Professional Ethics Executive Committee

Open meeting agenda

May 4–5, 2021

Virtual

Open meeting agenda — May 4–5, 2021

Professional Ethics Division

Professional Ethics Executive Committee

Phone access: +1 301 715 8592 (US toll) or +1 312 626 6799 (US toll) **Meeting ID:** 999 6683 8179 **| Web access:** https://aicpa.zoom.us/j/99966838179 **International numbers available:** https://aicpa.zoom.us/u/abxLdakcZw **Observers must register:** www.aicpa.org/PEECmeeting		
May 4		
10:00–10:05 EST	**Welcome** Mr. Lynch will welcome the committee members and discuss administrative matters.	
10:05–11:35	**SEC convergence** The task force will seek approval to expose revisions to the Loan interpretation, the Loans and Leases from Lending Institutions interpretation, and to the Client Affiliates interpretation.	Agenda items 1A–1G
11:35–12:05	**Client affiliates** The task force will seek approval to expose revisions to the definition of affiliate.	Agenda items 2A–2C
12:05–12:40	*Break before afternoon session*	
12:40–1:00	**Information systems services** The task force will provide the committee with an overview of the practice aid and seek input on the proposed direction.	Agenda item 3
1:00–1:45	**Compliance audits** The task force will provide the committee with an overview of its preliminary conclusions.	Agenda item 4

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1:45–1:55	**Assisting clients with implementing accounting standards** The task force will report on its kickoff meeting.	
1:55–2:10	**Confidentiality and data security** The working group will report on its kickoff meeting.	
2:10–2:25	**IESBA update** The committee will receive an update on IESBA's March 2021 meeting.	Agenda items 5A–5B
2:25–2:30	**Statements on Standards for Tax Services** The committee will receive an update on recent activities of the SSTS task force.	
May 5		
10:00–10:45 EST	**Definition of office** The task force will seek input on the proposed Q&A.	Agenda items 6A–6B
10:45–11:30	**Staff augmentation** The task force will seek input on the proposed Qs & As.	Agenda items 7A–7B
11:30–11:40	**Member enrichment update** The committee will receive an update on ongoing member enrichment projects not discussed elsewhere in the agenda.	
11:40–11:45	**Approval of February 2021 meeting minutes**	Agenda item 8

	Future meeting dates August 17–18, 2021 November 16–17, 2021	

Agenda item 1A

SEC convergence

Task force members

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

Observers

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

AICPA staff

Ellen Goria

Task force charge

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

Reason for agenda item

The task force is seeking approval to expose revisions to these interpretations, as presented in agenda items 1C–1D:

- Immediate Family Members
- Loans
- Loans and Leases From Lending Institutions
- Client Affiliates

Task force activities

Loans

During the February PEEC meeting, the committee expressed general support of the task force's direction on the loan revisions, proposed a clarifying edit and asked the task force to consider clarifying the following:

- Which mortgages are intended to be included in the home mortgage exception?
- The $10,000 cap on outstanding consumer loans means that the balances on consumer loans from any one lender must be aggregated.

  For example, when purchasing furniture on credit from one entity and cell phones on credit from another entity, if the lender used to finance these two purchases is the same, the member must aggregate the balances.

- Which parties are included in the loan exception provision of the "Client Affiliates" interpretation?

Loans included in the home mortgage exception

The task force chair explained during the February PEEC meeting that staff did not believe the AICPA's home mortgage exception was intended to be limited to primary residence mortgages.[1]

In addition to asking the task force to consider clarifying this through nonauthoritative guidance, the committee revised the subheading in the interpretation to emphasize that a home mortgage is just another type of secured loan.

To address the committee's request for nonauthoritative guidance to clarify that the home mortgage exception is not limited to primary residences, the task force worked with staff to develop the Q&A in agenda item 1B.

Cap on consumer loans

The committee asked the task force to clarify that the $10,000 cap on outstanding consumer loans means that the balances on consumer loans from any one lender must be aggregated.

For example, when purchasing furniture on credit from one entity and cell phones on credit from another entity, if the lender used to finance these two purchases is the same, the member must aggregate the balances.

To address the committee's concern, the task force revised item (*d*) of paragraph .05 of the "Loans and Leases with Lending Institutions" interpretation as shown in blue highlight. These revisions also align more closely to the SEC's language about keeping the loan balance under $10k on a current basis taking into consideration the payment's due date.

> 05. ~~Aggregate outstanding balances from C~~***c*onsumer loans *(for example,*** credit card***s, retail installment loans and home improvement loans)*** and overdraft reserve accounts ***from the same lending institution*** that have a***n 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.

Loan exception provision of the "Client Affiliates" interpretation

The committee asked the task force to clarify the parties who are included in the loan exception provision of the "Client Affiliates" interpretation.

To address the committee's concern, the task force used bullets to clarify the groups covered.

> a. ***During the period of the professional engagement a*** ~~A~~ covered member may

[1] The proposed limited scope in the July 9, 1991 exposure draft was not adopted.

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].~~

Other revisions identified during the review of the loan materials

While addressing the committee's concerns from the February meeting, the task force made some clarifying edits to the loan proposals included in agenda item 1C:

- Clarify in paragraph .03 of the "Immediate Family Member" interpretation that when materiality is identified as a factor that an immediate family member should consider as possibly affecting independence, this may be a factor for loans, as well as financial interests.
- Add a cross reference to paragraph .01 in the "Loans" interpretation to the exception for loans in the "Client Affiliates" interpretation.
- Add a cross reference to paragraph .07 in the "Loans and Leases from Lending Institutions" interpretation to the "Leases" interpretation

Client mergers and acquisitions

Sometimes members encounter situations in which a new affiliate relationship is created because a financial statement attest client or affiliate is involved in an acquisition or other business combination and the member has an interest or relationship with the new affiliate that would impair independence.

The AICPA, the SEC and IESBA all have guidance that provides some relief for these situations. Agenda items 1E, 1F, and 1G, respectively, present this guidance.

The SEC adopted its guidance in October 2020 and that guidance provides a transition framework to address inadvertent independence violations where the independence violation arises as a result of a corporate event, such as a merger or acquisition, and the services or relationships that are the basis for the violation would not have run afoul of the applicable independence standards prior to the corporate event.

Under this framework, relief is provided in the following circumstances:

a. The auditor is in compliance with any independence standards that are applicable to the entities involved in the transaction from the origination of the relationships or services in question and throughout the period in which the applicable independence standards apply.

b. The potential independence impairing service or relationship is addressed before the effective date of the merger or acquisition, unless doing so would cause significant disruption to the audit client.

   If it would cause the audit client significant disruption, the transition framework allows for some *limited* flexibility by requiring it be addressed promptly after the effective date.

   Although specific guidance is not included in the adopted rule regarding what “promptly” means, the discussion in the release makes it clear that the SEC envisions a timeline that does not linger and should not exceed six months.

   The release makes it clear that the six months is not intended to be used as a default timeframe.

c. That the firm’s quality control system has procedures and controls that require the firm be timely notified about the audit client’s merger and acquisition activity and upon notification, allows the firm to identify, before the effective date, services or relationships that could result in independence violations.

d. The discussion in the release (not the rule) explains that if the auditor encounters a service or relationship that would threaten its objectivity and impartiality, the auditor should not defer to the framework.

The SEC’s transition framework goes beyond the AICPA code in that the AICPA’s relief covers only situations in which

- an existing financial statement attest client is acquired,
- the member or member’s firm will not continue providing financial statement attest services to such client, and
- certain other conditions are met.

Though the SEC's transition framework goes beyond the AICPA code, it is a framework whereas IESBA's standard provides more detailed guidance.

To allow for consistent practice globally, the task force's proposal in agenda item 1D is closely aligned to the IESBA guidance and integrates the underlying components of the SEC's transition framework.

The task force's proposal is organized into the following categories. See subsequent paragraphs for more detail:

- An existing financial statement attest client is acquired, and the member or member's firm will not continue providing financial statement attest services to this client.
- An existing financial statement attest client or affiliate is involved in an acquisition or other business combination resulting in a new affiliate, and the member or member's firm expects to continue providing financial statement attest services to this client.
- An existing financial statement attest client is involved in an acquisition or other business combination and the member or member's firm will complete the existing engagement but will not continue providing financial statement attest services to this client after the date on which the attest report for the current financial statement attest engagement is issued.
- Other considerations when an existing financial statement attest client is involved in an acquisition or other business combination.

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

This category covers situations in which a new affiliate relationship is created because a financial statement attest client is acquired by another entity during the period of the professional engagement and the member or member's firm has an interest or relationship with that new affiliate (acquirer) that will impair independence.

This category stipulates that the interest or relationship does not need to be ended and independence will be maintained only if the ongoing financial statement attest service relates to periods prior to the effective date and the member or member's firm will not provide financial statement attest services for an attest period that is after the effective date.

The task force believes this category is consistent with the extant AICPA position and proposes the revisions to paragraph .05 in agenda item 1D to enhance readability.

An existing financial statement attest client or affiliate is involved in an acquisition or other business combination resulting in a new affiliate, and the member or member's firm expects to continue providing financial statement attest services to such client

This category covers situations in which a new affiliate relationship is created because a financial statement attest client is involved in an acquisition or other business combination and the member or member's firm has an interest or relationship with that new affiliate that will impair independence.

This new affiliate relationship could be one in which the financial statement attest client itself is involved (e.g., it acquires a new subsidiary) or one of its existing affiliates is involved (e.g., the parent of the financial statement attest client acquires a new material subsidiary and the financial statement attest client is also material to the parent).

Unlike the prior category in which the member or member's firm will not continue to provide attest services, in this category the member or member's firm will continue to provide financial statement attest services after the effective date.

Under the proposal, the member or member's firm will be permitted to delay ending the interest or relationship until after the effective date while continuing the financial statement attest engagement (without impairing independence) provided the interest or relationship *cannot reasonably be ended* by the effective date and other conditions are satisfied.

