AICPA

Professional Ethics Executive Committee

Open meeting agenda

November 10–11, 2022

Durham, NC

Open meeting agenda — November 10–11, 2022

Professional Ethics Division

Professional Ethics Executive Committee

Meeting link: https://aicpa.zoom.us/j/93038227544 Meeting ID: 930 3822 7544 Observers must register: www.aicpa.org/peecmeeting		
November 10		
9:00–9:05 ET	**Welcome** Mr. Lynch will welcome the committee members and discuss administrative matters.	
9:05–10:20	**Compliance audits** The task force will seek adoption of revisions to the code and input on member enrichment material to support implementation.	Agenda items 1A–1E
10:20–10:35	*Break*	
10:35–11:20	**IESBA convergence: Fees** The task force will seek input on the task force's approach and the proposed authoritative and nonauthoritative guidance.	Agenda items 2A–2C
11:20–11:50	**Solicitation or disclosure of CPA examination questions and answers** Staff will seek approval to expose revisions to the "Solicitation or Disclosure of CPA Examination Questions and Answers" interpretations.	Agenda items 3A–3B
11:50–12:35	**Information systems services** The task force will provide an overview of the recently issued nonauthoritative guidance and seek input on additional Q&As.	Agenda items 4A–4B

12:35–1:35	*Lunch break*	
1:35–1:55	**Assisting attest clients with implementing accounting standards** The task force will seek input on the proposed update to the nonattest services Q&A.	Agenda items 5A–5B
1:55–2:25	**IESBA convergence: Engagement quality reviewer** The task force will seek input on the proposed nonauthoritative guidance.	Agenda items 6A–6C
2:25–3:10	**Simultaneous employment or association with an attest client** The task force will provide an overview of recent activities and seek approval to move forward with drafting revisions to the code.	Agenda items 7A–7B
3:10–3:25	*Break*	
3:25–4:10	**IESBA convergence: Public interest entities** The task force will seek input on its proposed approach for converging with IESBA's public interest entity guidance.	Agenda items 8A–8B
4:10–4:25	**IESBA update** Update on IESBA's activities for the previous quarter including, tax planning; private interest entities; technology; engagement team; and other projects.	Agenda items 9A–9G
4:25–5:10	**Noncompliance with laws and regulations** The task force will provide an overview of recent activities and seek input on the proposed Q&As.	Agenda items 10A–10B

November 11		
9:00–9:15 ET	**Private equity investment in firms** Update on the AICPA cross-team collaborative activity.	
9:15–9:30	**DOL independence rules** Staff will provide an update on the revised independence rules and discuss the planned communication efforts.	
9:30–10:30	**Statements on Standards for Tax Services** The task force will provide an overview of recent activities and will seek input on the exposure draft and invitation to comment.	Agenda items 11A–11B
10:30–10:40	**AICPA Online Ethics Library** Staff will demonstrate new enhancements to the Online Ethics Library.	
	Future meeting dates February 21–22, 2023 May 9–10, 2023 August 9–10, 2023 November 8–9, 2023	

Agenda item 1A

Compliance audits

Task force members

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Observers

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Task force charge

To consider the following:

- How the independence requirements should be applied to compliance audits performed under the Statements on Auditing Standards
- Whether revisions to the AICPA Code of Professional Conduct (code) are warranted
- What nonauthoritative guidance is necessary

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 and whether the affiliate interpretations should apply.

Reason for agenda item

To seek adoption of the proposals in the June 2022 exposure draft related to compliance audits. and to solicit input on the nonauthoritative guidance developed to assist members with implementing the proposed revisions.

Task force activities

The task force recommends revisions based on the 17 comment letters received. These revisions are outlined in the following summary sections. See agenda item 1B for the full comment letter summary.

- Overall, the majority of commenters are supportive of the proposed revisions. Some commenters suggest revisions to the proposal and recommend nonauthoritative guidance.
- CL 13 supports the proposed revisions but says that they should apply when the member performs only the compliance audit for a client — not also the financial statement audit. See discussion of this comment letter in the section titled “Summary of

comments for proposed revisions when a member performs only a compliance audit for a client".

- CL 6 does not support the proposal, saying the proposed revisions are not sufficiently clear. Details of this concern are outlined in the following summary sections.

The task force has developed six questions and answers to assist members with implementing the proposed revisions to the code related to compliance audits.

> **NOTE:** For all proposed revisions in the following sections, refer to agenda items 1C (redline version) and 1D (clean version) for the full context.

Summary of comments for proposed new definition "compliance audit"

Nine letters say that the definition of "compliance audit" is clear (CL 2, CL 3, CL 5, CL 7, CL 8, CL 9, CL 10, CL 11, CL 12).

Six letters say that the definition of "compliance audit" is not clear and provided comments and suggestions for the task force to consider (CL 4, CL 6, CL 13, CL 14, CL 15, CL 17):

- Four letters say that AU-C section 806 should not be included as an example of a compliance audit, highlighting that reporting on compliance under AU-C section 806 is a "by-product" (term used in AU-C section 806) of the financial statement audit and prepared only as part of an engagement to audit financial statements (CL 13, CL 14, CL 15, CL 17).

