criteria that need to be considered when determining whether independence is impaired when providing information systems services:

1. Do the services relate to the attest client's financial statements or accounting records (i.e., involve the attest client's financial information system)?
2. If they do, then do those services involve the member designing or developing the financial information system?

When the answer is "yes" to both of these questions, then independence would be impaired.



However, if the answer is "no" to either of these questions, then the Task Force believes the member may be able to provide the services without impairing independence when certain safeguards are applied. When the services relate to a financial information system but do not involve the member designing or developing the system, the Task Force believes the system

involved will likely be a commercial-off-the-shelf (COTS) software solution and so the focus of the remaining interpretation is on such COTS software solutions.

The Task Force also believes it is important to explain that when a member designs or develops a template that performs a discrete calculation such as a tax provision or depreciation calculation, such would not constitute designing or developing an information system and would not automatically impair independence. However, the template must be performing a service (e.g. calculation of tax provision) that the member would be permitted to perform under the independence rules (e.g., certain types of valuations would be problematic).

**Question for the Committee**

1. Does the Committee agree with the Task Force's recommendations?

*Insignificant Modifications to Source Code*

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.

The sense of the Task Force is that their firms don't use the provision except to determine if independence was impaired when the firm inadvertently modified source code. The Task Force asked Staff to reach out to the PCPS Technical Issues Committee (TIC) to see if their firms use the provision and if not, do they think if it was eliminated that the guidance in the [Breach of an Independence Interpretation](#) would provide enough guidance. Staff will report to the PEEC.

**Question for the Committee**

1. Should the provision be eliminated?

**Effective Date**

Does the Committee believe a delayed effective date would be helpful?

**Action Needed**

The Committee's feedback would be appreciated.

**Communication Plan**

TBD.

**Materials Presented**

**Agenda Item 2B** Proposed Revised Information Systems Services Interpretation

**Proposed Revised Information Systems Services Interpretation**

- .01 When a member provides services related to an attest client's information systems, self-review and management participation threats to the covered member's compliance with the "Independence Rule" [1.200.001] may exist.
- .02 When performing information systems services for an attest client that are not related to the financial statements or accounting records, 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.
- .03 When a member designs or develops an information system that relates to an attest client's financial statements or accounting records ("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.
- .04 If the financial information system 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 all the requirements of this interpretation and the **Nonattest Services** subtopic [1.295] of the Independence Rule [1.200.001] are met. For example, the member should comply with the requirements of the:
  - a. "Management Responsibilities" interpretation [1.295.030] including not accepting responsibility for designing, implementing, or maintaining internal control or for the management of an attest client's project.
  - b. "General Requirements for Performing Nonattest Services" interpretation [1.295.040] including that all significant assumptions and matters of judgment are determined or approved by the attest client, and the attest client is in a position to have an informed judgment on, and accepts responsibility for, the results of the service.
  - c. "Advisory Services" interpretation [1.295.1050] when providing advice or recommendations related to information system services.

**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 ready to run or to large scale, complex enterprise applications.
  - b. Designing and developing 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. Developing an information system entails creating software

code, for individual or multiple modules, and testing such code to confirm it is functioning as designed. 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. Accordingly, such services 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].

- c. Interface: 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 and may involve the performance of an end-to-end transaction or pass data from one system to another for reporting purposes.
- d. Placing into Production: means that the system is now available for use on a regular basis for its intended purpose.

### **Commercial-Off-The-Shelf Financial Information Systems *Implementing a Commercial-Off-The Shelf Financial Information System Software Solution***

- .06 Implementation services involve any activity after the design and development of an information system that a member is engaged to provide related to an attest client's information systems. For example, implementation can include activities such as configuring, testing and placing into production a system, and supporting activities such as end-user training, change management and organizational communications. It can also involve installing, integrating, customizing and performing data conversions necessary for implementing a COTS software solution.
- .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.

### ***Installing a Commercial-Off-The Shelf Financial Information System Software Solution***

- .08 Installing a COTS financial information system software solution means the initial loading of software on a computer and would normally refer to loading the software on 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.

### ***Configuring a Commercial-Off-The Shelf Financial Information System Software Solution***

- .10 Configuring a COTS financial information system software solution means selecting the software features, functionality options, and settings of the COTS software solution, that when selected 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.

### ***Customization of a Commercial-Off-The Shelf Financial Information System Software Solution***

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

### ***Integrating a Commercial-Off-The Shelf Financial Information System Software Solution***

- .14 Integrating a new COTS financial information system software solution means interfacing the new software solution to one or more legacy or other third party solutions or both. If the integration involves designing and developing software code that allows data to pass from one system to another, 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.
- .15 If, however, the member provides integration services that do not involve designing or developing software code, 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. For example, a member may use an Application Program Interface (API) developed by a third party to integrate a COTS software solution with an attest client’s financial information system provided the member does not design or develop additional software code so that the API will function as required by the

attest client or will only develop data mapping rules that will be used to match data to be moved between systems connected by the API.

### **Data Conversion Services Related to a Commercial-Off-The Shelf Financial Information System Software Solution**

- .16 Data conversion services for a new COTS financial information system software solution means revising the format of the legacy system’s data, as applicable, so that such data is compatible in structure to that of the new COTS software solution.
- .17 If a member designs or develops the code used to convert an attest client’s legacy financial information system’s data so that the new COTS software solution can effectively function when the data is loaded, 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.
- .18 An Application Program Interface (API) that is developed by a third party may be used to convert legacy system data so that it is compatible in structure to that of a new COTS financial information system software solution. To determine whether the use of the API would create threats to independence that would be at an acceptable level, the member should determine if the member will design or develop code for the API to work. If the member will not design or develop code for the API to work, or if the member will develop data mapping rules to match data to be moved between systems connected by an API, threats would be at an acceptable level.

### **Other Commercial-Off-The Shelf Financial Information Systems Services**

- .19 If the member applies the “[General Requirements for Performing Nonattest Services](#)” interpretation [1.295.040] of the “[Independence Rule](#)” [1.200.001], *threats* would be at an *acceptable level* and *independence* would not be *impaired* when the member performs
  - a. training or instruction on a new COTS financial statement related software solution
- .20 However, *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*, and *independence* would be *impaired*, if, for example, a member performs professional services that involve accepting responsibility for maintaining internal control or the management of, an attest client’s COTS financial information system. Examples of such services include
  - a.

Nonauthoritative questions and answers regarding information systems design, implementation, and integration services are available at <a href="http://www.aicpa.org/InterestAreas/ProfessionalEthics/Resources/Tools/DownloadableDocuments/NonattestServicesFAQs.pdf">www.aicpa.org/InterestAreas/ProfessionalEthics/Resources/Tools/DownloadableDocuments/NonattestServicesFAQs.pdf</a> .
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## **Definition of Client**

### **Task Force Members**

Andy Mintzer (Chair), Bob Denham, George Dietz, Gregory Guin, Brian Lynch, and Debra Hahn  
Staff: Shannon Ziemba and Ellen Gorla

### **Task Force Charge**

The Client Task Force (Task Force) is charged with determining what, if any revisions are necessary to the definition of client to conform to the organizational independence requirements in the GAO Yellow Book. Also, determine if criteria “a.” and the phrase “and, if different, the person or entity with respect to which professional services are performed” should remain in the definition.

### **Reason for Agenda Item**

To review comments received on the proposed definitions and interpretations during exposure and adopt final standards.

### **Summary of Issues**

#### *Client Definition*

There was one significant issue which was raised by TIC (outside of their comment letter), Grant Thornton (CL8), and PICPA (CL11). The issue surrounds unintended consequences of clarifying and distinguishing the engaging entity and subject entity in the client definition. The concern revolves around what are the members obligations to the subject entity when it is not also the engaging entity. Below are examples provided to illustrate their concerns:

- From TIC – In litigation support and internal investigations engagements (usually under SSCS 1), a member would be hired directly by an attorney as the engaging entity to perform services for his 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. 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.
  - TIC is concerned that if it is clearer stated that you could have two client could it lead the assumption that there are two separate engagements.
- From Grant Thornton (CL8) – In an engagement where more than one party signs an engagement letter, such as litigation services where the law firm, attorney and the underlying client all sign, would both the law firm and the underlying client be the “client” because of the unique contractual rights and obligations?
- From PICPA (CL11) – PICPA is concerned about potential additional liability and contractual issues that would result from designating the subject matter entity a client, such as having to obtain engagement letters from the subject entities. PICPA believes this

could expand the CPA's contractual obligations and liability without any benefit to the CPA as there are no fees associated with the presumed added responsibility.

- Another concern is by designating certain subject entities as a client could cause a conflict of interest.

The Task Force discussed these concerns at length and reached unanimous agreement that the intent of the exposed clarification of the definition was not to imply or create the existence of multiple engagements requiring multiple engagement letters and thus decided to further clarify the definition by adding the following phrase to the last sentence of the definition: "When the engaging entity and the subject entity are different, *while there is only one engagement*, they are separate clients."

