



Professional Ethics Executive Committee

Open meeting agenda

August 17–18, 2021
Virtual

Open meeting agenda — August 17–18, 2021

Professional Ethics Division

Professional Ethics Executive Committee

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Meeting ID: 979 0525 7324 | **Web access:** <https://aicpa.zoom.us/j/97905257324>

International numbers available: <https://aicpa.zoom.us/u/aoNKntxop>

Observers must register: www.aicpa.org/PEECmeeting

August 17

10:00–10:05 EST	Welcome Mr. Lynch will welcome the committee members and discuss administrative matters	
10:05–11:05	SEC convergence The task force will seek approval to expose revisions to the “Client Affiliates” interpretation.	Agenda items 1A–1D
11:05–11:45	Client affiliates The task force will seek approval to expose revisions to the “Client Affiliates” interpretation and to the definition of “affiliate.”	Agenda items 2A–2C
11:45–12:30	Unpaid fees The task force will seek approval to revise its charge and to expose revisions to the “Unpaid Fees” interpretation.	Agenda items 3A–3F
12:30–1:00	<i>Break before afternoon session</i>	
1:00–1:45	Assisting attest clients with implementing accounting standards The task force will seek approval to revise its charge, expose a new interpretation “Assisting Attest Clients With the Implementation of Accounting Standards” and seek input on the	Agenda items 4A–4C

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	proposed Qs & As.	
1:45–2:15	<p>ISS practice aid</p> <p>The task force will seek input on the practice aid.</p>	Agenda items 5A–5B
2:15–2:30	<p>IESBA update</p> <p>The committee will receive an update on IESBA’s June 2021 meeting.</p>	Agenda items 6A–6F
2:30–3:00	<p>Compliance audits</p> <p>The committee will receive an update on recent activities of the Compliance Audit Task Force.</p>	
August 18		
10:00–10:20 EST	<p>Staff augmentation</p> <p>The task force will seek input on the proposed Qs & As.</p>	Agenda items 7A–7B
10:20–10:40	<p>NOCLAR</p> <p>The task force will provide the committee with an overview of the comments received on the NOCLAR exposure draft.</p>	
10:40–10:45	<p>IFAC convergence and monitoring</p> <p>The working group seeks approval to form a task force to determine the convergence needs for the fee-related standards IESBA issued in April 2021.</p> <p>Additional background: Basis for Conclusion</p>	Agenda item 8
10:45–10:50	<p>Statements on Standards for Tax Services</p> <p>The committee will receive an update on recent activities of the SSTS Task Force.</p>	

10:50–11:15	<p>Quality management</p> <p>The committee will receive an overview of the proposed revised quality management standards, which require firms to take a risk-based approach to their quality management system.</p> <p>Additional background:</p> <ul style="list-style-type: none"> • QM standards exposure draft explanatory memo • Additional information including executive summaries and the complete exposure draft are also available 	
11:15–11:20	<p>Member enrichment update</p> <p>The committee will receive an update on ongoing member enrichment projects not discussed elsewhere in the agenda.</p>	
11:20–11:25	Approval of May 2021 meeting minutes	Agenda item 9
	<p>Future meeting dates</p> <p>November 16–17, 2021</p> <p>February 16–17, 2022</p> <p>May 17–18, 2022</p> <p>August 10–11, 2022</p> <p>November 10–11, 2022</p>	

SEC convergence

Task force members

Jennifer Kary (chair), Cathy Allen, Anna Dourkourekas, Anika Heard, William McKeown, Katherine Savage, Lawrence Wojcik

Observers

Sonia Araujo, Chris Cahill, George Dietz, Faith Kim, Elizabeth McKneely, Jan Neil, Karen Liu Pham, Bella Rivshin

AICPA staff

Ellen Gorla

Task force charge

Evaluate the amended rules the SEC issued on October 16, 2020 to determine whether any revisions to the AICPA code are required.

Reason for agenda item

The committee is asked to approve exposing revisions to the “Client Affiliates” interpretation as outlined in agenda item 1B.

In addition, the task force recommends further refinements be made to the definition of *beneficially owned* and as such, requests the committee approve exposing these further revisions as outlined in agenda item 1C.

Task force activities

Loans

During the May 2021 meeting the committee agreed to expose revisions to the “Loans” interpretation, “Loans and Leases from Lending Institutions” interpretation, “Immediate Family Members” interpretation and to the definition of *beneficially owned*. The committee also agreed (with four abstentions) that the exposure draft should recommend the loan revisions be effective the last day of the month in which notice appears in the JofA.

The task force agreed, although not unanimously, to defer issuing the exposure draft until the committee determined whether to expose revisions to the “Client Affiliates” interpretation. This deferral was deemed appropriate because the “Client Affiliates” interpretation includes revisions related to the loan proposals and keeps the convergence proposals together in one exposure draft.

Revisions

Agenda item 1D contains the revisions to the to the “Loans” interpretation, the “Loans and Leases from Lending Institutions” interpretation and the “Immediate Family Members” interpretation that the committee approved for exposure during the May 2021 meeting.

During the fatal flaw review of the agenda materials for the August meeting, at the request of a task force member, staff made an additional change to paragraph .03 of the “Loans and Leases With Lending Institutions” interpretation (ET sec. 1.260.020). The final sentence of item (a) has been moved to item (b) and other minor resulting changes have been made.

The full task force has not reviewed or approved this change. The change is highlighted in yellow in agenda item 1D.

Q&A

During the May 2021 meeting, the committee was supportive of issuing a Q&A to clarify that permitted home mortgages apply to all loans collateralized by a borrower’s primary or other residence.

The committee acknowledged this was less restrictive than the SEC’s provision which applies only to a primary residence. Staff added the Q&A to the ethics division’s [General Ethics Questions](#) document.

Beneficially owned

When discussing the proposed revisions to the loan interpretations the committee agreed that because these revisions use the term *beneficial ownership interest* the definition of *beneficially owned* (ET sec. [0.400.06](#)) should be revised appropriately.

As currently drafted, the definition of *beneficially owned* could be read to imply that it does not include financial interests held by a record owner. The committee agreed that the definition should be revised as follows to clarify that the definition includes financial interests held by an individual or entity who may or may not be the record owner (additions are in bold italic and deletions are stricken).

Beneficially owned, *beneficial ownership interest*. Describes a *financial interest* of which ***providing*** an individual or entity, ***who may or may not be*** ~~is not~~ the record owner, ***the*** ~~but has~~ a right to some or all of the underlying benefits of ownership. These benefits include the authority to direct the voting or disposition of the interest or to receive the economic benefits of the ownership of the interest.

The committee unanimously agreed to expose for comment this revision to beneficial ownership.

The task force recommends further refinements be made to the definition of *beneficially owned*. Specific reference to the record owner is not necessary because the definition, as revised, makes it clear that a record owner who is not a beneficial owner is not included in the definition.

Beneficially owned, beneficial ownership interest. Describes a *financial interest* of which **providing** an individual or entity, ~~is not the record owner, but has a~~ **who has the** right to some or all of the underlying benefits of ownership. These benefits include the authority to direct the voting or disposition of the interest or to receive the economic benefits of the ownership of the interest.

Acquisitions and other transactions

During the May 2021 committee meeting the committee agreed that the acquisition and other business combination revisions need further refinement. The revisions requested along with the task force's response follow.

- *Request* – Replace the phrase “other business combinations” with something that would more broadly cover all the types of transactions covered by the proposal.

Response – Replace the phrase “other transaction” with “other business combinations” because it more broadly describes the transactions other than acquisitions that should be covered by the proposal.

- *Request* – Shorten the sub-headings.

Response – The task force discussed this suggestion at length but continues to believe that using headings that describe the types of situations covered will allow the reader to differentiate between the various situations presented. The task force did revise the sub-headings.

- *Request* – Consider moving or removing paragraph .06 so that it does not distract from the flow of the proposal.

Response – Because this paragraph provides an overall context of why this section is needed, the task force moved it, with some revisions, to the beginning of the section to introduce what will be covered. The new paragraph is now paragraph .05 in agenda item 1B.

- *Request* – Revise paragraph .10 so that readers can distinguish between situations covered by this paragraph and paragraph .05.

Response – To help readers distinguish between paragraph .10 and paragraph .06 (paragraph .05 was renumbered to .06 in the current draft) paragraph .10 was revised so that the lead in makes it clear that the current report may cover a period after the effective date of the acquisition, which is an important difference between the two paragraphs.

Additionally, a few members of the task force recommend adding clarification to the sub-headings preceding paragraph .06 and paragraph .10.

The subheading preceding paragraph .06 would clarify that the report does not include periods after the effective date of the acquisition and the subheading preceding paragraph .10 would indicate that the report may include periods after the effective date of the acquisition or other transaction.

Because these revisions were not unanimous, they appear in yellow highlight in agenda item 1B.

- *Request* – Develop parameters around what a “short period of time” is.

Response – Completing an engagement within a “short period of time” will be dependent upon the specific facts and circumstances of the engagement and should be left up to the member’s professional judgement.

As such, the task force has not proposed parameters at this time. The task force recommends that the explanation that accompanies the exposure draft highlight this so that if commenters have concern, they can address it in their comment letter.

Questions for the committee

1. Is the committee supportive of the proposed revision to paragraph .03 of the “Loans and Leases with Lending Institutions” interpretation (ET sec. 1.260.020)?
2. Does the committee approve the proposals in agenda items 1B and 1C for exposure?
3. Should the exposure period be for 60 or 90 days?
4. Does the committee agree that the proposals, if adopted, should be effective the last day of the month in which notice of the change appears in the *Journal of Accountancy*?
5. If the committee does not agree that the proposals, if adopted, should be effective upon publication, how long should the effective date be deferred?
6. If the committee believes the proposals should have a deferred effective date, should

early implementation be allowed?

Effective date

The task force, excepting one member, recommends that the revisions, if adopted, be effective when notice appears in the *Journal of Accountancy*. That task force member believes that because the proposals are substantive changes, there should be a delayed effective date to allow firms enough time to update their policies and procedures and quality control systems. The committee can allow early implementation for firms that can transition more quickly.

Action needed

The committee is asked to approve the proposals in agenda items 1B and 1C for exposure.

Communications plan

Staff will work with Ms. Mullins to develop an appropriate communications plan.

Materials presented

- Agenda item 1B: Proposed revised “Client Affiliates” interpretation
- Agenda item 1C: Proposed revised definition “beneficially owned”
- Agenda item 1D: Proposed revised “Loans” interpretation, “Loans and Leases with Lending Institutions” interpretation and “Immediate Family Members” interpretation

Proposed revised “Client Affiliates” interpretation

Additions appear in ***bold italic*** and deletions appear in ~~strikethrough~~.

Note: In addition to the revisions below proposed by the SEC Convergence Task Force, the Client Affiliates Task Force is proposing revisions to item (b) in paragraphs .02 and .03 of this interpretation. The Client Affiliate Task Force revisions are outlined in agenda item 2C, not in this agenda item.

1.224.010 Client Affiliates

.01 Financial interests in, and other relationships with, affiliates of a financial statement attest client may create threats to a member’s compliance with the [“Independence Rule”](#) [1.200.001].

.02 When a client is a financial statement attest client, members should apply the [“Independence Rule”](#) [1.200.001] and related interpretations applicable to the financial statement attest client to their affiliates, except in the following situations:

- a. ***During the period of the professional engagement a*** A covered member may have a loan to or from an
 - i. ***officer or director of an affiliate of a financial statement attest client unless the officer or director has the ability to affect the decision-making at the financial statement attest client.***
 - ii. ***individual with a beneficial ownership interest (known through reasonable inquiry) in an affiliate of a financial statement attest client, unless the ownership interest gives the individual significant influence over the financial statement attest client.***

~~individual who is an officer, a director, or a 10 percent or more owner of an affiliate of a financial statement attest client during the period of the professional engagement unless the covered member knows or has reason to believe that the individual is in such a position with the affiliate. If the covered member knows or has reason to believe that the individual is an officer, a director, or a 10 percent or more owner of the affiliate, the covered member should evaluate the effect that the relationship would have on the covered member’s independence by applying the [“Conceptual Framework for Independence”](#) [1.210.010].~~

- b. A member or the member's firm may provide prohibited nonattest services to entities described under items c–l of the definition of affiliate during the period of the professional engagement or during the period covered by the financial statements, provided that it is reasonable to conclude that the services do not create a self-review threat with respect to the financial statement attest client because the results of the nonattest services will not be subject to financial statement attest procedures. For any other threats that are created by the provision of the nonattest services that are not at an acceptable level (in particular, those relating to management participation), the member should apply safeguards to eliminate or reduce the threats to an acceptable level.
 - c. A firm will only have to apply the "Subsequent Employment or Association With an Attest Client" interpretation [1.279.020] of the "Independence Rule" if the former employee, by virtue of his or her employment at an entity described under items c–l of the definition of affiliate, is in a key position with respect to the financial statement attest client. Individuals in a position to influence the attest engagement and on the attest engagement team who are considering employment with an affiliate of a financial statement attest client will still need to report consideration of employment to an appropriate person in the firm and remove themselves from the financial statement attest engagement, even if the position with the affiliate is not a key position.
 - d. A covered member's immediate family members and close relatives may be employed in a key position at an entity described under items c–l of the definition of affiliate during the period of the professional engagement or during the period covered by the financial statements, provided they are not in a key position with respect to the financial statement attest client.
 - e. A covered member who is an individual on the attest engagement team, an individual in a position to influence the attest engagement, or the firm may have a lease that does not meet the requirements of the "Leases" interpretation [1.260.040] under the "Independence Rule" with an entity described under items c–l of the definition of affiliate during the period of the professional engagement. The covered member should use the "Conceptual Framework for Independence" to evaluate whether any threats created by the lease are at an acceptable level. If the covered member concludes that threats are not at an acceptable level, the covered member should apply safeguards to eliminate the threats or reduce them to an acceptable level.
- .03 A member must expend best efforts to obtain the information necessary to identify the affiliates of a financial statement attest client. If, after expending best efforts, a member is unable to obtain the information to determine which entities are affiliates of a financial statement attest client, threats would be at an acceptable level and independence would not be impaired if the member (a) discusses the matter, including the potential impact on

independence, with those charged with governance; (b) documents the results of that discussion and the efforts taken to obtain the information; and (c) obtains written assurance from the financial statement attest client that it is unable to provide the member with the information necessary to identify the affiliates of the financial statement attest client.

.04 This interpretation does not apply to a financial statement attest client that is covered by the “Entities Included in State and Local Government Financial Statements” interpretation [1.224.020] of the “Independence Rule” [1.200.001]. [Prior reference: paragraph .20 of ET section 101]

Acquisition Or Other Transaction Involving A Financial Statement Attest Client Or Its Affiliates That Results In The Creation Of A New Affiliate

.05 ***An entity may become a new affiliate of an existing financial statement attest client because of an acquisition or other transaction. A threat to independence and, therefore, to the ability of a member or member’s firm to continue a financial statement attest engagement might be created by previous or current interests or relationships between the member or member’s firm and the new affiliate. Paragraphs .06 – .13 provide guidance on how independence is impacted when such interests or relationships exist with a new affiliate.*** The exception in paragraph .06 would apply when (1) a financial statement attest client is acquired during the period of the professional engagement by either a nonclient or a nonattest client (acquirer), (2) the attest engagement covers only periods prior to the acquisition, and (3) the member or member’s firm will not continue to provide financial statement attest services to the acquirer.

An Existing Financial Statement Attest Client Is Acquired, And The Member Or Member’s Firm Will Not Continue Providing Financial Statement Attest Services To Such Client After The Current Attest Report Is Issued [And The Report Does Not Include Periods After The Effective Date Of The Acquisition]

.06 Independence will not be considered impaired with respect to the financial statement attest client because ***When*** a member or member’s firm has an interest in or relationship with the ***an*** acquirer that may otherwise impair independence as a result of the requirements of this interpretation or the definition of “attest client” (as it relates to the entity or person that engages the member or member’s firm to perform the attest engagement), ***independence with respect to the financial statement attest client will not be considered impaired if all of the following conditions are met:***

- a. The acquisition occurs during the period of the professional engagement.***
- b. The financial statement attest engagement covers only periods prior to the effective date of the acquisition.***
- c. The member or member’s firm will not continue to provide financial statement***

attest services to the existing financial statement attest client related to periods after the effective date of the acquisition.

~~.07 Notwithstanding paragraph .06, a member should give consideration to the requirements of the “Conflicts of Interest” interpretation [1.110.010], under the “Integrity and Objectivity Rule” [1.100.001], with regard to any relationships that the member knows or has reason to believe exist with the acquirer, the financial statement attest client, or the firm.~~

~~.08 A member should refer to paragraph .03 of “Application of the AICPA Code” [0.200.020] for guidance on circumstances involving foreign network firms.~~

An Existing Financial Statement Attest Client Or Its Affiliate Is Involved In An Acquisition Or Other Transaction And The Member Or Member’s Firm Expects To Continue Providing Financial Statement Attest Services To Such Client

.07 When an acquisition or other transaction creates a new affiliate of a financial statement attest client during the period of professional engagement and the member or member’s firm expects to continue providing financial statement attest services to the financial statement attest client after the effective date of the acquisition or other transaction:

- a. The member or member’s firm should identify and evaluate previous and current interests in and relationships with the new affiliate that, taking into account any actions taken to address the threat to independence, might affect its independence and therefore its ability to continue the financial statement attest engagement after the effective date of the acquisition or other transaction.***
- b. Except as provided for in paragraph .08, the member or member’s firm should take steps to end any interests in or relationships with the new affiliate that would impair independence by the effective date of the acquisition or other transaction.***

.08 As an exception to paragraph .07b., if the interest in or relationship with the new affiliate cannot reasonably be ended by the effective date of the acquisition or other transaction (for example, the new affiliate is not able to transition a nonattest service in an orderly manner to another service provider by that date), the member or member’s firm should do the following:

- a. Evaluate the threat to independence that is created by the interest or relationship. Factors that are relevant in evaluating the level of a threat when there are interests and relationships with a new affiliate that cannot reasonably be ended could include:***

- i. The nature and significance of the interest or relationship*
 - ii. The nature and significance of the affiliate relationship (for example, whether the affiliate is a subsidiary, parent or sister entity)*
 - iii. The length of time until the interest or relationship can reasonably be ended*
- b. Discuss with those charged with governance the reasons why the interest or relationship cannot reasonably be ended by the effective date of the acquisition or other transaction and the evaluation of the level of the threat.*
- .09 Following the discussion in paragraph .08 b., if those charged with governance request the member or member's firm to continue to provide financial statement attest services to the financial statement attest client, the member or member's firm should do so only under the following circumstances:**
- a. The interest in or relationship with the new affiliate that would impair independence will end as soon as reasonably possible but no later than six months after the effective date of the acquisition or other transaction.*
 - b. Any individual who has such an interest in or relationship with the new affiliate, including one that has arisen through performing a nonattest service that would impair independence under the "Nonattest Services" [1.295] subtopic of the "Independence Rule," [1.200.001] will not be a member of the attest engagement team or an individual responsible for the engagement quality control review.*
 - c. Transitional measures will be applied, as necessary, and discussed with those charged with governance.*

An Existing Financial Statement Attest Client Or Its Affiliate Is Involved In An Acquisition Or Other Transaction And The Member Or Member's Firm Will Complete The Existing Financial Statement Attest Engagement But Will Not Continue Providing Such Services After The Current Attest Report Is Issued [But The Report May Include Periods After The Effective Date Of The Acquisition Or Other Transaction]

- .10 When a member or member's firm will not continue to provide financial statement attest services to the financial statement attest client that is involved in an acquisition or other transaction, the member or member's firm may issue the current report covering a period after the effective date of the acquisition or other transaction if all of the following criteria are met:**
- a. The member or member's firm completed a significant amount of work on the current financial statement attest engagement prior to the effective date of the*

acquisition or other transaction.