  CL 17 also suggests that we align this definition with the definition in AU-C section 935 saying that if AU-C section 806 is not removed, we should revise the definition to clarify that it is for the sole purpose of applying the "Independence Rule" (ET sec. 1.200.001) and its interpretations.

- Two letters suggest either clarifying the definition or developing nonauthoritative guidance to explain how reporting under AU-C 725 or 805 may be part of an engagement to report on compliance as described in the exposure draft (CL 14, CL 17).

- Two letters suggest discontinuing the use of "compliance audit attest engagement" in the definition of "compliance audit" because using "audit" and "attest engagement" together is redundant (CL 4, CL 13).

  CL 13 also suggests that we do not include "attest engagement" when using the term "compliance audit."

- CL 15 suggests that we can better clarify the definition of "compliance audit" by expanding it to include a nongovernmental example of what might constitute a compliance audit.

- CL 6 says that the example included in the definition does not sufficiently illustrate how there could be multiple compliance audit clients that have amounts on the Schedule of Expenditures of Federal Awards in a compliance audit. They say the definition should provide more explanatory information to describe

  - how a compliance audit may have multiple compliance audit clients;
  - why this could happen;
  - the implications of having multiple attest clients;
  - whether there will be separate engagements for each attest client; and
  - whether there will be separate auditor's reports or one auditor's report

Task force recommendations

Because reporting under *Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements* (AU-C sec. 806) is a "by-product" of a financial statement audit, it is not appropriate for the proposed revisions to reflect that such reporting falls under the definition of "compliance audit."

Compliance Audits (AU-C sec. 935) is the only auditing standard applicable to compliance audits and the Auditing Standards Board (ASB) currently does not have plans to address compliance audits outside of AU-C section 935.

Based on this information and the comments in CL 13, CL 14, CL 15, and CL 17, the task force recommends that the first paragraph of the definition of "compliance audit" clarifies that a compliance audit is an attest engagement performed in accordance with AU-C section 935. This will remove the reference to AU-C section 806.

When a schedule or statement is included in the compliance audit, the member will also report on the accuracy of the schedule or statement in accordance with *Supplementary Information in Relation to the Financial Statements as a Whole* (AU-C sec. 725) or *Special Considerations — Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement* (AU-C sec. 805). When included as part of an attest engagement to report on compliance in accordance with AU-C section 935, reporting on the accuracy of the schedule or statement would not preclude the attest engagement from being a "compliance audit" so the task force recommends clarifying this in the definition.

Using “audit” and “attest engagement” together is indeed redundant and the task force recommends removing “attest engagement” from “compliance audit attest engagement” in the second paragraph of the definition.

The task force is not recommending revisions to address the comments in CL 15. The example in the proposed definition of “compliance audit” is broad enough to include compliance audits for governmental and nongovernmental entities.

We have nonauthoritative guidance (Q&A .02) to illustrate how there may be multiple attest clients in a compliance audit and this provides clarity related to the feedback in CL 6 and CL 15. However, this guidance does not address whether there will be separate engagements or auditor’s reports for each attest client as requested in CL 6 because such topics are addressed in the auditing standards.

Question for the committee

1. Does the committee agree with the recommended edits to the definition of “compliance audit”?

Summary of comments for proposed new definition “compliance audit attest client”

Thirteen letters agree that the proposed exception to the independence requirements in a compliance audit for entities that are not subject to compliance audit procedures and report amounts that are trivial and clearly inconsequential is appropriate (CL 2, CL 3, CL 5, CL 7, CL 8, CL 9, CL 10, CL 11, CL 12, CL 13, CL 14, CL 15, CL 17).

CL 4 expresses concern with the phrase “reports amounts that are trivial and clearly inconsequential” in the exception because compliance audits often do not report on any amounts.

Eight letters say that the “compliance audit attest client” definition is clear as written (CL 2, CL 3, CL 5, CL 8, CL 10, CL 11, CL 12, CL 14).

Eight letters say that the “compliance audit attest client” definition not is clear as written (CL 1, CL 4, CL 6, CL 7, CL 9, CL 13, CL 15, CL 17). Suggestions for clarifying are as follows:

- CL 4 suggests that “attest” be removed from the term “compliance audit attest client” as it is redundant because all audits are attest engagements.
- CL 4 and CL 9 say that the definition is not clear because it defines what is not a compliance audit attest client rather than what is a compliance audit attest client.
- CL 7 suggests that the definition would be clearer with the following revisions to

emphasize that the exception applies when there are multiple entities and that both conditions must be met in order for a client to fall under the exception.

> ~~An~~ **A reporting** entity with respect to which a compliance audit is performed. ~~unless the entity~~ **To the extent the reporting entity contains multiple entities, an individual entity would not be considered a compliance audit attest client if that particular entity**:
>
> a. is not **likely to be** subject to compliance audit procedures and
>
> b. reports amounts that are trivial and clearly inconsequential.
>
> When an entity meets this definition, it is not considered a financial statement attest client."