The Task Force could not identify a situation where there would be more than one engagement and thus proposed the clarification as a statement of fact as opposed to the more open-ended phrasing of "while there *may* be only one engagement..."

The Task Force recommends the following additions from the Exposure Draft. The additions are highlighted in yellow.

**Client.** Any person or entity, other than the member's employer, that engages a member or member's firm to perform professional services (*engaging entity*) and **also, if different, the a** person or entity with respect to which **a member or member's firm performs** professional services (*subject entity*) ~~are performed~~. **When the engaging entity and the subject entity are different, while there is only one engagement, they are separate clients.** For purposes of this definition, the term employer does not include the following:

- a. ~~Person or entity engaged in public practice.~~
- b. ~~Federal, state, and local government or component unit thereof, provided that the member performing professional services with respect to the entity is~~
  - i. ~~directly elected by voters of the government or component unit thereof with respect to which professional services are performed;~~
  - ii. ~~an individual who is (1) appointed by a legislative body and (2) subject to removal by a legislative body; or~~
  - iii. ~~appointed by someone other than the legislative body, so long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body.~~

[Prior reference: paragraph .03 of ET section 92]

**See paragraph .03 of the "Simultaneous Employment or Association With an Attest Client" interpretation [1.275.005] for independence guidance related to a member in a government audit organization that performs an attest engagement with respect to the government entity.**

**Questions for PEEC:**

- 1. Can PEEC think of any unintended consequence of using the phrase “while there is only one engagement” instead of “while there may be only one engagement”? Is there any case where there may actually be more than one engagement?**
- 2. Does the PEEC agree that the addition of “while there is only one engagement” is clarifying change and not a substantive change?**

*Attest Client Definition*

The comments received regarding the edits to the attest client definition were all positive in nature. Everyone was supportive of including the reference to the Integrity and Objectivity Rule and Conflicts of Interest interpretation into the definition. Grant Thornton (CL8) did recommend edits to the wording related to the independence of the engaging entity. The Task Force agreed with their edit since the use of the phrase “need not be independent” may lead a member to a conclusion the Task Force does not want the reader to reach.

The Task Force recommends the following changes from the Exposure Draft. The changes are highlighted in yellow.

**Attest client.** ~~A client that engages a member to perform an attest engagement~~ or **A person or entity** with respect to which an attest engagement is performed.

***If the person or entity that engages a member or member’s firm to perform professional services (engaging entity) is not also the attest client, the member and the member’s firm (member) need not be independent of the engaging entity except as may be required by should refer to the “Client Affiliate” interpretation [1.224.010] to determine if the member needs to be independent of the engaging entity. However, because threats to the member’s compliance with the “Integrity and Objectivity Rule” [1.100.001] and the “Conflicts of Interest” interpretation [1.110.010] may still exist with respect to the engaging entity, members should comply with this rule and interpretation.***

See the “Client Affiliate” interpretation [1.224.010] for acquisitions and business combinations that involve a financial statement attest client.

***See paragraph .03 of the “Simultaneous Employment or Association With an Attest Client” interpretation [1.275.005] for independence guidance related to a member in a government audit organization that performs an attest engagement with respect to the government entity.***

*“Simultaneous Employment or Association With an Attest Client” interpretation*

There were no comments received that took issue with relocating the government exception to Simultaneous Employment interpretation. Therefore, the Task Force recommends no changes from the Exposure Draft.

### **1.275.005 Simultaneous Employment or Association With an Attest Client**

- .01 In this interpretation, “simultaneous employment or association with an attest client” is serving as a director, an officer, an employee, a promoter, an underwriter, a voting trustee, a trustee for any pension or profit-sharing trust of the *attest client*, or in any capacity equivalent to that of a member of management of an *client* during the period covered by the financial statements or the period of the professional engagement.
- .02 If a partner or professional employee of the member’s firm is simultaneously employed or associated with an attest client, familiarity, management participation, advocacy, or self-review threats to the member’s 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. Accordingly, independence would be impaired. [Prior reference: paragraph .02C of ET section 101]
- .03 However, *threats* will be at an *acceptable level* and *independence* will not be *impaired* **when either of the following situations exists:**
- a. ~~if a~~ **A** partner or professional employee of a firm serves as an adjunct faculty member of an educational institution that is an attest client of the firm, ~~provided that~~ **and** the partner or professional employee meets all of the following safeguards:
    - i. Does not hold a key position at the educational institution.
    - ii. Does not participate on the attest engagement team.
    - iii. Is not an individual in a position to influence the attest engagement.
    - iv. Is employed by the educational institution on a part-time and non-tenure basis.
    - v. Does not participate in any employee benefit plans sponsored by the educational institution, unless participation is required.
    - vi. Does not assume any management responsibilities or set policies for the educational institution Upon termination of employment, the partner or professional employee should comply with the requirements of the “Former Employment or Association With an Attest Client” interpretation [1.277.010] of the “Independence Rule” [1.200.001]. [Prior reference: paragraph .21 of ET section 101].
  - b. **A member in a government audit organization performs an attest engagement with respect to the government entity and the head of the government audit organization meets at least one of the following:**
    - i. **Is directly elected by voters of the government entity with respect to which attest engagements are performed.**
    - ii. **Is appointed by a legislative body and is subject to removal by a legislative body.**
    - iii. **Is appointed by someone other than the legislative body, as long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body.**

## 1.000 Introduction

- .01 Part 1 of the Code of Professional Conduct (the code) applies to members in public practice. Accordingly, when the term member is used in part 1 of the code, the requirements apply only to members in public practice. When a member in public practice is also a member in business (for example, serves as a member of an entity's board of directors), the member should also consult [part 2](#) of the code, which applies to a member in business.
- .02 Government auditors within a government audit organization who audit federal, state, or local governments or component units thereof, that are structurally located within the government audit organization, are considered in public practice with respect to those entities provided the head of the **government** audit organization **meets at least one of the following**: ~~meets one of the organizational structures described in [paragraph .07b\(i-iii\)](#) of the "Client" definition (0.400.07).~~
- a. Is directly elected by voters of the government entity with respect to which attest engagements are performed*
  - b. Is appointed by a legislative body and is subject to removal by a legislative body*
  - c. Is appointed by someone other than the legislative body, so long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body*

### 1.224.020 Entities Included in State and Local Government Financial Statements (in part)

(Paragraphs .01–.07 are unchanged.)

- .08 However, if a covered member or a covered member's immediate family holds a key position within the primary government during the period of the professional engagement or during the period covered by the financial statements, 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. Accordingly, the covered member's independence would be impaired. For purposes of this interpretation, a covered member and the covered member's immediate family would not be considered employed by the primary government **if the criteria in the Introduction of part 1 [1.000.02] exceptions provided for in [paragraph .07b](#) of the "Client" definition (0.400.07) were met.** [Prior reference: paragraph .12 of ET section 101]

#### Questions for PEEC:

1. Interpretation 1.275.005.03 says that threats are at an acceptable level and independence is not impaired if the government exception criteria are met. Interpretation 1.224.020.08 says that if the government exception criteria are met then the covered member would not be considered employed by the primary government. Both interpretations conclude that independence is not impaired if

**the government exception criteria are met. Does the PEEC believe these interpretations as written will lead the members to the same conclusion?**

### *Disclosing Information to Clients*

There were two comments by Grant Thornton (CL8) received related to this interpretation. One comment related to the explanation of the edits to the interpretation which stated there was “a presumption” that “there would be an agreement” between the parties and they were concerned that the presumption of an agreement would imply a legal contract and proper consent would not be required per IRS or other laws. The interpretation references that member should consider legal implications of such disclosures and IRS Circular 230 so no edits to the exposed interpretations are warranted. Grant Thornton’s other concern is the tax examples included. The Task Force believes the addition of saying that even though you may have two clients but there is only engagement should alleviate Grant Thornton’s concern.

The Task Force decided to delete sentence about not needing consent from either spouse to provide information since NASBA (CL9) were concerns about what information could be provided. NASBA’s had the following example, a Schedule K-1 is included in the joint tax return, the spouse should be given the Schedule K-1 but should not be given the associated underlying business tax return unless the spouse was a participant in the business and would normally receive the business tax return. The Task Force did not cause an unintended consequence by adding this language so it was decided to just keep the example.

The Task Force recommends the following deletion from the Exposure Draft. The deletion is highlighted in yellow.

#### 1.700.030 Disclosing Information to ~~Persons or Entities Associated With~~ Clients

~~.01~~ When a *member* is engaged **by either spouse** to prepare a married couple’s joint tax return, **the two** both spouses are considered to be **one** the member’s *client*, even if the member **deals exclusively with** was engaged by **one** spouse and deals exclusively with that spouse.