- b. The member or member's firm expects to complete the remaining financial statement attest procedures within a short period of time.*
- c. Those charged with governance request that the member or member's firm complete the financial statement attest engagement despite the member or member's firm continuing to have an interest in or relationship with the new affiliate that would impair independence.*
- d. The member or member's firm has evaluated the level of the threat to independence and discussed the results with those charged with governance.*
- e. The member or member's firm complies with the requirements of paragraph .09 b and c.*
- f. The member or member's firm ceases to be the auditor no later than the date that the attest report is issued.*

Other Considerations When An Existing Financial Statement Attest Client Or Its Affiliate Is Involved In An Acquisition Or Other Transaction

Objectivity

.11 Even if all the requirements of paragraphs .06– .10 could be met, the member or member's firm should give consideration to the requirements of the "Conflicts of Interest for Members in Public Practice" interpretation [1.110.010] under the "Integrity and Objectivity Rule" [1.100.001], with regard to any circumstances identified in paragraphs .06, .07 or .10.

Documentation

.12 The member or member's firm should consider documenting the following:

- a. Any interests or relationships identified in paragraphs .07 or .10 that will not be ended by the effective date of the acquisition or other transaction and the reasons they will not be ended*
- b. The transitional measures applied, if appropriate*
- c. The results of the discussion with those charged with governance*
- d. The reasons the previous and current interests and relationships do not create a threat such that objectivity would be compromised*

Circumstances Involving Foreign Network Firms

.13 .08A member should refer to paragraph .03 of "Application of the AICPA Code" [0.200.020] for guidance on circumstances involving foreign network firms.

Proposed revised definition “beneficially owned”

(Additions are presented in bold italic text. Deletions are presented in strikethrough.)

0.400 Definitions

.06 Beneficially owned, *beneficial ownership interest*. Describes a *financial interest* of which ***providing*** an individual or entity, ~~is not the record owner, but has a~~ ***who has the*** right to some or all of the underlying benefits of ownership. These benefits include the authority to direct the voting or disposition of the interest or to receive the economic benefits of the ownership of the interest.

Proposed revised “Loans” interpretation

Additions are presented in ***bold italic*** text. Deletions are presented in ~~strikethrough~~.

1.260.010 Loans

.01 If a covered member has a loan to or from an attest client, any officer or director of the attest client ***who has the ability to affect decision-making***, or any individual ***with a beneficial ownership interest (known through reasonable inquiry) that gives the individual significant influence over***~~owning 10 percent or more of the attest client’s outstanding equity securities or other ownership interests~~, a self-interest threat to the covered member’s compliance with the “Independence Rule” [1.200.001] may exist. Threats would not be at an acceptable level and independence would be impaired if the loan exists during the period of the professional engagement, except as provided for in the

- a. “Loans and Leases With Lending Institutions” interpretation [1.260.020] of the “Independence Rule.”
- b. ***“Client Affiliates” interpretation [1.224.010] of the “Independence Rule.”***

Proposed revised “Loans and Leases with Lending Institutions” interpretation

(Additions are presented in ***bold italic*** text. Deletions are presented in ~~strikethrough~~.)

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 ***who has the ability to affect decision-making***, or any individual ***with a beneficial ownership interest (known through reasonable inquiry) that gives the individual significant influence over*** ~~owning 10 percent or more of the attest client’s outstanding equity securities or other ownership interests~~, except as provided for in this interpretation.

Home Mortgages, Other Secured Loans, and Immaterial Unsecured Loans, and Student Loans. ~~Secured loans, home mortgages, immaterial unsecured loans and student loans.~~

.02 The loans covered by paragraph .03 include secured loans, home mortgages, other secured loans, unsecured loans that are not material to the covered member’s net worth (that is, immaterial unsecured loans), and student loans.

.03 ~~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 ***any of the loans identified in paragraph .02*** ~~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~~ ***loans were*** obtained under the lending institution’s normal lending procedures, terms, and requirements. ~~In determining when the home mortgage, secured loan, or immaterial unsecured loans was were 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 loans were was~~ obtained in one of the following ways (In determining when the ~~home mortgage, secured loan, or immaterial unsecured loans was were~~ 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.)

c.

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 **the member** ~~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/professionalethics/community/downloadabledocuments/transistion%20periods.pdf are met.
- d. After becoming a covered member, any ~~home mortgage, secured loan, or immaterial unsecured loans~~ 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.
- e. The estimated fair value of the collateral for ~~a home mortgages~~ or other secured loans ~~must~~ **should** equal or exceed the outstanding balance during the term of the home mortgages or other secured loans. If the estimated fair value of the collateral is less than the outstanding balance of the home mortgages or other secured loans, the portion that exceeds the estimated fair value of the collateral may not be material to the covered member's net worth.

Loans to Partnerships and Other Similar Entities

.04 For purposes of applying the loan provision in paragraph .02 when the covered member is a partner in a partnership, a loan to a limited partnership (or similar type of entity) or general partnership would be ascribed to each covered member who is a partner in the partnership on the basis of his or her legal liability as a limited or general partner if

- a. the covered member's interest in the limited partnership, either individually or combined with the interest of one or more covered members, exceeds 50 percent of the total limited partnership interest, or
- b. the covered member, either individually or together with one or more covered members, can control the general partnership.

Even if no amount of a partnership loan is ascribed to the covered member(s) previously identified, 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 through the application of safeguards if the partnership renegotiates a loan or obtains a new loan that is not a permitted loan, as described in paragraph .04 of this interpretation. Accordingly, independence would be impaired.

Other Loans and Leases

- .05 Threats would be at an acceptable level and independence would not be impaired if a covered member obtains one of the following types of loans or leases under the lending institution's normal lending procedures, terms, and requirements, provided the covered member complies with the terms of the loan or lease agreement at all times (for example, keeping payments current):
- a. Automobile loans and leases collateralized by the automobile
 - b. Loans fully collateralized by the cash surrender value of an insurance policy
 - c. Loans fully collateralized by cash deposits at the same lending institution (for example, passbook loans)
 - d. ~~Aggregate outstanding balances from~~ **Consumer loans (for example, credit cards, retail installment loans, and home improvement loans)** and overdraft reserve accounts **from the same lending institution** that have an **aggregate outstanding** balance of \$10,000 or less **on a current basis taking into consideration the** after payment ~~of the most recent monthly statement made by the due date or within~~ **and** any available grace period

Other Matters

- .06 Members should consider that certain state and federal agencies may proscribe more restrictive requirements over lending institutions that are subject to their oversight and that, in turn, impose more restrictive requirements upon members that perform attest engagements for these lending institutions. For example, the Securities and Exchange Commission (SEC) proscribes more restrictive requirements over members providing attest services to lending institutions and broker-dealers within their purview. [Prior reference: paragraph .07 of ET section 101 and paragraphs .150–.151 of ET section 191]
- .07 Covered members may be subject to additional restrictions, as described in the “Depository Accounts” interpretation [1.255.010], ~~and the~~ “Member of a Credit Union” interpretation [1.280.040] **and the “Leases” interpretation [1.260.040]** of the “Independence Rule” [1.200.001].

Proposed revised “Immediate Family Members” interpretation

(Additions are presented in ***bold italic*** text. Deletions are presented in ~~strike through~~.)

1.270.010 Immediate Family Members (excerpt)

.03 When materiality of a financial interest ***or a loan*** is identified as a factor affecting independence in the interpretations of the “Independence Rule” [1.200.001], interests of the immediate family member and the covered member should be combined to determine materiality to the covered member.

Client affiliates

Task force members

Lisa Snyder (chair), Marie Brilmyer, Robert Denham, Anna Dourdourekas, Ryan Willers, Lawrence Wojcik

Observers

David Bibb, Alina Kalachyuk, Liz McKneely, Lori West

AICPA staff

Ellen Gorla, John Wiley

Task force charge

Determine whether current client affiliates guidance should be applied to individuals and whether any other aspects of the client affiliate interpretation need clarification (e.g., pooled employee benefit plans, SEC merger and acquisition guidance).

Reason for agenda item

The committee is asked to approve exposing revisions to the definition of an affiliate as outlined in agenda item 2B and revisions to the “Client Affiliates” interpretation as outlined in agenda item 2C.

Background

Definition of affiliate

The definition of “affiliate” currently extends to common ownership by entities and not common ownership by individuals. The strategy and work plan consultation paper indicated that there are frequent inquiries regarding whether entities that are owned by the same individual should be considered affiliates.

Task force activities

The task force considered whether revisions should be made to the definition of *affiliate* (i.e., authoritative guidance) or whether non-authoritative guidance such as a Q&A would be sufficient. Because the current definition of affiliate does not apply to individuals, the task force believes it would be inappropriate to issue non-authoritative interpretive guidance and agrees that the definition itself should be revised.

The task force believes the following:

- The definition of affiliate should include the circumstances in which affiliate relationships are created when both entities and individuals are involved.
- The definitions of control and significant influence, which are integral to the definition of

an affiliate, can be applied to individuals.

- A member should not form a different conclusion based on whether the individual decides to establish a corporation, partnership, or other type of entity to operate the business.
- Only defined affiliates (c), (d) and (e) require revision because these affiliates involve upstream or “up and over” situations in which the individual would have either control or significant influence over the financial statement attest client.
- Affiliates (a) and (b) do *not* need to be revised because these involve downstream situations in which a financial statement attest client would have to either control or have significant influence over an individual.
- Affiliates (f) and (i) do *not* need to be revised because, as drafted, the terminology (i.e., trustee, investment advisor, general partner) could be extended to individuals that are trustees or have control/ significant influence over a fund.

Summary of issues

Board members and members of management

During the May PEEC meeting the committee questioned whether the task force had considered the implications of board members or members of management being scoped in as an affiliate if individuals are added to the affiliate definition.

The task force had considered that the proposed revisions include individuals — affiliates (c), (d), and (e) in agenda item B — but did not specifically discuss board members or members of management.

When preparing initial revisions for PEEC’s consideration, the task force concluded that an individual should be considered an affiliate and subject to the current affiliates independence guidance in agenda item C if that individual has a direct financial interest in the attest client as well as significant influence over the attest client and the financial interest in the attest client is material to that individual. In the original context, individual is the business owner, and the application of the affiliates guidance regarding independence requirements is be the same as it would be to upstream and downstream entities today.

Upon considering the committee’s questions, the task force concluded that the same affiliate relationships could occur with board members or members of management. An example is if a member of management has a material investment in the company that provides them with significant influence over the company.

If a board member or member of management is determined to be an affiliate and subject to the independence guidance, any nonattest services provided to these individuals will generally not create independence issues when the exception described in paragraph .02b of the “Client

Affiliates” interpretation is applicable.

A board member or member of management should not be considered an affiliate solely because that person might have significant influence over the company. However, if an ownership interest material to that person is present, then paragraph .02d is applicable.

Multiple employer employee benefit plans

If the committee agrees to issue an exposure draft to revise the definition of affiliate for individuals, the task force recommends the exposure draft include a clarification for multiple employer employee benefit plans (MEP).

While developing Qs & As in response to inquiries about pooled employer plans, staff learned from members of the Employee Benefit Plan Expert Panel that though a participating employer may be named as the plan administrator for these plans, other entities can also hold this position.

This is important because under item (i) of the affiliate definition, the code considers a participating employer an affiliate only when the employer is the plan administrator:

- i.* The participating employer that is the plan administrator of a multiple employer employee benefit plan financial statement attest client.

In researching the question, staff looked at the division’s existing [FAQs: Application of the independence rules to affiliates of employee benefit plans](#). One of those Qs & As explains that when it comes to a MEP, the participating sponsor that has overall responsibility for plan governance is the party that should be considered an affiliate of the plan. This is the party who oversees the day to day operations of the plan, whether directly or by outsourcing

Given this conclusion, staff recommended, and the task force concurred at its July meeting, that item (i) in the definition of an affiliate should be revised and exposed as follows to make it clear that any entity that is the plan administrator, should be considered an affiliate of a MEP financial statement attest client as included in agenda item 2B:

- i.* The ~~participating employer that is the~~ plan administrator of a multiple employer employee benefit plan financial statement attest client.

“Client Affiliates” interpretation

During the May PEEC meeting, the committee noted that certain areas in the “Client Affiliates” interpretation need to be updated to reflect the proposed addition of individuals to the definition of affiliates. These updates are shown in bold italics in agenda item C.

Effective date

The task force discussed whether a delayed effective date would be appropriate and concluded that as there may be diversity in practice on how firms currently apply the affiliate rules to individuals, a six-month delayed effective date would be appropriate.

Questions for the committee

1. Does the committee agree that the affiliate definition should be revised to include individuals?
2. Does the committee believe that there are no unintended consequences of board members and members of management becoming affiliates of the attest client under the proposed changes to the affiliate definition?
3. Does the committee agree with the proposed revision to item (i) of the affiliate definition as discussed above regarding MEPs?
4. Does the committee agree with the proposed revisions to the “Client Affiliates” interpretation to reflect the addition of individuals to the affiliate definition?
5. Does the committee agree with the proposed six-month delay of the effective date?

Action needed

The committee is asked to approve the proposals in agenda items 2B and 2C for exposure and to decide what effective date would be appropriate.

Communication plan

Staff will work with Ms. Mullins to develop an appropriate communications plan.

Materials presented

- Agenda item 2B: Definitions of affiliate, significant influence, and control
- Agenda item 2C: Text of “Client Affiliates” interpretation

Definitions of affiliate, significant influence, and control

Proposed additions appear in ***boldface italic***. Deletions appear in ~~strikethrough~~. The definitions of control and significant influence are included for reference purposes only.

0.400.02 Affiliate

.02 The following entities are affiliates of a financial statement attest client:

- a. An entity (for example, subsidiary, partnership, or limited liability company [LLC]) that a financial statement attest client can control.
- b. An entity in which a financial statement attest client or an entity controlled by the financial statement attest client has a direct financial interest that gives the financial statement attest client significant influence over such entity and that is material to the financial statement attest client.
- c. An ***individual or*** entity (for example, parent, partnership, or LLC) that controls a financial statement attest client when the financial statement attest client is material to such ***individual or*** entity.
- d. An ***individual or*** entity with a direct financial interest in the financial statement attest client when that ***individual or*** entity has significant influence over the financial statement attest client, and the interest in the financial statement attest client is material to such ***individual or*** entity.
- e. A sister entity of a financial statement attest client if the financial statement attest client and sister entity are each material to the ***individual or*** entity that controls both.
- f. A trustee that is deemed to control a trust financial statement attest client that is not an investment company.
- g. The sponsor of a single employer employee benefit plan financial statement attest client.
- h. Any entity, such as a union, participating employer, or a group association of employers, that has significant influence over a multiemployer employee benefit plan financial statement attest client and the plan is material to such entity.
- i. ~~The participating employer that is the~~ plan administrator of a multiple employer employee benefit plan financial statement attest client.
- j. A single or multiple employer employee benefit plan sponsored by either a financial statement attest client or an entity controlled by the financial statement attest client. All participating employers of a multiple employer employee benefit plan are considered sponsors of the plan.

- k. A multiemployer employee benefit plan when a financial statement attest client or entity controlled by the financial statement attest client has significant influence over the plan and the plan is material to the financial statement attest client.
- l. An investment adviser, a general partner, or a trustee of an investment company financial statement attest client (fund) if the fund is material to the investment adviser, general partner, or trustee that is deemed to have either control or significant influence over the fund. When considering materiality, members should consider investments in, and fees received from, the fund.

0.400.10 Control, controls, controlled

.10 As used in FASB Accounting *Standards Codification* (ASC) 810, *Consolidation*. When used in the “Client Affiliates” interpretation [1.224.010] of the “Independence Rule” [1.200.001], control depends upon the entity in question. For example, when used for not-for-profit entities, control is as used in FASB ASC 958-805-20; for commercial entities, control is as used in FASB ASC 810.

For reference purposes, FASB ASC 958-805-20 defines Control - The direct or indirect ability to determine the direction of management and policies through ownership, contract, or otherwise.

0.400.45 Significant Influence

.45 As defined in FASB ASC 323-10-15.

For reference purposes, FASB ASC 323-10-15-6 Ability to exercise significant influence over operating and financial policies of an investee may be indicated in several ways, including the following:

- a. Representation on the board of directors
- b. Participation in policy-making processes
- c. Material intra-entity transactions
- d. Interchange of managerial personnel
- e. Technological dependency
- f. Extent of ownership by an investor in relation to the concentration of other shareholdings (but substantial or majority ownership of the voting stock of an investee by another investor does not necessarily preclude the ability to exercise significant influence by the investor).

15-7 Determining the ability of an investor to exercise significant influence is not always clear and applying judgment is necessary to assess the status of each

investment.

15-8 An investment (direct or indirect) of 20 percent or more of the voting stock of an investee shall lead to a presumption that in the absence of predominant evidence to the contrary an investor has the ability to exercise significant influence over an investee. Conversely, an investment of less than 20 percent of the voting stock of an investee shall lead to a presumption that an investor does not have the ability to exercise significant influence unless such ability can be demonstrated. The equity method shall not be applied to the investments described in this paragraph insofar as the limitations on the use of the equity method outlined in paragraph 323-10-25-2 would apply to investments other than those in subsidiaries.

15-9 An investor's voting stock interest in an investee shall be based on those currently outstanding securities whose holders have present voting privileges. Potential voting privileges that may become available to holders of securities of an investee shall be disregarded.

15-10 Evidence that an investor owning 20 percent or more of the voting stock of an investee may be unable to exercise significant influence over the investee's operating and financial policies requires an evaluation of all the facts and circumstances relating to the investment. The presumption that the investor has the ability to exercise significant influence over the investee's operating and financial policies stands until overcome by predominant evidence to the contrary. Indicators that an investor may be unable to exercise significant influence over the operating and financial policies of an investee include the following:

- a. Opposition by the investee, such as litigation or complaints to governmental regulatory authorities, challenges the investor's ability to exercise significant influence.
- b. The investor and investee sign an agreement (such as a standstill agreement) under which the investor surrenders significant rights as a shareholder. (Under a standstill agreement, the investor usually agrees not to increase its current holdings. Those agreements are commonly used to compromise disputes if an investee is fighting against a takeover attempt or an increase in an investor's percentage ownership. Depending on their provisions, the agreements may modify an investor's rights or may increase certain rights and restrict others compared with the situation of an investor without such an agreement.)
- c. Majority ownership of the investee is concentrated among a small group of shareholders who operate the investee without regard to the views of the investor.
- d. The investor needs or wants more financial information to apply the equity method

than is available to the investee's other shareholders (for example, the investor wants quarterly financial information from an investee that publicly reports only annually), tries to obtain that information, and fails.

- e. The investor tries and fails to obtain representation on the investee's board of directors.

15-11 The list in the preceding paragraph is illustrative and is not all-inclusive. None of the individual circumstances is necessarily conclusive that the investor is unable to exercise significant influence over the investee's operating and financial policies. However, if any of these or similar circumstances exists, an investor with ownership of 20 percent or more shall evaluate all facts and circumstances relating to the investment to reach a judgment about whether the presumption that the investor has the ability to exercise significant influence over the investee's operating and financial policies is overcome. It may be necessary to evaluate the facts and circumstances for a period of time before reaching a judgment.

Text of “Client Affiliates” interpretation

Proposed additions appear in ***boldface italic***. The definitions of control and significant influence are included for reference purposes only.

Note: In addition to the revisions below proposed by the Client Affiliates Task Force, the SEC Convergence Task Force is proposing revisions to item (a) in paragraph .02 and paragraphs .05–.09 of this interpretation. The SEC convergence revisions are outlined in agenda item 1B, not in this agenda item.

1.224.10 Client Affiliates

- .01 *Financial interests* in, and other relationships with, *affiliates* of a *financial statement attest client* may create *threats* to a *member’s* compliance with the [“Independence Rule”](#) [1.200.001].
- .02 When a client is a *financial statement attest client*, *members* should apply the [“Independence Rule”](#) [1.200.001] and related interpretations applicable to the *financial statement attest client* to their *affiliates*, except in the following situations:
- a. A *covered member* may have a *loan* to or from an individual who is an officer, a director, or a 10 percent or more owner of an *affiliate* of a *financial statement attest client* during the *period of the professional engagement* unless the *covered member* knows or has reason to believe that the individual is in such a position with the *affiliate*. If the *covered member* knows or has reason to believe that the individual is an officer, a director, or a 10 percent or more owner of the *affiliate*, the *covered member* should evaluate the effect that the relationship would have on the *covered member’s independence* by applying the [“Conceptual Framework for Independence”](#) [1.210.010].
 - b. A *member* or the *member’s firm* may provide prohibited nonattest services to ***individuals or*** entities described under items *c–l* of the definition of *affiliate* during the *period of the professional engagement* or during the *period covered by the financial statements*, provided that it is reasonable to conclude that the services do not create a self-review threat with respect to the *financial statement attest client* because the results of the nonattest services will not be subject to *financial statement attest procedures*. For any other *threats* that are created by the provision of the nonattest services that are not at an *acceptable level* (in particular, those relating to management participation), the *member* should apply *safeguards* to

eliminate or reduce the *threats* to an acceptable level.