- CL 6 indicates that the underlying rationale for including criterion (*a*) — not subject to compliance audit procedures — is unclear and that the definition could be improved by incorporating additional explanatory information to clarify and make it more understandable.

- CL 17 recommends that criterion (*b*) include a point of reference for determining whether an amount is trivial and clearly inconsequential. They say that there is a risk that readers will assess "trivial and clearly inconsequential" in a vacuum without considering other amounts or factors, such as the financial statements or the program itself.

  Paragraph .A7 in AU-C section 935 states that "materiality" is in relation to the government program. The "State and Local Government Client Affiliates" interpretation (ET sec. 1.224.020) states that "trivial and clearly inconsequential" is in relation to the financial statements as a whole. The criterion in the definition lacks similar guidance for determining what is considered trivial and clearly inconsequential.

- Four letters suggest revisions to the phrase "trivial and clearly inconsequential" (CL 1, CL 3, CL 13, CL 15):

  - CL 1 notes that the phrase "trivial and clearly inconsequential" is used only once in the code and that "clearly inconsequential" is used twice. As such, CL 1 has the following suggestions:

    - If "trivial" and "clearly inconsequential" have different meanings, then definitions for each should be included.

    - If the terms have the same meaning, pick one of the terms or a new term and define it. Using two terms that have the same meaning is both redundant and confusing.

- The concept of "trivial and clearly inconsequential" needs to be conveyed in an example, such as the example in paragraphs .28–.30 of the exposure draft (entity reporting $1,000 of expenditures in a SEFA that includes $1 billion of expenditures). This will provide clarity and promote consistency of practice.

– CL 13 recommends that the phrase be changed to "clearly trivial and inconsequential" (to move "clearly" before "trivial") to be consistent with how similar concepts are articulated in other standards.

– Two letters say the definition would be clearer if the phrase was changed to "clearly trivial" as that term is term used in paragraphs .05 and .A2 of *Evaluation of Misstatements Identified During the Audit* (AU-C sec. 450) (CL 3, CL 15).[1]

  Similarly, CL 6 recommends that criterion (*b*) include the context and basis for which the auditor is to determine "trivial and clearly inconsequential" and points out that "trivial" is similar to "clearly trivial" defined in AU-C section 450.

– CL 3 requests consideration of raising the threshold from "trivial and clearly inconsequential" to "immaterial."

- CL 17 says that there is no reasonable third-party test or guidance regarding the viewpoint from which the amounts should be considered trivial and clearly inconsequential. AU-C section 935 states that materiality is influenced by the needs of the grantor. The definition is not clear from whose viewpoint amounts should be considered trivial and clearly inconsequential.

- CL 4 points out that the definition does not address situations where the member firm is engaged by someone other than the entity that is subject to the compliance audit.

Task force recommendations

The definition of "compliance audit attest client" is describing an entity that reports amounts in the schedule or statement rather than the compliance audit reporting on amounts as indicated in

[1] Paragraph .A2 of AU-C section 450 explains that "[p]aragraph .05 requires the auditor to accumulate misstatements identified during the audit other than those that are clearly trivial. "Clearly trivial" is not another expression for "not material." Misstatements that are clearly trivial will be of a wholly different (smaller) order of magnitude, or of a wholly different nature, than those that would be determined to be material and will be misstatements that are clearly inconsequential, whether taken individually or in the aggregate and whether judged by any criteria of size, nature, or circumstances. When there is any uncertainty about whether one or more items are clearly trivial, the misstatement is considered not to be clearly trivial."

CL 4. A compliance audit may include a schedule or statement. Though AU-C section 935 does not address reporting on the accuracy of that schedule or statement, the governmental audit requirements may require such schedule to be included in the compliance audit, for example, a compliance audit performed in accordance with Uniform Guidance includes a Schedule of Expenditure of Federal Awards. Therefore, criterion (*b*) can be applied as it is not uncommon for a schedule or statement to be included in a compliance audit.

The task force agrees that "attest" in the proposed term "compliance audit attest client" is redundant and recommends removing "attest" from the proposed term.

The original purpose of the phrase "attest client" in the proposed term "compliance audit attest client" was to acknowledge that this client is an attest client and that the independence requirements applicable to attest clients are also applicable to "compliance audit clients" (as revised).

Considering this and the suggestion that the term be changed to "compliance audit client," the task force recommends including in the definition that members should apply the independence requirements applicable to an attest client to a compliance audit client.

Consequently, the task force also recommends clarifying that when the two criteria — (*a*) and (*b*) — are met, the entity is not a compliance audit client, and the independence requirements do not apply.

The task force is also recommending revisions to clarify what is and is not a compliance audit client, similar to edits proposed in CL 7 and to address concerns raised in CL 4 and CL 9.

The suggested revision in CL 7 to revise criterion (b) to say "is ***not likely to*** be subject to compliance audit procedures" make the criterion less clear. Therefore, the task force is not recommending this edit.

Criterion (b) is clear as originally proposed. The task force will continue to evaluate the need for nonauthoritative guidance to explain what the phrase "not subject to compliance audit procedures" means.