~~.02~~ Accordingly, ~~the member would not need consent from either spouse in order to provide information related to the couple’s joint tax return to the other spouse. For example,~~ if the married couple is undergoing a divorce and one spouse directs the member to withhold joint tax information from the other spouse, the member may provide the information to both spouses in compliance with the “[Confidential Client Information Rule](#)” [1.700.001], because both are the member’s client. The member should consider reviewing

- a. the legal implications of such disclosure with an attorney and
- b. responsibilities under any tax performance standards, such as Section 10.29 of IRS Circular 230. [Prior reference: paragraphs .031–.032 of ET section 391].

~~.02–03~~ **When a person or entity engages a member to perform professional services (engaging entity) for the benefit of another person or entity (beneficiary), the engaging entity and the beneficiary are considered two separate clients. Accordingly, the member should not disclose confidential client information of either client to the other without consent of the client whose confidential information is to be disclosed. For example, if a**

**company engages a member to perform personal tax services for the benefit of its** ~~If a member provides professional services to a company's executives request of the company, the member's disclosure of the executives' confidential client information to the company without the consent of the applicable executive would be a violation of the "Confidential Client Information Rule" [1.700.001] even if the company is not otherwise a client. [Prior reference: paragraphs .041-.042 of ET section 391]~~

#### *Other Interpretations Addressed in Exposure Drafts*

There were comments received related to some of the clarifying edits to other interpretations. Staff will only address the ones that were comments on. Any edits from the Exposure Draft are highlighted in yellow.

State of Tennessee's Department of Audit (CL3) wanted to include engagement materiality to criteria to consider when looking at Actual or Threatened Litigation. Staff concluded that looking at the definition of materiality is outside the scope of this Task Force. State of Tennessee's Department of Audit (CL3) also commented that the phrasing "other assets clients" could be confusion and recommended an edit which appear below in green bold double-strike through.

#### **1.290.010 Actual or Threatened Litigation (in part)**

.07 If threatened or actual litigation is unrelated to the performance of *an client's* attest engagement and is for an amount that is not material to the covered member's firm or the attest client, threats to the covered member's compliance with the "Independence Rule" [1.200.001] would be at an acceptable level, and independence would not be impaired. Such claims may arise, for example, out of immaterial disputes regarding billings for services, results of tax or management services advice, or similar matters.

.11 If only the underwriter or officers or directors of **the covered member's** other *attest* clients ~~of the covered member~~ file cross-claims against the covered member, threats to the covered member's compliance with the "Independence Rule" [1.200.001] would be at an acceptable level unless other circumstances create threats to compliance with the "Independence Rule."

Staff has prepared a comment letter summary that lists each comment and the Task Force's response to each comment (Agenda 3D).

#### **Action Needed:**

1. The Committee is asked to review the comment letter summary and Task Force responses. Edits made as a result of comments are highlighted in yellow.
2. The Committee is asked to approve the proposed definitions interpretations for adoption.

**Materials Presented**

Agenda 3A – This Agenda Item

Agenda 3B – Proposed definitions and interpretations

Agenda 3C – Proposed definitions and interpretations (clean version)

Agenda 3D – Comment Letter Summary

(Edits made to the exposed standard are highlighted)

**Client.** Any person or entity, other than the member's employer, that engages a member or member's firm to perform professional services (**engaging entity**) and **also**, if different, the ~~a~~ person or entity with respect to which **a member or member's firm performs** professional services (**subject entity**) are performed. **When the engaging entity and the subject entity are different, while there is only one engagement, they are separate clients.** For purposes of this definition, the term employer does not include the following:

- a. ~~Person or entity engaged in public practice.~~
- b. ~~Federal, state, and local government or component unit thereof, provided that the member performing professional services with respect to the entity is~~
  - i. ~~directly elected by voters of the government or component unit thereof with respect to which professional services are performed;~~
  - ii. ~~an individual who is (1) appointed by a legislative body and (2) subject to removal by a legislative body; or~~
  - iii. ~~appointed by someone other than the legislative body, so long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body.~~

[Prior reference: paragraph .03 of ET section 92]

**See paragraph .03 of the "Simultaneous Employment or Association With an Attest Client" interpretation [1.275.005] for independence guidance related to a member in a government audit organization that performs an attest engagement with respect to the government entity.**

**Attest client.** ~~A client that engages a member to perform an attest engagement or~~ **A person or entity** with respect to which an attest engagement is performed.

**If the person or entity that engages a member or member's firm to perform professional services (engaging entity) is not also the attest client, the member and the member's firm (member) need not be independent of the engaging entity except as may be required by should refer to the "Client Affiliate" interpretation [1.224.010] to determine if the member needs to be independent of the engaging entity. However, because threats to the member's compliance with the "Integrity and Objectivity Rule" [1.100.001] and the "Conflicts of Interest" interpretation [1.110.010] may still exist with respect to the engaging entity, members should comply with this rule and interpretation.**

See the "Client Affiliate" interpretation [1.224.010] for acquisitions and business combinations that involve a financial statement attest client.

**See paragraph .03 of the "Simultaneous Employment or Association With an Attest Client" interpretation [1.275.005] for independence guidance related to a member in a government**

**audit organization that performs an attest engagement with respect to the government entity.**

**1.275.005 Simultaneous Employment or Association With an Attest Client**

.01 In this interpretation, simultaneous employment or association with an attest client is serving as a director, an officer, an employee, a promoter, an underwriter, a voting trustee, a trustee for any pension or profit-sharing trust of the *attest client*, or in any capacity equivalent to that of a member of management of an *client* during the period covered by the financial statements or the period of the professional engagement.

.02 If a partner or professional employee of the member's firm is simultaneously employed or associated with an attest client, familiarity, management participation, advocacy, or self-review threats to the member's 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. Accordingly, independence would be impaired. [Prior reference: paragraph .02C of ET section 101]

.03 However, *threats* will be at an *acceptable level* and *independence* will not be *impaired* **when either of the following situations exists:**

a. ~~if a~~ **A** partner or professional employee of a firm serves as an adjunct faculty member of an educational institution that is an attest client of the firm, ~~provided that~~ **and** the partner or professional employee meets all of the following safeguards:

- i. Does not hold a key position at the educational institution.
- ii. Does not participate on the attest engagement team.
- iii. Is not an individual in a position to influence the attest engagement.
- iv. Is employed by the educational institution on a part-time and non-tenure basis.
- v. Does not participate in any employee benefit plans sponsored by the educational institution, unless participation is required.
- vi. Does not assume any management responsibilities or set policies for the educational institution. Upon termination of employment, the partner or professional employee should comply with the requirements of the "Former Employment or Association With an Attest Client" interpretation [1.277.010] of the "Independence Rule" [1.200.001]. [Prior reference: paragraph .21 of ET section 101].

**b. A member in a government audit organization performs an attest engagement with respect to the government entity and the head of the government audit organization meets at least one of the following:**

- i. Is directly elected by voters of the government entity with respect to which attest engagements are performed.**
- ii. Is appointed by a legislative body and is subject to removal by a legislative body.**

- iii. ***Is appointed by someone other than the legislative body, as long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body.***

### **1.000 Introduction**

.01 Part 1 of the Code of Professional Conduct (the code) applies to members in public practice. Accordingly, when the term member is used in part 1 of the code, the requirements apply only to members in public practice. When a member in public practice is also a member in business (for example, serves as a member of an entity's board of directors), the member should also consult [part 2](#) of the code, which applies to a member in business.

.02 Government auditors within a government audit organization who audit federal, state, or local governments or component units thereof, that are structurally located within the government audit organization, are considered in public practice with respect to those entities provided the head of the **government** audit organization **meets at least one of the following**: ~~meets one of the organizational structures described in [paragraph .07b\(i-iii\)](#) of the "Client" definition (0.400.07).~~

- a. ***Is directly elected by voters of the government entity with respect to which attest engagements are performed***
- b. ***Is appointed by a legislative body and is subject to removal by a legislative body***
- c. ***Is appointed by someone other than the legislative body, so long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body***

### **1.224.020 Entities Included in State and Local Government Financial Statements (in part)**

(Paragraphs .01-.07 are unchanged.)

.08 However, if a covered member or a covered member's immediate family holds a key position within the primary government during the period of the professional engagement or during the period covered by the financial statements, 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. Accordingly, the covered member's independence would be impaired. For purposes of this interpretation, a covered member and the covered member's immediate family would not be considered employed by the primary government **if the criteria in the Introduction of part 1 [1.000.02]** ~~exceptions provided for in [paragraph .07b](#) of the "Client" definition (0.400.07) were met.~~ [Prior reference: paragraph .12 of ET section 101]

### **1.400.200 Records Requests (in part)**

Terminology

**.01** The following terms are defined here solely for use with this interpretation:

- a. A client includes current and former *clients*.
- b. A member means the *member* or the *member's firm*.
- c. Client-provided records are accounting or other records, including hardcopy and electronic reproductions of such records, belonging to the client that were provided to the member by, or on behalf of, the client.
- d. Member-prepared records are accounting or other records that the member was not specifically engaged to prepare and that are not in the client's books and records or are otherwise not available to the client, thus rendering the client's financial information incomplete. Examples include adjusting, closing, combining, or consolidating journal entries (including computations supporting such entries) and supporting schedules and documents that the member proposed or prepared as part of an engagement (for example, an audit).
- e. Member's work products are deliverables set forth in the terms of the engagement, such as tax returns.
- f. Working papers are all other items prepared solely for purposes of the engagement and include items prepared by the
  - i. member, such as audit programs, analytical review schedules, and statistical sampling results and analyses.
  - ii. client at the request of the member and reflecting testing or other work done by the member.