These conditions include items such as

- evaluating the threat created by the interest or relationship,
- discussing the situation with those charged with governance (TCWG) including any planned transitional measures the member or member's firm will take,
- ending the interest or relationship as soon as reasonably possible (but no later than six months after the effective date),
- and keeping individuals involved with the interest or relationship off of the attest engagement and not responsible for an engagement quality control review.

Paragraphs .06–.09 in agenda item 1D outline the requirements for members to use this provision.

The task force believes the proposal is substantially equivalent to IESBA's guidance. The only difference is that the proposal *does not* include, as application guidance, IESBA's examples of transitional measures that a member or member's firm might apply.

This application guidance was not included because the examples are too prescriptive and could be impractical, especially for smaller firms.

Following are the main formatting and editorial differences between the proposal and the IESBA guidance. The proposal

- aligns application guidance with the requirements as opposed to adding them to separate paragraphs after the requirement.

  This allows for the overall interpretation to be streamlined and the application guidance to be read in conjunction with its related requirement.

- uses the broader phrase “acquisition or other business combination” instead of referring to the transaction as a merger or acquisition.
- replaces certain IESBA terminology (such as, related entity, audit, auditor, firm, nonassurance) with equivalent AICPA terminology.
- introduces the term “new affiliate” to enhance readability.

An existing financial statement attest client is involved in an acquisition or other business combination and the member or member’s firm will complete the existing engagement but will not continue providing financial statement attest services to such client after the date on which the attest report for the current financial statement attest engagement is issued

This category covers situations in which a new affiliate relationship is created because a financial statement attest client is involved in an acquisition or other business combination and the member or member’s firm has an interest or relationship with the new affiliate that would impair independence but after the ongoing attest engagement is complete, will cease providing attest services.

It differs from the first category described above because the financial statement attest services could involve periods after the effective date or the financial statement attest client is the acquirer.

It differs from the second category because the member will not continue to provide financial statement attest services and the situation does not involve existing affiliates’ acquisitions or other business combinations.

In this category, because the member or member’s firm will no longer provide attest services after the issuance of the current attest report, the interest or relationship will not need to end

- if a significant amount of attest work was completed prior to the effective date,
- the remaining work can be completed shortly after the effective date, and
- other criteria are met, including
  - evaluating the threat created by the interest or relationship,
  - discussing the situation with TCWG including any planned transitional measures

the member or member's firm will take, and

- keeping individuals involved with the interest or relationship off of the attest engagement.

The task force believes the proposal is substantially equivalent to IESBA's guidance. The only difference is that the proposal does not require the member or member's firm to end the relationship as soon as reasonably possible.

The task force did not include this requirement in the proposal because the member or member's firm will not continue to provide attest services and will be completing the engagement shortly after the effective date.

Other considerations when an existing financial statement attest client is involved in an acquisition or other business combination

This subsection discusses matters that are appliable to all the categories above.

Paragraphs .11 and .13 are in the AICPA extant guidance and the task force continues to believe they are important considerations. The recommendation to consider documenting the situation in paragraph .12 is new to the AICPA code.

The IESBA code requires members to document the situation as outlined in paragraph .12, but the task force is recommending only that the member consider documenting, because PEEC does not usually require documentation in the independence interpretations.

Questions for the committee:

1. Does the committee approve the proposals in agenda items 1C and 1D for exposure?
2. Does the committee believe 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* or does the committee believe the proposals should have a deferred effective date?
3. Does the committee have any suggestions on staff's Q&A to clarify that the home mortgage exception is not intended to be limited to primary residences?

Action needed

The committee is asked to approve the proposals in agenda items 1C and 1D for exposure and to decide what effective date would be appropriate.

Communications plan

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

Materials presented

- Agenda item 1B: Proposed Q&A related to the “Loans and Leases With Lending Institutions” interpretation
- Agenda item 1C: Affected interpretations for the loan revisions
- Agenda item 1D: Proposed revised “Client Affiliates” interpretation
- Agenda item 1E: Extant “Client Affiliates” interpretation
- Agenda item 1F: SEC standard
- Agenda item 1G: IESBA standard

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Agenda item 1B

Proposed Q&A related to the "Loans and Leases With Lending Institutions interpretation"

Loans included in the home mortgage exception of the "Loans and Leases With Lending Institutions" interpretation

Question: The "Loans and Leases with Lending Institutions" interpretation (ET 1.260.020) permits a covered member and that member's immediate family to have a home mortgage from an attest client when all specified safeguards are met. Does this provision apply to other loans collateralized by the borrower's primary or other residence?

Answer: Yes. The home mortgage loans covered by paragraphs .02 and .03 of the interpretation apply to all loans collateralized by a borrower's primary residence (for example, a home equity line of credit) or non-primary residence (for example, a secondary or vacation home).

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Agenda item 1C

Affected interpretations for the loan revisions

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

1.270.010 Immediate Family Members (excerpt)

.03 When materiality of a financial interest ***or a loan are*** ~~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.

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."

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, t~~*T*hreats 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~~ loan**s** ~~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~~ loan***s were*** ~~was~~ obtained

   i. from the lending institution prior to it~~s~~ 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.

c. After becoming a covered member, any ~~home mortgage, secured loan, or immaterial unsecured~~ loan**s** must be kept current regarding all terms***,*** at all times, and the terms may not change in any manner not provided for in the original agreement. Examples of changed terms are a new or extended maturity date, a new interest rate or formula, revised collateral, and revised or waived covenants.

d. The estimated fair value of the collateral for ~~a~~ home mortgage***s*** or other secured loan***s*** ~~must~~ ***should*** equal or exceed the outstanding balance during the term of the home mortgage***s*** or other secured loan***s***. If the estimated fair value of the collateral is less than the outstanding balance of the home mortgage***s*** or other secured loan***s***, 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 card***, retail installment loans, and home improvement loans)*** and overdraft reserve accounts ***from the same lending institution*** that have a***n 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].

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Agenda item 1D

Proposed revised "Client Affiliates" interpretation

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

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]

Acquisitions and other business combinations that involve a financial statement attest client or its affiliates

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

~~.05The 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.~~

.05 ~~.06Independence 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 financial statement attest client is acquired during the period of professional engagement by another entity, the acquirer.

b. The attest engagement covers only periods prior to the effective date of the acquisition or other business combination.

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 an attest period that is after the effective date of the acquisition or other business combination.

~~07Notwithstanding 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.~~

~~.08A 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 affiliate is involved in an acquisition or other business combination resulting in a new affiliate, and the member or member's firm expects to continue providing financial statement attest services to such client

.06 An entity may become a new affiliate of an existing financial statement attest client

because of an acquisition or other business combination. A threat to independence and, therefore, to the ability of a member to continue a financial statement attest engagement might be created by previous or current interests or relationships between a member or member's firm and the new affiliate. Paragraphs .07–.13 are applicable when an acquisition or other business combination creates a new affiliate for a financial statement attest client during the period of professional engagement and the member or member's firm will continue to provide financial statement attest services to the financial statement attest client.

.07 The following are applicable when the circumstances in paragraph .06 exist:

- ***a. The member or member's firm should identify and evaluate previous and current interests and relationships with the new affiliate that, taking into account any actions taken to address the threat, might affect its independence and therefore its ability to continue the financial statement attest engagement after the effective date of the acquisition or other business combination.***

- ***b. Except as provided for in paragraph .08, the member or member's firm should take steps to end any interests or relationships with the new affiliate that would impair independence by the effective date of the acquisition or other business combination.***

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

- ***a. Evaluate the threat that is created by the interest or relationship. Factors that are relevant in evaluating the level of a threat created by the acquisition or other business combination 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 or parent)***

  - ***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 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 or relationship with the new affiliate will end as soon as reasonably possible but no later than six months after the effective date of the acquisition or other business combination.

b. Any individual who has such an interest 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 is involved in an acquisition or other business combination and the member or member's firm will complete the existing engagement but will not continue providing financial statement attest services to such client after the date on which the attest report for the current financial statement attest engagement is issued

.10 The member or member's firm might have completed a significant amount of work on the financial statement attest engagement prior to the effective date of the acquisition or other business combination and might be able to complete the remaining financial statement attest procedures within a short period of time. In such circumstances, if those charged with governance request the member or member's firm complete the financial statement attest engagement while continuing with an interest or relationship identified in paragraph .08, the member or member's firm shall only do so if the following criteria are met:

a. The member or member's firm has evaluated the level of the threat and discussed the results with those charged with governance.

b. The member or member's firm complies with the requirements of paragraph .09 b and c.

c. The member or member's firm ceases to be the auditor no later than the date that the audit report is issued.

Other considerations when an existing financial statement attest client is involved in an acquisition or other business combination

Objectivity

.11 Even if all the requirements of paragraphs .05– .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 .05, .08 or .10.

Documentation

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

- ***a. Any interests or relationships identified in paragraphs .06 or .10 that will not be ended by the effective date of the acquisition or other business combination and the reasons they will not be ended***
- ***b. The transitional measures applied***
- ***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 ~~.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.

Extant “Client Affiliates” interpretation

This interpretation is effective as of May 2021.

1.224.010 Client Affiliates (excerpt)

.01 …

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.

[See Revision History Table.]

SEC standard

The following is an excerpt of the SEC transition framework, extracted from https://www.sec.gov/rules/proposed/2019/33-10738.pdf

(e) *Transition provisions for mergers and acquisitions involving audit clients*. An accounting firm's independence will not be impaired because an audit client engages in a merger or acquisition that gives rise to a relationship or service that is inconsistent with this rule, provided that:

(i) The accounting firm is in compliance with the applicable independence standards related to the services or relationships when the services or relationships originated and throughout the period in which the applicable independence standards apply;

(ii) The accounting firm's lack of independence under this rule has been or will be corrected as promptly as possible under relevant circumstances as a result of the occurrence of the merger or acquisition;

(iii) The accounting firm has in place a quality control system as described in Rule 2-01(d)(3) that has the following features:

(A) Procedures and controls that monitor the audit client's merger and acquisition activity to provide timely notice of a merger or acquisition; and

(B) Procedures and controls that allow for prompt identification of potential violations after initial notification of a potential merger or acquisition that may trigger independence violations, but before the transaction has occurred.