A point of reference for determining whether an amount is trivial and clearly inconsequential will provide clarity in the definition. The task force recommends revising criterion (*b*) to clarify that it refers to "amounts ***in the schedule or statement*** that are trivial and clearly inconsequential ***to the schedule or statement as a whole***" (additions in bold italics).

The phrase "trivial and clearly inconsequential" is appropriate because it is consistent with the phrase used in the "State and Local Government Client Affiliates" interpretation. The phrase appropriately considers language in AU-C section 450, which uses "clearly trivial" and "clearly inconsequential" and language in the International Code of Ethics for Professional Accountants,

which uses the phrase “trivial and inconsequential.”

The proposed revisions should not include detailed factors to consider when determining what is “trivial and clearly inconsequential.” The code has historically not provided these details, including the viewpoint or user from which the amount should be considered trivial and clearly inconsequential. A nonauthoritative Q&A will serve to remind members that this evaluation is based on the member’s judgment, considering quantitative and qualitative factors.

It is not appropriate for the definition of “compliance audit client” (as revised) to address situations where the engaging party is different from the compliance audit client as this topic is addressed in the definition of “attest client.”

For consistency “reports” should be changed to “includes” in criterion (*b*). This is how amounts are described in the schedule or statement in other parts of the proposed definitions for “compliance audit” and “compliance audit client.”

The definition of “compliance audit client” should be carved out of the definition of “financial statement attest client.” This will clarify the effect on the application of independence requirements and align with revisions that explain when the independence requirements do or do not apply. With all recommended clarifying revisions, the final sentence of the definition will read as follows:

> When an entity meets ***the*** ~~this~~ definition ***of a compliance audit client***, it is not considered a financial statement attest client ***and, therefore, the “Client Affiliates” interpretation [1.224.010] and the “State and Local Government Client Affiliates” interpretation [1.224.020] would not apply***.”

Question for the committee

2. Does the committee agree with the recommended edits to the definition of “compliance audit client”?

Summary of comments for proposed revisions to the definition of “financial statement attest client” and the affiliate interpretations

Thirteen letters agree that the affiliate requirements should not apply in a compliance audit (CL 2, CL 3, CL 5, CL 7, CL 8, CL 9, CL 10, CL 11, CL 12, CL 13, CL 14, CL 15, CL 17):

- CL 15 agreement assumes that the revisions relate solely to audits performed under AU-C section 935.
- CL 7 agreement assumes the auditor is performing only the compliance audit. Please

see the following summary section for more on this.

CL 4 says the issue is adequately addressed in the affiliate interpretations, which state that they apply to financial statement attests clients. The reminder being proposed in the interpretations may be useful, but it is not required.

Thirteen letters agree that the revision in each of the affiliates interpretations serves as a useful reminder that these interpretations do not apply to specific attest engagements — for example compliance audits and engagements performed under the SSAEs (CL 2, CL 3, CL 5, CL 7, CL 8, CL 9, CL 10, CL 11, CL 12, CL 13, CL 14, CL 15, CL 17).

- CL 13 suggests that the affiliates interpretations should be revised to state, "This interpretation does not apply to a compliance audit attest client or …" (in other words, they recommend the revision refer to the client rather than the engagement).

Task force recommendations

A compliance audit may include a schedule or statement, notwithstanding CL 4's position that this is rare, so the proposed revisions are not required. Such schedule or statement is a financial statement as defined in the code. Consequently, an entity including amounts in the schedule or statement is a financial statement attest client as defined by the code. Without the carve out for affiliates as proposed in the revisions, members will need to be independent of a compliance audit client's affiliates as well.

To be consistent with the recommended edits in the definition of "compliance audit client", the task force recommends the following edits to the definition of "financial statement attest client":

a. Remove "attest" from the term "compliance audit attest client" that is used to carve out such clients from the definition of "financial statement attest client"

b. Add the following sentence to be consistent with the language in the definition of "compliance audit client": "***Therefore, the "Client Affiliates" interpretation [1.224.010] and the "State and Local Government Client Affiliates" interpretation [1.224.020] would not apply."***

Many commenters agree that the revisions to the client affiliate interpretations are useful. However, the clarifying revisions to the definition of "financial statement attest client" make a revision to the client affiliate interpretations unnecessary; therefore, the suggestions provided in CL 13 are no longer applicable.

The exposure draft also included a reminder that the client affiliate interpretations do not apply to engagements performed under the Statements on Standards for Attestation Engagements (SSAEs). The task force considered whether it would be helpful to indicate in the definition of "financial statement attest client" that a financial statement attest client does not include a

responsible party as described in the "Application of the Independence Rule to Engagements Performed in Accordance With Statements on Standards for Attestation Engagements" interpretation (ET sec. 1.297.010).

This is generally understood to be true in practice based on extant requirements in the code. As well, determining whether clarity is necessary for such engagements is outside the scope of this task force. If we include such clarifying revisions in this project, we could imply that these engagements are considered compliance audits, thereby confusing members who perform similar compliance related engagements under the SSAEs. Therefore, the task force is not recommending including a reminder that the client affiliate interpretations do not apply to engagements performed under the SSAEs.