#### **Applicability**

**.02** *When a person or entity engages a member to perform professional services (engaging entity) with respect to, or for the benefit of, another person or entity, the member will be considered in compliance with the requirements of this interpretation related to client-provided records if the member returns these records to the person or entity that gave the records to the member.*

**.03** *When an engaging entity engages a member to perform professional services for the benefit of another person or entity (beneficiary), the member will be considered in compliance with the requirements of this interpretation related to a member's work products if the member provides such work products to the beneficiary. For example, if a company engages a member to perform personal tax services for the benefit of its executives, the member would be in compliance with the interpretation if the member provides the tax returns to the executives (See the "Confidential Client Information Rule" [1.700.001]).*

**.04** *When an engaging entity engages a member to perform professional services with respect to another entity that is not the beneficiary of the professional services, absent an agreement stating otherwise, the member would be in compliance with the requirements of this interpretation related to a member's work products, if the member provides such work products to the engaging entity. For example, if a company engages a member to value the assets of another company for a possible acquisition, absent an agreement stating otherwise, the member would be in compliance with this interpretation if the member provides the valuation report only to the engaging entity.*

#### **Interpretation**

**.05** Members must comply with the rules and regulations of authoritative regulatory bodies, such as the member's state board(s) of accountancy, when the member performs services for a client and is subject to the rules and regulations of such regulatory body. For example, a member's state board(s) of accountancy may not permit a member to withhold certain records, even though fees are due to the member for the work performed. Failure to comply with the more restrictive provisions of the applicable regulatory body's rules and regulations concerning the return of certain records would constitute a violation of this interpretation.

#### 1.700.030 Disclosing Information to ~~Persons or Entities Associated With~~ Clients

**.01** When a *member* is engaged **by either spouse** to prepare a married couple's joint tax return, **the two** both spouses are considered to be **one** the member's *client*, even if the member **deals exclusively with** ~~was engaged by one spouse and deals exclusively with that spouse.~~

~~.02 Accordingly, the member would not need consent from either spouse in order to provide information related to the couple's joint tax return to the other spouse. For example,~~ if the married couple is undergoing a divorce and one spouse directs the member to withhold joint tax information from the other spouse, the member may provide the information to both spouses in compliance with the "[Confidential Client Information Rule](#)" [1.700.001], because both are the member's client. The member should consider reviewing

- a. the legal implications of such disclosure with an attorney and
- b. responsibilities under any tax performance standards, such as Section 10.29 of IRS Circular 230. [Prior reference: paragraphs .031–.032 of ET section 391].

~~.02–.03~~ **When a person or entity engages a member to perform professional services (engaging entity) for the benefit of another person or entity (beneficiary), the engaging entity and the beneficiary are considered two separate clients. Accordingly, the member should not disclose confidential client information of either client to the other without consent of the client whose confidential information is to be disclosed. For example, if a company engages a member to perform personal tax services for the benefit of its** ~~if a member provides professional services to a company's executives request of the company, the member's disclosure of the executives' confidential client information to the company without the consent of the applicable executive would be a violation of the "[Confidential Client Information Rule](#)" [1.700.001] even if the company is not otherwise a client. [Prior reference: paragraphs .041–.042 of ET section 391]~~

#### 1.290.010 Actual or Threatened Litigation (in part)

**.07** If threatened or actual litigation is unrelated to the performance of *an client's* attest engagement and is for an amount that is not material to the covered member's firm or the attest client, threats to the covered member's compliance with the "Independence Rule" [1.200.001] would be at an acceptable level, and independence would not be impaired. Such claims may arise, for example, out of immaterial disputes regarding billings for services, results of tax or management services advice, or similar matters.

- .11 If only the underwriter or officers or directors of **the covered member's** other **attest** clients of ~~the covered member~~ file cross-claims against the covered member, threats to the covered member's compliance with the "Independence Rule" [1.200.001] would be at an acceptable level unless other circumstances create threats to compliance with the "Independence Rule."

#### **1.295.040 General Requirements for Performing Nonattest Services (in part)**

- .02 The safeguards in paragraph .01 and the "Documentation Requirements When Providing Nonattest Services" interpretation [1.295.050] of the "Independence Rule" [1.200.001] do not apply to certain routine activities performed by the member, such as providing advice and responding to the attest client's questions as part of the **attest** client-member relationship. However, in providing such services, the member must not assume management responsibilities, as described in the "Management Responsibilities" interpretation [1.295.030] of the "Independence Rule." [Prior reference: paragraph .05 of ET section 101]

#### **1.295.120 Bookkeeping, Payroll, and Other Disbursements (in part)**

- .01 If the member applies the "General Requirements for Performing Nonattest Services" interpretation [1.295.040] of the "Independence Rule" [1.200.001], threats would be at an acceptable level and independence would not be impaired. For example, a member may
- a. record transactions to an *attest client's* general ledger when management has determined or approved the account classifications for the transaction.
  - b. post ~~client-coded~~ transactions **coded by the attest client** to ~~an~~ **the** attest client's general ledger.
  - c. prepare financial statements based on information in the attest client's trial balance.
  - d. post attest client-approved journal or other entries to an attest client's trial balance.
  - e. propose standard, adjusting, or correcting journal entries or other changes affecting the financial statements to the attest client. Prior to the member posting these journal entries or changes, the member should be satisfied that management has reviewed the entries and understands the nature of the proposed entries and the effect the entries will have on the attest client's financial statements.
  - f. generate unsigned checks using source documents or other records provided and approved by the attest client.
  - g. process an attest client's payroll using payroll time records that the attest client has provided and approved.
  - h. transmit attest client-approved payroll or other disbursement information to a bank or similar entity subsequent to the attest client's review and authorization for the member to make the transmission. Prior to such transmission, the attest client is responsible for making the arrangements with the bank or similar entity to limit the corresponding individual payments regarding the amount and payee. In addition, once transmitted, the attest client must authorize the bank or similar entity to process the payroll information.
  - i. prepare a reconciliation (for example, bank and accounts receivable) that identifies reconciling items for the attest client's evaluation.

### 1.295.140 Forensic Accounting (in part)

.02 *Attest client*. For purposes of this interpretation, the term *attest client* refers to ~~an underlying party to the litigation for whom~~ **the attest client with respect to which** the member is providing **litigation** services, not the law firm that engages the member on behalf of the law firm's client. If the law firm that engages the member on behalf of the member's attest client is also an attest client of the member, the member should consider the applicability of the "Cooperative Arrangements With Attest Clients" interpretation [1.265.010] of the "Independence Rule" [1.200.001].

### 1.295.150 Internal Audit (in part)

.10 Members should use judgment in determining whether otherwise permitted internal audit services performed may result in a significant management participation threat to independence, considering factors such as the significance of the controls being tested, the scope or extent of the controls being tested in relation to the overall financial statements of the **attest** client, as well as the frequency of the internal audit services. If the threat to independence is considered significant, the member should apply safeguards to eliminate or reduce the threat to an acceptable level. If no safeguards could reduce the threat to an acceptable level, then independence would be impaired.

### 1.510.040 Contingent Fee Arrangements With an Investment Advisory Services Nonattest Client That Is Related to a Client (in part)

.01 A member or member's firm may provide investment advisory services for a contingent fee to

- owners, officers, or employees of a client ~~for whom~~ **with respect to which** the member performs a service listed in paragraph .01a of the "Contingent Fees Rule"
- a nonattest client employee benefit plan that is sponsored by ~~an attest client for whom~~ **with respect to which** the member performs a service listed in paragraph .01a of the "Contingent Fees Rule."

### 1.510.050 Investment Advisory Services (in part)

.01 A member or member's firm may provide investment advisory services for a fee based on a percentage of the investment portfolio to a client ~~for whom~~ **with respect to which** the member performs a service listed in paragraph .01a of the "Contingent Fees Rule" [1.510.001] without violating that rule if all of the following safeguards are met:

- The fee is determined based on a specified percentage of the **attest** client's investment portfolio.
- The dollar amount of the portfolio on which the fee is based is determined at the beginning of each quarter (or longer period of time as may be agreed upon) and is adjusted only for the **attest** client's additions or withdrawals during the period.
- The fee arrangement is not renewed with the **attest** client more frequently than on a quarterly basis. [Prior reference: paragraphs .047–.048 of ET section 391]

**Client.** Any person or entity, other than the *member's* employer, that engages a *member* or *member's firm* to perform *professional services* (engaging entity) and also, a person or entity with respect to which a *member* or *member's firm* performs *professional services* (subject entity). When the engaging entity and the subject entity are different, while there is only one engagement, they are separate clients.