IESBA standard

Following is the IESBA standard related to threats created during a client merger. It is extracted from the September 2019 version of the IESBA code with a January 2020 copyright ©.

When a Client Merger Creates a Threat

400.70 A1 An entity might become a related entity of an audit client because of a merger or acquisition. A threat to independence and, therefore, to the ability of a firm to continue an audit engagement might be created by previous or current interests or relationships between a firm or network firm and such a related entity.

R400.71 In the circumstances set out in paragraph 400.70 A1,

(a) The firm shall identify and evaluate previous and current interests and relationships with the related entity that, taking into account any actions taken to address the threat, might affect its independence and therefore its ability to continue the audit engagement after the effective date of the merger or acquisition; and

(b) Subject to paragraph R400.72, the firm shall take steps to end any interests or relationships that are not permitted by the Code by the effective date of the merger or acquisition.

R400.72 As an exception to paragraph R400.71(b), if the interest or relationship cannot reasonably be ended by the effective date of the merger or acquisition, the firm shall:

(a) Evaluate the threat that is created by the interest or relationship; and

(b) Discuss with those charged with governance the reasons why the interest or relationship cannot reasonably be ended by the effective date and the evaluation of the level of the threat.

400.72 A1 In some circumstances, it might not be reasonably possible to end an interest or relationship creating a threat by the effective date of the merger or acquisition. This might be because the firm provides a non-assurance service to the related entity, which the entity is not able to transition in an orderly manner to another provider by that date.

400.72 A2 Factors that are relevant in evaluating the level of a threat created by mergers and acquisitions when there are interests and relationships that cannot reasonably be ended include:

- The nature and significance of the interest or relationship.
- The nature and significance of the related entity relationship (for example, whether the related entity is a subsidiary or parent).
- The length of time until the interest or relationship can reasonably be ended.

R400.73 If, following the discussion set out in paragraph R400.72(b), those charged with governance request the firm to continue as the auditor, the firm shall do so only if:

(a) The interest or relationship will be ended as soon as reasonably possible but no later than six months after the effective date of the merger or acquisition;

(b) Any individual who has such an interest or relationship, including one that has arisen through performing a non-assurance service that would not be permitted by Section 600 and its subsections, will not be a member of the engagement team for the audit or the individual responsible for the engagement quality control review; and

(c) Transitional measures will be applied, as necessary, and discussed with those charged with governance.

400.73 A1 Examples of such transitional measures include:

- Having a professional accountant review the audit or non-assurance work as appropriate.
- Having a professional accountant, who is not a member of the firm expressing the opinion on the financial statements, perform a review that is equivalent to an engagement quality control review.
- Engaging another firm to evaluate the results of the non-assurance service or having another firm re-perform the non-assurance service to the extent necessary to enable the other firm to take responsibility for the service.

R400.74 The firm might have completed a significant amount of work on the audit prior to the effective date of the merger or acquisition and might be able to complete the remaining audit procedures within a short period of time. In such circumstances, if those charged with governance request the firm to complete the audit while continuing with an interest or relationship identified in paragraph 400.70 A1, the firm shall only do so if it:

(a) Has evaluated the level of the threat and discussed the results with those charged with governance;

(b) Complies with the requirements of paragraph R400.73(a) to (c); and

(c) Ceases to be the auditor no later than the date that the audit report is issued.

If Objectivity Remains Compromised

R400.75 Even if all the requirements of paragraphs R400.71 to R400.74 could be met, the firm shall determine whether the circumstances identified in paragraph 400.70 A1 create a threat that cannot be addressed such that objectivity would be compromised. If so, the firm shall cease to be the auditor.

Documentation

R400.76 The firm shall document:

(a) Any interests or relationships identified in paragraph 400.70 A1 that will not be ended by the effective date of the merger or acquisition and the reasons why they will not be ended;

(b) The transitional measures applied;

(c) The results of the discussion with those charged with governance; and

(d) The reasons why the previous and current interests and relationships do not create a threat such that objectivity would be compromised.

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Agenda item 2A

Client affiliates

Task force members

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

Observers

David Bibb, Liz McKneely, Lori West

AICPA Staff

Ellen Goria, John Wiley

Task force charge

To determine whether current client affiliates guidance should apply to individuals and whether there are any other aspects of the client affiliate interpretation that need clarification (e.g., pooled employee benefit plans, SEC merger and acquisition guidance).

Reason for agenda item

The task force is seeking approval to expose revisions to the definition of an affiliate as outlined in agenda item 2B.

Background

Definition of affiliate

The definition of an "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.

Strategy and work plan direction for client affiliates

The November 2019 PEEC Strategy and Work Plan consultation paper sought feedback on

- how firms currently apply guidance related to the affiliate definition in a situation in which entities are owned by the same individual and
- what additional guidance related to client affiliates, if any, would be helpful.

Most of the commenters supported this project, recommending clarification of the definition of an "affiliate." Analysis of the consultation paper feedback indicates there is inconsistency in the application of current guidance.

PEEC created this task force to determine whether the guidance should apply to individuals and whether there are other aspects of the definition of "affiliate" or the "Client Affiliate" interpretation

that need clarification.

In the initial development of the affiliate definition in 2010, the task force focused on converging with the IESBA's and SEC's related entity/client affiliate guidance. Neither of these standards explicitly extended guidance to common ownership by individuals so PEEC limited its proposed definition to common ownership by entities.

When responding to hotline inquires involving individuals, staff typically applies the definition of affiliate by analogy. Task force members do the same when addressing situations within their firms. Here are some of the common fact patterns:

- A firm has an audit client that is owned by a family and that business is material to the family. The family approaches the firm to perform personal bill pay services for them. The bills that would be paid are all personal and are not related to the business. The personal bill pay services are not subject to the general requirements so the firm's independence would be impaired with respect to the family.

  However, if the firm treats the family as an entity under the affiliate definition (i.e., entity that can control the audit client), then consideration of the self-review threat could mitigate the independence issue: If it is reasonable to conclude that the bill pay services do not create a self-review threat with respect to the audit client because the results of the bill pay services will not be subject to audit procedures, independence will not be impaired.

- An individual owns and controls many different businesses that are attest clients of the firm. The individual is active as a board member and serves as an officer in those businesses. The individual has a company (non-attest client) that is material to the individual and the firm loans staff to this company.

  Because the individual has control over the attest clients, the firm considers the individual, by analogy, an upstream affiliate for those attest clients that are material to the individual.

  In addition, the businesses under common control that are material to the individual would be treated as sister affiliates.

  Because there is an exception in the client affiliates guidance that allows staff augmentation services for sister affiliates when threats are at an acceptable level, the firm believes that the loaned staff services are allowable without impairing independence of the other attest clients.

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 question and answer 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.

The task force recommends that the revisions to the definition in agenda item 2B be exposed for comment and that the exposure draft ask commenters the following:

- Are there any unintended consequences caused by the proposal and if so, how should the proposal be revised to address these consequences?
- Does the proposed effective date provide enough time for members to address any relationships that would be prohibited under the revised definition? If not, what would an appropriate period be and why?

Effective date

The task force did not discuss a proposed effective date. Staff believes a delayed effective date is necessary because this revision could result in firms having to re-evaluate all of their attest client financial statement affiliate relationships.

Another option the committee could consider is requiring that the new provisions be applied prospectively to all new attest clients after the effective date.

Questions for the committee:

1. Does the committee agree that the affiliate definition should be revised to address its application to individuals?
2. Are there any unintended consequences caused by the proposal and if so, how should the proposal be revised to address these consequences?
3. What are the committee's thoughts on a proposed delayed effective date?

Staff recommendation — Multiple employer employee benefit plans

If the committee agrees to issue an exposure draft to revise the definition of affiliate for individuals, staff recommends the exposure draft include a clarification for multiple employer employee benefit plans (MEP). This recommendation came after the task force's most recent meeting and the task force *has no*t discussed it.

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 recommends that item (*i*) in the definition of an affiliate 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:

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

Since this revision was not discussed with the task force, staff has not included it in agenda item 2C.

Action needed

The committee is asked to approve exposing the revised definition of affiliate 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 interpretation “Client Affiliates”

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Agenda item 2B

Definitions of affiliate, significant influence, and control

Proposed additions appear in ***boldface italic***. 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 interpretation “Client Affiliates”

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. 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 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]

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.

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Agenda item 3

Information system services

Task force members

Anna Dourdourekas (chair), Cathy Allen, Danielle Cheek, John Ford, Katie Jaeb, Nancy Miller, Dan O'Daly

Observers

Kimberly M. Kuhl, SanDee Priser

AICPA staff

Liese Faircloth, Ellen Goria, Iryna Klepcha

Task force charge

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

Reason for agenda item

This agenda item will supplement the verbal update on the task force’s activities and provides a project summary.

Task force activities

The task force met three times since the last committee meeting to discuss the structure of the practice aid. This agenda item provides an outline 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:

Step 1: Determine whether a member’s firm meets the requirements of the "Nonattest Services" subtopic [1.295] of the “Independence Rule”.

> This step addresses the requirements of the “Nonattest Services” subtopic (e.g., management responsibilities, a designated individual who possesses suitable skills, knowledge and/or experience, documentation requirements).

Step 2: Determine whether independence will be impaired when the services a member provides to an attest client relate to a financial or nonfinancial system that is already in operation.

> This step addresses post-implementation services and provides factors to consider in determining whether the attest client will outsource an ongoing function, process or

activity to a member that would result in the member assuming a management responsibility (e.g., degree to which the attest client relies on a member, scope and scale of services)

Step 3: Determine whether the services provided meet the exception for tools.

This step assists members in determining whether a tool is not a financial information system (FIS); that is, it performs only discrete calculations that the attest client can understand and can evaluate, and the attest client accepts responsibility for the input and assumptions.

Step 4: Determine whether the services are related to a FIS.