- c. A *firm* will only have to apply the “[Subsequent Employment or Association With an Attest Client](#)” interpretation [1.279.020] of the “Independence Rule” if the former employee, by virtue of his or her employment at an entity described under items c–l of the definition of *affiliate*, is in a *key position* with respect to the *financial statement attest client*. *Individuals in a position to influence the attest engagement* and on the *attest engagement team* who are considering employment with an *affiliate* of a *financial statement attest client* will still need to report consideration of employment to an appropriate person in the *firm* and remove themselves from the *financial statement attest engagement*, even if the position with the *affiliate* is not a *key position*.
- d. A *covered member’s immediate family members* and *close relatives* may be employed in a *key position* at an entity described under items c–l of the definition of *affiliate* during the *period of the professional engagement* or during the period covered by the *financial statements*, provided they are not in a *key position* with respect to the *financial statement attest client*.
- e. A *covered member* who is an individual on the *attest engagement team*, an individual in a position to influence the *attest engagement*, or the *firm* may have a lease that does not meet the requirements of the “[Leases](#)” interpretation [1.260.040] under the “[Independence Rule](#)” with an entity described under items c–l of the definition of *affiliate* during the period of the professional engagement. The *covered member* should use the “[Conceptual Framework for Independence](#)” to evaluate whether any *threats* created by the lease are at an *acceptable level*. If the *covered member* concludes that *threats* are not at an *acceptable level*, the *covered member* should apply *safeguards* to eliminate the *threats* or reduce them to an *acceptable level*.

.03 A *member* must expend best efforts to obtain the information necessary to identify the *affiliates* of a *financial statement attest client*. If, after expending best efforts, a *member* is unable to obtain the information to determine which ***individuals or*** entities are *affiliates* of a *financial statement attest client*, *threats* would be at an *acceptable level* and *independence* would not be *impaired* if the *member* (a) discusses the matter, including the potential impact on *independence*, with *those charged with governance*; (b) documents the results of that discussion and the efforts taken to obtain the information; and (c) obtains written assurance from the *financial statement attest client* that it is unable to provide the *member* with the information necessary to identify the *affiliates* of the *financial statement attest client*.

.04 This interpretation does not apply to a *financial statement attest client* that is covered by the “[Entities Included in State and Local Government Financial Statements](#)” interpretation [1.224.020] of the “Independence Rule” [1.200.001]. [Prior reference: paragraph .20 of ET section 101]

Acquisitions and Other Business Combinations That Involve a Financial Statement Attest Client

- .05 The exception in [paragraph .06](#) would apply when (1) a *financial statement attest client* is acquired during the *period of the professional engagement* by either a non-client or a nonattest client (acquirer), (2) the *attest engagement* covers only periods prior to the acquisition, and (3) the *member* or *member's firm* will not continue to provide *financial statement* attest services to the acquirer.
- .06 *Independence* will not be considered *impaired* with respect to the *financial statement attest client* because a *member* or *member's firm* has an interest in or relationship with the acquirer that may otherwise *impair independence* as a result of the requirements of this interpretation or the definition of "*attest client*" (as it relates to the entity or person that engages the member or member's firm to perform the *attest engagement*).
- .07 Notwithstanding [paragraph .06](#), a *member* should give consideration to the requirements of the "[Conflicts of Interest](#)" interpretation [1.110.010], under the "Integrity and Objectivity Rule" [1.100.001], with regard to any relationships that the *member* knows or has reason to believe exist with the acquirer, the *financial statement attest client*, or the *firm*.
- .08 A member should refer to [paragraph .03](#) of "Application of the AICPA Code" [0.200.020] for guidance on circumstances involving foreign network firms.

Effective Date

- .09 [Paragraphs .01–.04](#) are *effective* for engagements covering periods beginning on or after January 1, 2014. Early implementation is allowed.

Unpaid fees

Task force members

Bill McKeown (chair), Tom Campbell, Jeff Lewis, Alan Long, Susan Siegmund, Douglas Warren

Observers

Hanna Baillie, Dan Dodson, Jan Neal, Shana Wolfson

AICPA staff

Michele Craig, Ellen Gorla, Summer Young

Task force charge

Develop a framework for members to determine whether unpaid fees are, in substance, equivalent to a loan. Further, given the current situation related to the COVID-19 pandemic, the task force will consider whether a bright line of one year is appropriate.

The task force believes this charge should be expanded to converge with other standard setters, such as IESBA, the US SEC, and for consistency with other provisions of the AICPA code. In addition, the task force believes a principle-based framework will assist with addressing some of the issues raised as a result of the COVID-19 pandemic as well as future unusual situations. Accordingly, the task force recommends that the charge be revised as follows:

Develop a principles-based framework for members to determine when unpaid fees impair independence.

Reason for agenda item

The committee is asked to approve the proposed revised task force charge and to approve exposing revisions to the “Unpaid Fees” interpretation as outlined in agenda item 3B.

Task force activities

Background

The “Unpaid Fees” interpretation concludes that independence is impaired when a covered member has unpaid fees, regardless of the amount, from an attest client for any previously rendered professional service provided more than one year prior to the date of the current year report. The current related Q&A adds that this situation essentially constitutes a debt to the firm.

On the division’s ethics hotline, staff routinely responds to questions regarding the “Unpaid Fees” interpretation:

- Can fees be written off in order to obtain independence? (This is the most common question on the hotline regarding unpaid fees.)

- What if a client needs an issued audit report to obtain bank financing and the unpaid fees can be paid only after the client obtains the financing?
- What if a client needs an issued audit report to obtain an equity raise and the unpaid fees can be paid only after the client obtains the capital?
- Is there an exception to the “Unpaid Fees” interpretation given the COVID-19 pandemic? (Staff notes the only current exception allowed in the “Unpaid Fees” interpretation is for clients in bankruptcy.)

Anecdotally, staff and the task force noted that members sometimes refer to the “Unpaid Fees” interpretation to facilitate collection of past due amounts from clients.

Recommendations

The committee should implement a principles-based framework as the task force agrees, in general, that the current interpretation is too restrictive.

As the interpretation is currently written, an unpaid fee of \$0.01 would technically impair independence if a member provided professional services related to the unpaid fee more than one year prior to the date of the current year attest report. Having a principles-based framework would converge the AICPA with IESBA and the SEC.

The task force agreed to retain the one-year bright-line threshold as the trigger event to evaluate threats to independence although IESBA and the SEC do not include such a threshold.

The IESBA standards focus on potential threats created when a significant part of fees is not paid before the audit report for the following year is issued. The SEC standards focus on potential threats created when the prior year audit fee and other unpaid professional fees are not paid before the current audit engagement starts.

The task force also agreed that fees for all professional services should be considered when evaluating unpaid fees in relation to attest services, which is consistent with the SEC’s guidance.

The task force recommends the following revisions to the “Unpaid Fees” interpretation (see agenda item 3B):

- Principles-based framework – Provides less restrictive rules and allows for member judgment
 - Factors to consider – See paragraph .02
 - Significance of fees
 - Time outstanding

- Client's ability to pay
- Threshold – See paragraph .03
 - It is not appropriate to set a specific dollar or percentage threshold in this interpretation. Instead, the term “clearly insignificant” should be used. This is the term used in the “Gifts and Entertainment” interpretation (ET sec. 1.285.010), and “significant” as opposed to “material” to align with IESBA and the SEC.
 - Essentially, unpaid fees that are clearly insignificant and less than a year overdue will not impair independence. Alternatively, significant fees unpaid for more than one year will result in significant threats to a *covered member's* compliance with the “Independence Rule” (ET sec. 1.200.001).
 - The one-year timeframe should continue to be the triggering event to evaluate unpaid fees as a threat to independence but the dollar threshold would allow members to use professional judgment and apply safeguards if needed.
- Examples of actions that might be safeguards – See paragraph .04
 - Provide an additional level of review
 - Offer a partial payment or payment schedule
 - Suspend work on current engagement and not accept new engagements
 - Communicate with those charged with governance
- Advocacy threat – The advocacy threat does not apply and should be removed from the interpretation.

Other considerations

The task force considered whether there are threats to independence when the attest client needs the firm's audit report to obtain financing from which the member's fees will be paid. As unpaid fees would not be more than a year overdue, the task force noted the conceptual framework should be applied and proposes adding a non-authoritative Q&A (agenda item 3D).

Effective date

The task force recommends a six-month deferred effective date with early adoption permitted.

Questions for the committee

1. Does the committee agree with the proposed revision to the task force charge?
2. Does the committee have suggestions on the draft interpretation or concerns with using a principles-based framework, or both?
3. Does the committee agree the safeguards in .04a and .04d are clearly delineated?
4. Does the committee agree that independence considerations exist when the attest client needs the firm's audit report to obtain financing from which the member's fees will be paid?
5. Does the committee agree the concern in question 4 should be addressed in a non-authoritative Q&A? Does the committee have changes to the proposed language of that Q&A?
6. Does the committee approve the proposal in agenda item 3B for exposure?
7. Does the committee agree the exposure period should be limited to 60 days?
8. Does the committee agree a six-month deferred effective date with early implementation is appropriate?

Action needed

The committee is asked to approve the proposals in agenda item 3B for exposure and agenda item 3D for publication.

Communications plan

Staff will work with Ms. Mullins to develop an appropriate communications plan.

Materials presented

- Agenda item 3B: Proposed revised "Unpaid Fees" interpretation (red line)
- Agenda item 3C: Proposed revised "Unpaid Fees" interpretation (clean)
- Agenda item 3D: Proposed Q&A related to unpaid fees
- Agenda item 3E: SEC excerpt: Unpaid fees Q&A
- Agenda item 3F: IESBA excerpt: Unpaid fees

Proposed revised “Unpaid Fees” interpretation (red line)

Proposed additions appear in ***boldface italic***. Deletions appear in ~~strikethrough~~.

1.230.010 *Unpaid Fees*

.01 The existence of unpaid fees to a *covered member* for *professional services* previously rendered to an *attest client* may create self-interest, ~~or~~ ***undue influence, or advocacy threats*** to the *covered member’s* compliance with the “Independence Rule” [1.200.001]. ***Unpaid fees include fees that are unbilled or a note receivable arising from such fees.***

.02 ***Factors to consider when evaluating whether threats are at an acceptable level include:***

- a. ***The significance of the unpaid fees to the covered member.***
- b. ***The length of time the fees have been due from the attest client.***
- c. ***The covered member’s assessment of factors affecting the ability and willingness of the attest client to pay the fees.***

.03 ~~Threats to the covered member’s compliance with the “Independence Rule” [1.200.001] would not be~~ ***are at an acceptable level when unpaid fees are both clearly insignificant to the covered member and relate to*** and could not be reduced to an ~~acceptable level~~ by the application of ~~safeguards~~ if a ~~covered member~~ has unpaid fees from an ~~attest client~~ for any previously rendered professional services provided ~~more~~ ***less*** than one year prior to the issue date of the current-year ***attest*** report. ***Alternatively, threats would not be at an acceptable level when unpaid fees are both significant to the covered member and relate to professional services provided more than one year prior to the issue date of the current-year attest report. Other situations require judgment to assess the threats to the covered member’s compliance with the “Independence Rule”.*** ~~Accordingly, independence would be impaired.~~ Unpaid fees include fees that are unbilled or a note receivable arising from such fees.

.04 ***If the covered member concludes that threats are not at an acceptable level, then the covered member should apply safeguards to eliminate the threats or reduce them to an acceptable level. If safeguards are not available or cannot be applied to eliminate or reduce the threats to an acceptable level, then independence would be impaired.***

Examples of actions that might be safeguards:

- a. ***Have an appropriate reviewer who has not provided attest or nonattest services to the attest client review the attest work performed before the current-year attest report is issued.***
- b. ***Obtain partial payment of the unpaid fees balance.***

- c. Agree to a payment schedule before the current-year attest report is issued.*
- d. Select the current attest engagement for pre-issuance or post-issuance review.*
- e. Suspend further work on current attest engagements and not accept new engagements until the unpaid fees are clearly insignificant to the covered member.*
- f. Communicate with those charged with governance regarding the unpaid fees and the other safeguards applied.*

.035 This interpretation does not apply to ~~fees outstanding~~ **unpaid fees** from an *attest client* in bankruptcy. [Prior reference: paragraphs .103–.104 of ET section 191]

.046 Refer to the “Fees and Other Types of Remuneration” topic [1.500] for additional guidance.

Proposed revised “Unpaid Fees” interpretation (clean)

1.230.010 *Unpaid Fees*

.01 The existence of unpaid fees to a *covered member* for *professional services* previously rendered to an *attest client* may create self-interest or undue influence *threats* to the *covered member's* compliance with the “Independence Rule” [1.200.001]. Unpaid fees include fees that are unbilled or a note receivable arising from such fees.

.02 Factors to consider when evaluating whether *threats* are at an *acceptable level* include:

- a. The significance of the unpaid fees to the *covered member*.
- b. The length of time the fees have been due from the *attest client*.
- c. The *covered member's* assessment of factors affecting the ability and willingness of the *attest client* to pay the fees.

.03 *Threats* to the *covered member's* compliance with the “Independence Rule” [1.200.001] are at an *acceptable level* when unpaid fees are both clearly insignificant to the *covered member* and relate to *professional services* provided less than one year prior to the issue date of the current-year attest report. Alternatively, *threats* would not be at an *acceptable level* when unpaid fees are both significant to the *covered member* and relate to *professional services* provided more than one year prior to the issue date of the current-year attest report. Other situations require judgment to assess the *threats* to the *covered member's* compliance with the “Independence Rule”.

.04 If the *covered member* concludes that *threats* are not at an *acceptable level*, then the *covered member* should apply *safeguards* to eliminate the *threats* or reduce them to an *acceptable level*. If *safeguards* are not available or cannot be applied to eliminate or reduce the *threats* to an *acceptable level*, then *independence* would be impaired. Examples of actions that might be *safeguards*:

- a. Have an appropriate reviewer who has not provided attest or nonattest services to the *attest client* review the attest work performed before the current-year attest report is issued.
- b. Obtain partial payment of the unpaid fees balance.
- c. Agree to a payment schedule before the current-year attest report is issued.
- d. Select the current *attest engagement* for pre-issuance or post-issuance review.
- e. Suspend further work on current *attest engagements* and not accept new engagements until the unpaid fees are clearly insignificant to the *covered member*.
- f. Communicate with *those charged with governance* regarding the unpaid fees and the other *safeguards* applied.

.05 This interpretation does not apply to unpaid fees from an *attest client* in bankruptcy. [Prior reference: paragraphs .103–.104 of ET section 191]

.06 Refer to the “Fees and Other Types of Remuneration” topic [1.500] for additional guidance.

Proposed Q&A related to unpaid fees

Unpaid fees and independence

Inquiry – What independence considerations exist when the attest client needs the firm’s attest report to obtain financing from which the member’s fees will be paid?

Response – In applying the conceptual framework to this situation, the member should consider two competing interests.

First, no conclusion of impairment should necessarily arise from the fact that the member anticipates being paid from the proceeds of the financing that requires the attest engagement. Rather, that fact should be one consideration in determining whether there is an unacceptable threat to the member's compliance with the “Independence Rule” (ET sec. 1.200.001).

Second, the possibility of an unacceptable threat arising in this context is not necessarily eliminated or reduced to an acceptable level simply because the fees have remained unpaid for less than one year.

SEC excerpt: Unpaid fees Q&A

Question 2 (issued June 27, 2019)

Q: How do unpaid prior professional fees affect auditor independence?

A: Generally, prior year audit and other unpaid professional fees should be paid before a current audit engagement is commenced in order for the accountant to be deemed independent with respect to the current audit. However, normally a question would not be raised in such situations if, at the time the current audit engagement is commenced, a definite commitment is made by the client to pay the prior professional fees before the current year audit report is issued, or an arrangement is agreed upon for periodic payments to settle the delinquent fees and there is reasonable assurance that the current audit fee will be paid before the audit of the ensuing year begins. But, if audit and other professional services fees are owed to an accountant for an extended period of time and become material in relation to the fee expected to be charged for a current audit, there may be a question concerning the accountant's independence with regard to the current audit because the accountant may appear to have a direct interest in the results of operations of the client.

IESBA excerpt: Unpaid Fees

Part 4A

INDEPENDENCE FOR AUDIT AND REVIEW ENGAGEMENTS

Fees-Overdue (410.7 A1 to R410.8)

410.7 A2

A self-interest threat might be created if a significant part of fees is not paid before the audit report for the following year is issued. It is generally expected that the firm will require payment of such fees before such audit report is issued. The requirements and application material set out in [Section 511](#) with respect to loans and guarantees might also apply to situations where such unpaid fees exist.

410.7 A2

Examples of actions that might be safeguards to address such a self-interest threat include:

- Obtaining partial payment of overdue fees.
- Having an appropriate reviewer who did not take part in the audit engagement review the work performed.

R410.8

When a significant part of fees due from an audit client remains unpaid for a long time, the firm shall determine:

- a. Whether the overdue fees might be equivalent to a loan to the client; and
- b. Whether it is appropriate for the firm to be re-appointed or continue the audit engagement.

Part 4B

INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

Fees-Overdue (905.4 A1 to R905.5)

905.4 A1

A self-interest threat might be created if a significant part of fees is not paid before the assurance report, if any, for the following period is issued. It is generally expected that

the firm will require payment of such fees before any such report is issued. The requirements and application material set out in [Section 911](#) with respect to loans and guarantees might also apply to situations where such unpaid fees exist.

905.4 A2

Examples of actions that might be safeguards to address such a self-interest threat include:

- Obtaining partial payment of overdue fees.
- Having an appropriate reviewer who did not take part in the assurance engagement review the work performed.

R905.5

When a significant part of fees due from an assurance client remains unpaid for a long time, the firm shall determine:

- a. Whether the overdue fees might be equivalent to a loan to the client; and
- b. Whether it is appropriate for the firm to be re-appointed or continue the assurance engagement.

Assisting attest clients with implementing accounting standards

Task force members

Jennifer Kary (chair), Nancy Beacham, Mike Brand, Jason Evans, Alan Long, Jim Newhard

Observers

Vincent DiBlanda, John Ford, Erik Lange, Liz McKneely

AICPA staff

Liese Faircloth, Shannon Ziemba

Task force charge

Provide guidance on how members may assist attest clients with implementing a new accounting standard without impairing independence.

The task force recommends that the term “new” be stricken from the charge so that the guidance developed could also be applicable in other situations, such as when an attest client changes from non-GAAP to GAAP financials and the member assists the attest client with implementing accounting standards that the attest client has not previously adopted.

Reason for agenda item

The committee is asked to approve the proposed revised charge, to approve exposing a new interpretation, and to provide feedback on related Qs & As.

Task force activities

Authoritative guidance

An authoritative interpretation that combines key elements in other applicable extant nonattest services interpretations (e.g., advisory, information systems services, and internal audit interpretations) will help members understand more easily how they may assist an attest client with implementing or applying an accounting standard without impairing independence.

A challenge with assisting an attest client implementing an accounting standard is to ensure the attest client has someone with suitable knowledge, skill and/or experience (SKE) to oversee the service.

The task force discussed this at length and even considered adding content into the interpretation reminding the member that someone at the attest client needs to be able to understand the accounting standard adequately in order to make the necessary judgements and decisions regarding the implementation of the accounting standard. However, since this challenge is not unique to implementing an accounting standard, the task force decided not to include this reminder in the proposed interpretation.

Effective date

The task force recommends the proposal be effective when notice appears in the *Journal of Accountancy*. The task force does not believe a delayed effective date is necessary as the proposed interpretation simply combines elements of existing interpretations.

Questions for the committee

1. Does the committee approve the proposed revision to the task force charge?
2. Does the committee agree that it is not necessary to include guidance in the interpretation reminding members that the attest client needs to have someone with suitable SKE to oversee the project?
3. Does the committee believe additional authoritative guidance related to SKE should be added to the “General Requirements for Performing Nonattest Services” interpretation and if so, should this task force’s charge be expanded to include this, or should another task force be appointed to develop this guidance?
4. Does the committee approve the proposal in agenda item 4B for exposure?
5. Does the committee agree that if adopted the effective date of the new interpretation should not be delayed?