[Prior reference: paragraph .03 of ET section 92]

See paragraph .03 of the “Simultaneous Employment or Association With an Attest Client” interpretation [1.275.005] for *independence* guidance related to a *member* in a government audit organization that performs an *attest engagement* with respect to the government entity.

**Attest client.** A person or entity with respect to which an *attest engagement* is performed.

If the person or entity that engages a *member* or *member's firm* to perform *professional services* (engaging entity) is not also the attest client, the *member* and the *member's firm* (member) should refer to the “Client Affiliate” interpretation [1.224.010] to determine if the member needs to be independent of the engaging entity. However, because threats to the member's compliance with the “Integrity and Objectivity Rule” [1.100.001] and the “[Conflicts of Interest](#)” interpretation [1.110.010] may still exist with respect to the engaging entity, members should comply with this rule and interpretation.

See the “Client Affiliate” interpretation [1.224.010] for acquisitions and business combinations that involve a financial statement attest client.

See paragraph .03 of the “Simultaneous Employment or Association With an Attest Client” interpretation [1.275.005] for independence guidance related to a member in a government audit organization that performs an *attest engagement* with respect to the government entity.

### **1.275.005 Simultaneous Employment or Association With an Attest Client**

.01 In this interpretation, simultaneous employment or association with an *attest client* is serving as a director, an officer, an employee, a promoter, an underwriter, a voting trustee, a trustee for any pension or profit-sharing trust of the *attest client*, or in any capacity equivalent to that of a member of management of an *client* during the period covered by the financial statements or the *period of the professional engagement*.

.02 If a *partner* or professional employee of the *member's firm* is simultaneously employed or associated with an *attest client*, familiarity, management participation, advocacy, or self-review threats to the member's 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. Accordingly, independence would be impaired. [Prior reference: paragraph .02C of ET section 101]

- .03 However, *threats* will be at an *acceptable level* and *independence* will not be *impaired* when either of the following situations exists:
- a. A *partner* or professional employee of a *firm* serves as an adjunct faculty member of an educational institution that is an attest client of the firm *and* the *partner* or professional employee meets all of the following safeguards:
    - i. Does not hold a key position at the educational institution.
    - ii. Does not participate on the attest engagement team.
    - iii. Is not an individual in a position to influence the attest engagement.
    - iv. Is employed by the educational institution on a part-time and non-tenure basis.
    - v. Does not participate in any employee benefit plans sponsored by the educational institution, unless participation is required.
    - vi. Does not assume any management responsibilities or set policies for the educational institution Upon termination of employment, the partner or professional employee should comply with the requirements of the “Former Employment or Association With an Attest Client” interpretation [1.277.010] of the “Independence Rule” [1.200.001]. [Prior reference: paragraph .21 of ET section 101].
  - b. A member in a government audit organization performs an *attest engagement* with respect to the government entity and the head of the government audit organization meets at least one of the following:
    - i. Is directly elected by voters of the government entity with respect to which attest engagements are performed.
    - ii. Is appointed by a legislative body and is subject to removal by a legislative body.
    - iii. Is appointed by someone other than the legislative body, as long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body.

## 1.000 Introduction

- .01 Part 1 of the Code of Professional Conduct (the code) applies to *members* in public practice. Accordingly, when the term *member* is used in part 1 of the code, the requirements apply only to *members* in public practice. When a *member* in public practice is also a *member in business* (for example, serves as a member of an entity’s board of directors), the *member* should also consult [part 2](#) of the code, which applies to a *member in business*.
- .02 Government auditors within a government audit organization who audit federal, state, or local governments or component units thereof, that are structurally located within the government audit organization, are considered in public practice with respect to those entities provided the head of the government audit organization meets at least one of the following:
- a. Is directly elected by voters of the government entity with respect to which attest engagements are performed
  - b. Is appointed by a legislative body and is subject to removal by a legislative body

- c. Is appointed by someone other than the legislative body, so long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body

#### **1.224.020 Entities Included in State and Local Government Financial Statements (in part)**

(Paragraphs .01–.07 are unchanged.)

.08 However, if a *covered member* or a *covered member's immediate family* holds a *key position* within the primary government during the *period of the professional engagement* or during the period covered by the financial statements, 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*. Accordingly, the *covered member's independence* would be *impaired*. For purposes of this interpretation, a *covered member* and the *covered member's immediate family* would not be considered employed by the primary government if the criteria in the Introduction of part 1 [1.000.02] were met. [Prior reference: paragraph .12 of ET section 101]

#### **1.400.200 Records Requests (in part)**

##### Terminology

.01 The following terms are defined here solely for use with this interpretation:

- a. A client includes current and former *clients*.
- b. A member means the *member* or the *member's firm*.
- c. Client-provided records are accounting or other records, including hardcopy and electronic reproductions of such records, belonging to the client that were provided to the member by, or on behalf of, the client.
- d. Member-prepared records are accounting or other records that the member was not specifically engaged to prepare and that are not in the client's books and records or are otherwise not available to the client, thus rendering the client's financial information incomplete. Examples include adjusting, closing, combining, or consolidating journal entries (including computations supporting such entries) and supporting schedules and documents that the member proposed or prepared as part of an engagement (for example, an audit).
- e. Member's work products are deliverables set forth in the terms of the engagement, such as tax returns.
- f. Working papers are all other items prepared solely for purposes of the engagement and include items prepared by the
  - i. member, such as audit programs, analytical review schedules, and statistical sampling results and analyses.
  - ii. client at the request of the member and reflecting testing or other work done by the member.

##### Applicability

- .02 When a person or entity engages a member to perform professional services (engaging entity) with respect to, or for the benefit of, another person or entity, the member will be considered in compliance with the requirements of this interpretation related to client-provided records if the member returns these records to the person or entity that gave the records to the member.
- .03 When an engaging entity engages a member to perform professional services for the benefit of another person or entity (beneficiary), the member will be considered in compliance with the requirements of this interpretation related to a member's work products if the member provides such work products to the beneficiary. For example, if a company engages a member to perform personal tax services for the benefit of its executives, the member would be in compliance with the interpretation if the member provides the tax returns to the executives (See the "Confidential Client Information Rule" [1.700.001]).
- .04 When an engaging entity engages a member to perform professional services with respect to another entity that is not the beneficiary of the professional services, absent an agreement stating otherwise, the member would be in compliance with the requirements of this interpretation related to a member's work products, if the member provides such work products to the engaging entity. For example, if a company engages a member to value the assets of another company for a possible acquisition, absent an agreement stating otherwise, the member would be in compliance with this interpretation if the member provides the valuation report only to the engaging entity.

#### Interpretation

- .05 Members must comply with the rules and regulations of authoritative regulatory bodies, such as the member's state board(s) of accountancy, when the member performs services for a client and is subject to the rules and regulations of such regulatory body. For example, a member's state board(s) of accountancy may not permit a member to withhold certain records, even though fees are due to the member for the work performed. Failure to comply with the more restrictive provisions of the applicable regulatory body's rules and regulations concerning the return of certain records would constitute a violation of this interpretation.

### 1.700.030 Disclosing Information to Clients

- .01 When a *member* is engaged by either spouse to prepare a married couple's joint tax return, the two spouses are considered to be one *client*, even if the *member* deals exclusively with one spouse. Accordingly, if the married couple is undergoing a divorce and one spouse directs the *member* to withhold joint tax information from the other spouse, the *member* may provide the information to both spouses in compliance with the "[Confidential Client Information Rule](#)" [1.700.001], because both are the member's *client*. The member should consider reviewing
  - a. the legal implications of such disclosure with an attorney and
  - b. responsibilities under any tax performance standards, such as Section 10.29 of IRS Circular 230. [Prior reference: paragraphs .031–.032 of ET section 391].
- .02 When a person or entity engages a *member* to perform *professional services* (engaging entity) for the benefit of another person or entity (beneficiary), the engaging entity and the beneficiary are considered two separate *clients*. Accordingly, the *member* should not disclose confidential client information of either *client* to the other without consent of the *client* whose

confidential information is to be disclosed. For example, if a company engages a member to perform personal tax services for the benefit of its executives, the *member's* disclosure of the executives' confidential client information to the company without the consent of the applicable executive would be a violation of the "[Confidential Client Information Rule](#)" [1.700.001]. [Prior reference: paragraphs .041–.042 of ET section 391]

#### **1.290.010 Actual or Threatened Litigation (in part)**

.07 If threatened or actual litigation is unrelated to the performance of an *attest engagement* and is for an amount that is not material to the *covered member's firm* or the *attest client*, threats to the covered member's compliance with the "Independence Rule" [1.200.001] would be at an *acceptable level*, and *independence* would not be *impaired*. Such claims may arise, for example, out of immaterial disputes regarding billings for services, results of tax or management services advice, or similar matters.