This step assists members in determining whether the services are related to a FIS based on the definitions in the interpretation and provides factors to consider or examples to assist in making that determination.

Step 5: Determine whether independence will be impaired when a member provides an attest client with design, development, or implementation services that are not related to a FIS.

If a member designs, develops, or provides implementation services to an attest client that do not relate to a FIS, this step directs members to consider whether the calculation performed by the tool or system is a permitted service.

Step 6: Determine whether the services that relate to an attest client's FIS would impair independence.

This step assists members in determining whether independence will be impaired if a member provides design, development, or implementation services related to a FIS, and provides factors to consider or examples to assist in making that determination.

Questions for committee

1. What are the common issues firms expect to encounter in applying the new guidance?
2. Does the committee have any feedback on the task force's proposed approach?

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Agenda item 4

Compliance audits

Task force members

Nancy Miller (chair), Ian Benjamin, George Dietz, Anna Dourdourekas, John Good, Staci Henshaw, Kelly Hunter, Lee Klumpp, Flo Ostrum, Lewis Sharpstone, Brittney Williams

Observers

Ralph DeAcetis, Barbra Jicha, Stephanie Sauer-Watts

AICPA staff

Ellen Goria, Jennifer Kappler, Melissa Powell, Michael Schertzinger

Task force charge

To consider how the independence requirements for compliance audits performed under the Statements on Standards for Auditing Services (SASs) should be applied and whether those independence requirements should differ in the following circumstances.

A compliance audit only is performed versus a compliance audit performed in conjunction with the audit of the financial statements of the same attest client. Within this circumstance, consider the following:

- The compliance audit includes reporting on a financial statement (for example, a schedule of expenditures of federal awards or comparable schedule).
- The compliance audit does not include reporting on a financial statement (for example, a compliance audit of a proprietary school required by the U.S. Department of Education Office of Inspector General's *Guide For Audits of Proprietary Schools and For Compliance Attestation Engagements of Third-Party Services Administering Title IV Programs*).

Reason for agenda item

To update the committee on the task force's preliminary conclusions and to solicit feedback on those conclusions as well as possible future considerations to be deliberated by the task force.

Task force activities

The task force met three times since the last committee meeting to discuss how independence applies in compliance audits performed under the SASs when only a compliance audit is performed (and not the audit of the GAAP financial statements for the same attest client) and includes reporting on a financial statement (for example, a schedule of expenditures of federal awards or comparable schedule).

A key component in evaluating how to apply the independence requirements will be to determine

- what entity should be considered the attest client in the compliance audit,
- who should be considered the covered member, and
- whether guidance should differ when there is a single program subject to the compliance audit versus multiple programs.

The task force believes nonauthoritative guidance is needed, but if during deliberations, it becomes apparent that a modification to the AICPA Code of Professional Conduct (code) may be needed, the task force will bring the proposed modification back to the full committee.

Summary of issues

Compliance audit engagements are financial statement attest engagements. Independence is required with respect to the attest client. The attest client includes any entity that reports amounts in the financial statement.

All entities reporting amounts in the financial statement (for example, schedule of expenditures of federal awards or comparable schedule) will be subject to the compliance audit that includes reporting on the financial statement. As a result, those entities should be considered attest clients under the code. This does not seem to be consistently applied in practice. Therefore, the task force recommends developing additional guidance to assist practitioners in applying the code.

As an example for state and local government entities, using the schedule of expenditures of federal awards (SEFA) in illustration 1 in this agenda item, each of the departments of the entity on the SEFA (departments A–F) would be considered an attest client under the code.

Therefore, because the auditor provides an opinion on the SEFA as a whole, independence requirements apply to each of those departments as an attest client, regardless of whether the programs were considered “major programs” in the compliance audit.

Similarly, for other attest clients, a practitioner may be performing a compliance audit for a consolidated group of entities that includes reporting on a number of programs (comparable to the SEFA in illustration 1, except instead of departments, there may be subsidiaries). The same concept applies in that the entities that report amounts on the SEFA would be the attest clients.

This understanding does not seem to be consistently applied in practice. Some practitioners may be applying independence only to entities that are considered a “major program” and may also be taking an engagement team approach to applying independence rather than a covered persons approach.

The committee is asked to modify the task force charge to allow consideration of whether it would be reasonable to make an exception to the independence requirements for entities that report amounts in the financial statement that are trivial or clearly inconsequential.

Using the SEFA in illustration 1, the task force would consider whether significant threats may exist for the practitioner with respect to Department E, who reports federal expenditures of $12 for one program on the schedule when there are 998 other programs and a total of $980 million federal expenditures on the schedule.

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**		

In looking at entities outside of the state and local government environment (for example, commercial entities, not-for-profits), the task force considered instances in which a compliance audit is required and the subject of the compliance audit primarily relates to one department or division within a legal entity.

Illustration 2 provides an example of a trivial or inconsequential division within a large publicly traded company (the legal entity) that receives and manages funding related to one federal program and requires a program-specific audit.

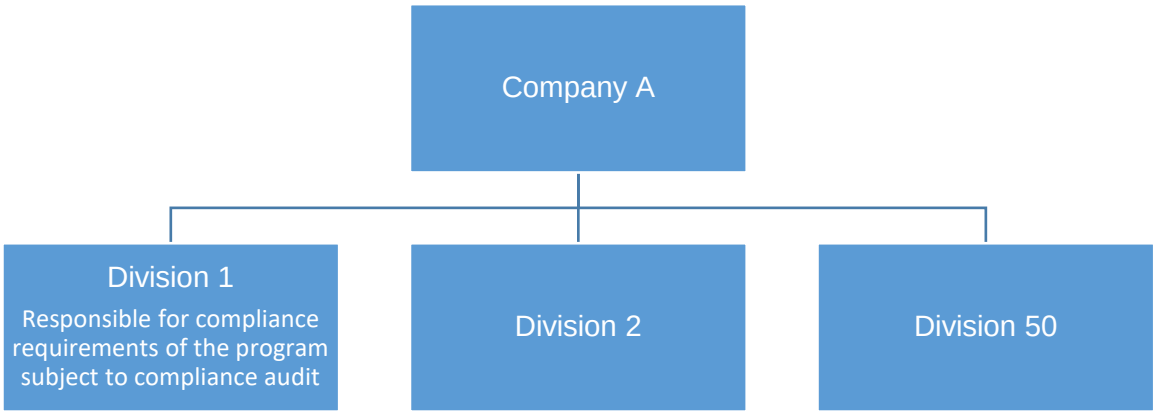
The task force considered whether the attest client could be the division rather than the overall company itself. The answer likely depends on the company's governance and control structure, but the task force also considered whether threats to a practitioner's integrity and objectivity

would be significant if the practitioner owned shares in the company when the division and funding subject to the compliance audit is clearly inconsequential to the overall company.

The code does not provide clear guidance on whether an attest client has to be a legal entity or whether it could be a division or a department, depending on facts and circumstances.

As it relates to these considerations, the committee is asked for feedback on whether the attest client can be considered something other than a legal entity. Based on this feedback, the task force will consider the need for additional guidance.

Illustration 2



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?
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?

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.

Neither the code nor nonauthoritative guidance clearly addresses how practitioners should evaluate these situations. The task force recommends developing additional nonauthoritative guidance to assist practitioners in such situations.

For example, a central procurement department of a state and local government processes contracts for all departments within the state and local government. Although the procurement department does not have amounts reported on the financial statement associated with the compliance audit, the procurement department's processes and controls may be subject to the compliance audit.

Therefore, circumstances or relationships (such as employment relationships or nonattest services) that may exist related to the procurement department should be evaluated under the conceptual framework.

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?

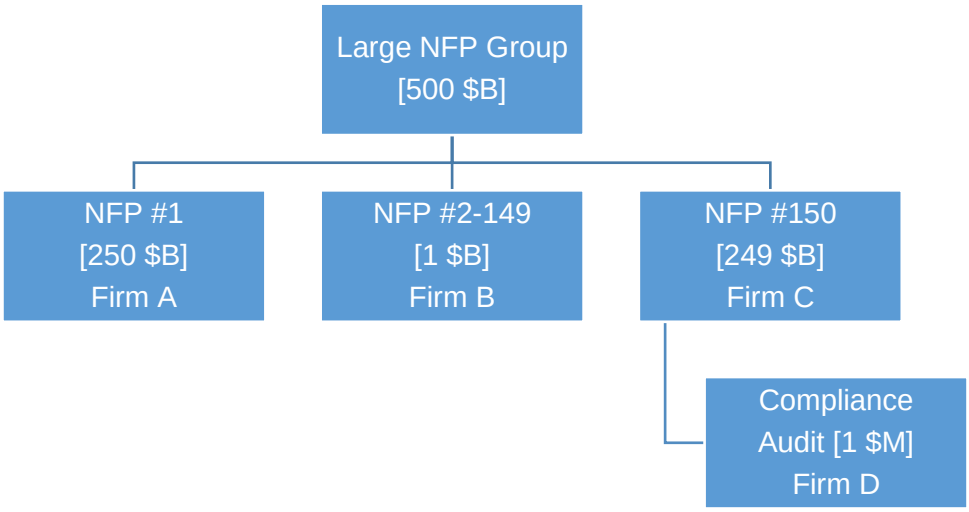
The "Client Affiliates" interpretation applies to financial statement attest clients outside of the state and local government environment.

When the compliance audit includes reporting on a financial statement (for example, a schedule of expenditures of federal awards or comparable schedule), the attest client is considered a financial statement attest client, and therefore, the "Client Affiliates" interpretation would apply.

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. The committee is asked for feedback on whether circumstances in which the "Client Affiliates" interpretation should not apply should be explored.

For example, in illustration 3, Large NFP Group controls NFP #1 and NFP #150 and each is material to the Large NFP Group, therefore under the "Client Affiliates" interpretation, NFP #1 and NFP #150 are affiliates of each other. Should Firm D (performing the compliance audit only for NFP #150) always be required to be independent of NFP #1?

Illustration 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?