Non-authoritative guidance

Regarding permitted activities for members assisting attest clients with implementing accounting standards, non-authoritative guidance would be helpful to address three points:

- To remind members that they should ensure the individual overseeing their services has suitable SKE to oversee the services.
- To remind members to ensure that the scope of the services does not expand during the engagement to a point that the member performs a service that impairs independence.
- To provide members some guidance when an attest client changes their basis of accounting.

Questions for the committee

6. Does the committee have any edits to the Qs & As as presented?
7. Does the committee believe that the Qs & As should be issued prior to exposure of the new proposed interpretation?

Communications plan

Staff will work with Ms. Mullins to develop a communications plan.

Materials presented

- Agenda item 4B: Proposed new interpretation
- Agenda item 4C: Proposed Qs & As

Proposed new interpretation

1.295.113 Assisting an attest client with implementing accounting standards

- .01 When a *member* assists an *attest client* with planning and executing the implementation of an accounting standard, self-review or management participation *threats* to compliance with the “[Independence Rule](#)” [1.200.001] may exist.
- .02 If a *member* applies the “[General Requirements for Performing Nonattest Services](#)” interpretation [1.295.040] of the “Independence Rule”, *threats* would be at an *acceptable level* and *independence* would not be *impaired*. For example, a *member* may
- a. develop and provide training to *attest client* personnel on the effects of the standard.
 - b. research, provide advice, make recommendations and assist management in identifying *financial statement* account balances, contracts, and transactions to be assessed under the standard.
 - c. assist the *attest client* with summarizing their analysis and policies related to the accounting position under the standard.
 - d. provide observations and recommendations on management’s overall project plan timeline to adopt the accounting standard.
 - e. assist management in drafting implementation strategies or methods used to implement the accounting standard.
 - f. assist the *attest client* in developing implementation templates including those related to specific calculations under the standard that meet the discrete tool exception in paragraph .03a of the “[Information Systems Services](#)” interpretation [1.295.145] under the “Independence Rule.”
 - g. propose standard journal entries or adjustments to existing journal entries necessary for adoption of the standard. These would be subject to *attest client* approval.
 - h. provide recommendations related to application of the standard, including those related to possible revisions to existing policies and procedures and improvements to existing internal controls.
 - i. provide recommendations related to existing or new information technology systems as a result of the accounting standard.
- .03 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

- a. leads any implementation team at the attest client.*
- b. makes decisions on how to implement the accounting standard.*
- c. sets any policy or procedures related to the accounting standard.*
- d. designs new or redesigns existing internal controls over financial reporting.*
- e. designs new or redesigns existing financial information systems.*

Proposed Qs & As related to assisting attest clients with implementing accounting standards

Determining suitable skills, knowledge, and/or experience when assisting attest clients in implementing an accounting standard

Inquiry – A *member's attest client* is preparing to implement an accounting standard and the controller at the *attest client* will oversee the project. Because a member of senior management has been assigned to oversee the project, what does the *member* need to do in order to assist the *attest client* with implementing the accounting standard without impairing their independence?

Response – The *member* must use professional judgement to determine whether the controller has suitable skill, knowledge and/or experience (SKE) to oversee the implementation project.

If the *member* concludes that the controller does have the SKE but does not have the necessary knowledge to make significant judgments and decisions to implement the standard, then the *member* cannot proceed with assisting the *attest client*.

However, if the *member* concludes the controller can be educated on the substance of the standard and believes through education, information, and advice the controller can obtain the required knowledge, the *member* may be able move forward with assisting the *attest client* with the implementation of the accounting standard.

Assisting attest clients with revising processes, accounting policies, and internal controls when implementing an accounting standard

Inquiry – The *attest client* is implementing an accounting standard and has requested the *member* assist management in revising their processes, accounting policies, and internal controls to adhere to the requirements of the accounting standard. May the *member* provide such assistance without *impairing* their *independence*?

Response – As long as the *member* does not assume any management responsibilities outlined in the [“General Requirements for Performing Nonattest Services”](#) interpretation (ET sec. 1.295.040) of the “Independence Rule,” the *member* may provide guidance, advice and recommendations. The *member* may also assist the *attest client* with summarizing the analysis and policies and drafting implementation strategies or methods.

The *member* and the *attest client* should have a clear understanding of the services the *member* will perform and the *attest client's* responsibilities regarding changes to their processes, policies, and internal controls. Maintaining processes, policies, and internal controls is a management responsibility; however, the *member* may propose recommendations and provide advice to assist the *attest client* in adopting, implementing, and adhering to the requirements of the

accounting standard.

The *attest client* must have the suitable skills, knowledge, and/or experience to evaluate any advice and recommendations the *member* proposes, determine which recommendations to implement using their own professional judgment, and assume all management responsibilities.

Assisting attest clients with moving to a different basis of accounting

Inquiry – A *member's attest client* is preparing to implement a different basis of accounting (for example moving to GAAP from a modified cash basis or other special purpose framework) and has asked the *member* for assistance. May the *member* perform these services without *impairing independence*?

Response – As long as the *member* does not make any decisions about framework application and meets the other requirements of the “[General Requirements for Performing Nonattest Services](#)” interpretation (ET sec. 1.295.040), the *member* may provide education, advice, and recommendations to the *attest client*.

Further, the *member* should be satisfied that the individual designated by the *attest client* to oversee the nonattest services has the suitable skills, knowledge, and/or experience to evaluate the framework recommendations and can advise and make significant judgements and decisions regarding what, if any of the framework recommendations and advice, should be implemented.

The *member* and the *attest client* should have a clear understanding of the services the *member* will perform and the *attest client's* responsibilities for any changes to processes, policies, and internal controls (and related decisions) that may be required in conjunction with the intended financial reporting framework.

It is important to keep in mind that adopting, applying, and maintaining processes, policies, and internal controls are management responsibilities.

Information systems services

Task force members

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Observers

Kimberly M. Kuhl, SanDee Priser

AICPA staff

Liese Faircloth, Ellen Gorla, Iryna Klepcha

Task force charge

Develop guidance to assist members with implementing the “Information Systems Services” interpretation (1.295.145).

Reason for agenda item

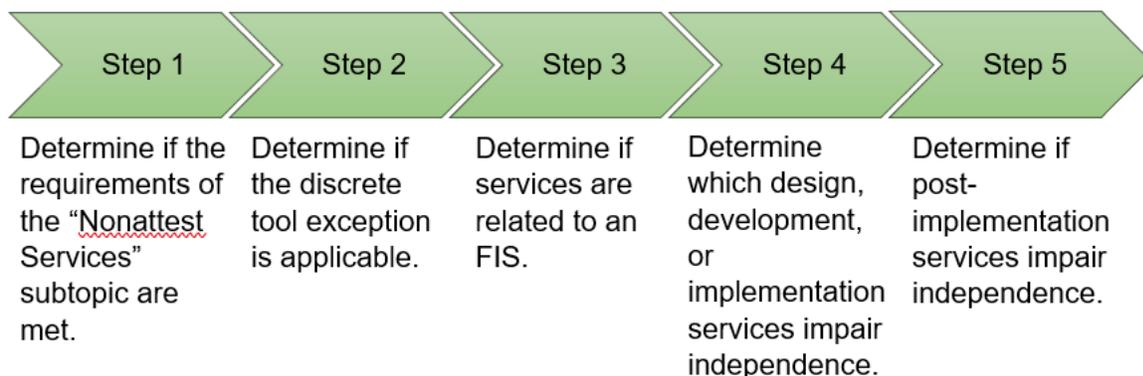
The task force is seeking input on the practice aid.

Task force activities

The task force met two times since the May committee meeting to discuss the structure and content of the practice aid. Agenda item 5B provides a draft of the practice aid.

Practice aid overview

The practice aid applies to information systems services — a nonattest service — that a member provides to an attest client. The framework has several steps to help members identify the type of service being provided and the effect on independence:



Each step includes a series of questions that walk the user through services included in the “Information Systems Services” interpretation. As users complete the questions, they are encouraged to consider various aspects of the services and are provided a space to document their conclusions if they so choose. Most of the questions include factors to consider or examples to assist users in coming to a determination about whether the proposed service falls under the interpretation.

Questions for committee

1. Does the committee have any feedback on the practice aid draft?
2. Given the pending effective date of January 1, 2022, does the committee believe the task force should develop scenarios or should the practice aid be issued without scenarios?
3. Does the committee want to review the practice aid again before it is issued or should the task force work with staff to finalize?

Materials presented

Agenda item 5B: The information system services practice aid draft

The information systems services practice aid draft

Practice aid

Understanding circumstances that may impair your independence when you're providing services related to information systems

XXX, 2021

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The practice aid: What's it all about?

Do you know how the technology-related service an attest client asked you to provide will affect your independence under the newly revised “Information System Services” interpretation (ET sec. 1.295.145)?^{1, 2}

This practice aid can help you determine just that. Along with questions for consideration [and sample scenarios], you'll find factors to consider, examples of permitted and prohibited activities and references to the AICPA Code of Professional Conduct (code), as well as other nonauthoritative guidance to help you maintain your independence.

Extant or revised interpretation... Where do your services fall?

In June 2019, the AICPA issued revised interpretation “Information System Services” (ET sec. [1.295.145](#)) under the “Independence Rule” (ET sec. [1.200.001](#)). The revised interpretation is effective January 1, 2022, and early implementation is allowed.

This means that if you've provided services allowed under the extant interpretation but prohibited under the revised interpretation during the [period of the professional engagement](#) or during the period covered by the [financial statements](#), your independence will not be impaired as long you discontinue those services by December 31, 2021.

The practice aid is nonauthoritative

The code is the only authoritative source of AICPA ethics rules and interpretations. The staff of the Professional Ethics Division developed the nonauthoritative content of this practice aid from hotline inquiries and queries raised during interviews with members to assist our members and other interested parties in applying the revised interpretation.

The guidance in this practice aid does not address the requirements of other standard-setters or regulatory bodies, such as the state boards of accountancy, the SEC, and the U.S. GAO, whose positions may differ from the AICPA.

To learn more about nonattest services, consider reading the [Nonattest services FAQs](#). If you provide nonattest services not addressed in this practice aid, consider using the [Nonattest Services Toolkit](#), which provides an illustration of the steps for evaluating independence and an easy to use checklist.

Terms that are defined in the code are italicized. The first instance of a defined term or code citation links to the code.

¹ Formerly “Information Systems Design, Implementation, or Integration” interpretation.

² All ET sections are located in AICPA *Professional Standards*.

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How can this practice aid help you?

The “Information System Services” interpretation (ET sec. [1.295.145](#)) applies when a *member* provides nonattest services related to an *attest client’s* information systems. When the subject matter of the *attest engagement* does not involve *financial statements*, you should define a financial information system (FIS)³ as any information system that is subject to your attest procedures.

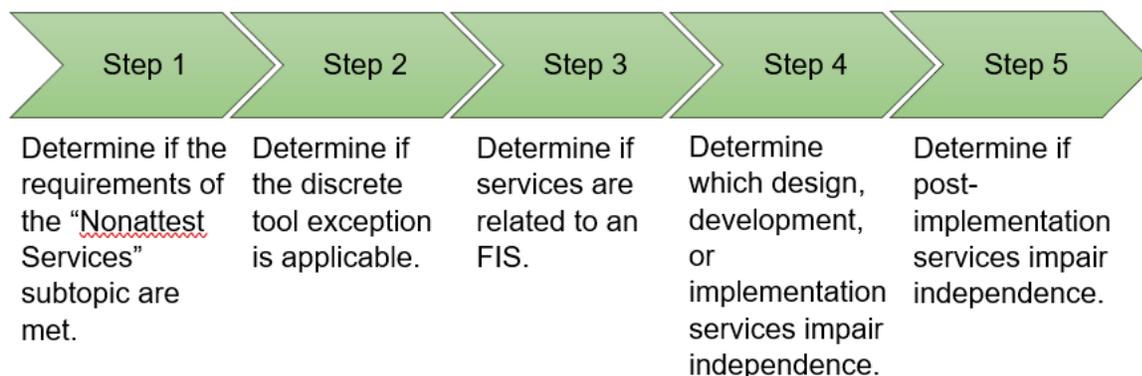
This practice aid applies to information systems services — a nonattest service — that a *member* provides to an *attest client*. Some examples are operating the *attest client’s* information technology help desk, loading commercial off-the-shelf software (COTS) for the *attest client*, and being responsible for the maintenance of an *attest client’s* network performance. A *firm’s* tools used in an *attest engagement* are not subject to this interpretation.

The framework [[and scenarios](#)] in this practice aid focus on factors and examples to illustrate the application of the rule that a *member* should consider when determining whether *independence* will be *impaired* in accordance with the “Information System Services” interpretation (ET sec. [1.295.145](#)).

Keep in mind as you use this practice aid that the term *member* includes the *member’s firm* (ET sec. [1.295.010](#)).

What’s included in this practice aid?

There are several steps in this framework to help you identify the type of service being provided and the effect on your *independence*:



³ The “Information Systems Services” interpretation defines an FIS as “a system that aggregates source data underlying the financial statements or (i) the tool performs only discrete calculations; (ii) the attest client evaluates and accepts responsibility for the input and assumptions; and (iii) the attest client has sufficient information to understand the calculation and the results.

We suggest that you use the practice aid to evaluate each individual information systems service prior to providing the service. Although documentation is not required, we are including text boxes for you to document the information you believe is relevant to reach your conclusion or refer to your working papers.

[The scenarios in this practice aid...]

Framework

Step 1: Determine if the requirements of the “Nonattest Services” subtopic are met

The [interpretations](#) under the “Nonattest Services” subtopic (ET sec. [1.295](#)) include examples of nonattest services that *impair independence* even if the general requirements⁴ are met. In this practice aid, we refer to these as “prohibited services.”

These *interpretations* also provide examples of services that do not *impair independence* as long as the general requirements are met. In this practice aid, we refer to these as “permitted services.”

Before agreeing to perform the services related to information systems, answer the following questions. If you answer yes to all the questions in step 1, you can proceed to step 2.

If you answer no to any of these questions, providing the service would *impair your independence*.

- a. Does the functionality of the tool or system, including any calculations performed within the tool, encompass a permitted service under interpretations [1.295.105–143](#) and [1.295.150–160](#)?

You can see an example of a prohibited service under the “Appraisal, Valuation, and Actuarial Services” interpretation (ET sec. 1.295.110). If preparation of a valuation involves a significant degree of subjectivity and that valuation is material to the *attest client’s financial statements*, it is prohibited. Therefore, if a tool or system performs such functionalities, it performs a prohibited service.

You can see examples of permitted services under the “Bookkeeping, Payroll, and Other Disbursements” (ET sec. 1.295.120) and “Appraisal, Valuation, and Actuarial Services” interpretations. Preparation of *financial statements* based on information in the *attest client’s* trial balance or preparation of a valuation that is not material to the *attest client’s financial statements* are permitted. If a tool or system performs such functionalities, it performs a permitted service.

- No. *Independence will be impaired.*
- Yes.

⁴ In this practice aid, the phrase “general requirements” means the requirements outlined in the “General Requirements for Performing Nonattest Services” interpretation ([ET sec. 1.295.040](#)).

Documentation or reference to documentation:

- b. Has management agreed to assume all management responsibilities as required under the “Management Responsibilities” interpretation (ET sec. [1.295.030](#))?

Management responsibilities involve leading and directing an entity, including making significant decisions regarding the acquisition, deployment, and control of human, financial, physical, and intangible resources. Here are some examples of management responsibilities:

- Setting policy or strategic direction
- Directing or accepting responsibility for actions of the *attest client’s* employees
- Deciding which recommendation of the *member* or other third parties to implement
- Accepting responsibility for the management of an *attest client’s* project
- Accepting responsibility for designing, implementing, or maintaining internal control

Nonauthoritative questions and answers regarding management responsibilities and controllership services are available in the [Nonattest services FAQs](#).

No. *Independence will be impaired.*

Yes.

Documentation or reference to documentation:

- c. Has the *attest client’s* management designated an individual — preferably someone within senior management — who possesses suitable skills, knowledge and/or experience (SKE) to oversee the service?

In assessing whether the individual designated by the *attest client* has SKE to oversee a nonattest service, you might consider the following factors as they pertain to the individual:

- Understanding of the nature of the service
- Knowledge of the *attest client's* operations
- Knowledge of the *attest client's* industry
- General business knowledge
- Level of education
- Position at the *attest client*

Note that the requirements for SKE do not mean that the individual must have the expertise to perform or re-perform the services in question. For more information on SKE, see the related questions and answers in the [Nonattest services FAQs](#).

No. *Independence will be impaired.*

Yes.

Documentation or reference to documentation:

d. Has management agreed to evaluate the adequacy and results of the service and accept responsibility for the results of the service?

No. *Independence will be impaired.*

Yes.

Documentation or reference to documentation:

e. At times, the general requirements may not by themselves reduce [threats](#) to an [acceptable level](#). One such circumstance is when you perform multiple nonattest services. In such circumstances you should evaluate the *threats* in the aggregate to ensure that the [safeguards](#) in the “General Requirements for Performing Nonattest Services” (ET sec. [1.295.040](#)) interpretation continue to adequately reduce *threats* to an *acceptable level*.

If you provide multiple nonattest services, have you evaluated whether the general

requirements reduce *threats* to an *acceptable level* and when necessary, have you applied additional *safeguards* to reduce *threats* to an *acceptable level*?

No. *Independence* will be *impaired*.

Yes.

Documentation or reference to documentation:

f. Before performing the services, have you established and documented in writing your understanding with the *attest client* regarding the following?

- Objectives of the engagement
- Services to be performed
- *Attest client's* acceptance of its responsibilities
- *Member's* responsibilities
- Any limitations of the engagement

No. You would violate the "Compliance With Standards Rule" (ET. sec. [1.310.001](#)) unless you document your understanding established with the *attest client*.

Yes. You can proceed to step 2.

Documentation or reference to documentation:

Step 2: Determine if the discrete tool exception is applicable.

The "Information System Services" interpretation includes an exception that we refer to in this practice aid to as the "discrete tool exception." When specific conditions are met, the information system is considered a "tool" and not an FIS. You can provide an *attest client* with services related to this tool without *impairing independence*.

To meet the discrete tool exception, the tool must perform a discrete calculation, the *attest client* must evaluate and accept responsibility for the input and assumptions and have sufficient information to understand the calculation and the results.

To help you determine whether the services you plan to provide would qualify for the discrete tool exception, answer the following questions. If you answer yes to all the questions in this section, the *firm's* service meets the discrete tool exception and, therefore, is not considered an FIS.

- a. Does the service involve a tool that performs only discrete calculation (for example, an excel spreadsheet that calculates depreciation)?

Here are some factors that may help you determine this:

- Whether the calculation is separate and distinct
- Whether the purpose of the calculation is narrow and specific
- Whether substantially the same result will be produced using a different system

Yes. Proceed to question (b).

No. Proceed to step 3.

Documentation or reference to documentation:

- b. Does the *attest client* evaluate and accept responsibility for the inputs to the tool and the assumptions underlying those inputs?

Here are some factors to consider:

- The *attest client* determines the assumptions used as input to the tool.
- The *attest client* can articulate why the inputs used in the tool are appropriate (history, market factors, etc.).

Yes. Proceed to question (c).

No. Proceed to step 3.

Documentation or reference to documentation:

c. Does the *attest client* have sufficient information to understand the calculation performed in the tool and the results?

Here are some factors that may help you determine the *attest client's* ability to take responsibility for the use or output of the tool:

- Whether the *attest client* can do the calculation another way and receive the same answer
- Whether the *attest client* has sufficient information to obtain a general understanding of the activity in the tool
- Whether the *attest client* has sufficient information to evaluate if the results are adequate and to accept responsibility for the output from the tool

Yes. The service meets the discrete tool exception. The service is permitted under the "Information Systems Services" interpretation as long as all requirements of the "[Nonattest Services](#)" subtopic are met (refer to step 1). If the *firm* also provides post-implementation services, proceed to step 5.

No. The service does not meet the discrete tool exception. Proceed to step 3.

Documentation or reference to documentation:

Step 3: Determine if services are related to an FIS

Under the "Information System Services" interpretation, design, development, and certain implementation services that are related to an FIS are prohibited services.