Questions for the committee

3. Does the committee agree with the recommended edits to the definition of "financial statement attest client"?

4. Does the committee agree with the recommendation not to move forward with the proposed revision in each of the client affiliate interpretations?

Summary of comments for proposed revisions for when a member performs only a compliance audit for a client

CL 13 says that the proposed revisions should apply only when a compliance audit is performed on a "stand-alone" basis, meaning that the member does not also audit the client's financial statement. Following are their suggestions and comments to clarify this position:

- Revise the definition of "financial statement attest client" to say "this definition does not include a compliance audit client that is not also a financial statement attest client."

- Revise the definition of "compliance audit client" to exclude entities that are also financial statement attest clients: "An entity, other than a financial statement attest client, with respect to which a compliance audit is performed, unless …"

- Remove the final sentence of the definition as a "compliance audit client" could also be a "financial statement attest client."

As previously noted, CL 7 expresses agreement that the affiliate exception is appropriate "if the auditor is performing only the compliance audit."

Task force recommendation

The proposed revisions should not strictly apply when the member performs only the

compliance audit for a client because the entities in which the member should be independent may differ for each engagement.

For example, if the engagement is a financial statement attest engagement, members need to be independent of affiliates and when the engagement is a compliance audit, members need to be independent of entities that don't meet the carve out in the compliance audit client definition. Applying the proposed revisions only to a compliance audit when it is the only engagement performed for a client will limit the applicability to that scenario when the threats to independence that exist for a compliance audit are the same regardless of whether other engagements, such as the financial statement audit, are also performed for the same client.

This circumstance is not unique to compliance audits. Under the extant code, when members perform multiple engagements for a client they should be complying with the most restrictive requirements. An example is when members perform a financial statement audit and an engagement in accordance with SSAEs for the same client.

The proposed revisions appropriately apply to all compliance audits and the task force is not recommending changes to address comments. Q&A .06 will help clarify how to apply independence requirements when performing a financial statement audit and compliance audit for the same client.

Question for the committee

5. Does the committee agree with the recommendation that no changes be made to address these comments?

Summary of comments related to engagements performed under the Statements on Standards for Attestation Engagements

Thirteen letters agree that entities are not considered responsible parties if they are not subject to compliance attestation procedures in an engagement performed under the SSAEs. Therefore they are not subject to the "Independence Standards for Engagements Performed in Accordance with Statements on Standards for Attestation Engagements" subtopic (ET sec. 1.297) (CL 2, CL 3, CL 5, CL 7, CL 8, CL 9, CL 10, CL 11, CL 12, CL 13, CL 14, CL 15, CL 17).

CL 14 requests consideration of whether the nonattest services exception outlined in paragraph .03 of the "The "Engagements, Other Than AUPs, Performed in Accordance With SSAEs" interpretation (ET sec. 1.297.030) should be included in the proposed revisions for compliance audits. Paragraph .03 states

> When providing nonattest services that would otherwise impair independence under the interpretations of the "Nonattest Services" subtopic [1.295], threats would be at an

acceptable level and independence would not be impaired if the following safeguards are met:

a. Nonattest services do not relate to the specific subject matter of the SSAE engagement.

b. The "General Requirements for Performing Nonattest Services" interpretation [1.295.040] of the "Independence Rule" [1.200.001] are met when providing the nonattest service. [Prior reference: paragraph .13 of ET section 101]

The rationale is that this is appropriate because compliance examination engagements are similar to compliance audits, so without these provisions, members may reach different conclusions on independence though the objectives of the engagements are the same and therefore, threats would be the same.

Task force recommendations

The task force discussed various interpretations under the "Nonattest Service" subtopic (ET sec. 1.295) in considering this comment and did not identify any examples of when the nonattest services exception in the "Engagements, Other Than AUPs, Performed in Accordance With SSAEs" interpretation is necessary for compliance audits.

Paragraph .02 of the "Information Systems Services" interpretation (ET sec. 1.295.145) that will be effective January 1, 2023, requires members to apply this interpretation to all attest engagements. The interpretation defines a financial information system as any information system that is subject to the attest procedures when the subject matter is not financial statements.

Prior to adoption of the "Information Systems Services" interpretation that includes this paragraph, the nonattest services exception in "Engagements, Other Than AUPs, Performed in Accordance With SSAEs" interpretation may have been necessary for the proposed revisions for compliance audits because the previous requirements referred only to financial information. However, the revised interpretation includes guidance on how to apply those requirements when the subject matter of the engagement is not financial statements. Given this, no further changes to the proposed revisions are necessary.

Any revisions that may be necessary for the independence requirements for engagements subject to the SSAEs are outside the scope of this task force.

Question for the committee

6. Does the committee agree with the recommendation that no changes be made to address this comment?

Effective date

Fourteen letters agree that the proposed effective date provides adequate time to implement the proposed revisions. The proposed effective date is for compliance audits commencing after June 15, 2023, with early implementation allowed (CL 2, CL 3, CL 4, CL 5, CL 7, CL 8, CL 9, CL 10, CL 11, CL 12, CL 13, CL 14, CL 15, CL 17).