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

The task force would like to explore how the interpretation "Breach of an Independence Interpretation" (ET sec. 1.298.010) would apply to inadvertent breaches of independence in a compliance audit.

For example, it is not uncommon for an entity to receive funding that must be reported in the financial statement when such funding has not been received in prior years and may not be received in subsequent years, such as a FEMA award for a natural disaster. Practitioners may identify a new attest client as a result of new funding during the period of the professional engagement. A circumstance or relationship may already exist that would cause the firm's independence to be impaired (for example, the partner's spouse is in a key position with respect to an entity that manages a FEMA award that is subject to the compliance audit).

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?

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

Though compliance audits are intended to be carved out of the “State and Local Government Client Affiliates” interpretation, that language is not included in the interpretation. Depending on the conclusions reached by this task force and the committee’s consideration of those conclusions, the task force may need to address whether these engagements should be subject to the interpretation.

This interpretation requires consideration of all entities required to be included in the reporting entity’s financial statement in determining whether those entities are affiliates. Considering the task force’s preliminary conclusions on who is the attest client in a compliance audit as well as the understanding that the financial statement included in a compliance audit is not the reporting entity’s financial statement as described in that interpretation, application of the interpretation to compliance audits may not be practical.

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?

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 5B: Engagement team
- Agenda item 5C: IESBA tax planning and related services

Engagement team

Project description

The IAASB changed the definition of engagement team in ISA 220 for quality management purposes 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 in the context of a group audit.

The purpose of this project is to ensure that International Independence Standards (IIS) provide clear and consistent guidance with respect to 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 engagement partner take responsibility for obtaining a confirmation from component auditors that ethical requirements have been fulfilled relevant to 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 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

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)

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.

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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). This would be the PIE provisions, where the component is a PIE, or more frequently, the non-PIE provisions if the component is not a PIE in its own right.

Status

At its March 2021 meeting, IESBA's Engagement Team — Group Audits Independence Task Force reported that a few other matters still need consideration, including the following:

- How the independence principles should apply at the service provider level
- The reconciliation of the concept of "related entity" as used in the IESBA code based on a legal structure with the revised definition of component as conceptualized in proposed ISA 600 (Revised) and the implication for the independence provisions
- Recent changes to the code (effective December 2022) in the context of group audits

For additional background, refer to the preliminary recommendations presented at IESBA's October 2020 meeting as well as the updates presented at the December 2020 meeting.

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 the respective definition that individuals who can directly influence the outcome of the engagement, include those who are engaged by the firm and then 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*** quality ***reviews*** ~~control~~ for the audit engagement, including those who perform the engagement quality ~~control~~

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.

review ~~for the engagement~~; and

- Assurance team (b)(iii): Those who ~~provide~~ ***perform*** quality ***reviews*** ~~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*** quality ***reviews*** ~~control~~ for the engagement, including those who perform the engagement quality ~~control~~ review ~~for the engagement~~; and

…

Definition of engagement team and team recommendations

The task force continues to recommend revising the extant definition of engagement team to align with the definition of engagement team per International Standard on Quality Management (ISQM) 1. The task force continues to recommend including additional guidance to clarify the nature of the various teams in reference to the different parts of the code.

As of March 2021, the task force recommends the definition of engagement team be revised as follows. The yellow highlighted text reflects the changes made since the December 2020 meeting.

> 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 expert~~s 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 provide***s*** direct assistance on an ~~audit~~ engagement ~~when the external auditor complies with the requirements of ISA 610 (Revised 2013), *Using the Work of Internal Auditors*~~. ***In Part 4A, the term "engagement team" refers to individuals performing ~~the~~ audit or review procedures on the audit or review engagement, respectively. In Part 4B, the term "engagement team" refers to individuals performing ~~the~~ assurance procedures on the assurance engagement***. ***ISA 220 (Revised) provides ~~For~~ further guidance on the definition of engagement team in the context of an audit of financial statements~~, see ISA 220 (Revised) issued by International Auditing and Assurance standards Board~~.***

During the March 2021 meeting, IESBA encouraged the task force 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.

Individual independence

There was no update on this during IESBA's March 2021 meeting.

During the 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 component[5] 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 a preliminary direction (IESBA's term is "strawman") for a new Group Audits section 405. The preliminary direction 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.

Firm independence

IESBA did not receive an update during its March 2021 meeting.

During the 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 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

5 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."

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.

During IESBA's December 2020 meeting, the task force presented a strawman for a new Group Audits section 405. The strawman 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 strawman also required the group engagement partner 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 strawman 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.

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 to the March 2021 meeting. Appendix 2 in the agenda material 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 in the agenda material explains the task force's preliminary approach for dealing with a breach of independence at a component auditor firm.

The task force received feedback that included 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.
- Breach of a component auditor should not automatically impair the group auditor's independence.

Convergence considerations

Staff's initial assessment of the definition of an attest engagement team in the AICPA code seems to be drafted broadly enough to include these:

- EQRs, as the definition states in part that the attest engagement team are "Those individuals participating in the *attest engagement*, including those who perform concurring and ***engagement quality reviews***." (Emphasis added)
- Component auditors, as the definition states in part that "The attest engagement team includes all employees and ***contractors retained by the firm who participate in the attest engagement,*** regardless of their functional classification (for example, audit, tax, or management consulting services)." (Emphasis added)

Because draft text has not been provided for the preliminary conclusions related to individual

and firm independence or breaches, AICPA Professional Ethics Division staff has not performed an initial assessment.

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Agenda item 5C

IESBA tax planning and related services

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 February 2021 meeting, the IESBA's Tax Planning and Related Services Working Group (TPWG) reported on its fact finding and preliminary observations. The TPWG reported that it plans to explore the merit of developing a principles-based decision-making framework to guide professional accountants in identifying indicators of what is deemed acceptable or unacceptable tax planning. The TPWG intends to brief IESBA on its preliminary recommendations during the June 2021 meeting.

Preliminary observation: terminology

The TPWG reported that there does not appear to be a clear line between tax planning and aggressive tax planning and so it would be difficult to adequately define *aggressive tax planning* on a global scale.

The TPWG reported that an important goal of the project is to raise awareness. As such, they will explore the notion of unacceptable tax planning practices and behavior and delineate indicators of unacceptable tax planning by professional accountants versus aggressive tax planning.

To do this, the TPWG will explore the merit of a principles-based decision-making framework to guide professional accountants in their tax planning activities and assist them in identifying what would be deemed acceptable or unacceptable tax planning behavior.

As part of this further analysis, the TPWG will also consider how rigor could be built into such a framework, such as through documentation of the professional accountant's judgments in making decisions or reaching conclusions. The TPWG noted it will also give some consideration to how culture may influence what is acceptable in a given jurisdiction as perceptions may be completely different across borders.

Following is some of IESBA's feedback provided to the working group during its March 2021 meeting:

- A clearer distinction between "black" and what is "gray" is necessary, so the TPWG should focus on the grayer areas. It will be helpful to link the guidance to the provisions of the code that address responding to NOCLAR and recently released role and mindset

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provisions. This will help emphasize the importance of professional accountants' responsibility to act in both the public interest and the organizational culture.

- While the TPWG has moved away from the term "aggressive tax planning," there is a question about whether the same challenges will arise in attempting to define or describe what would be considered "unacceptable tax planning," given that views will vary around the world.
- Perceptions of what is acceptable or unacceptable tax planning practice will vary depending on tax laws and policies as well as the jurisdictional economic framework. The evolving context also may affect perceptions. For example, in the COVID-19 pandemic, some policies or actions that would not be considered acceptable pre-pandemic are now viewed as acceptable.
- As an ethics standard setter, IESBA should reflect on where opportunities to codify expected behaviors regarding tax planning beyond compliance with tax laws and regulations. Equally, there may also be opportunity to develop nonauthoritative material on the topic.
- Though identifying the appropriate terminology may not be a straightforward exercise, it would nevertheless be important for IESBA to coalesce around some specific terms based on criteria.
- The shift in terminology from "aggressive" to "unacceptable" tax planning is worth exploring further as there is at least some commonality of perceptions in several jurisdictions.
- If going down the path of acceptable versus unacceptable tax planning, it might be worth reflecting on factors that might guide the professional accountant's judgments or feature within a "reason to believe" framework. Also, it might be useful to consider the "intent" model in the inducements provisions of the IESBA code.
- The importance of education and raising awareness concerning the issues should not be underplayed.
- Consideration should be given to the fact that some tax professionals in several jurisdictions are not subject to the code.
- Focus should be on senior level professionals as they are the ones involved with providing tax planning advice.

Preliminary observation: transparency and accountability

The TPWG observed that the frameworks used by international policy makers include considerations of transparency and accountability. For example, the EU Council adopted new rules to increase transparency to deter aggressive cross-border tax planning practices and the Global Reporting Initiative, a sustainability standard setter, issued its first global standard for

public reporting on tax, where global businesses are called to use a framework to provide detailed public information about their tax practices.

The TPWG's shared three options for how they could proceed:

- Option A: Develop overarching material in the code that will assist professional accountants in complying with the fundamental principles and applying the conceptual framework. The TPWG considered the suitability of this material addressing the ethical considerations relating to tax planning activities.
- Option B: Develop material under one or more specific fundamental principles, such as objectivity and professional competence and due care, to explain the expected behavior of a professional accountant in performing tax planning activities.

  With respect to developing material for one or more fundamental principles, the TPWG is of the initial view that such an approach would contradict stakeholders' views and its own view that the expected behavior of professional accountants performing tax services is the same for all professional accountants across the five fundamental principles in an interrelated manner.

- Option C: Develop material outside the code (such as staff Qs & As or case studies) on the types and magnitude of the threats that are created when professional accountants perform tax planning activities. The TPWG has heard from stakeholders who recommended this approach, cautioned against adding more material to the code, and suggested guidance would be more beneficial.