.11 If only the underwriter or officers or directors of the *covered member's* other *attest clients* file cross-claims against the *covered member*, threats to the covered member's compliance with the "Independence Rule" [1.200.001] would be at an *acceptable level* unless other circumstances create *threats* to compliance with the "Independence Rule."

#### **1.295.040 General Requirements for Performing Nonattest Services (in part)**

.02 The safeguards in paragraph .01 and the "Documentation Requirements When Providing Nonattest Services" interpretation [1.295.050] of the "Independence Rule" [1.200.001] do not apply to certain routine activities performed by the *member*, such as providing advice and responding to the *attest client's* questions as part of the *attest client-member* relationship. However, in providing such services, the *member* must not assume management responsibilities, as described in the "Management Responsibilities" interpretation [1.295.030] of the "Independence Rule." [Prior reference: paragraph .05 of ET section 101]

#### **1.295.120 Bookkeeping, Payroll, and Other Disbursements (in part)**

.01 If the member applies the "General Requirements for Performing Nonattest Services" interpretation [1.295.040] of the "Independence Rule" [1.200.001], *threats* would be at an *acceptable level* and *independence* would not be *impaired*. For example, a member may

- a. record transactions to an *attest client's* general ledger when management has determined or approved the account classifications for the transaction.
- b. post transactions coded by the *attest client* to the *attest client's* general ledger.
- c. prepare financial statements based on information in the *attest client's* trial balance.
- d. post attest client-approved journal or other entries to an *attest client's* trial balance.
- e. propose standard, adjusting, or correcting journal entries or other changes affecting the financial statements to the *attest client*. Prior to the *member* posting these journal entries or changes, the *member* should be satisfied that management

has reviewed the entries and understands the nature of the proposed entries and the effect the entries will have on the *attest client's* financial statements.

- f. generate unsigned checks using source documents or other records provided and approved by the *attest client*.
- g. process an *attest client's* payroll using payroll time records that the *attest client* has provided and approved.
- h. transmit *attest client*-approved payroll or other disbursement information to a bank or similar entity subsequent to the *attest client's* review and authorization for the member to make the transmission. Prior to such transmission, the *attest client* is responsible for making the arrangements with the bank or similar entity to limit the corresponding individual payments regarding the amount and payee. In addition, once transmitted, the *attest client* must authorize the bank or similar entity to process the payroll information.
- i. prepare a reconciliation (for example, bank and accounts receivable) that identifies reconciling items for the *attest client's* evaluation.

#### **1.295.140 Forensic Accounting (in part)**

.02 *Attest client*. For purposes of this interpretation, the term *attest client* refers to the attest client with respect to which the member is providing litigation services, not the law firm that engages the member on behalf of the law firm's client. If the law firm that engages the member on behalf of the member's attest client is also an attest client of the member, the member should consider the applicability of the "Cooperative Arrangements With Attest Clients" interpretation [1.265.010] of the "Independence Rule" [1.200.001].

#### **1.295.150 Internal Audit (in part)**

.10 Members should use judgment in determining whether otherwise permitted internal audit services performed may result in a significant management participation threat to *independence*, considering factors such as the significance of the controls being tested, the scope or extent of the controls being tested in relation to the overall financial statements of the attest client, as well as the frequency of the internal audit services. If the *threat* to *independence* is considered significant, the *member* should apply safeguards to eliminate or reduce the *threat* to an *acceptable level*. If no *safeguards* could reduce the *threat* to an *acceptable level*, then *independence* would be *impaired*.

#### **1.510.040 Contingent Fee Arrangements With an Investment Advisory Services Nonattest Client That Is Related to a Client (in part)**

.01 A *member* or *member's firm* may provide investment advisory services for a contingent fee to

- a. owners, officers, or employees of a *client* with respect to which the member performs a service listed in paragraph .01a of the "Contingent Fees Rule"
- b. a nonattest *client* employee benefit plan that is sponsored by an *attest client* with respect to which the member performs a service listed in paragraph .01a of the "Contingent Fees Rule."

**1.510.050 Investment Advisory Services (in part)**

.01 A *member* or *member's firm* may provide investment advisory services for a fee based on a percentage of the investment portfolio to a *client* with respect to which the *member* performs a service listed in paragraph .01a of the "Contingent Fees Rule" [1.510.001] without violating that rule if all of the following safeguards are met:

- a. The fee is determined based on a specified percentage of the *attest client's* investment portfolio.
- b. The dollar amount of the portfolio on which the fee is based is determined at the beginning of each quarter (or longer period of time as may be agreed upon) and is adjusted only for the *attest client's* additions or withdrawals during the period.
- c. The fee arrangement is not renewed with the *attest client* more frequently than on a quarterly basis. [Prior reference: paragraphs .047–.048 of ET section 391]



**COMMENT SUMMARY**  
**PROPOSED Revised Definitions of “Client” and “Attest Client” as well as related definitions, interpretations and other guidance**

<b>Comment Letter</b>	<b>Feedback Highlights</b>	<b>Task Force Response</b>
<b>CL 1</b> LCPA Ethics Committee <b>Support</b>	<ul style="list-style-type: none"> <li>The Committee agrees with the proposed revisions and concurs with the changes.</li> </ul>	No response needed
<b>CL 2</b> TSCPA Professional Standards Committee <b>Support</b>	<ul style="list-style-type: none"> <li>The Committee is basically in agreement with the issues addressed. The Committee believes the guidance was well thought out and the examples were both clearly presented and relevant to the concepts being addressed. The Committee believes the issue surrounding the “Integrity and Objectivity Rule” requirement should be included in the definition.</li> </ul>	No response needed.
<b>CL 3</b> State of Tennessee Comptroller of the Treasury, Department of Audit, Division of State Audit (TN Dept of Audit) <b>Support with recommendations</b>	<ul style="list-style-type: none"> <li>TN Dept of Audit agree with the PEEC that the inclusion in the “attest client” definition of the requirement to comply with the “Integrity and Objectivity Rule” and its interpretations is the correct location to minimize the member overlooking this requirement.</li> </ul> <p><b>Recommendations:</b></p> <ul style="list-style-type: none"> <li>ET 1.224.020 – The last sentence needs to clarify the conclusion that the covered member and the covered member’s immediate family would not be considered</li> </ul>	<ul style="list-style-type: none"> <li>Sent email to TN Dept of Audit requesting clarification. Staff believes TN Dept of Audit is trying to contact ET1.224.020 which says members who meet criteria of</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>“employed: by the primary government. Agree with the government auditor exception in 1.000.02 but not sure how this conclusion fits within the logic of the part 1 requirement.</p> <ul style="list-style-type: none"> <li>• ET 1.400.200 – the .01d examples including adjusting, closing, combining, or consolidating journal entries that are member-prepared records, not from client records or the client explicitly agreeing to responsibility, create a potential independence impairment based on similar guidance in the generally accepted government auditing standards. Recommend providing guidance similar to what is in the Yellow Book.</li> <li>• ET 1.400.200 – the guidance indicate there is a “presumption” there would be an agreement between the engaging party and the subject entity. Recommend that verification be part of the process.</li> <li>• ET 1.290.010.07 – the materiality concept appears limited to the covered member’s firm or the attest client. However, there is no mention about materiality to the attest client engagement. Should engagement materiality also be included in this actual or threatened litigation section?</li> <li>• ET 1.290.010.07 – Assumed “disputes” is referring to litigation filed by either the firm or client. Is that the intended interpretation?</li> <li>• ET 1.290.010.11 – what is meant by “other” attest clients? Recommended</li> </ul>	<p>gov’t exception are not considered employees of primary gov’t. ET1.275.005 says if member meeting criteria of gov’t exception then would not be in violation of “Simultaneous Employment or Association With an Attest Client” interpretation.</p> <ul style="list-style-type: none"> <li>• Task Force does not recommend making a change as this change is outside the scope of this Task Force.</li> <li>• Task Force discussed this comment and realized it was based on the narrative of the Exposure Draft which mentioned the presumption concept but in the actual interpretation requires written consent. Task Force agrees no change needed.</li> <li>• Task Force does not recommend making a change as this change is outside the scope of this Task Force.</li> <li>• Assumption is correct.</li> <li>• Task Force agrees with the recommended rewrite.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>rewording the sentence as follows: “If only the underwriter, officers, or directors of the covered member’s other attest clients file cross-claims against the covered member,…”</p> <ul style="list-style-type: none"> <li>• ET 1.295.040.02 – Recommend changing the “attest client-member relationship” to “attest client-member engagement”</li> <li>• ET 1.295.120.01a – Recommend the following modification: “...determined or approved the <b>transaction details</b> and account classification....” This modification is create consistency between the Code and new Yellow Book exposure draft which defines preparing financial statements based on information in the attest client’s trial balance as a significant threat.</li> <li>• ET 1.295.140.02 – Replace the phrase “with respect to which” to “for whom” throughout the proposed amendments. The current proposed phrase results in an awkward sentence.</li> <li>• ET 1.295.150 – Seriously concerned allowing members to perform internal audit functions and then also performing the attest engagement, especially if management can control the results of the internal audit services performed for the client (e.g., demand findings are not written).</li> <li>• ET 1.510.040 – 1.510.050 – Believe it would be difficult for members to perform these services without impacting their independence. At the very least, do not</li> </ul>	<ul style="list-style-type: none"> <li>• Task Force does not recommending changing “relationship” to “engagement” since it is not part of the specific engagement.</li> <li>• Task Force does not recommend making this change. This change is not related to this exposure draft but related to the Yellow Book’s exposure draft. A new Task Force needs to be set-up to address the changes in the Yellow Book.</li> <li>• Task Force does not recommend making a change to the phrase “with respect to which”. The Task Force discussed and decided on this phrasing.</li> <li>• This change was a clarifying change and it outside the scope of this Task Force to address their concern regarding internal audit and independence.</li> <li>• These changes were clarifying changes and it outside the scope of this Task Force to address these concerns regarding the Contingent Fees interpretations.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>believe that government auditors should perform these services and likely would not to begin with. These types of services appear to open the door to audit failures of the past when the lines between audit and non-audit services (and resultant revenues) led to independence failures. Believe any safeguards allowed should establish a high threshold to meet.</p>	
<p><b>CL 4</b> AICPA Private Companies Practice Section (PCPS) through the Technical Issues Committee (TIC) <b>Support</b></p>	<ul style="list-style-type: none"> <li>• The TIC supports the changes to the definition of an attest client to only require independence of the subject entity, when the subject entity is different from the engaging entity.</li> <li>• The TIC also supports the clarification that married couples are to be considered one client for tax returns will assist tax practitioners.</li> <li>• The TIC supports the inclusion of the reminder that member needs to comply with the “Integrity and Objectivity” rule and its interpretations.</li> </ul>	<p>No response needed.</p>
<p><b>CL 5</b> Office of the Auditor General (OAG) <b>Support with Recommendations</b></p>	<ul style="list-style-type: none"> <li>• OAG concur with the PEEC conclusion that members should be required to be independent only of the entity subject to the audit, and not the engaging entity, when those entities are not one and the same. OAG also agree that it is appropriate to include a reminder in the definition of “attest client” that members must still comply with the “Integrity and Objectivity” Rule since threats to this rule</li> </ul>	