In this step, it is critical that you determine whether the system is an FIS. If your engagement is not related to *financial statements*, replace references to “*financial statement*” and “financial reporting” throughout this section with the phrase “subject matter of the attest engagement.”

If the service affects information systems that the *attest client* will use only in connection with controlling the efficiency and effectiveness of operations, the service is not related to an FIS and is permitted under the “Information Systems Services” interpretation as long as all requirements of the "[Nonattest Services](#)" subtopic are met. A non-financial compliance tool and an operational benchmarking tool are good examples of this type of service.

To help you determine whether the services you plan to provide are related to an FIS, answer the following questions.

a. Does the system aggregate source data that is significant to the *financial statements*?

Here are some factors that can help you determine this:

- Whether the nonattest service affects a data-gathering system, such as an analytical or reporting tool, that is used in management’s decision-making about matters that could significantly affect financial reporting
- Whether the system is management’s primary source of information for decision making on matters significant to the *financial statements* or is used only to present alternative formatting or display of information (for example, graph versus table)
- Whether management needs to consider results produced by the system along with other inputs to make a decision on matters significant to the *financial statements*
- Whether the results produced by the system are deterministic and would lead management to a certain conclusion

An example of an analytical tool that is unlikely to significantly affect financial reporting is a tool used in the healthcare industry to analyze clinical information. Providers use tools like this to improve their operations and their treatment of patients. Management would consider a number of various inputs in addition to the information produced by the analytical tool before taking any improvement actions.

Yes. Proceed to step 4.

No. Proceed to question (b).

Documentation or reference to documentation:

b. Does the system aggregate source data that is significant to a financial process?

Here are some factors to help you determine this:

- Whether the nonattest services will affect a data-gathering system, such as an analytical or reporting tool, that is used in management's decision-making about matters that could significantly affect financial reporting
- Whether the nonattest services will affect a system that is part of the *attest client's* internal controls over financial reporting, including information systems used to effect internal controls over financial reporting (for example, a system used to ensure that information produced for the financial statements is accurate)
- How the system interconnects with other systems across the entity to facilitate financial reporting

Examples of financial processes include these:

- Budgeting
- Budget to actual reporting
- Pricing models
- Cash flow planning/projections
- Inventory process
- Reconciliations could be considered a financial process or a control

Yes. Proceed to step 4.

No. Proceed to question (c).

Documentation or reference to documentation:

c. Does the system generate data that is significant to the *financial statements*?

When determining whether the data generated by the system will be significant to the *financial statements*, you may find it helpful to consult with the *attest client* or the individual responsible for the audit at the *firm*.

Here are some factors to help you determine this:

- Whether the nonattest service will affect system controls or system output that will be subject to attest procedures

- Whether the nonattest service will affect a system that generates data that is used as an input to the *financial statements*, including data or information that is either reflected in or used in determining amounts and disclosures included in the *financial statements*

Examples of such systems include the following:

- Materials management systems
- Revenue order and processing or transaction systems
- Inventory control systems
- Supply chain management systems

Yes. Proceed to step 4.

No. Proceed to question (d).

Documentation or reference to documentation:

d. Does the system generate data that is significant to a financial process?

A wide array of systems that create transactions with cost or revenue implications, such as inventory control, supply chain, and production scheduling often generate data that can be used in an entity's financial reporting processes.

Consider these factors:

- Whether the nonattest service will affect system controls or system output that will be subject to attest procedures
- Whether the nonattest service will affect a data-gathering system, such as an analytical or reporting tool, that is used in management's decision-making about matters that could significantly affect financial reporting
- Whether the nonattest service will affect a system that is part of the *attest client's* internal controls over financial reporting, including information systems used to effect internal controls over financial reporting (for example, a system used to ensure that information produced for the financial statements is accurate)

- Yes. The system would be an FIS. Proceed to step 4.
- No. The system is not an FIS. If the services relate to design, development, or implementation services, you can provide these without *impairing independence* as long as you meet all requirements of the “Nonattest Services” subtopic (refer to step 1). However, if you provide post-implementation services, proceed to step 5 to determine if *independence* will be *impaired*.

Documentation or reference to documentation:

Step 4: Determine which design, development, or implementation services impair independence.

Based on your responses in step 3, you have concluded that the services in question either relate to an FIS or are connected to the subject matter of the *attest engagement*. Now you need to determine whether the underlying service will *impair* your *independence* because some services related to an FIS are prohibited under the “Information Systems Services” interpretation.

The “Information System Services” interpretation differentiates between software solutions that are developed, distributed, maintained, and supported by the *member* or *member’s firm* and by a third party.

If the *firm* designs or develops a solution *independence* is *impaired*. If a third-party vendor designs or develops it, you may be able to provide certain types of services without *impairing independence*.

This practice aid refers to software solutions that are developed, distributed, maintained, and supported by an entity (or entities) other than the *member* or *member’s firm* as either a third-party solution or a commercial-off-the-shelf (COTS) solution. Here are some examples of third-party solutions you’re probably familiar with:

- Cloud-based or desktop based small business bookkeeping software, such as QuickBooks
- Customer relationship management (CRM) software, such as Salesforce CRM
- Enterprise resource planning (ERP) software
- Spreadsheet software, such as Excel
- Data visualization programs, such as PowerBI and Tableau

a. Will your *firm* design or develop the system?

Here are some factors to help you determine this:

- 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)
- Providing a blueprint or schematic for the development of software code (programs) and data structures
- Creating software code for individual or multiple modules
- Testing software code to confirm it is functioning as designed

Here are some examples of design and development services:

- Defining the elements of a system and their flow
- Determining what the output will be (That is, your *firm* will determine how a certain transaction functions specifically.)

Here are some examples of services that are not design or development services:

- Assisting management with conducting a gap analysis (that is, identifying the current state and where the *attest client* wants to be in order to point out gaps present in the system)
- For educational purposes, presenting an *attest client* with a schematic diagram that shows functions typical for companies in a particular industry

Yes. The *firm* will design or develop a software solution; therefore, *independence* will be *impaired*.

No. The *firm* will not design or develop the software solution, rather a third-party vendor will design and develop the software solution. The software solutions discussed in questions (b)–(f) in this section all assume a third-party vendor designed and developed the software solution. Proceed to question (b).

Documentation or reference to documentation:

b. Will your *firm* install the software solution?

In this practice aid, this service is limited to the initial loading of the software on the *attest client's* designated hosting site and does not include activities after the initial loading.

- Yes. *Independence* will not be *impaired* as long as all requirements of the "[Nonattest Services](#)" subtopic are met (refer to step 1). If the firm is not providing other implementation services, proceed to step 5. Otherwise proceed to question (c).
- No, the firm will not install the software solution. Proceed to question (c).

Documentation or reference to documentation:

c. Will your *firm* provide configuration activities that *impair independence*?

Here are a couple of examples of configuration activities that will *impair* your *independence*:

- Designing or developing new software code or features
- Modifying the functionality of the software not predefined by the third-party vendor

Here are some examples of configuration activities that won't *impair* your *independence*:

- Inputting the client-selected features and functionality options, which determines how the software will perform certain transactions and process data
- Selecting the predefined format of certain data attributes and the inclusion or exclusion of these attributes
- Assisting the client in understanding the various configuration options and the implications of various choices, and then making the selections within the system based on the client's decisions

- Yes, the *firm* will provide configuration activities that *impair independence*.
- No, the *firm* will provide configuration activities that do not *impair independence* and all requirements of the "[Nonattest Services](#)" subtopic are met (refer to step 1). If the firm is not providing other implementation services, proceed to step 5. Otherwise proceed to question (d).
- No, the *firm* will not provide configuration activities. If the *firm* provides other services, proceed to question (d).

Documentation or reference to documentation:

d. Will your *firm* customize the FIS software solution?

Because customizing the software solution means the *firm* will modify or enhance the features and functions in ways that go beyond the options provided by the third-party vendor, these services will *impair independence*.

Following are examples of activities that involve customizing software that will *impair* your *independence*:

- Altering the COTS code to change or add to the functionality provided by the third-party vendor
- Writing new code that enhances the COTS to provide additional functionality

Yes. *Independence* will be *impaired*.

No. The *firm* will not customize the software solution. If the firm is not providing other implementation services, proceed to step 5. Otherwise proceed to question (e).

Documentation or reference to documentation:

e. Will the *firm* provide interface (sometimes referred to as integration) services for the software solution that impair independence?

If the interface services involve the *firm* connecting two or more systems by designing and developing software code that allows data to be passed between one or more systems, your independence will be impaired. An example of this is developing code that enables migration of data in an old system to a new system.

If the interface services involve the *firm* using a third-party vendor's application, such as an API, to interface legacy solutions to a new software solution, *independence* will not be *impaired*. This is because the *firm* will not be designing or developing software code.

Of course, this means that the *firm* cannot design or develop code for the third-party vendor's application to work.

- Yes. The *firm* will provide interface services that impair independence because it will design or develop the software code that allows data to be passed between systems.
- No. The *firm* will not provide interface services that impair independence because the firm will use a third-party vendor's application and will not design or develop code in order for the application to work. Also, all the requirements of the "[Nonattest Services](#)" subtopic are met (refer to step 1).
- No. The *firm* will not provide interface services for the software solution. If the firm is not providing other implementation services, proceed to step 5. Otherwise proceed to question (f).

Documentation or reference to documentation:
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f. Will the *firm* provide data translation services for the software solution that will *impair independence*?

If the data translation services involve the *firm* designing and developing the rules or logic necessary to convert legacy system data to a format compatible with that of the new system, your independence will be impaired.

If your firm will use a third-party vendor's application, such as an API, to convert legacy system data to a format compatible with that of the new system, your independence will not be impaired. This is because your *firm* will not be designing or developing code for the application to work.

Of course, this means that the *firm* cannot design or develop code for the third-party vendor's application to work.

- Yes. The *firm* will provide data translation services that impair independence because the firm will be designing or developing the rules or logic (that is, the code)

necessary to convert the data so that it is compatible with the new system.

- No. The *firm* will not provide data translation services that impair independence because the firm will use a third-party vendor's application and will not design or develop code in order for the application to work. Also, all the requirements of the "[Nonattest Services](#)" subtopic are met (refer to step 1). If you provide post-implementation services, proceed to step 5.
- No. The *firm* will not provide data translation services. If you provide post-implementation services, proceed to step 5.

Documentation or reference to documentation:

Step 5: Determine if post-implementation services impair independence

This practice aid refers to services for a system that has already been implemented as "post-implementation services." Such services may involve system maintenance, support, and monitoring services. When the services involve aspects covered in Step 4, evaluate the service using that step.

If you are providing post-implementation services, *independence* no longer hinges on whether the system is an FIS. Rather, you need to focus on whether the service the *attest client* is asking you to provide is a management responsibility.

The scope of management responsibilities is vast, and the code dedicates an entire interpretation to this topic. You can read more about these responsibilities in the "Management Responsibilities" interpretation (ET section [1.295.030](#)).

In the context of post-implementation services, you may find it useful to consider whether the services the *attest client* is asking you to provide will involve outsourcing an ongoing function, process, or activity to you.

If this occurs, your *independence* is *impaired* even if an individual with SKE from client management is overseeing the services.

If your *firm* is not providing post-implementation services, then this step is not applicable. If the *firm* will provide post-implementation services related to a *financial* or nonfinancial system that has already been implemented at an *attest client*, then proceed to question (a) below.

- a. Will the *attest client* outsource an ongoing function, process or activity to your *firm* that will result in your assuming a management responsibility outlined in the “Management Responsibilities” interpretation?

Here are some factors that may help you determine whether the service will result in your *firm* assuming management responsibility:

- Scope and scale of services
- Frequency of the services
- Duration of the engagement

These are some examples of services that will result in your accepting responsibility for maintaining, supporting, or monitoring the *attest client's* system:

- Operating the *attest client's* network, such as managing the *attest client's* systems or software applications
- Having responsibility for performing ongoing network maintenance, such as updating virus protection solutions, applying routine updates and patches, or configuring user settings
- Operating or managing the *attest client's* information technology help desk,
- Having responsibility for maintaining the security of the *attest client's* networks and systems

These are examples of services that generally would not result in your accepting responsibility for maintaining, supporting, or monitoring the *attest client's* system:

- Applying a specific patch to the system for the client on an ad hoc basis
- Providing post-production stabilization support for a new system to ensure it is free of major software issues. This level of support is part of the final stage of an implementation project and lasts for only a limited amount of time.
- Providing advice, training, or instruction on a software solution

- No. The attest client has not outsourced an ongoing function, process, or activity to the *firm* that results in the firm assuming a management responsibility. *Independence* will not be *impaired* as long as all the requirements of the “Nonattest Services” subtopic are met (refer to step 1).
- Yes. The attest client has outsourced an ongoing function, process, or activity to the *firm* that results in the firm assuming a management responsibility. *Independence* is *impaired*.

Documentation or reference to documentation:

[Scenarios (possible)]

TBD

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IESBA update

Reason for agenda item

This agenda item supplements the quarterly verbal update on IESBA's activities and provides project summaries for some of IESBA's projects and task forces. Division staff welcomes the committee's comments on the project, including any concerns it believes should be monitored.

Materials presented

- Agenda item 6B: IESBA engagement team
- Agenda item 6C: IESBA tax planning and related services
- Agenda item 6D: IESBA quality management related conforming amendments
- Agenda item 6E: IESBA benchmarking independence provisions for audits of PIEs
- Agenda item 6F: IESBA technology

IESBA engagement team

Convergence considerations

Staff's initial assessment of IESBA's recent activity in this area is that PEEC may not need a convergence project for engagement quality reviewers (EQRs) as the definition of an attest engagement team seems to be drafted broadly enough to include EQRs.

The definition reads "Those individuals participating in the *attest engagement*, including those who perform concurring and ***engagement quality reviews***." (Emphasis added)

However, PEEC may need a convergence project to provide guidance related to component auditors who are outside of the network firm since the code does not provide any specific guidance for these auditors.

The following sections present IESBA's recent activity.

Project description

For quality management purposes, the IAASB changed the definition of *engagement team* in ISA 220 to include component auditors that are not part of the network firm and service providers. This revision raised several questions about these individuals' compliance with the International Independence Standards (IISs) in the context of a group audit.

The purpose of this project is to ensure that IISs provide clear and consistent guidance on independence for the following:

- Engagement quality reviewers who are not in the firm or network
- Component auditors who are performing audit procedures and who are outside of the audit firm's network (i.e., individual independence requirements)
- The firms that these component auditors are in (i.e., firm independence requirements)

The proposed ISA 600 (Revised), like the extant ISA 600, establishes a requirement that the group audit engagement partner take responsibility for obtaining a confirmation from component auditors that ethical requirements have been fulfilled for the group audit engagement, including those related to independence.¹

If the component auditor does not meet the independence requirements relevant to the group audit, the proposed ISA 600 (Revised) requires the group engagement team to obtain sufficient appropriate audit evidence relating to the work performed at the component without involving

1 Exposure draft of Proposed ISA 600 (Revised) (ED-ISA 600), *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, paragraph 20(c)

that component auditor.²

Under the extant IESBA code, if a component auditor is from the same network as the group auditor, the component auditor will apply the same independence requirements applicable to the group engagement team when auditing a component. For example, if the parent entity is a public interest entity (PIE),³ all network firms are required to comply with the provisions on nonassurance services (NAS) that apply to the PIE and its related entities (applying the related entity principle in paragraph R400.20).⁴

In contrast, the IESBA code is effectively silent on the principles that should apply to a component auditor outside the group auditor's network. Accordingly, subject to a different agreement between the group auditor and the component auditor, the component auditor will apply the independence requirements in the IESBA code relevant to its audit client (i.e., the component).

Status

At its June 2021 meeting, IESBA's Engagement Team — Group Audits Independence Task Force presented a more developed draft of its [preliminary draft text](#)⁵. The task force also reported that a few other matters still need consideration, including the following:

- How the independence principles should apply at the service provider level
- How components are conceptualized in ED-ISA 600 (Revised)
- Recent changes to the code (effective December 2022) in the context of group audits

For additional background, refer to the following:

- IESBA's [project page](#)

2 ED-ISA 600, paragraph 22

3 The code defines a "public interest entity" as (a) a listed entity; or (b) an entity: (i) defined by regulation or legislation as a public interest entity; or (ii) for which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. Such regulation might be promulgated by any relevant regulator, including an audit regulator.

4 Paragraph R400.20 states the following: As defined, an audit client that is a listed entity includes all of its related entities. For all other entities, references to an audit client in this Part include related entities over which the client has direct or indirect control. When the audit team knows, or has reason to believe, that a relationship or circumstance involving any other related entity of the client is relevant to the evaluation of the firm's independence from the client, the audit team shall include that related entity when identifying, evaluating and addressing threats to independence.

5 The IESBA uses the term "strawman" to describe text that it presents that the task force knows needs to be refined but nonetheless provides to the board in an effort to give them something to see. When strawman text is provided, the task force is generally seeking conceptual feedback as opposed to drafting feedback.

- The [preliminary recommendations](#) presented at IESBA's October 2020 meeting
- The [updates](#) presented at IESBA's December 2020 meeting
- The more developed draft of its [preliminary draft text](#) from the June 2021 meeting

During the June 2021 meeting, IESBA asked the task force to consider providing nonauthoritative guidance, such as Qs & As to clarify how to determine whether an individual can “directly influence the outcome of the group audit.”

Engagement quality reviewers

Because the extant definitions of the terms *audit team*, *review team*, and *assurance team* scope in only engagement quality reviewers (EQRs) within the firm or the network, the task force recommends these definitions be revised to scope in EQRs from outside of the firm or network.

To do this, the task force added to all three definitions that individuals who can directly influence the outcome of the engagement include those who are engaged by the firm. They also revised item (b) (iii) in each definition as follows (excerpted from the “Glossary, Including Lists of Abbreviations” section of the IESBA code):

- Audit team (b)(iii): Those who ~~provide~~ **perform an engagement quality review, or review consistent with the objective of** control for the audit engagement, ~~including those who perform the~~ **an** engagement quality control review, for the engagement; and
- Assurance team (b)(iii): Those who ~~provide~~ **perform an engagement quality review, or review consistent with the objective of an engagement quality review,** control for the assurance engagement, ~~including those who perform the~~ engagement quality control review for the engagement; and
- Review team (b)(iii): Those who ~~provide~~ **perform an engagement quality reviews, or review consistent with the objectives of an engagement quality review,** control for the engagement, ~~including those who perform the~~ engagement quality control review for the engagement; and

Definition of engagement team recommendations

The task force continues to recommend

- revising the extant definition of *engagement team* to align with the definition of that term in International Standard on Quality Management (ISQM) No. 1.
- including additional guidance to clarify the nature of the various teams in reference to the different parts of the code.

As of June 2021, the task force recommends the definition of *engagement team* be revised as shown in the following paragraph. The green highlighted text reflects the changes made to the

preliminary draft text subsequent to the March 2021 meeting. The revision addresses IESBA's recommendation to add back into the definition that ISA 610 needs to be complied with in order to exclude individuals within the client's internal audit function from the engagement team who provide direct assistance. Given this, the task force also proposed to include a reference to ISA 620 to highlight that there is a specific ISA that addresses the use of an auditor's expert on an audit engagement.

Engagement team: All partners and staff performing the engagement, and any **other** individuals engaged by the firm or network firm who perform assurance procedures on the engagement. This excludes **excluding an** external experts engaged by the firm or by a network firm **and internal auditors**. The term "engagement team" also excludes individuals within the client's internal audit function who provides direct assistance on **the an** audit engagement when the external auditor complies with the requirements of ISA 610 (Revised 2013), *Using the Work of Internal Auditors*. This excludes external experts engaged by the firm or by a network firm.

In Part 4A, the term "engagement team" refers to individuals performing audit or review procedures on the audit or review engagement, respectively.

ISA 220 (Revised) provides further guidance on the definition of engagement team in the context of an audit of financial statements.

ISA 620 deals with the auditor's responsibilities relating to the work of an individual or organization in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

ISA 610 (Revised 2013) deals with the auditor's responsibilities if using the work of internal auditors, including using internal auditors to provide direct assistance on the audit engagement.

In Part 4B, the term "engagement team" refers to individuals performing assurance procedures on the assurance engagement. ISA 220 (Revised) provides further guidance on the definition of engagement team in the context of an audit of financial statements.