IESBA's feedback to the working group during the March 2021 meeting on these three approaches included the following:

- Consider how to coordinate with the technology work stream as it is also considering the issues of transparency and accountability.
- Pursue option C, especially in support of practitioners. However, consideration should be given to the nature and type of nonauthoritative guidance to develop beyond the already issued IFAC tax guide.
- Consider pursuing both options A and C together.
- Be sure to consider the implications of the issues for professional accountants in business and professional accountants in public practice.

Convergence considerations

AICPA Professional Ethics Division staff has not performed a preliminary assessment given the early stages of the workstream.

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Agenda item 6A

Definition of office

Task force members

Kelly Hunter (chair), Catherine Allen, Thomas Campbell, Anna Dourdourekas, Bella Rivshin, Peggy Ullmann

Observers

Girish Kirpalani, Julie Lau, and Liz McKneely

AICPA staff

Ellen Goria, Michael Schertzinger

Task force charge

To provide members with non-authoritative guidance on how to apply the definition of office in a virtual work environment.

Reason for agenda item

The task force is seeking input from the committee on their recommendation to issue a question and answer (Q&A).

Background

Definition of covered member

In 2001 as part of the Independence Modernization Project, PEEC developed the definition of a covered member. This definition identified individuals who should be required to remain independent of attest clients because relationships between attest clients and those individuals and entities generally pose the greatest threat to independence. One category of individuals included in the definition of covered member is as follows:

> A partner or partner equivalent *in the office* (emphasis added) in which the lead attest engagement partner or partner equivalent primarily practices in connection with the attest engagement.

The white paper issued in connection with the 2001 Independence Modernization Project explained that these individuals may appear to affect attest engagements because of their *physical proximity* to lead engagement partners, which gives them a greater opportunity to have regular professional interaction with those partners.

Strategy and work plan direction for definition of office

The November 2019 PEEC Strategy and Work Plan consultation paper noted that PEEC was considering undertaking a standard-setting project connected to the definition of office. Given changes in working environments over the past 20 years, the committee considered updating

the definition of office because the definition is used to determine, in part, which partners or partner equivalents are covered members and, therefore, need to remain independent of certain attest clients.

Those who commented on the consultation paper expressed a common concern: Is it appropriate to use the definition of office to determine who should be considered a covered member given that the common understanding of “office” is a physical location rather than personnel interactions and assigned reporting channels?

Current definition of office

The current definition of office in the AICPA Code of Professional Conduct (code) does convey that substance should govern the office classification and personnel interactions and that assigned reporting channels may be more important than physical location. The definition reads as follows (0.400.36):

> A reasonably distinct subgroup within a firm, whether constituted by formal organization or informal practice, in which personnel who make up the subgroup generally serve the same group of clients or work on the same categories of matters. Substance should govern the office classification. For example, the expected regular personnel interactions and assigned reporting channels of an individual may well be more important than an individual’s physical location. [Prior reference: paragraph .26 of ET section 92]

Given how broadly drafted the extant definition is, rather than forming a task force for a new standard-setting project the committee agreed to undertake a member enrichment project to determine if the definition of an office needs further clarification.

Task force activities

The task force met three times since February. The task force believes the current definition of an office is broadly defined enough to cover working in both a physical and virtual environment. The task force recommends the Q&A in agenda item 6B be issued to provide guidance on how to address independence when a partner or partner equivalent in the office has a relationship with an attest client that would impair independence. The task force believes this Q&A can be applied whether working in a physical or virtual work environment.

Question for the committee

1. Does the committee have any input on the proposed Q&A?

Materials presented

Agenda item 6B: Proposed Q&A related to the definition of office

Text of proposed nonauthoritative Q&A related to the definition of office

Addressing an independence impairing issue created by office classification

Question: If a firm had a potentially independence-impairing issue with a partner or partner equivalent in a particular office or distinct subgroup, would moving the partner or partner equivalent to a different office or distinct subgroup address the potential independence impairment?

Answer: Yes, as long as the partner or partner equivalent is not otherwise be considered a covered member, such as an individual in a position to influence the attest engagement.

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Agenda item 7A

Staff augmentation

Task force members

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

AICPA Staff

Ellen Goria, John Wiley

Task force charge

To 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 task force is seeking input on their recommendation to issue the two Qs & As in agenda item 7B.

Questions for the committee

1. Does the committee believe a staff augmentation arrangement will generally require the member or member's firm to perform some level of planning and supervision?
2. Does the committee have any input on the proposed Qs & As?

Materials presented

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

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Agenda item 7B

Proposed Qs & As related to staff augmentation arrangements

Staff augmentation versus nonattest services engagement

Question: What is the key difference between a staff augmentation (that is, loaned staff) arrangement with a client and a typical nonattest service engagement?

Answer: The key difference is that in a staff augmentation arrangement, the client agrees to be responsible for the direction and supervision of the activities performed by the member's or member's firm's staff. In the typical nonattest services engagement, the member or member's firm is solely responsible for the direction and supervision of the staff's activities.

[Because the client agrees to be responsible for the direction and supervision of the staff's activities, a staff augmentation arrangement will generally require the member or member's firm to perform less planning and supervision than when providing typical nonattest services].

Another difference is that a typical nonattest services engagement generally results in the issuance of a work product (that is, deliverable) 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 unexpected situations

Question: The "Staff Augmentation Arrangements" interpretation (ET sec. 1.275.007) under the "Independence Rule" [1.200.001] requires specific safeguards be met, including the following (emphasis added):

- The staff augmentation arrangement is being performed due to an *unexpected situation* that would create a significant hardship for the attest client to make other arrangements.
- The augmented staff arrangement is not expected to *reoccur*.

What constitutes an "unexpected situation" and if such a situation does reoccur, is the member prohibited from providing another staff augmentation arrangement?

Answer: An unexpected situation is an event or set of circumstances that the *attest client* did not plan for and did not foresee. 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.

Members should use professional judgment in determining whether *not* loaning staff in the unexpected situation will create significant hardship for the attest client.

In making this determination, the member may need to weigh factors such as the urgency of the need against the length of time it would take the client to make alternative arrangements.

The unexpected situation that gives rise to the staff augmentation arrangement should be of a nature that the member and *attest client* reasonably expect will not need to occur again.

However, if another unexpected situation does arise and the client would experience significant hardship in making other arrangements, the member needs to evaluate the facts and circumstances to determine whether to loan staff again. In performing this evaluation, the member should consider factors such as these:

- The length of time that has passed since the previous staff augmentation arrangement
- Whether the situation giving rise to the need for augmented staff arrangement 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
- What other options the client has
- Whether the member should have reasonably expected that the client would need the staff augmentation arrangement again

Agenda item 8

Open meeting minutes – February 9, 2021

Professional Ethics Division
Professional Ethics Executive Committee

The Professional Ethics Executive Committee (PEEC or committee) held a duly called meeting on February 9, 2021. The virtual meeting convened at 10:00 a.m. and adjourned at 3:25 p.m.

We sent agenda materials for this meeting to PEEC members and observers on January 22, 2021 and posted them to aicpa.org.

Contents

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

AICPA Professional Ethics Division staff

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

Guests

See exhibit 1 in the appendix of this document.

Key votes in this meeting

Motions approved

- Re-exposure of proposed interpretations "Responding to Noncompliance With Laws and Regulations"
- Adoption of new interpretation "Staff Augmentation Arrangements" and related revisions with effective date of November 30, 2021
- Adoption of revised interpretation "Records Requests"

Welcome

Mr. Lynch welcomed the committee and discussed administrative matters.

NOCLAR

Mr. Denham updated PEEC on the task force's activities since the November meeting (agenda item 1A) and requested PEEC's approval to re-expose the proposed interpretations "Responding to Noncompliance With Laws and Regulations" (NOCLAR; agenda item 1B).

Items of note include the following:

- Update on Auditing Standards Board (ASB) activities and revisions for NOCLAR to AU-C section 210
- Revisions to the 2017 PEEC NOCLAR exposure draft

To review these in detail, please see agenda item 1A in the February meeting agenda.

Discussion

Exposure period

PEEC's and the ASB's exposure drafts will be issued at the same time and will have the same comment period.

PEEC and ASB representatives discussed the comment period with an eye toward ensuring that state boards will have enough time to consider the implications of the new guidance.

PEEC and the ASB agreed that the comment period will end June 30, 2021.

Effective date

PEEC's proposed effective date for its interpretations is one year after the final interpretations are published in the *Journal of Accountancy*. ASB's proposed effective date is December 15, 2022.

A committee member raised concerns about the effective date of ASB's proposal and

preparations auditors will need to make if the standard is adopted.

The ASB believes impediments to adoption are not great enough to warrant a change in the effective date of their standard, which is December 15, 2022. However, the exposure draft has a question about whether the exposure period is appropriate, so there is a potential for change.

Exclusion of certain nonattest services

The committee agreed to remove the phrase "and subject to" from paragraph .06*b* of the interpretation for members in public practice.

The concern was that the phrase limits the exception to only engagements covered by the Statement on Standards for Forensic Services No. 1.

> A litigation or investigation engagement as defined in, and subject to, the AICPA's Statement on Standards for Forensic Services No. 1.

The paragraph was revised as follows:

> A litigation or investigation engagement as defined in the AICPA's Statement on Standards for Forensic Services No. 1.

Explanation of noncompliance in paragraph .09

The committee agreed to eliminate the examples of action that could cause substantial harm from paragraph .09 of the interpretation for members in public practice because these examples (i.e., perpetration of a fraud resulting in significant financial losses to investors and breaches of environmental laws and regulations endangering the health or safety of employees or the public) are better suited for member enrichment materials than for inclusion in the code.

Appropriate source of information

A question arose about whether complying with the last sentence in paragraph .20 of agenda item 1B could be construed as providing legal advice. The committee retained the phrase because this sentence doesn't impose a requirement on the member, rather only suggests the member provide the attest client with appropriate sources of information so the client can understand legal or regulatory responsibilities related to the NOCLAR.

Outreach to members in business

A committee member noted the need for outreach to members in business as this interpretation will affect them if it is adopted.