Task force recommendation

The task force recommends that the proposed revisions be effective for compliance audits commencing after June 15, 2023, with early implementation allowed.

Question for the committee

7. Does the committee agree with the task force's recommendation that the proposals be effective for compliance audits commencing after June 15, 2023, with early implementation allowed?

Nonauthoritative guidance

Four letters say more guidance is needed on specific quantitative and qualitative factors to consider when evaluating what is trivial and clearly inconsequential. The rationale is that the example in the exposure draft is too conservative without additional factors to consider (CL 2, CL 3, CL 10, CL 17).

Related to this, CL 17 also suggests that guidance include a reasonable third-party test or guidance regarding the viewpoint from which the amounts should be evaluated (for example, whether the evaluation is influenced by the needs of grantors). This letter requests nonauthoritative guidance to clarify what the amounts should be compared to when considered what is trivial and clearly inconsequential.

CL 4 suggests clarification on the requirements that apply to engagement parties versus responsible parties.

Two letters suggest defining or describing what constitutes a "compliance audit procedure" in criterion (*b*) in the definition of "compliance audit client" (CL 5, CL 10).

Related to this, CL 5 suggests that "compliance audit procedures" be described for a

compliance audit other than a compliance audit performed under the Uniform Guidance.

Two letters suggest that the explanatory material included in the exposure draft be incorporated in nonauthoritative guidance (CL 4, CL 8).

CL 9 suggests nonauthoritative guidance be developed to provide specific examples that will assist members who perform few of these types of engagements in determining applicability of the requirements, considering the number of clients that may be undergoing a compliance audit for the first time.

CL 12 suggests that the explanation in the exposure draft that references multiple entities being departments or agencies in a state and local government indicates that an entity does not need to be a legally separate entity. The letter suggests clarifying whether there is a legal entity concept associated with "entity."

CL 13 says it is unclear how an entity responsible for compliance requirements is not considered a compliance audit client. This letter requests that guidance include examples of how to apply the conceptual framework to the circumstances described in the conceptual framework section of the exposure draft.

CL 14 expresses support for the proposed topics to be addressed in nonauthoritative guidance as discussed during the August meeting, which are the topics addressed in Q&A .01–.05 of agenda item 1E.

Two letters suggest that nonauthoritative guidance clarify that engagements outside of AU-C section 935 that include reporting under AU-C sections 725 or 805 are not compliance audits (CL 14, CL 17).

CL 17 suggests that nonauthoritative guidance address inadvertent breaches due to subsequent changes in trivial and clearly inconsequential amounts considering that the possibility of inadvertent breaches increases under these requirements.

Task force recommendation

Certain topics should be addressed through Q&As to assist members in implementing the proposed revisions. Agenda item 1E includes Q&As for the five topics presented at the August committee meeting plus an additional topic considered by the task force subsequent to the August committee meeting. The task force will continue deliberations on additional nonauthoritative guidance requests from the comment letters at future meetings.

- **Q&A .01** provides examples of what will and won't be considered a compliance audit. Often members in practice refer to compliance related examination engagements as "compliance audits" when those engagements are performed under the SSAEs and do not meet the definition of "compliance audit" under the proposed revisions.

Providing specific examples of what is a compliance audit and what is not a compliance audit will be useful in helping members appropriately identify the engagements subject to these proposed revisions. This Q&A addresses the requests in CL 9, CL 14, and CL 17 to help explain the applicability of the proposed revisions to specific engagements.

- **Q&A .02** elaborates on when a compliance audit may include multiple compliance audit clients. The proposed definition of "compliance audit" introduces to the code the concept of multiple compliance audit clients. This is an important concept that will help members apply the proposed revisions and identify all compliance audit clients.

- **Q&A .03** broadly addresses how a member should evaluate what is "trivial and clearly inconsequential." Neither the code nor previous nonauthoritative guidance has mentioned such evaluation, but a reminder that this evaluation is a matter of professional judgment will be helpful to members.

  A member will evaluate "trivial and clearly inconsequential" using similar factors or concepts as when evaluating amounts under the Statements on Auditing Standards (such as, AU-C section 450). This is also reflected in this Q&A.

- **Q&A .04** reminds members to be alert to changes in the entities considered to be compliance audit clients. In a compliance audit subject to the Uniform Guidance, for example, amounts could change from being trivial and clearly inconsequential to more than trivial and clearly inconsequential, and therefore, the entity could become a compliance audit client for the first time during the period of professional engagement.

  Due to the nature of such compliance audits, the task force believes that this reminder will be helpful for members. This Q&A meets the requests made by CL17 to address inadvertent breaches due to changes in trivial and clearly inconsequential amounts.

- **Q&A .05** reminds members that there may be circumstances or relationships outside of the proposed revisions that create threats to independence and that those threats should be evaluated using the conceptual framework. It's an important reminder in case threats do exist related to those entities now carved out of the definition of "compliance audit client" or those entities that are no longer considered affiliates. This Q&A addresses the requests in CL13 for an explanation of how an entity could be subject to compliance audit procedure, yet not considered a compliance audit client.