IESBA did not provide specific comments or feedback on these changes.

Individual independence

During IESBA's October 2020 meeting, the task force explained that the same independence considerations that apply to individuals from component auditor firms within the network should be applied to component auditors outside of the group auditor's network. This is because the

work of the individuals from the non-network firms contributes to the audit opinion on the group financial statements just as much as the work performed by individuals from component auditor firms within the network.

The task force believes that taking a consistent approach to personal independence, whether an individual is from a network firm or non-network firm, will eliminate any perception that the independence of component auditors on the engagement team outside the network is less important than that of component auditors on the engagement team within the network.

In addition, because the concept of a component⁶ under ED-ISA 600 is no longer limited to a corporate entity, the IIS should also require independence of the individuals involved in the group audit engagement of any components that are not related entities.

During IESBA's December 2020 meeting, the task force presented [preliminary draft text](#) for a new Group Audits section 405. The preliminary draft text requires that all members of the engagement team be independent of the group audit client and indicates that the task force would consider providing guidance on what a related entity is for a component within the scope of ISA 600. In the June 2021 papers, the preliminary draft text presented during the December 2020 meeting was further refined as reflected by the green highlighted text:

R405.4 All members of the **group audit engagement** team shall be independent of the group audit client.

405.4 A1 ***In the context of a group audit, the independence provisions that apply to the audit team in Part 4A apply to the group audit team with respect to the group audit client.*** ~~The relevant provisions set out in Sections 510, 511, 520, 521, 522, 524 and 525 apply to all members of the engagement team, their immediate family members and, where applicable, close family members.~~

Firm independence

During IESBA's October 2020 meeting, the task force explained it is not recommending revisions for component auditors within the group auditor's network because the IESBA code

6 ED-ISA 600 (Revised) defines a "component" as follows: "A location, function or activity (or combination of locations, functions or activities) determined by the group engagement team for purposes of planning and performing audit procedures in a group audit." Paragraph A4 of ED-600 notes that "the group engagement team uses professional judgment in determining the components for which audit procedures will be performed (by the group engagement team or component auditors on its behalf). The manner in which components are viewed for purposes of planning and performing a group audit may be influenced by the group structure, but may or may not be aligned with the way in which the group is organized, which could be, for example, by legal entities, geographic locations, or lines of business."

already requires network firms to be independent. Accordingly, the discussion focused on firms that are outside of the group auditor's network.

The general rule proposed is that a firm that is outside of the group auditor's network (and any of its network firms), should

- be independent of the component it is auditing as well as any related entities that the component can control using the PIE or non-PIE standard that is applicable to the group audit client.
- apply the conceptual framework with respect to all other related entities of the component.

In addition, the task force believes the component firm should *not* have a financial interest in the group audit client when the group audit client is a PIE and does not believe that the level of the threats to independence would warrant going upstream of the group audit client, if the group audit client itself were not the ultimate holding entity, given the further degree of separation. This prohibition, however, would not extend to the component firm's network firms.

The previously mentioned [preliminary draft text](#) for a new Group Audits section 405 required a firm issuing the audit opinion on the group financial statements and its network firms be independent of the group audit client, its related entities (and any other components scoped in under proposed ISA 600 (Revised)).

It also indicated that the task force would monitor ISA 600 and propose any necessary changes and would consider whether to include the "chain of command" at the component auditor's firm when the firm is outside of the network.

For component audit firms that are outside of the network, the preliminary draft text also required the group engagement partner to take responsibility for determining that component auditor firms have been made aware of relevant ethical requirements, including independence requirements, that are applicable given the nature and circumstances of the group audit engagement.

The preliminary draft text goes on to require the component auditor firm do the following:

- Be independent of the component audit client.
- Evaluate and address any relationships or circumstances it has that it knows or has reason to believe create a threat to its independence when such relationship or circumstance involves a related entity of the component audit client other than controlled related entities.
- Evaluate and address any interests or relationships a firm within its network has with a component audit client that it knows or has reason to believe create a threat to its

independence.

- Comply with the independence provisions that apply to public interest entities with respect to the component audit client, when the group audit client is a public interest entity.

During IESBA's June 2021 meeting, the board revised the preliminary draft text presented at the December 2020 meeting:

- Formatting – The text was reorganized to present the need to be independent in separate requirement paragraphs by type of entity (i.e., group audit firm, component auditor within network and component auditor outside of network).
- Substantive – Added a requirement that a component auditor firm that is outside of the group audit firm's network not have a direct or material indirect financial interest in the group audit client when that entity is a PIE.

Breaches of an independence requirement by a component auditor

During the March 2021 IESBA meeting, the task force explained the key principles it believes are appropriate for these situations:

- Breach of independence by a component auditor that is inside the network may impair the independence of the group auditor. Breaches could be addressed via additional actions and safeguards by the group auditor for the purposes of the group audit. This is in the extant code.
- Breach of independence by a component auditor that is outside of the network does not translate to a breach of the group auditor's independence. Breaches could be addressed via additional actions and safeguards by the group auditor for the purposes of the group audit. This is not in the extant code.

Overall, the task force proposed that the process that should be followed by a component auditor that is outside of the network should be the same as one that is in the network, except they would not need to communicate with those charged with governance.

To demonstrate the requirements, the task force developed flowcharts included as appendixes to the agenda materials for the March 2021 meeting. [Appendix 2](#) summarizes the process for addressing a breach of independence under the extant code in the context of audits of financial statements, including the statutory audit of group financial statements. [Appendix 3](#) explains the task force's preliminary approach for dealing with a breach of independence at a component auditor firm.

IESBA provided feedback, including the following:

- The group auditor should lead the discussion with those charged with governance.

- There was concern with the terms “significant” versus “very significant” as used in items (I) and (J) of appendix 3 when a breach is not considered inconsequential in relation to the group audit.
- A breach of a component auditor should not automatically impair the group auditor’s independence.

During the June 2021 meeting, the task force presented its [preliminary draft text](#). The preliminary draft text outlines the process that would apply when component auditor identifies a breach. At a high level, the process would be as follows:

- Evaluate the breach and communicate locally within the firm including those who need to act.
- Report to the group audit partner.
- Group audit partner evaluates and determines whether the breach would prohibit them from relying on the component auditor.

The IESBA asked the task force to clarify

- whether the component auditor or the group audit partner had to address the breach.
- what a standalone audit is.
- whether the group auditor had to communicate to TCWG that they could no longer rely on the component auditor.
- what was meant by the requirement that the component auditor “Evaluate the significance of the breach and its impact on the component auditor firm’s objectivity and ability to issue an audit opinion on the component audit client’s financial information for group reporting purposes (Ref: Para 400.80 A2).”

IESBA tax planning and related services

Convergence considerations

Staff has not performed a preliminary assessment of convergence. However, staff is keeping the tax division abreast of developments.

PEEC input on the project

This is the first update division staff have provided on this project. Staff welcomes PEEC's comments on the project including any concerns it believes should be monitored.

The following sections present IESBA's recent activity.

Project description

The objective of IESBA's initiative is to obtain an understanding of regulatory, practice, and other developments in corporate and individual tax planning for professional accountants in business (PAIBs) and professional accountants in public practice (PAPPs) and determine whether there is a need for enhancements to the IESBA code or further actions.

Status

At the June 2021 IESBA meeting, the Tax Planning and Related Services Working Group (TPWG) reported on its [fact finding and preliminary recommendations](#). The TPWG provided IESBA with a [preliminary version of its report](#). The TPWG plans to submit its final report and recommendation to the board at the September 2021 meeting.

Preliminary recommendation

The preliminary recommendation is that IESBA undertake a standard setting project to address ethical considerations when professional accountants (PAs) provide tax planning services to their employing organizations or clients by developing a principles-based framework. The TPWG preliminary recommendations also suggest that suitable terminology be developed to facilitate the understanding and use of the framework and consideration be given to the development of non-authoritative material.

Rationale for recommendation

The TPWG explained that the following are the drivers for their recommendation:

- The topic of tax planning has risen to a high level of public interest importance.
- Stakeholders' expectations that PAs act ethically in relation to tax planning have increased significantly.
- Other frameworks and guidance materials overlap to varying degrees but are not consistent because they do not serve the same purposes or address the same audience.

- There is a compelling need for a unifying framework in the code that would codify and embody the principles and best practices.
- Businesses' tax planning has become an important aspect of the growing ESG movement.

Preliminary components of framework

During the June 2021 meeting, the TPWG provided IESBA with an overview of components of the framework. At a high level, the framework would accomplish the following:

- Provide guidance to assist the professional accountant (PA) in identifying what might be deemed acceptable or unacceptable tax planning behavior.
- Address circumstances in which there might be undue pressure.
- Recognize that an inducement might be offered to achieve certain tax outcomes in strict non-compliance with tax legislation.
- Provide guidance on when communication with management or those charged with governance (TCWG) would be appropriate.
- Provide guidance on when and with whom to consult (internally or externally), which might be a part of specific actions to address identified threats.
- Address considerations relating to transparency balanced against a PAs' duty of confidentiality under the code.
- Address any documentation expectations for the PA.

Feedback provided during the June 2021 meeting

Though there was support for the proposed recommendation, IESBA provided feedback to the working group during the June 2021 meeting, including the following:

- Consider the challenge of unifying the different frameworks and to trying to define acceptable and unacceptable tax planning behavior.
- Consider developing indicators instead of trying to define acceptable and unacceptable tax planning behavior.
- Consider the approach used for inducements.
- Tie the recommendations back to public interest not to the greater societal role.
- Clarify whether the recommendations apply to just PIEs or if they also apply to non-PIEs.
- Clarify that the recommendations apply to tax planning done for both wealthy individuals and corporations.
- Clarify any differences between professional accountants in business and those in public practice.

IESBA quality management related conforming amendments

Convergence considerations

Staff has not performed a preliminary assessment.

PEEC input on the project

PEEC has not provided input on the project because the [project proposal](#) and the [draft proposal for exposure](#) was first brought to IESBA during its June 2021 meeting.

AICPA staff will work with the IFAC Convergence and Monitoring Working Group and the chairs¹ of the ASB's Quality Management Exposure Draft Task Force to develop a comment letter on the exposure draft.

Any member of PEEC not on the working group who would like to be involved with the comment letter process should reach out to Ms. Gorla.

The following sections present IESBA's recent activity.

Project description

The objective of this project is to develop conforming amendments to IESBA's code to ensure alignment and interoperability with ISQM 1 and ISQM 2. The project is focused on relevant provisions in parts 1, 3, 4A and 4B of the code that refer to ISQM 1 or ISQM 2, or terms and concepts used or defined in those two quality management (QM) standards.

Status

At the June 2021 meeting, IESBA approved not only the project proposal but a proposal for exposure. The exposure draft is due out the end of July 2021.

Feedback provided during the June 2021 meeting

During the June 2021 meeting, IESBA agreed that the following revisions be made to the proposals:

- The proposed deletion in 300.7 A5 should not be made since acceptance of the engagement lies with both the engagement partner and the firm.

The engagement partner having authority within the firm for decisions concerning compliance with the fundamental principles, ~~including decisions about accepting or providing services to a client.~~

- The term *operated* should be added to 400.53 A4.

¹ Sara Lord and Jon Heath.

Common quality ~~control~~ management policies **or and** procedures are those designed, implemented, **operated**, and monitored across the larger structure. (Ref: Para. R400.53(c)).

IESBA benchmarking independence provisions for audits of PIEs

Convergence considerations

Staff has not performed a preliminary assessment.

PEEC input on the project

This is the first written update division staff has provided on this project. Staff welcomes PEEC's comments on the project including any concerns it believes should be monitored.

The following sections present IESBA's recent activity.

Project description

IESBA is undertaking this initiative to compare the provisions in the International Independence Standards (IIS) that are applicable to public interest entities (PIEs) to the relevant independence requirements that apply in major jurisdictions, starting first with the requirements of the US SEC and the US PCAOB.

The goal of the initiative is an assessment of the alignment of the IIS and independence requirements in major jurisdictions and will help identify any substantive differences.

IESBA envisions that the outcome of this initiative will promote awareness and adoption of the IIS and the IESBA code more broadly. In addition, it will also help IESBA understand whether it should evaluate specific areas and, if appropriate, address as part of its future strategy and work plan.

Status

At the June 2021 IESBA meeting, the working group reported that it will focus only on topics¹ that are of greatest interest to stakeholders and will highlight the similarities and differences in the two sets of standards.

The working group will provide an overview of the differences between the IIS and the US SEC and US PCAOB requirements that are related to the approach taken. Differences that are not substantive or arise solely from the different context (i.e., global framework versus jurisdictional framework) will not form part of this comparison. The comparison will also highlight areas where the two sets of requirements are substantively similar in approach or outcome or both.

Report structure

The report resulting from this project needs to be easy to navigate and digest. Accordingly, the working group believes that it is essential that the report on phase 1 is of optimal length so as not to overburden readers or create barriers. It will also be important to summarize the overall

¹ The appendix to the [June agenda](#) lists the topics that the working group plans to focus on.

findings, including the key issues considered and the methodology or approach taken.

The working group believes there is merit to including a discussion about the differences between the remit of IESBA and national standards setters and regulators and the implications for the two sets of independence standards.

To avoid the deliverables becoming overly lengthy and complicated, mapping tables will not be a focus of the final deliverables for phase I of the initiative. Those will serve as the basis of the working group's analysis and will be available upon request.

The results of the initiative could potentially be viewed as interpretative in nature or "rule-making" outside of the code. To avoid this, the streamlined report will highlight the substantive differences and similarities between the two sets of standards and will focus on key issues. In addition, it will not include working group commentary with conclusions that might potentially be viewed as interpretive of certain provisions of the code (for example, with respect to the application of the conceptual framework).

IESBA technology

Convergence considerations

Staff has not performed a preliminary assessment given the early stages of the workstream.

PEEC input on the project

This is the first written update division staff has provided on this project. Staff welcomes PEEC's comments on the project including any concerns it believes should be monitored.

The following sections present IESBA's recent activity.

Project description

The project has two workstreams. The standard setting workstream is being performed by the Technology Task Force (TTF) and is focused on proposing technology related revisions to the IESBA code.

The fact finding¹ and development of non-authoritative material (NAM)² is being conducted by the Technology Working Group (TWG).

Status of the TF activities

The TTF shared its [draft proposals](#) for incorporating technology related revisions into the IESBA code. In addition to providing feedback on the specific additions an overall concern several members of IESBA expressed was that the proposals need to be more closely tied to technology. The TTF will continue to advance development of the enhancements to the code with a view to providing updated proposals in September 2021.

To provide further context of the proposals, following are summaries of some of the specific proposals.

Confidentiality

There was robust discussion around the proposed revisions to the *Confidentiality* subsection which were intended to emphasize the professional accountant's role in more actively protecting confidential information given changes in public expectations. To provide the TTF with

¹ The TWG will conduct fact-finding and information gathering on disruptive technologies and related issues, including blockchain (e.g., Cryptocurrencies and Initial Coin/ Security Token Offerings), cyber-security, cloud-based services, internet of things (IoT) and data governance.

² The TWG plans to develop NAM related to Ethical Leadership in an Era of Complexity and Digital Change; Confidentiality and Privacy; Auditor Independence; and Accountability and Transparency.

directional input, IESBA was asked to weigh in on two options.

The first option minimizes the changes to the subsection while the changes in the second option were more extensive.

The goal of the second option was to present a principles-based summarized description that would be at less risk of becoming obsolete. Both options accomplish the following:

- Add a more active and scalable action word “protect” in paragraph R114.1.
- Modernize terminology by adding “or access is granted” in paragraph 114.1 A2.
- Provide guidance for professional accountants when setting governance policies and procedures by adding new application material in paragraph 114.1 A3.
- Promote consistent understanding of what information is confidential and highlight the relevance of privacy by proposing a description of “confidential information” to be included in the glossary.

The feedback favored the first option, noting that it would require PAOs to make fewer revisions to text and acknowledged that professional accountants should take steps to protect confidentiality.

Preparation and presentation of information by professional accountants in business

The proposed additions to the *Preparation and Presentation of Information* section added explicit references to technology relating to relying on the work of others when preparing and presenting information and provided guidance as to what is reasonable reliance on technology and when the professional accountant *is* in a position to determine the reasonableness.

With respect to when the professional accountant is in a position *to* determine the reasonableness of the information, there was some concern that seniority would not necessarily lead someone to knowing more.

Business relationships: Technology sold/licensed between firm and audit client

The proposed additions to the *General* subsection of the *Business Relationships* section of the IIS were to highlight examples of what could constitute a close business relationship when technology is sold/licensed between the firm and audit client. One member of IESBA requested the TTF further reflect on the additions since they seemed to go beyond the SEC’s rules.

Business relationships: Consideration of nonassurance services

The TTF proposed adding a new subsection to the *Business Relationships* section of the IIS to address the fact that the results of the 2020 technology survey indicated that about 24 percent of respondents did not think that the non-assurance provisions in the code are relevant when a firm licenses technology that performs a non-assurance service. To drive consistent practice, the TTF proposed adding a new *Consideration of Non-assurance Services* subsection to the

Business Relationships section of the IIS to include an explicit provision that the code is applicable.

Accounting and Bookkeeping Services

The TTF proposed adding the following application guidance to the *Accounting and Bookkeeping Services* subsection of the IIS to highlight that automated nonattest services are not necessarily routine and mechanical.

Accounting and bookkeeping services that are routine or mechanical can either be manual or automated. Automated services might appear to be routine or mechanical because of the ease with which the task can be completed due to the relative lack of human involvement. In determining whether the nature of an automated service is routine or mechanical, consideration should be given as to how the technology functions and whether the technology provides expertise or judgement attributable to the firm or the network firm.

Information technology system services

The TTF proposed adding the following application guidance to the *Information Technology System Services* subsection of the IIS to do the following:

- Clarify that the TTF believes that implementing “off-the-shelf” accounting or financial information reporting software might create a self-review threat and involves a risk of potentially affecting the audit of the financial statements on which the firm will express an opinion or might form part of the client’s internal control.
- Provide an expanded description of IT systems services to highlight that the services related to IT systems extend outside of the design, development, and implementation of hardware or software systems.
- Incorporate a conforming change to the lead-in of 606.2 A1 so that it encompasses other IT systems services.
- Incorporate the TTF’s view that the provision of services related to operating, maintaining, monitoring, updating or hosting IT systems should be prohibited.

Status of the TWG activities

During Q2 2021, the TWG developed a to support its outreach information gathering activities. The briefing note is informational and intended to provide stakeholders with background on IESBA’s multi-workstream technology initiative.

It highlights the areas of focus with respect to technology information-gathering, including the questions and topics that are being explored about the ethical implications of developing, implementing and using technology in relation to accounting and finance, including auditing.

The TWG also contributed to the development of a thought-leadership paper titled “Complexity and the Professional Accountant.” The paper was informed by a virtual workshop jointly hosted by CPA Canada, the Institute of Chartered Accountants of Scotland (ICAS), and IFAC in February 2021.

The workshop participants, including IESBA representatives, exchanged views and perspectives having considered an exploratory paper titled “[Ethical Leadership in an Era of Complexity and Digital Change](#).” The paper is the first in a series. Subsequent titles will include the following:

- Technology is a Double-edged Sword
- Identifying and Mitigating Bias and Mis-/Disinformation
- Mindset and Enabling Skills

In addition, the TWG participated in targeted stakeholder outreach, evaluated submissions from the technology surveys and continued to perform desktop research. Based upon this research, and to inform IESBA’s ongoing deliberations about ethics and independence issues that might arise from the use of blockchain technology in accounting and financial reporting as well as audit and assurance, the TWG arranged for two informational presentations for IESBA members during the June 2021 meeting.

The first presentation titled “Use of Blockchain in Corporate and Financial Reporting, and Regulatory Implications” draws from relevant academic research on:

- How blockchain, including cryptocurrency, is being used in corporate and financial reporting as well as audit and assurance, and the potential ethics and independence issues that might arise.
- Key regulatory developments relating to blockchain, including recent decisions made and deliberations being undertaken by regulators and standards setters such as the International Accounting Standards Board (IASB), the US FASB, and the US SEC.