Vote

The committee voted unanimously with no abstentions to release the revised exposure draft *Proposed interpretations and definition "Responding to Noncompliance With Laws and Regulations*."

The comment period ends June 30, 2021.

Staff augmentation

Ms. Snyder updated PEEC on the task force's activities since the December meeting (agenda item 2A) and requested approval to adopt the new interpretation "Staff Augmentation Arrangements" (agenda item 2D) and related revisions to other interpretations (agenda items 2E–2H).

Items of note include the comment letter summary (agenda item 2B) and analysis (agenda item 2C).

Discussion and questions for the committee

Following are the questions from agenda item 2A the task force posed to the committee as well as answers.

Does the committee agree with the task force's recommendations as outlined in agenda item 2A?

In discussion of this question, a committee member representing the National Association of State Boards of Accountancy (NASBA) noted that NASBA's comments on proposed language were not accepted and asked whether the task force would consider addressing some of these issues in future Qs & As.

Ms. Snyder affirmed that the task force would consider this. The committee raised no other concerns.

Does the committee still believe that staff augmentation arrangements should be permitted in any circumstances?

The committee raised no concerns on this point.

Does the committee still believe that staff augmentation arrangements should be permitted in certain circumstances?

The committee raised no concerns on this point and indicated agreement.

Should additional nonauthoritative guidance be considered for significant hardship, unexpected situation, not expected to reoccur, and nonattest services that have minimal oversight?

A NASBA representative noted a fact pattern NASBA submitted that the committee might find helpful in drafting Qs & As and added that the 30-day requirement could also be addressed as a Q&A.

The committee raised no other concerns on this point.

Does the committee believe that the term “rebuttable presumption of 30 days” is still appropriate based on feedback received?
Committee members noted two concerns:

- NASBA has concerns about slippage. Members may see “rebuttable presumption” and extend arrangements beyond 30 days. This doesn’t seem to align with PEEC’s intent in the exposure draft. That is, a stricter limit should be in place.
- With NASBA’s concerns about language (noted in the previous list item) and the GAO concerns about the subject nature of the safeguards, challenges could be experienced with getting more state boards to adopt the AICPA code.

The task force chair noted that given the robust safeguards (i.e., expected not to exceed 30 days, unexpected hardships, and significant hardships) required to perform staff augmentation services, the service is essentially prohibited unless it is truly in the public interest to provide that service.

The committee raised no other issues on this point.

Does the committee agree with the recommendation of the task force on proposed exceptions for certain affiliates?
The committee raised no concerns on this question.

Does the committee agree with the task force that the proposed exception for engagements under the Statements on Standards for Attestation Engagements (SSAE) other than agreed upon procedures (AUP) engagements should not be allowed?
Committee members noted the following during the discussion of this question:

- If the service does not relate to the subject matter of the AUP engagement, it makes sense to allow the AUP exception to other SSAE engagements where the self-review threat can be controlled.
- Others believed that for SSAE engagements other than AUPs, there is a higher level of independence required, so the self-review threat becomes more prominent.

There was discussion of the simultaneous employment threat, and the committee concluded that threat would not be any different between the different level of assurance services offered.

The task force chair noted that though some commenters supported the exception for SSAE engagements other than AUPs, other commenters and a couple of task force members believed that conceptually there are opinions being provided, and in some cases this is equivalent to an audit, so they believed the self-review threat for that level of assurance was too high.

The committee raised no other concerns with this.

Does the committee agree that the exception for AUP engagements should still be allowed?

The committee raised no concerns on this point.

Does the committee believe that six months is a long enough delayed effective date?

The committee raised no concerns on this point.

Votes

The committee voted unanimously with no abstentions to adopt the new interpretation "Staff Augmentation Arrangements" and related revisions to the following interpretations:

- Client Affiliates
- Agreed-Upon Procedure Engagements Performed in Accordance with SSAEs
- Scope and Applicability of Nonattest Services

The committee also voted unanimously with no abstentions on an effective date of November 30, 2021.

The new interpretation and revisions to existing interpretations will be live in the online code with the March 2021 update and notice will appear in the May 2021 issue of the *Journal of Accountancy*.

Records requests

Ms. Ullman updated PEEC on the task force's activities since the November meeting (agenda item 3A) and requested approval to adopt the revised interpretation "Records Requests" (agenda item 3C) and input on four related Qs & As (agenda item 3E).

Discussion and questions for the committee

Does the committee have any concerns with staff issuing the Qs & As related to records requests?

Following are points for clarification raised by the committee as well as answers:

- With regard to returning client documents in a different format, if the member no longer has the original papers, can copies be provided from the member's portal?

  The task force did not address this in the Qs & As but believes that any usable format is acceptable.

- With regard to returning client documents to a client who has moved from the member's local area, a concern was raised about the phrase "by any means necessary" being too strong.

  To address this concern the committee agreed to change the language to "using

reasonable means."

Does the committee believe the member should have an obligation to provide records to divorcing or divorced spouses?

Committee members discussed the following:

- What if a spouse requests records several years later, even after the records retention date? Are members now in a position that they need to provide every tax return twice?
- Given that PEEC is aligning AICPA requirements to the IRS circular 230, what if circular 230 changes in the future? Is there an issue then?

After discussion, a committee member pointed out that the concerns expressed have more to do with risk management and therefore should not be addressed in the code as ethical considerations.

Does the committee agree with the edits to the interpretation from what was presented in November?

A committee member requested that "if applicable to" be added before "beneficiary" in the final sentence of paragraph .07.

There were no other substantive revisions. The committee agreed with the edits and the 60-day delayed effective date.

Vote

The committee voted unanimously with no abstentions to adopt the revised interpretation "Records Requests."

The revisions will be live in the online code with the March 2021 update and notice will appear in the May 2021 issue of the *Journal of Accountancy*.

The revisions will be effective July 31, 2020.

SEC convergence

Ms. Kary updated the committee on the task force's activities since the November meeting (agenda item 4A). The committee had no concerns with the task force's proposed charge. The committee expressed general support of the task force's direction on the loan revisions outlined in agenda item 4B, proposed a clarifying edit and asked the task force to consider clarifying the following:

- What mortgages are intended to be included in the home mortgage exception.
- That the $10,000 cap on outstanding consumer loans means that the balances on consumer loans from any one lender must be aggregated. For example, if purchasing

furniture on credit from one entity and cell phones on credit from another entity, if the lender used to finance these two purchases is the same, the member must aggregate the balances.

- Who the parties are in the loan exception provision of the “Client Affiliates” interpretation

The task force will address these concerns and also present its recommendations to address the SEC’s revisions related to mergers and acquisitions in May.

Compliance audit

Ms. Miller updated the committee on the task force’s activities since the December meeting. Details are in exhibit 2 in the appendix of this document.

The committee had no discussion and expressed no concerns with the task force charge (slide 4 of exhibit 2).

IFAC convergence

Ms. Brack updated the committee on the task force’s activities since the December meeting.

In its January meeting, the task force concluded that the AICPA code is substantially converged with IFAC on role and mindset. The task force did not propose revisions for PEEC to consider.

The task force does think that the concept of an inquiring mind and bias application guidance that were included in the pronouncement would be useful to include in certain nonauthoritative guidance published by the AICPA.

Staff and the task force will work on these changes and bring them to PEEC for final approval.

Details are in exhibit 3 in the appendix of this document.

IESBA update

Ms. Goria updated the committee on the task force’s activities since the December meeting (agenda item 5A):

- IESBA issued its public interest entity (PIE) exposure draft and division staff is in the process of analyzing it.

  The main takeaway is that auditors of public interest entities or PIEs are subject to more robust independence standards and in order to be a PIE there has to be significant public interest in the financial condition of the entity.

  The proposal provides broad categories of entities that IESBA believes should be considered by local jurisdictions as PIEs but will allow jurisdictions to refine these categories.

- IESBA adopted their nonassurance services (agenda item 5B) and the fees (agenda item 5C) projects at their December meeting and division staff is waiting for the final standards and basis documents before proceeding with convergence projects.
- The purpose of the engagement team project is to ensure that the international independence standards provide clear and consistent guidance on independence for
    - 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); and
    - the firms that these component auditors are in (i.e., firm independence requirements).

At IESBA's December meeting, the task force presented their revised recommendations. These are outlined in agenda item 5D.

Details are in exhibit 4 in the appendix of this document.

Statements on Standards for Tax Services

Ms. Saunders updated the committee on the task force's activities since the December meeting.

The task force is still working to get input from various committees before the draft of the revised standards goes to the general membership for comment. It is anticipated that these meetings and information gathering will continue until May.

The task force will update PEEC again at the May meeting and expects to issue the exposure draft by the end of 2021.

Approval of November and December meeting minutes

The committee voted to approve the minutes of the November and the December meetings.