- **Q&A .06** addresses how a member would apply independence requirements when performing the financial statement audit and compliance audit for the same client. Though similar situations exist today (for example, a member could perform the financial statement audit and an engagement subject to SSAEs for the same client and be subject to the independence requirements applicable to each attest engagement), a Q&A to

address this for compliance audits may be useful.

Questions for the committee

8. Does the committee have any suggestions or concerns on the Q&As as presented in agenda item 1E? For purely editorial revisions, please email melissa.powell@aicpa-cima.com.

9. Does the committee believe there should be additional Q&As?

Action needed

The committee is asked to adopt the proposed revisions in agenda item 1D, as amended, and that those revisions be effective for compliance audits commencing after June 15, 2023, with early implementation allowed.

Materials presented

- Agenda item 1B: Comment letter summary
- Agenda item 1C: Proposed revisions (redline)
- Agenda item 1D: Proposed revisions (clean)
- Agenda item 1E: Proposed Q&As for compliance audits

Comment letter summary: General and by question

Proposed new definitions, a revised definition, and revised interpretations related to compliance audits

Exposure draft dated June 3, 2022

This table presents a summary of the letters that support, support with comments, or do not support the new and revised definitions and interpretations for compliance audits and provided general feedback:		
Supports: 15 (several commenters had suggestions or comments as detailed herein) Conditional support: 1 (believes application should be limited) Does not support: 1 (believes revisions are not sufficiently clear)		
CL 1	Terrill W. Ramsey	**Supports** Staff note: The comments received focus on clarification of the phrase "trivial and clearly inconsequential" in the definition of compliance audit attest client.
CL 2	National State Auditors Association	**Supports** Agree with questions *a.-g.* in the exposure draft.
CL 3	Office of the Washington State Auditor	**Supports** Agree with questions *a.-g.* in the exposure draft.
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**Supports** PEEC's proposed revisions to the AICPA Code of Professional Conduct, consisting of new and revised definitions and revised interpretations, provide additional guidance that will be helpful in addressing independence issues that often arise

		when conducting compliance audits. The stated goal of these additions and revisions, to align requirements and applicable risks, is most appropriate. We believe, however, that it would be especially useful if explanatory material were provided as part of the revisions, such as that included in the Exposure Draft. This additional material could be provided either as part of the new and revised definitions and interpretations, or as supplementary, nonauthoritative guidance.
CL 5	Tennessee Comptroller of the Treasury	**Supports** Agree with questions *a.-g*. in the exposure draft.
CL 6	U.S. Government Accountability Office (GAO)	**Does not support** In our view, the proposed changes are not sufficiently clear. These proposed changes may not produce appropriate and consistent responses by auditors. We are concerned with the potential impact these proposed changes could have on GAGAS engagements. We believe our comments should be addressed before the proposed changes are issued.
CL 7	CliftonLarsonAllen LLP (CLA)	**Supports** Agree with questions *a.-g.* in the exposure draft.
CL 8	Grant Thornton LLP	**Supports** Grant Thornton supports PEEC's proposal for new and revised definitions and revised interpretations relating to compliance audits. We agree the revisions provide both clarity and relief to members who perform compliance audits by aligning the requirements under the "Independence Rule" (ET sec. 1.200.001) with applicable risks. We also agree the revisions will support the alignment of the cost of compliance with the potential threats to independence and consistent application by

		members in practice. While Grant Thornton supports the revisions and definitions set forth in the Exposure Draft, we have provided comments for PEEC's consideration.
CL 9	Texas Society of CPAs (TXCPA)	**Supports** Staff note: They agree with questions *a.-g.* in the exposure draft. However, they believe the definition of compliance audit attest client should explain what it is rather than what it is not.
CL 10	Auditor of Public Accounts (Virginia APA)	**Supports** Agree with questions *a.-g*. in the exposure draft.
CL 11	Crowe LLP	**Supports** We support the PEEC's efforts to clarify the independence guidance applicable to compliance audits and provide relief to members who perform compliance audits by aligning the requirements with applicable risks.
CL 12	KPMG LLP	**Supports** Overall, we are supportive of the proposed revisions and PEEC's efforts to update and improve the effectiveness of its independence interpretations and definitions, such that they do not create arbitrary independence violations in situations that do not impair an auditor's objectivity, integrity, or professional skepticism.
CL 13	RSM US LLP	**Supports with conditions** We believe the new and revised definitions and interpretations should only apply when a compliance audit is performed on a "stand-alone" basis, that is, the compliance auditor does not also audit the client's financial statements. The Exposure Draft indicates that compliance audits could encompass reports issued in accordance with AU-C sections 725, Supplementary Information in Relation to the