The second presentation titled “Blockchain and Internal Control – Relevant Insights and Perspectives” highlighted key aspects of an August 2020 paper titled, [Blockchain and Internal Control: The COSO Perspective](#) that was commissioned by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The paper

- provides perspectives for using the COSO Internal Control – Integrated Framework (2013) to evaluate risks related to the use of blockchain in the context of financial reporting and to design and implement controls to address such risks.
- is intended to help inform decisions regarding oversight, risks, and internal control over financial reporting (ICFR) in a blockchain environment.

Staff augmentation

Task force members

Lisa Snyder (chair), Coalter Baker, Jeff Lewis, Brian Lynch, Nancy Miller

AICPA Staff

Ellen Gorla, John Wiley

Task force charge

Study the issue of staff augmentation as it relates to independence and determine whether additional guidance for members is warranted.

Reason for agenda item

The committee is asked for input on the recommendation to issue the four Qs & As in agenda item 7B.

Task force activities

Two draft Qs & As were presented to the committee for consideration during the May 2021 meeting. The committee provided feedback and the task force deliberated and made changes as follows.

Staff augmentation arrangement versus nonattest services engagement

The first Q&A discussed the difference between a staff augmentation arrangement and a nonattest engagement. This Q&A focused on two differences:

1. In a staff augmentation arrangement, the attest client, not the member, is responsible for the direction and supervision of the activities performed by the loaned staff.
2. Nonattest services generally result in the issuance of a work product or deliverable that is subject to the firm's quality control process.

Based on the committee's feedback, the task force simplified the Q&A to reflect that the member's supervision of the arrangement is limited to ensuring compliance with the terms of the arrangement rather than the activities of the loaned staff.

After considering the suggestion of listing the attributes of a staff augmentation arrangement versus a nonattest engagement, the task force concluded that there were not many to list and that the two differences identified would be the most direct answer.

Reoccurrence of staff augmentation arrangements

The second draft Q&A discussed the reoccurrence of unexpected situations. The committee noted that the Q&A should be split into two separate Qs & As, one discussing the meaning of "unexpected situation that creates a significant hardship," and the other discussing what

happens if such a situation reoccurs.

The task force split this into three Qs & As.

For the first, the member needs to use professional judgement to determine whether making other arrangements during the unexpected situation will create a significant hardship for the attest client that could be avoided with a staff augmentation arrangement.

Two additional Qs & As address what constitutes an unexpected situation and a significant hardship, respectively.

Effective date

A question arose concerning application of the effective date of the interpretation. The interpretation is effective November 30, 2021. Staff requests the committee's input on whether that means all staff augmentation arrangements must be terminated by that date, or if that means if a member had a staff augmentation arrangement during the period covered by the financial statements ending November 30, 2021, the member would not be independent. Staff prepared a Q and A regarding the application of the effective date stating that to maintain independence, the safeguards provided for in the interpretation must be met for any new arrangements entered into after the effective date, and arrangements that are ongoing as of the effective date.

Questions for the committee

1. Does the committee agree with the task force's conclusion regarding the Q&A for the differences between a staff augmentation arrangement and a nonattest service?
2. Does the committee agree with the task force's conclusion regarding the Q&A for reoccurrence of a staff augmentation arrangement?
3. Does the committee agree with the task force's conclusion regarding the Qs & As for what constitutes an unexpected situation and a significant hardship?
4. Does the committee agree with staff's proposed Q&A for application of the interpretation's effective date?
5. Does the committee have any other input on the proposed Qs & As?

Materials presented

- Agenda item 7B: Proposed Qs & As related to staff augmentation arrangements

Proposed Qs & As related to staff augmentation arrangements

Staff augmentation versus nonattest services engagement

Inquiry – What are the differences between a staff augmentation arrangement with a *client* and a nonattest services engagement?

Response – In a staff augmentation arrangement, the *client* agrees to be responsible for the direction and supervision of the activities performed by the loaned staff. The *member's* supervision of the arrangement is limited to ensuring compliance with the terms of the arrangement rather than the overseeing the activities of the loaned staff.

In a nonattest services engagement, the *member* or *member's firm* is solely responsible for the direction and supervision of the staff's activities. A nonattest services engagement generally results in the *member's* issuance of a work product that is subject to the *firm's* quality control process, including a review of the staff's work prior to signing off on the final work product.

Reoccurrence of staff augmentation arrangements

Inquiry – The “[Staff Augmentation Arrangements](#)” interpretation (ET sec. 1.275.007) under the “[Independence Rule](#)” [1.200.001] requires that the augmented staff arrangement is not expected to reoccur.

If the *member* or *member's firm* has loaned staff for a prior unexpected situation and the *attest client* experiences a new unexpected situation, is the *member* prohibited from entering into another staff augmentation arrangement?

Response – It depends. If another unexpected situation does arise and the *attest client* will experience significant hardship in making other arrangements, the *member* needs to evaluate the facts and circumstances to determine whether loaning staff again will *impair independence*. In performing this evaluation, the *member* should consider factors such as the following:

- Whether the *member* should have reasonably expected that the *attest client* would need another staff augmentation arrangement in the future
- The length of time that has passed since the previous staff augmentation arrangement
- Whether the situation giving rise to the need for loaned staff is different than what existed for the prior arrangement
- Whether the work to be performed and the loaned staff will be different from the work and staff involved in the prior arrangement
- Whether there are other options available to the *attest client*

Staff augmentation and unexpected situations

Inquiry – The “[Staff Augmentation Arrangements](#)” interpretation (ET sec. 1.275.007) under the “[Independence Rule](#)” [1.200.001] says that such arrangements are allowable only if there is an unexpected situation that would create a significant hardship for the *attest client* to make other arrangements.

What constitutes an unexpected situation?

Response – An unexpected situation is an event or set of circumstances that was not planned for or was unforeseen by the *attest client*. Examples of unexpected situations that can affect an *attest client* include the sudden loss of a key employee, natural disasters, and casualty losses such as fire or theft.

Staff augmentation and significant hardship

Inquiry – The “[Staff Augmentation Arrangements](#)” interpretation (ET sec. 1.275.007) under the “[Independence Rule](#)” [1.200.001] says that such arrangements can only be performed if there is an unexpected situation that would create a significant hardship for the *attest client* to make other arrangements.

What constitutes a significant hardship?

Response – *Members* should use professional judgment in determining whether the unexpected situation will create a significant hardship for the *attest client*. In making this determination, the *member* should weigh factors such as the urgency of the need against the length of time it would take the *attest client* to make alternative arrangements.

Staff augmentation interpretation effective date

Inquiry – The “[Staff Augmentation Arrangements](#)” interpretation (ET sec. 1.275.007) under the “[Independence Rule](#)” [1.200.001] is effective November 30, 2021. How is the effective date applied to maintain *independence*?

Response – To maintain *independence*, the *safeguards* provided for in the *interpretation* must be met for the following:

- New arrangements entered into after November 30, 2021
- Existing arrangements that are in place as of November 30, 2021

Any existing arrangements should be terminated by November 30, 2021 if the required safeguards cannot all be met as of that date.

IFAC convergence and monitoring

Working group members

Brian Lynch (chair), Cathy Allen, Nancy Miller, Katherine Savage, Lisa Snyder

AICPA staff

Sarah Brack, Ellen Gorla, Iryna Klepcha, Summer Young

Working group charge

The International Federation of Accountants (IFAC) Convergence and Monitoring Working Group is charged with identifying projects that need to be undertaken due to inconsistencies between the AICPA and IFAC codes.

Reason for agenda item

The working group seeks approval to form a task force to determine the convergence needs for the [fee-related standards](#) IESBA issued in April 2021.

Working group activities

The working group discussed the AICPA and the IESBA codes on this topic and believes there are enough differences to warrant appointing a task force to determine the necessary convergence steps. The IESBA code has the following requirements or, in the case of public interest entities (PIEs), are developing requirements that are absent from the AICPA code:

- A requirement that the audit fee not be influenced by services other than the audit engagement except for cost savings due to experience derived from the provision of those services.
- A requirement that the firm apply certain safeguards when, for each of five consecutive years, total fees from an audit client that is not a public interest entity (non-PIE) represent, or are likely to represent, more than 30 percent of the total fees received by the firm.
- Requirements specific to PIEs. The working group recommends the appointed task force wait until IESBA issues its revised PIE standard before determining whether convergence steps should be taken.

Another difference the working group noted (that existed between the two codes prior to IESBA's April 2021 revisions) relates to contingent fees. Because the committee has not formally evaluated contingent fees from a convergence perspective, the working group recommends the task force include contingent fees within its scope. Two differences between the codes in this area are as follows:

- The IESBA code permits charging an attest client a contingent fee for nonattest services provided they are not material to the firm or a network firm that participates in a significant part of the audit.
- The IESBA code prohibits a firm from indirectly charging an attest client a contingent fee for an audit engagement while the AICPA code does not include a concept for indirect contingent fees.

Action needed

The committee is asked to consider appointing a task force to determine the necessary convergence steps and staff welcomes input on the timing of the project given the committee's current project timetable.

Open meeting minutes – May 4–5, 2021

Professional Ethics Division Professional Ethics Executive Committee

The Professional Ethics Executive Committee (PEEC or committee) held a duly called meeting May 4–5, 2021. Day 1 of the virtual meeting convened at 10 a.m. EST on May 4 and adjourned at 2:35 p.m., Day 2 convened at 10 a.m. on May 5 at and adjourned at 12:15 p.m.

We sent agenda materials for this meeting to PEEC members and observers on April 15, 2021 and posted them to aicpa.org.

Contents

- Attendance
- Key votes in this meeting
- Welcome
- SEC convergence
- Client affiliates
- Information systems services
- Compliance audits
- Assisting clients with implementing accounting standards
- Confidentiality and data security
- IESBA update
- Statements on Standards for Tax Services
- Definition of office
- Staff augmentation
- Member enrichment update
- Approval of February meeting minutes
- Appendix

Attendance

Members

Brian Lynch, Chair
Catherine Allen
Christopher Cahill
Thomas Campbell
Robert Denham
Anna Dourdourekas
Anika Heard
Kelly Hunter
Sharon Jensen
Jennifer Kary
Jeff Lewis
Alan Long
William McKeown
James Newhard
Stephanie Saunders
Lewis Sharpstone
Lisa Snyder
Peggy Ullmann
Douglas Warren
Lawrence Wojcik

Guests

See exhibit 1 in the appendix of this document.

AICPA Professional Ethics Division staff

James Brackens, Vice President –
Ethics and Practice Quality
Toni Lee-Andrews, Director
Ellen Gorla, Associate Director
Jennifer Clayton, Associate Director
Michele Craig
Elaine Bagley
Sarah, Brack
Emily Daly
Liese Faircloth
Jennifer Kappler
Iryna Klepcha
Hanna Mayle
Kelly Mullins
Melissa Powell
Karen Puntch
Michael Schertzinger
John Wiley
Heidi Winn
Summer Young
Shannon Ziemba

Key votes in this meeting

Motions approved

- Issue an exposure draft of the revisions to the loan provisions for SEC convergence.
- If adopted, the loan provisions should be effective the last day of the month in which notice appears in the *Journal of Accountancy*

Welcome

Mr. Lynch welcomed the committee and discussed administrative matters.

SEC convergence

Ms. Kary updated PEEC on task force activities since the last February meeting ([agenda item 1A](#)) and sought approval for revisions to the “Loans” interpretation, the “Loans and Leases from Lending Institutions” interpretation, and the “Client Affiliates” interpretation (SEC convergence; [agenda items 1A–1G](#)).

Items of note include the following:

- Issuance of the non-authoritative Q&A
- Revision to the “Immediate Family Members,” “Loans,” “Loans and Leases from Lending Institutions,” and “Client Affiliates” interpretations.

To review these in detail, [see agenda item 1A](#) in the May meeting agenda.

Discussion

The committee discussed the affected interpretations and agreed to the following:

- Revision to the definition of *beneficially owned*, as follows (additions in bold italic; deletions in strikethrough)

0.400 Definitions

.06 Beneficially owned, **beneficial ownership interest**. Describes a *financial interest providing* of which an individual or entity, **who may or may not be** ~~is not~~ the record owner, ~~but has~~ **the** a right to some or all of the underlying benefits of ownership. These benefits include the authority to direct the voting or disposition of the interest or to receive the economic benefits of the ownership of the interest.

The explanation accompanying the exposure draft clarified that for the loan to create an issue, the individual at the affiliate must have the ability to affect decision-making at the financial statement attest client or have significant influence over the financial statement attest client.

- The acquisition and other business combination revisions need further refinement. The committee asked the task force to consider the following:
 - Replace the phrase “other business combinations” with something that would more broadly cover all the types of transactions covered by the proposal.
 - Shorten the sub-headings.
 - Consider moving paragraph .06 so that it does not distract from the flow of the proposal.
 - Revise paragraph .10 so that readers can distinguish between situations covered by this paragraph and paragraph .05.
 - Develop parameters around what a “short period of time” is.

Votes

The committee voted unanimously with no abstentions to issue an exposure draft of the revisions to the loan provisions.

The committee agreed by vote of 14 for with 4 abstentions that if adopted, the loan provisions should be effective the last day of the month in which notice appears in the *Journal of Accountancy*.

Client affiliates

Ms. Snyder updated PEEC on the task force’s activities and sought approval for revisions to the “Client Affiliates” interpretation ([agenda items 2A–2C](#)).

- The task force’s purpose is to determine whether the current client affiliates guidance in the AICPA Code of Professional Conduct (code) should apply to individuals, and whether other aspects of the definition of “affiliate” may need revision.
- The task force concluded that new authoritative guidance is necessary because the current definition does not address individuals and three types of affiliates in the current “affiliates” definition are subject to revision.
- The committee noted the client affiliates interpretation may need to be revised to reflect the addition of individuals and supported the task force’s initial conclusions.
- The task force will meet to determine revisions to bring to the committee at the August meeting.

Information systems services

Ms. Dourdourekas updated PEEC on the task force’s recent activities and sought input on the proposed direction for the practice aid in development ([see agenda item 3](#)).

The task force provided an overview of the toolkit step approach language including the following:

- Are the general requirements of the 1.295 subtopic met?
- Are the criteria for the discrete exception met?
- Are the services related to a Financial Information System (FIS)?
 - If not related to an FIS, do they impair independence?
 - If related to an FIS, do they impair independence?
- Do the post-implementation services impair independence?

Discussion

Question 1: What are the common issues firms expect to encounter in applying the new guidance?

The committee recommended

- helping members in evaluating whether a system is a FIS by understanding how it interconnects with other systems across the entity (important to see the architecture).
- including examples of what financial processes are.

Question 2: Does the committee have any feedback on the task force's proposed approach?

The committee recommended including examples of when members are developing spreadsheets for calculations (e.g., Nexus).

Compliance audits

Ms. Miller provided PEEC with an overview of the task force's preliminary conclusions regarding compliance audit application and solicited feedback on the task force's conclusions ([agenda item 4](#); also see exhibit 3 of this document).

Discussion

Question 1 – Are there any questions or concerns related to the task force's conclusion of who is the attest client and the need for additional nonauthoritative guidance?

The committee expressed no concerns.

Question 2 – Is the committee in favor of the task force exploring the possibility of a change in the code that would allow relief from the independence requirements as they relate to entities reporting trivial or inconsequential amounts on the financial statement that is associated with a compliance audit?

The committee had no objections to the task force exploring relief for entities that report trivial or

inconsequential amounts on the financial statement.

Question 3 – For attest clients outside of a state and local government environment, does the committee believe that the attest client could be an “entity” that is less than the legal entity when the member is only performing a compliance audit for that “entity”? If so, does the committee believe that this should be clarified in the code or in nonauthoritative guidance?

The committee believed that members should look to the legal entity to determine independence.

Question 4 – Are there any questions or concerns related to the task force’s conclusion and the need for additional nonauthoritative guidance?

The committee had no concerns.

Question 5 – Are there any questions or concerns related to the task force’s conclusion related to affiliates (outside of the state and local government environment)?

The committee had no concerns.

Question 6 – What are the committee’s views on whether the task force should explore circumstances that could support exceptions to the “Client Affiliates” interpretation for compliance audits?

The committee had no objections to the task force considering affiliate exceptions.

Question 7 – Does the committee have any concerns with the task force expanding its charge to explore application guidance of the “Breach of an Independence Interpretation” to particular circumstances in a compliance audit?

The committee had no objections to expanding the charge to consider breaches guidance.

Question 8 – Does the committee have any questions or concerns related to the task force’s consideration of the “State and Local Government Client Affiliates” interpretation?

The committee had no concerns.

The committee wanted the task force to keep in mind consistency with other aspects of the code, in particular the consideration of trivial and inconsequential entities on the financial statement and potential exceptions to the affiliate interpretation.

Assisting clients with implementing accounting standards

Ms. Kary updated PEEC on the task force’s kickoff meeting.

The task force is still undecided whether authoritative or non-authoritative guidance or a combination of both is appropriate. The task force will decide once its direction is clarified and expects to present more at the August meeting.

Confidentiality and data security

Mr. Campbell updated PEEC on the task force's kickoff meeting.

- The task force agreed that the current resources from the AICPA's Private Companies Practice Section (PCPS) need to be updated.
- PCPS is currently updating two of the documents listed in their resource center:
 - Cyber security checklist
 - Article on the occurrence of a hack or data breach
- The task force provided feedback to PCPS on areas where members need guidance on protecting client data.
- The task force plans to review the updated articles from PCPS once completed and then decide how to alert members of the updates.

IESBA update

Mr. Mintzer and Ms. Gorla provided PEEC with an update on IESBA's March 2021 meeting and the following IESBA projects ([agenda items 5A–5C](#); also see exhibit 2 of this document):

- Engagement team ([agenda item 5B](#))
- Tax planning and related services ([agenda item 5C](#))
- Benchmarking
- Technology

Statements on Standards for Tax Services

Ms. Saunders provided PEEC with an update on recent activities of the SSTS task force.

- The task force continues to meet with individual AICPA committees and technical resource panels soliciting feedback on the proposed standards.
- Due to COVID and changing tax deadlines, few meetings have been held with other tax groups during 2021.
- The task force will have meetings throughout the summer and plans to bring the next draft of the revised standards back to PEEC during its closed meeting in August.
- The task force anticipates exposure of the standards in late 2021. The exposure period may be extended through June 2022 to accommodate tax season.

Definition of office

Mr. Hunter updated PEEC on the task force's activities and sought input on the proposed Q&A ([agenda items 6A–6B](#)).

The current definition of office was drafted broadly enough to cover the changes to a virtual

working environment.

PEEC decided an [Ethically Speaking podcast episode](#) on the definition of office is a more appropriate approach than Qs & As with examples.

Staff augmentation

Ms. Snyder updated PEEC on the task force's activities and sought input from PEEC on two proposed Qs & As ([agenda items 7A–7B](#)).

The committee discussed the language in both Qs & As and recommended that the second one be split into two questions, one clarifying what constitutes an unexpected situation and the other clarifying the meaning of “not expected to reoccur.”

The committee discussed revising the second Q&A for unexpected situations with a list of factors to give practitioners more guidance in determining whether the staff augmentation arrangement meets the criteria of the interpretation.

The task force will incorporate the committee's comments and report back at the August meeting.

Member enrichment update

Ms. Gorla provided PEEC with a status update of member enrichment projects not covered by specific agenda discussions.

- The inducements practice aid and GAO comparison should be published before the August meeting.
- Division staff is drafting nonauthoritative Qs & As to guide members in explaining hosting services to their clients.
- The division plans to expand the *Ethically Speaking* podcast and has identified three new series:
 - What's hot on the hotline? – [The first episode in this series](#) is published and covers records requests and nonattest services. Staff expects to publish episodes at least quarterly, if not more often.
 - Back to basics – Staff expects to publish this series in weekly installments during 3Q.
 - Maintaining ethics in challenging times – Staff expects to publish episodes periodically.
- Division staff is drafting an ethics quiz for the *Journal of Accountancy* featuring common issues surrounding EAQ (enhancing audit quality) initiatives.

- Division staff is updating non-authoritative practice aids with recommendations on IESBA's role and mindset project that the committee offered at the February meeting.
- Division staff is participating in a cross-functional campaign (Single Audit Content Squad) to educate auditors whose clients need a single audit for the first time this year due to receiving COVID relief funding.
- Division staff is working with the Assurance and Advisory Innovation team to develop SOC 2 Qs & As on SOC 2 software tools.
- Operational enhancements to the code are in process, including the creation of an online ethics library and relocation of all ethics Qs & As into AICPA *Technical Questions and Answers*.