Comment Letter	Feedback Highlights	Task Force Response
	<p>may still exist with respect to the engaging entity.</p> <p><b>Recommendations:</b></p> <ul style="list-style-type: none"> <li>OAG recommends incorporating the fourth criteria from the <i>Government Auditing Standards</i> paragraph 3.29d in order to define a member in public practice and describing the head of the government audit organization.</li> </ul>	<ul style="list-style-type: none"> <li>Task Force does not recommend incorporating the fourth criteria from the <i>Government Auditing Standards</i> paragraph 3.29d into the Code. This was the original topic of this Task Force and it was decided not to add the fourth criteria. It was believed that adding the fourth criteria would broaden the term client and the Task Force was concerned it would be similar to adding internal auditors to the client definition.</li> </ul>
<p><b>CL 6</b></p> <p>US Government Accountability Office (GAO)</p> <p><b>Support with Recommendations</b></p>	<ul style="list-style-type: none"> <li>GAO agreed that it is appropriate to include a reminder in the definition of “attest client” that members must still comply with the “Integrity and Objectivity” Rule since threats to this rule may still exist with respect to the engaging entity.</li> </ul> <p><b>Recommendations:</b></p> <ul style="list-style-type: none"> <li>GAO recommends incorporating the fourth criteria from the <i>Government Auditing Standards</i> paragraph 3.29d in order to define a member in public practice and describing the head of the government audit organization.</li> </ul>	<ul style="list-style-type: none"> <li>Task Force does not recommend incorporating the fourth criteria from the <i>Government Auditing Standards</i> paragraph 3.29d into the Code. This was the original topic of this Task Force and it was decided not to add the fourth criteria. It was believed that adding the fourth criteria would broaden the term client and the Task Force was concerned it would be similar to adding internal auditors to the client definition</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<ul style="list-style-type: none"> <li>1.295.120 – recommends expanding the Code to require that auditors (1) conclude that any services related to preparing accounting records and financial statements, other than those defined as impairment to independence, create significant threats to auditors’ independence and document their assessment of the significance of the threat to independence posed by the auditors’ preparation of the attest client financial statements, including documentation of any safeguards that were applied.</li> </ul>	<ul style="list-style-type: none"> <li>Task Force does not recommend this change. This relates to changes being proposed in the Yellow Book exposure draft and those changes should be reviewed by another Task Force.</li> </ul>
<p><b>CL 7</b> Commonwealth of Virginia Auditor of Public Accounts <b>Support</b></p>	<ul style="list-style-type: none"> <li>Auditor of Public Accounts agrees with PEEC’s efforts to provide further guidance on how an auditor should define client, attest clients, as well as related definitions, interpretations and other guidance. Auditor of Public Accounts also agree that the definition is the ideal location of the requirement to comply with the “Integrity and Objectivity Rule”. Auditor of Public Accounts encourages the PEEC to move forward with the changes.</li> </ul>	<p>No response needed.</p>
<p><b>CL 8</b> Grant Thornton <b>Support with Recommendations</b></p>	<ul style="list-style-type: none"> <li>Grant Thornton supports the revisions set forth in the exposure draft with some recommendations for consideration</li> </ul> <p><b>Recommendations for definition of client:</b></p> <ul style="list-style-type: none"> <li>Recommend in the client definition to pluralize “any person or entity” as there could be more than one person or entity.</li> </ul>	<ul style="list-style-type: none"> <li>Task Force was neutral on pluralizing “any person or entity”. Staff looked at extant</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<ul style="list-style-type: none"> <li>• Recommend using the term “engaging party” opposed to “engaging entity” which Grant Thornton reflect a more accurate relationship.</li> <li>• Recommend creating a practice aid or FAQs to assist members to better understand what is or is not a client. Some examples given were: <ul style="list-style-type: none"> <li>○ Would a general partner, that is a separate legal entity, who engages a member for tax services because it has the requisite legal authority to do son behalf of a limited partnership (subject entity), be considered a separate engaging party? If engaged to provide tax services by the general partner for the limited partner, under applicable tax law, the general partner is not considered a separate client.</li> <li>○ In engagements where more than one party signs an engagement letter, such as litigation services where the law firm, attorney and the underlying client all sign, would both the law firm and the underlying client be the “client” because of unique contractual rights and obligations?</li> <li>○ Would a partner company (or other investor) who engages a member to audit a subsidiary (or an</li> </ul> </li> </ul>	<p>Code and determined that most times the singular form is used.</p> <ul style="list-style-type: none"> <li>• Take Force does not believe that engaging entity is confusing and recommends not making this change.</li> <li>• Task Force agreed that some FAQs might clarify whether a person or entity is client or not if there is an issue in the future. Task Force decided not to issue FAQs at this time but is open to issuing them in the future based on hotline inquiries.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>investee) that is a separate legal entity be considered an engaging entity?</p> <ul style="list-style-type: none"> <li>Recommend adding the Integrity and Objectivity interpretation to the client definition as was done in the attest client definition.</li> </ul> <p><b>Recommendation for definition of attest client:</b></p> <ul style="list-style-type: none"> <li>Recommend in the client definition to pluralize “any person or entity” as there could be more than one person or entity.</li> <li>Recommend not using the phrase a member “need not be independent of the engaging entity” as it may contradict the main purpose of the attest client definition. In recommend the following phrasing (changes in <b>bold</b>): <ul style="list-style-type: none"> <li>If the persons or entities that engage a member or member’s firm to perform professional services (engaging <b>party</b>) is not also the attest client, the member and the member’s firm (member) <del>need not be independent of the engaging entity except as may be required by</del> <b>should consider</b> the “Client Affiliate” interpretation [1.224.010] <b>in order to determine if the</b></li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>Task Force does not agree with this recommendation. The reason it is in the attest client definition relates to the engaging entity not necessarily needing to be independence but reminding them to consider their obligations under the Integrity and Objectivity Rule. These same circumstances are not in the client definition.</li> <li>Similar to the client definition.</li> <li>Task Force agreed with the re-wording. It does make the sentence read easier.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p><b>member needs to be independent of the engaging party.</b> However, because threats to the members compliance with the “Integrity and Objectivity Rule” [1.100.001] and the “Conflict of Interest” interpretation [1.110.010] may still exist with respect to the engaging <b>party</b>, members should comply with this rule and interpretation.</p> <p><b>General Comments:</b></p> <ul style="list-style-type: none"> <li>• Agree with placement and inclusion of the reference to the “Integrity and Objectivity Rule” requirement in the definition of attest client but as noted above would also like to see it in the definition of client.</li> <li>• In the explanation of the proposed revised “Disclosing Information to Persons or Entities Associated with Clients” interpretation [1.700.030] it states, “the presumption is that there would be an agreement between the engaging entity or the subject entity allowing the member to perform the professional services on the subject entity and to disclose the results of the services and other relevant information to the engaging entity.” However, the interpretation should be clear, it is not intended to imply the existence of a legal relationship between the parties suggesting one party can legally contract on behalf of another or that parties may share information without</li> </ul>	<ul style="list-style-type: none"> <li>• No response needed.</li> <li>• The interpretation already states that member should consult an attorney and consider IRS Circular 230 so the Task Force believes this comment has already been addressed.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>the proper consent as may be required under IRS or other laws or requirements. Suggest consideration be given to adding clarification on the presumption of agreements between parties.</p> <ul style="list-style-type: none"> <li>• Should consider adding a general statement indicating that relationships between members and clients, including but not limited to confidentiality, sharing tax return information with third parties, and conflict of interest, are governed by existing AICPA guidance, IRS Circular 230, and applicable federal and state law. Compliance with such applicable guidance and tax standards where such standards exist and are directly applicable is required where such standards differ from guidance in this interpretation regardless of whether such guidance is more restrictive or not.</li> <li>• Recommend the removal of the tax examples in proposed revised Records Requests interpretation [1.400.200] and proposed revised “Disclosing Information to Persons or Entities Associated with Clients” interpretation [1.700.030] as Grant Thornton does not believe those examples represent what is applied, or in some cases required, in tax practice. <ul style="list-style-type: none"> <li>○ For example, in practice when engaged to prepare the joint tax return, both spouses sign the tax return and the engagement letter, rendering the both clients. If a company engages a member to</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• The Code already addresses this as discussed in previous comment.</li>   <li>• Task Force does not agree with the removal of the tax examples. Task Force believes the addition of the phrase “while there is only one engagement” in the client definition will address Grant Thornton’s concerns.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>perform personal tax services for the benefit of its executives, the member's client for professional standards purposes is the employee not the employer. The member would not provide the executives personal tax return to the company without advance written taxpayer consent.</p> <ul style="list-style-type: none"> <li>○ The example of an employer engaging a return preparer is problematic as it could be read as suggesting that a member does not need an engagement letter between itself and the "actual" client (the employee).</li> <li>● Agrees with no delayed effective date.</li> </ul>	
<p><b>CL 9</b></p> <p>NASBA <i>Support with Recommendations</i></p>	<ul style="list-style-type: none"> <li>● NASBA agrees with the placement of the reminder to the member that they must comply with the Integrity and Objectivity Rule.</li> </ul> <p><b>Recommendations:</b></p> <ul style="list-style-type: none"> <li>● Recommend a provision that, if the subject entity is a different party, a member must gain the agreement of the subject entity at the commencement of the engagement as to the sharing of the subject entity information with the engaging entity.</li> <li>● Recommend more clarity in the Disclosing Information to Client interpretation [1.700.030] on what the member can</li> </ul>	<ul style="list-style-type: none"> <li>● Task Force does not agree that this requirement needs to be added. 1.700.030.02 already says you must obtain consent for either party if subject entity and engaging entity are different and the the addition of the phase "while there is only one engagement" in the client definition will address NASBA's concerns.</li> <li>● The Task Force removed some language from the proposal in order to address this concern.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>share with the spouse. For example if a Schedule K-1 is included in the joint tax return, the spouse should be given the Schedule K-1 but should not be given the associated underlying business tax return unless the spouse was a participant in the business and would normally receive the business tax return.</p>	
<p><b>CL 10</b> Crowe Horwath <i>Support with Recommendations</i></p>	<ul style="list-style-type: none"> <li>• Agree that the revisions to clarify the client definition will assist members in applying the definition to current practices.</li> <li>• Agree with the clarification that members should be required to be independent only of the subject entity when the engaging entity and the subject entity are different entities.</li> <li>• Agree that it is important to include the requirement to comply with the “Integrity and Objectivity Rule” for engaging entities as proposed.</li> </ul> <p><b>Recommendation:</b></p> <ul style="list-style-type: none"> <li>• Recommend clarifying the term “beneficiary” through further definition or examples. Crowe Horwath believes most situations the beneficiary of the service will be clear, but there may be situations where it is unclear which party is benefitting. <ul style="list-style-type: none"> <li>○ For example, if the engaging entity engages the member to provide an audit of a subject entity as part of an acquisition, there may be uncertainty regarding whether the</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Task Force believes this is address through existing the examples. 1.400.200.04 shows an example related to an acquisition.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>audit benefits the engaging entity or the subject entity. This uncertainty could be addressed by requiring the engagement letter to specify which party is the beneficiary.</p>	
<p><b>CL 11</b> Pennsylvania Institute of Certified Public Accountants (PICPA) <b>Support with Recommendations</b></p>	<ul style="list-style-type: none"> <li>• PICPA agrees with PEEC's objective of clarifying the confidentiality and records request requirements for subject entities when the subject entity and the client are separate entities. PICPA is concerned regarding unintended consequences from designating the subject entity as a client, and believes the guidance can be clarified using the term "subject entity" rather than "client".</li> <li>• PICPA is concerned about the potential additional liability and contractual issues that would result from designating the subject entity a client, such as having to obtain engagement letters from the subject entities. This could expand the CPA's contractual obligations and liability without any benefit to the CPA as there are no fees associated with the presumed added responsibility. Additionally, has the PEEC considered the ramifications of CPAs performing pro bono work for these clients? Furthermore, does designating certain subject entities as a client raise new conflicts of interest? <ul style="list-style-type: none"> <li>○ Example, in a divorce case a CPA could have a conflict of interest by retaining both spouses as clients. In the event one spouse contracts</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• No response needed.</li> <li>• Task Force believes the addition of the phrase "while there is only one engagement" in the client definition will address PICPA's concerns.</li> </ul>