Appendix

Exhibit 1: Guests in attendance at the February 2021 meeting

	Name	Company
1.	Barbara Andrews,	AICPA, Director – Forensics, Technology and Management Consulting
2.	Teresa Bordeaux	AICPA, Senior Manager – Governmental Auditing and Accounting
3.	Mike Glynn	AICPA, Senior Manager – Audit and Attest Standards
4.	Henry Grzes	AICPA, Lead Manager, Tax Practice and Ethics
5.	Carl Peterson	AICPA, Vice President, Small Firms – PA
6.	Kent A. Absec	Idaho State Board of Accountancy
7.	Sonia Araujo	PwC
8.	Coalter Baker	Baker and Cockburn, PLLC CPAs
9.	Paul Balas	State of Michigan Board of Accountancy
10.	Rita Barnard	Kansas Society of CPAs
11.	Ian Benjamin	Chair–AICPA Enforcement Subcommittee
12.	Claire Blanton	RSM US LLP
13.	Tammie Brown	U.S. Department of Health and Human Service
14.	D. Boyd Busby	Alabama State Board of Public Accountancy
15.	David Kirklan Cloniger	RSM US LLP
16.	Allan Cohen	RSM US LLP
17.	Giles T. Cohen	PwC

18.	Harry Cohen	KPMG
19.	Colleen Conrad	NASBA
20.	Karen Cookson	U.S. Department of Housing and Urban Development
21.	Debbie Cutler	Debra A. Cutler CPA PC
22.	James Dalkin	U.S. Government Accountability Office
23.	George Dietz	PwC
24.	Anna Durst	Nevada Society of CPAs
25.	Dan Dustin	NASBA
26.	Jason Evans	BDO
27.	Sarah Ference	CNA Insurance
28.	Lea Fletcher	KPMG
29.	Wendy Garvin	Tennessee State Board of Accountancy
30.	Harrison E. Greene, Jr.	Federal Deposit Insurance Corporation
31.	Andrew Gripp	Crowe LLP
32.	Elliot Hendler	Elliot Hendler, CPA
33.	Annette Hill	Anderson ZurMuehlen & Co.
34.	Pamela Ives Hill	Missouri Society of CPAs
35.	Kelly Hnatt	External Counsel
36.	Becca Huber	New York State Society of CPAs
37.	Frank Jakosz	CapinCrouse LLP
38.	Nigel James	U.S. Securities and Exchange Commission

39.	Karen Jones	PwC
40.	Kristi Justice	West Virginia Board of Accountancy
41.	Vassilios Karapano	U.S. Securities and Exchange Commission
42.	Elizabeth Knipscheer	Arkansas Society of CPAs
43.	Kimberly Kuhl	KPMG
44.	Tricia LaValle	AICPA Enforcement Subcommittee
45.	Elliot Lesser	Berdon LLP– Retired
46.	Jasdeep Mangat	U.S. Securities and Exchange Commission
47.	William Mann	Mayer Hoffman McCann P.C.
48.	Elizabeth McKneely	Deloitte
49.	Sherri McPherson	Oregon Society of CPAs
50.	Kathleen Meyer	Missouri Society of CPAs
51.	Nancy Miller	KPMG
52.	Angela Miratsky	BKD, LLP
53.	Karen Moncrieff	EY
54.	Christina Moser	Plante Moran
55.	Jessica Mytrohovich	Georgia Society of CPAs
56.	Jan Neal	Deloitte
57.	Jennifer Noble	RSM LLP
58.	Donna Oklok	Accountancy Board of Ohio

59.	Jay Perry	Deloitte
60.	Christine Piche'	CliftonLarsonAllen
61.	Victoria Pitkin	New York State Society of CPAs
62.	Rachel Reardon	Michigan Association of CPAs
63.	J. Michael Reese	The Hanover Insurance Group
64.	Mark Reynolds	Creative Value Consulting LLC
65.	John Robinson	RSM US LLP
66.	Deborah Rood	CNA Insurance
67.	Kathy Savage	Deloitte
68.	April Sherman	CliftonLarsonAllen
69.	Byron Shinn	Carr, Riggs & Ingram, LLC
70.	Rachel Sinks	CliftonLarsonAllen
71.	Ola Marie Smith	State of Michigan
72.	Susan Speirs	Utah Association of CPAs
73.	Annette Stalker	Stalker Forensics
74.	Marc Stepper	Washington Society of CPAs
75.	John M Szczomak	New Jersey Society of CPAs
76.	Joseph Tapajna	University of Notre Dame
77.	Jessica Tomc	EY
78.	Paula Tookey	Deloitte
79.	Stephen Valenti	Steven Valenti, CPA

80.	Shelly Van Dyne	BDO
81.	Sharron Waugh	Tennessee State Board of Accountancy
82.	Jim West	BDO
83.	Les Williford	BDO
84.	Paula Young	EisnerAmper, LLP
85.	Darlene Zibart	Kentucky Society of CPAs
86.	Paul Ziga	Georgia State Board of Accountancy

AICPA

Compliance Audit Task Force

An update on task force activities and request for approval of the task force's charge

1

Update on task force activities

January 15, 2021 meeting:

- Finalized draft of charge
- Began assessing application in an example

As we discussed at the December PEEC meeting, a survey was sent to practitioners to understand how they are interpreting and applying the independence requirements in their compliance audits, and the task force has reviewed those results.

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2

Highlights of survey results

A total of 107 responses were received, indicating that

- Approximately 50% of respondents believe additional guidance in this area is needed.
- When performing a compliance audit and the audit of the financial statements for the same attest client, approximately 50% of respondents believe that an evaluation of independence as it relates to the financial statement audit results in an appropriate evaluation of independence for the compliance audit, while half of the respondents believe that a separate independence evaluation is necessary for the compliance audit.
- Of the respondents that perform a compliance audit only for clients (meaning another firm performs the financial statement audit), 80% of those practitioners evaluate independence in the compliance audit the same as they would in the audit of the financial statements and believe that evaluation is appropriate.
- Diversity in practice was also evident in the responses when asked which entities should the independence requirements apply to in a compliance audit that includes a schedule of expenditures for federal awards or a similar schedule versus a compliance audit that does not include such schedule.

3

Response demographics:

Overall:
Government – 20%
Public practice – 80%

Public practice:
<$1.5M – 22%
>$10M – 41%

3

Proposed task force charge

To consider how the independence requirements for compliance audits performed under the SASs should be applied and whether those independence requirements should differ in the following circumstances

- When a compliance audit only is performed versus when a compliance audit is performed with the audit of the financial statements of the same attest client, and within these circumstances, consider
  - When the compliance audit includes reporting on a financial statement (for example, a schedule of expenditures of federal awards or comparable schedule), and
  - When the compliance audit does not include reporting on a financial statement (for example, a compliance audit of a proprietary school required by the U.S. Department of Education Office of Inspector General's *Guide For Audits of Proprietary Schools and For Compliance Attestation Engagements of Third-Party Services Administering Title IV Programs*)

A key component in evaluating how to apply the independence requirements will be to determine what entity should be considered the attest client in the compliance audit, who should be considered the covered member, and whether guidance should differ when there is a single program subject to the compliance audit vs. multiple programs.

The task force believes nonauthoritative guidance is needed, but if during its deliberations, it becomes apparent that a modification to the Code may be needed, the task force will bring the proposed modification back to PEEC.

4

4

Association of International Certified Professional Accountants

The unified voice of AICPA and CIMA

Role and Mindset

IFAC Convergence and Monitoring Task Force

February 9, 2021

1

Final pronouncement released

- Reinforce public interest responsibility
- Addition of inquiring mind
- Enhanced awareness of risk of bias

Effective December 31, 2021

2

2

Code is substantially equivalent

3

3

Revisions to the fundamental principles

Behave in a manner that is consistent with the profession's responsibility to act in the public interest	• Covered by our principles of The Public Interest and Responsibilities
Have the strength of character to act appropriately	• Covered by the Integrity principle and the Integrity and Objectivity Rule
Undue reliance on individuals, organizations, and technology	• Code addresses the substance and additional guidance can be provided through member enrichment materials
Part of maintaining competence requires a continuing awareness and an understanding of technology-related developments	• Code addresses competence and any further detail would be appropriate for member enrichment materials

4

4

Additions to the conceptual framework

Inquiring mind

- Consider the source, relevance and sufficiency of information obtained, taking into account the nature, scope and outputs of the professional activity being undertaken;
- Being open and alert to a need for further investigation or other action

Bias

- Highlight the impact of bias on exercising professional judgement and applying the conceptual framework

5

Code addresses the substance and consider enhancing member enrichment material

5

Association of International Certified Professional Accountants
AICPA CIMA

Thank you

6

Association of International Certified Professional Accountants

The unified voice of AICPA and CIMA

IESBA update

February 9, 2021

Ellen Goria, Associate Director

1

Public interest entity

Exposure draft issued

Comments due May 3rd

2

2

PIE: basic premise

Where the public has significant interest in the financial condition of an entity, auditors of those entities should be subject to more robust ethical requirements so that the public's confidence in the audit and related financial statements is enhanced

3

3

Factors to consider when determining the level of public interest in an entity

- Nature of an entity's business or activities and covers those entities that take on financial obligations to the public as a key element of their business model
- Whether the entity is subject to regulatory supervision designed to provide confidence that the entity will meet its financial obligations
- Size of the entity
- The importance of the entity to the sector in which it operates including how easily replaceable it is in the event of financial failure
- Number and nature of stakeholders including investors, customers, creditors and employees
- The potential systemic impact on other sectors and the economy as a whole in the event of financial failure of the entity

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Broad list

- Tightening the definitions
- Setting size criteria
- Adding or exempting entities

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Broad list

- Publicly traded entity
- An entity, one of whose main functions is to take deposits from the public
- An entity one of whose main functions is to provide insurance to the public
- An entity whose function is to provide post-employment benefits
- An entity whose function is to act as a collective investment vehicle and which issues redeemable financial instruments to the public
- An entity specified as a PIE by law or regulation to meet the objective of enhancing confidence in the financial statements by enhancing confidence in the audit

6

Publicly traded entity:

An entity that issues financial instruments that are transferrable and publicly traded.

6

Nonassurance services and fees proposals

Adopted at the December meeting

Effective December 15, 2022

7

7

Tax services

Not provide a tax service or recommend a transaction to an audit client if the service or transaction relates to marketing, planning, or opining in favor of a tax treatment that was initially recommended, directly or indirectly, by the firm or network firm, and a significant purpose of the tax treatment or transaction is tax avoidance, unless the firm is confident that the proposed treatment has a basis in applicable tax law or regulation that is likely to prevail

8

8

Engagement team: provide clear and consistent independence guidance for

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

The firms that these component auditors are in

Use the generic term "team" to denote a team of individuals who perform an engagement

9

9

Updated individual recommendations

All members of the engagement team be independent of the group audit client.

Would consider providing guidance on what a related entity is for a component within the scope of ISA 600

10

10

Updated firm recommendations

Firm issuing the audit opinion on the group financial statements, and its network firms be independent of		Component audit firms that are outside of the network	
Group audit client and its related entities	Other components scoped in under ISA 600 (Revised)	Be independent of component audit client	Group engagement partner responsible for determining that firm made aware of applicable ethical requirements

11

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