Approval of February meeting minutes

The committee voted unanimously with no abstentions to approve the minutes of the February meeting.

Appendix

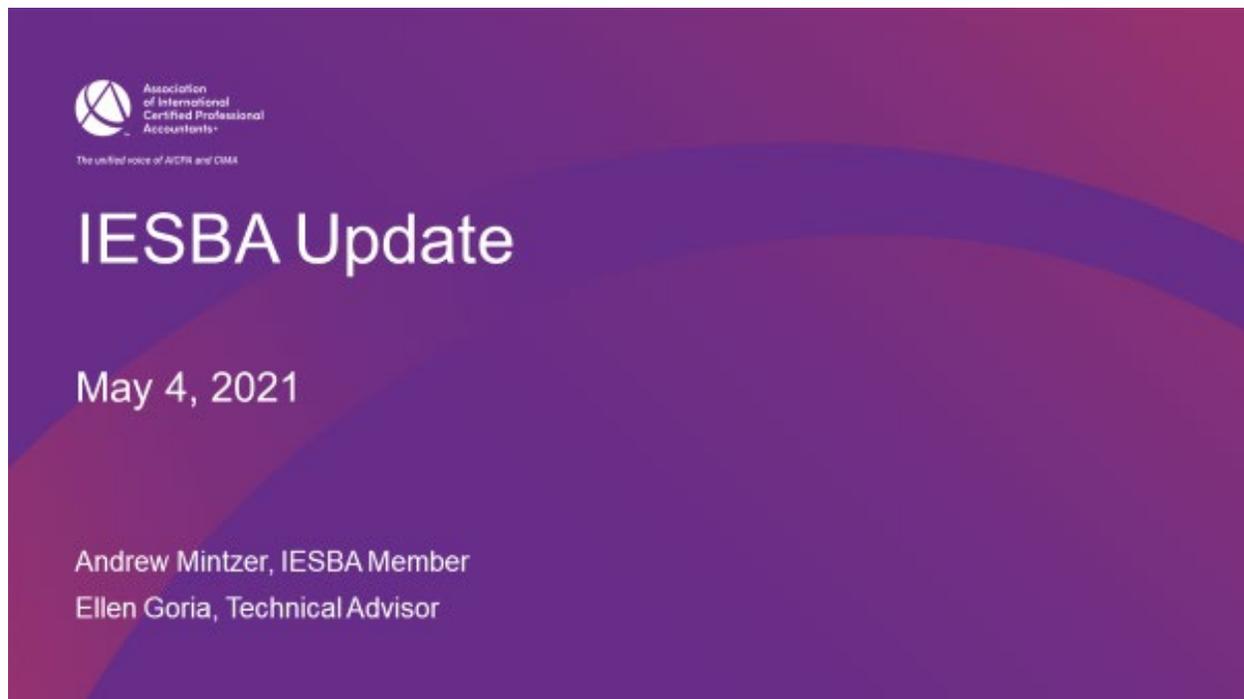
Guests in attendance at the February 2021 meeting

	Name	Company
1.	Christine Cutti-Fox	AICPA, Senior Manager, Forensics
2.	Henry Grzes	AICPA, Lead Manager, Tax Practice and Ethics
3.	Carl Peterson	AICPA, Vice President, Small Firms – PA
4.	Sonia Araujo	PwC
5.	Arthur Auerbach	Arthur Auerbach, CPA
6.	Rita Barnard	Kansas Society of CPAs
7.	Ian Benjamin	Chair–AICPA Enforcement Subcommittee
8.	Claire Blanton	RSM US LLP
9.	Sheila Border	Wipfli, LLP
10.	David Kirklan Cloniger	RSM US LLP
11.	Allan Cohen	RSM US LLP
12.	Karen Cookson	U.S. Department of Housing and Urban Development
13.	Debbie Cutler	Debra A. Cutler CPA PC
14.	James Dalkin	U.S. Government Accountability Office
15.	Anna Durst	Nevada Society of CPAs
16.	Dan Dustin	NASBA
17.	Jason Evans	BDO

18.	Jeremy Farrah	Runyon Kersteen Ouellette
19.	Greg Fiedler	Sikich LLP
20.	Andrew Gripp	Crowe LLP
21.	Becky Grupe	BKD, LLP
22.	Mary Beth Halpern	Maryland Association of CPAs
23.	Bethany Hearn	CliftonLarsonAllen
24.	Kelly Hnatt	External Counsel
25.	Patricia Hutson	Jenkins & Company, P. C.
26.	Laura Hyland	Moss Adams
27.	Nigel James	U.S. Securities and Exchange Commission
28.	Diane Jules	IESBA
29.	Vassilios Karapano	U.S. Securities and Exchange Commission
30.	Peggy Kitzmiller	Aldrich Technology
31.	Elizabeth Knipscheer	HoganTaylor LLP
32.	Ken Kortas	Wipfli, LLP
33.	Kimberly Kuhl	KPMG
34.	Laura Lantz	Idaho Society of CPAs
35.	Christine LeGrand	PwC
36.	Elliot Lesser	Berdon LLP– Retired
37.	Stacey Lockwood	Society of Louisiana CPAs
38.	Jasdeep Mangat	U.S. Securities and Exchange Commission

39.	William Mann	Mayer Hoffman McCann P.C.
40.	Joe Marchbein	Rice Sullivan, LLC
41.	Elizabeth McKneely	Deloitte
42.	Kathleen Meyer	Missouri Society of CPAs
43.	Nancy Miller	KPMG
44.	Andy Mintzer	Hemming Morse, LLP
45.	Angela Miratsky	BKD, LLP
46.	Karen Moncrieff	EY
47.	Christina Moser	Plante Moran
48.	Jessica Mytrohovich	Georgia Society of CPAs
49.	Jan Neal	Deloitte
50.	Jennifer Noble	RSM US LLP
51.	Donna Oklok	Accountancy Board of Ohio
52.	Christine Piche'	CliftonLarsonAllen
53.	Paul Pierson	Illinois CPA Society
54.	Chris Rabin	Sikich LLP
55.	Terrill Ramsey	Terrill Ramsey, CPA
56.	Jacqueline Reardon	Rosen, Sapperstein & Friedlander, LLC
57.	Mark Reynolds	Creative Value Consulting LLC
58.	John Robinson	RSM US LLP

59.	Deborah Rood	CNA Insurance
60.	Stephanie Sauer-Watts	PwC
61.	Kathy Savage	Deloitte
62.	April Sherman	CliftonLarsonAllen
63.	Rachel Sinks	CliftonLarsonAllen
64.	Ola Marie Smith	State of Michigan
65.	Susan Speirs	Utah Association of CPAs
66.	Annette Stalker	Stalker Forensics
67.	Marc Stepper	Washington Society of CPAs
68.	John M. Szczomak	New Jersey Society of CPAs
69.	Joseph Tapajna	University of Notre Dame
70.	Jessica Tomc	EY
71.	Stephen Valenti	Steven Valenti, CPA
72.	Dan Vuckovich	Anderson ZurMuehlen
73.	Jim West	BDO
74.	Ellen Wisbar	CBIZ, Inc.
75.	Paula Young	EisnerAmper, LLP
76.	Darlene Zibart	Kentucky Society of CPAs



Association of International Certified Professional Accountants
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IESBA Update

May 4, 2021

Andrew Mintzer, IESBA Member
Ellen Gorla, Technical Advisor

Tax Planning and Related Services



2



Tax Planning – Described Terms

No clear line between tax planning and aggressive tax planning
Some jurisdictions may use several approaches to encourage tax compliance and to discourage unacceptable tax planning practices <ul style="list-style-type: none">• Tax regulations to deal with <u>unacceptable tax planning</u> practices, for example• General Anti-Avoidance Rule• Targeted Anti-Avoidance and Mandatory Disclosure Rules
Acceptable versus unacceptable tax planning

3

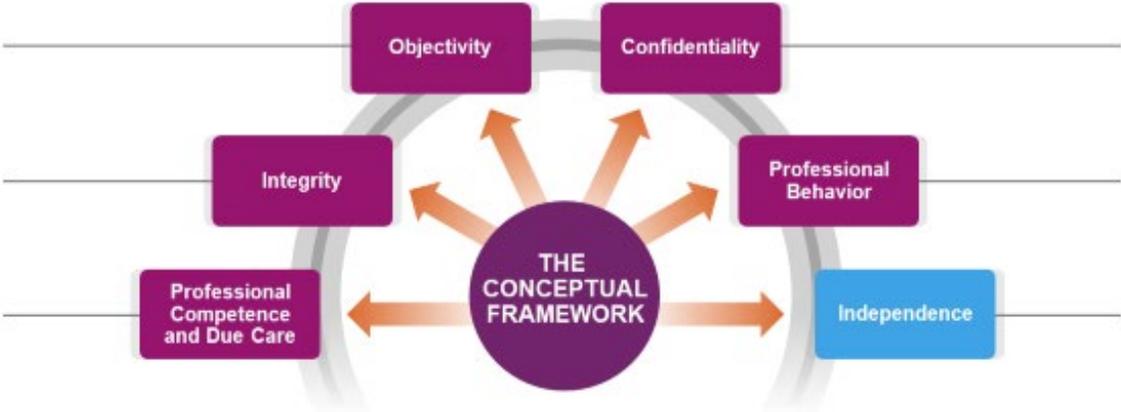
Working Group – Preliminary Views

	Difficult to adequately define aggressive tax planning on a global scale
	Tax planning is a defined term in most jurisdictions
	Lack of authoritative literature that clearly defines aggressive tax planning
	To explore merit of a principles-based decision-making framework to guide PAs: <ul style="list-style-type: none">Identify what would be deemed acceptable or unacceptable tax planning behaviorConsider use of indicators

Transparency and accountability



Ethical Behaviors of PAs in Tax Planning



Options

Option
A

- Develop overarching material in the Code to assist PAs comply with FPs and apply CF

Option
B

- Develop material under one or more specific FPs to explain expected behavior of PAs performing tax planning activities

Option
C

- Develop material outside the Code (e.g. Q&As or case studies) on the types and magnitude of threats created when PAs perform tax planning activities.

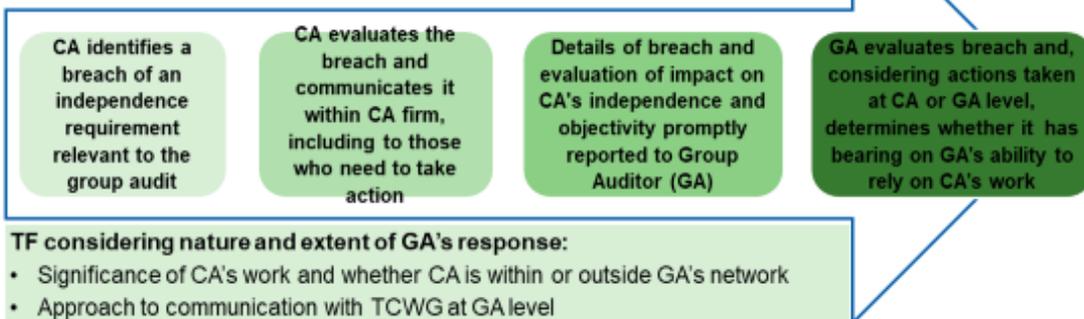
Engagement team

Proposed Revised Definition – Engagement Team – Extant Code vs. Mar 2021 (Marked Up)

Terminology	Extant Code Described Terms	Proposed Definitions – March 2021 Meeting (Marked Up against Extant Code)
Engagement team Applicable to all types of engagements	All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform assurance procedures on the engagement. This excludes external experts engaged by the firm or by a network firm. The term "engagement team" also excludes individuals within the client's internal audit function who provide direct assistance on an audit engagement when the external auditor complies with the requirements of ISA 610 (Revised 2013), <i>Using the Work of Internal Auditors</i> .	All partners and staff performing the engagement, and any other individuals engaged by the firm or a network firm who perform assurance procedures on the engagement, excluding an This excludes external experts and internal auditors who provide direct assistance on the engagement. engaged by the firm or by a network firm. <u>The term "engagement team" also excludes individuals within the client's internal audit function who provide direct assistance on an audit engagement when the external auditor complies with the requirements of ISA 610 (Revised 2013), <i>Using the Work of Internal Auditors</i>.</u> <u><i>In Part 4A, the term "engagement team" refers to individuals performing audit or review procedures on the audit or review engagement, respectively.</i></u> <u><i>In Part 4B, the term "engagement team" refers to individuals performing assurance procedures on the assurance engagement.</i></u> <u><i>(ISA 220 (Revised) provides further guidance on the definition of engagement team in the context of an audit of financial statements)</i></u>

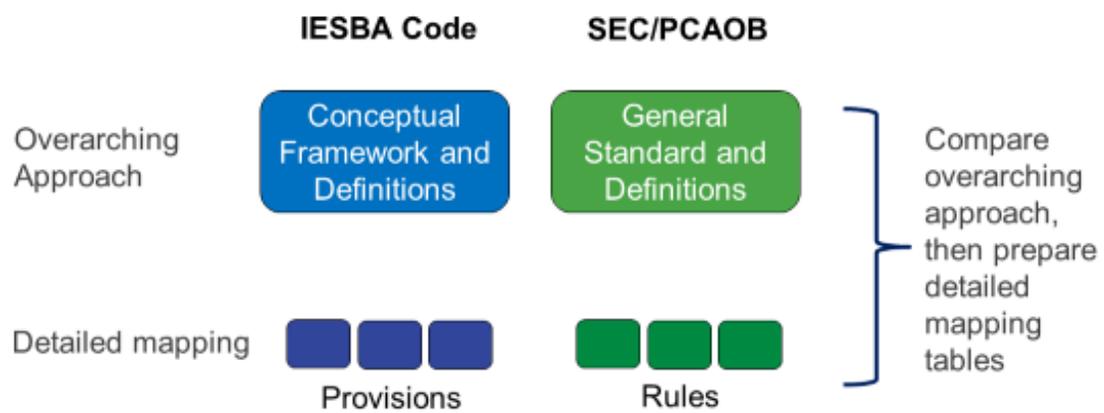
Breach of Independence by Component Auditor (CA)

Codification of process being contemplated:



Benchmarking

Benchmarking



Timeline



Other matters

Other matters



Technology



Long association post
implementation review

Jurisdictional provision
questionnaire





Compliance audits

An update on task force activities and request for feedback on preliminary conclusions and future considerations.

Compliance audits background

Compliance audits are engagements performed under the auditing standards. Examples of compliance audits include both Single audits (NPO/SLG) and program specific audits. Federal government commonly requests compliance audits to monitor compliance with laws, regulations and contractual terms and conditions.

- How do the independence requirements be applied in a compliance audit for various types of entities?
 - Which entities require independence?
 - Does the affiliate interpretation apply?
- Is a compliance audit a financial statement attest client?
- Is guidance needed to assist practitioners?

Preliminary conclusion #1

Compliance audit engagements are financial state attest engagements.

- Independence is required with respect to the attest client.
- The attest client includes any entity (for example, a department within a state and local government or a subsidiary in a consolidated group of companies) that reports amounts in the financial statement.
- See Illustration 1.

Nonauthoritative guidance is needed.

3

Illustration 1

Schedule of Expenditures of Federal Awards			
Grant	Federal Expenditures	Entity	Major program
Cluster:			
Program 1	\$ 50,000.00	Department B	
Program 2	700,000.00	Department A	
Program 3	5,000.00	Department A	
Total Cluster	755,000.00		No
Program 4	1,000,000.00	Department C	Yes
Program 5	2,500,000.00	Department D	Yes
Program 6	12.00	Department E	No
...	
Program 999	200,000.00	Department F	No
Total Federal Expenditures	\$ 980,495,000.00		

4

Conclusion 1 - Questions for the committee

1. Are there any questions or concerns related to the task force's conclusion of who is the attest client and the need for additional nonauthoritative guidance?
2. Is the committee in favor of the task force exploring the possibility of a change in the code that would allow relief from the independence requirements as they relate to entities reporting trivial or inconsequential amounts on the financial statement that is associated with a compliance audit?

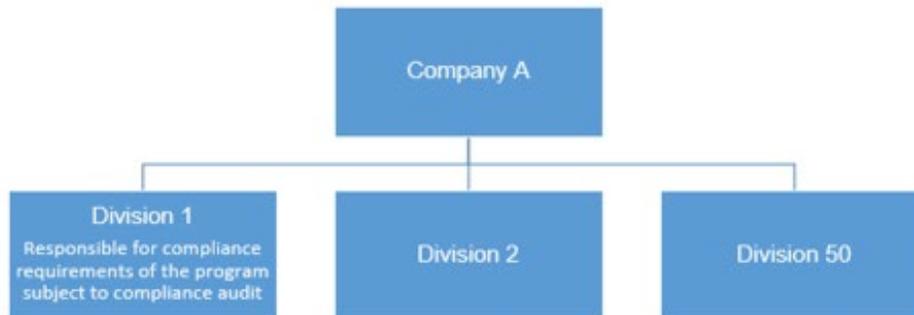
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Conclusion 1 - Questions for the committee (continued)

3. For attest clients outside of a state and local government environment, does the committee believe that the attest client could be an "entity" that is less than the legal entity when the member is only performing a compliance audit for that "entity"? If so, does the committee believe that this should be clarified in the code or in nonauthoritative guidance? See Illustration 2.

6

Illustration 2



7

Preliminary conclusion #2

Independence may need to be evaluated for other entities not included on the financial statement.

- There may be other entities that do not report amounts on the financial statement but are subject to the compliance audit.
- Threats to independence as a result of circumstances or relationships with those entities should be evaluated under the conceptual framework.

Nonauthoritative guidance is needed.

8

Conclusion 2 - Question for the committee

4. Are there any questions or concerns related to the task force's conclusion and the need for additional nonauthoritative guidance?

9

Preliminary conclusion #3

The "Client Affiliates" interpretation applies to financial statement attest clients outside of the state and local government environment.

- Based on an entity's governance structure and control, application of the "Client Affiliates" interpretation may be appropriate in some circumstances but not in others.

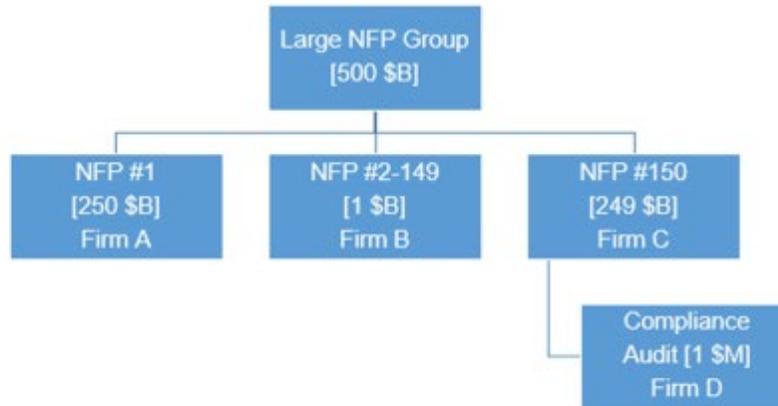
Nonauthoritative guidance is needed.

The task force should explore whether there could be exceptions to the "Client Affiliates" interpretation for compliance audits.

- See Illustration 3

10

Illustration 3



11

Conclusion 3 - Questions for the committee

5. Are there any questions or concerns related to the task force's conclusion related to affiliates (outside of the state and local government environment)?
6. What are the committee's views on whether the task force should explore circumstances that could support exceptions to the "Client Affiliates" interpretation for compliance audits?

12

Preliminary conclusion #4

Inadvertent breaches of independence are likely.

- Due to the nature of compliance audits, inadvertent breaches of independence will likely occur.

The task force should explore application guidance of the "Breach of an Independence Interpretation."

13

Conclusion 4 - Question for the committee

7. Does the committee have any concerns with the task force expanding its charge to explore application guidance of the "Breach of an Independence Interpretation" to particular circumstances in a compliance audit?

14



Preliminary conclusion #5

The "State and Local Government Client Affiliates" interpretation may apply to compliance audits.

- The "State and Local Government Client Affiliates" interpretation was not intended to apply to compliance audits, but this clarification is missing from the code.

The task force should consider whether these engagements should be subject to this interpretation.

16

Conclusion 5 - Question for the committee

8. Does the committee have any questions or concerns related to the task force's consideration of the "State and Local Government Client Affiliates" interpretation?

16





Thank you

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