Comment Letter	Feedback Highlights	Task Force Response
	<p>the CPA to value the business of the other spouse currently the CPA would not be conflicted as the subject entity (the spouse's business) is not the CPA's client. However, if the spouse is now designated as a client, the CPA could be conflicted, owing a duty to each client on opposing sides of a legal dispute.</p> <ul style="list-style-type: none"> <li>○ Example, in the event a CPA is performing litigation for a client and is requested to perform certain procedures on this subject client, will the CPA be in an adversarial position to this subject entity?</li> <li>○ Example, in a business valuation situation there will be similar duties to the subject entity if they are considered a client that are not expected or contracted for.</li> </ul> <p><b>Recommendations:</b> PICPA believes that the objectives of the PEEC can be achieved without fundamentally changing the relationships with the subject entities.</p>	

**State Tax Tribunals****Reason for Agenda Item**

To determine what action if any should be taken to heighten awareness of non-authoritative guidance currently found in the Basis for Conclusions - Nonattest Services document.

**Summary of Issues**

When adopting the Tax Services interpretation [1.295.160] (Interpretation 101-3 Performance of Nonattest Services prior to December 15, 2014) in 2007, the Committee agreed that for purposes of the interpretation, a court should encompass a tax, district, or federal court of claims and the equivalent state, local, or foreign forums and that representation before forums that are equivalent to a court would impair independence. The Committee agreed that the following criteria would be indicative that the forum is equivalent to a court and added these criteria to the Basis for Conclusions Nonattest Services document:

- The forum is presided over by a trier of fact who is independent of the taxing authority and is empowered to render a determination that is binding (absent appeal);
- The forum conducts formal proceedings governed by a set of procedural rules dealing with matters such as evidence and testimony;
- The forum is the last opportunity for the parties to present new factual evidence, so that any appeal of the forum's decisions would only involve a review of the forum's records, including its factual or legal findings, and not an evidentiary hearing.

Staff confirmed with the AICPA's Tax Division that these criteria continue to be relevant and accurate. However, Staff believes that this guidance may be overlooked by members in its current location and recommends adding the criteria for indicating if a forum is equivalent to a court to the Nonattest Services FAQ document. Accordingly, Staff is recommending the following FAQ for the Committee's consideration:

**The [Tax Services](#) interpretation [1.295.160] under the Independence rule [1.200.001] provides that a “court encompasses a tax, district, or federal court of claims and the equivalent state, local, or foreign forums.” Are there any criteria that members could use that would indicate a forum is equivalent to a court?**

To determine what other forums may be equivalent to a court, members may consider criteria such as the following:

- The forum is presided over by a trier of fact who is independent of the taxing authority and is empowered to render a determination that is binding (absent appeal);
- The forum conducts formal proceedings governed by a set of procedural rules dealing with matters such as evidence and testimony;
- The forum is the last opportunity for the parties to present new factual evidence, so that any appeal of the forum's decisions would only involve a review of the forum's records, including its factual or legal findings, and not an evidentiary hearing. [Added X 20xx].

**Effective Date**

Not applicable.

**Action Needed**

The Committee's feedback would be appreciated.