		Financial Statements as a Whole, 805, Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts, or Items of Financial Statement, 806, Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements or 935, Compliance Audits. However, AU-C sections 725, 805 and 806 all involve reporting on financial statements, supplementary financial information or compliance with contractual or regulatory requirements in connection with an audit of financial statements. Consequently, we do not understand how the independence requirements for the compliance audit could be bifurcated from the independence requirements for the financial statement audit and therefore that the relevant proposed changes would apply in those circumstances. We understand a compliance audit under AU-C section 935 or a compliance attestation under AT-C section 315, Compliance Attestation, could be performed by an auditor or accountant that does not audit the client's financial statements and therefore should be the focus of the new and revised definitions and revisions to the Client Affiliates and State and Local Government Client Affiliates interpretations. ***Definition of Financial Statement Attest Client*** Accordingly, to reinforce the understanding we have noted above, we believe the proposed addition to the definition in proposed paragraph .18 of ET 0.400, *Definitions*, should be revised to include that "this definition does not include a compliance audit attest client that is not also a financial statement attest client" (also see comments on the definition of "compliance audit attest client" below).
CL 14	PricewaterhouseCoopers LLP (PwC)	**Supports** We agree with the PEEC's proposal to clarify the independence requirements applicable to compliance audits and align the requirements with the applicable threats to independence. We also support the changes proposed by the Committee to establish a limited exemption from compliance with ET section 1.200.001 (the "Independence Rule") and its interpretations with respect to: (1) entities that report trivial and clearly inconsequential amounts on the reporting entity's schedule or

		statement and are not subject to the member's compliance audit procedures, and (2) affiliates of entities that meet the proposed definition of a "compliance audit attest client." We agree with the Committee that the proposed approach appropriately considers the threats to the member's objectivity and impartiality created by interests in and relationships with those entities that are in scope of the limited exemption. However, as described further in Appendix A, we recommend that the PEEC align the proposed definition of a "compliance audit" with the definition used in AU-C section 935, *Compliance Audits,* paragraph 11.
CL 15	National Association of State Boards of Accountancy (NASBA)	**Supports** Staff note: They believe the revisions should be clarified but agree with the exceptions provide for through the revisions, and with the proposed effective date.
CL 16	BDO, USA LLP	**Supports** We support the PEEC's endeavor in proposing changes to the code that will provide clarity with the new definitions and minor related revisions to one definition and two interpretations. • New definition compliance audit (ET sec. 0.400.09) • New definition compliance audit attest client (ET sec. 0.400.10) • Revised definition of financial statement attest client (ET sec. 0.400.18, currently 0.400.16) • Revised "Client Affiliates" interpretation (ET sec. 1.224.010) • Revised "State and Local Government Client Affiliates" interpretation (ET sec. 1.224.020) We believe this exposure draft provides clarity and improvements to the current code.

CL 17	Deloitte LLP	**Supports** We agree that consistency and uniformity in practice will better serve the public interest and we support the PEEC's efforts to protect the public interest through facilitation of members' understanding and compliance.

Question *a*: Is the definition of "compliance audit" clear? If not, please explain how it should be clarified.		
Yes: 9 No: 6 No response: 2		
CL 1	Terrill W. Ramsey	**No response**
CL 2	National State Auditors Association	**Yes**
CL 3	Office of the Washington State Auditor	**Yes**
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**No** The definition of "compliance audit" refers to a "compliance audit attest engagement." We believe that the use of both "audit" and "attest" in the same term is redundant and unnecessary. All audit engagements are, by definition, attest engagements. Therefore, all "compliance audit" engagements are attest engagements and do not require the addition of "attest" to identify the engagement appropriately. Contrast this to the definition of a "financial statement attest client" where the attest engagement could be an audit, a review, or a compilation where the accountant is independent of the client. The specific nature of the attest engagement is unclear in the "financial statement attest client" term, while in the "compliance audit attest engagement" the member already knows it is an audit engagement, and therefore should understand an audit engagement to be an attest

		engagement. We propose discontinuing use of the term “compliance audit attest engagement.”
CL 5	Tennessee Comptroller of the Treasury	**Yes**
CL 6	U.S. Government Accountability Office (GAO)	**No** The compliance audit definition in paragraph .09 states that a compliance audit is an “attest engagement that is performed under the Statements on Auditing Standards when the member is requested to report on an entity’s compliance with specific requirements.” It further states that a “compliance audit attest engagement may include multiple compliance audit attest clients.” Although the definition asserts that a compliance attest engagement may have multiple compliance attest clients, it does not explain how or why this could happen or the implications of having multiple attest clients. It also does not address whether there will be separate engagements for each attest client, or whether there will be separate auditor’s reports or one auditor’s report. We believe the definition could be improved by incorporating additional explanatory information to make it more clear and understandable. The compliance audit definition in paragraph .09 also states that “For example, multiple compliance audit attest clients may have amounts included in a schedule of expenditures of federal awards (SEFA) in a compliance audit performed in accordance with the Uniform Guidance.” Paragraph .09 does not sufficiently elaborate on “multiple compliance audit attest clients.” The example is unclear and does not explain or illustrate how there could be multiple compliance audit attest clients that have amounts on the SEFA in a compliance audit performed in accordance with title 2 of the *U.S. Code of Federal Regulations*, part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance).

		In addition, paragraph 28 provides another example that states “For example, a state government compliance audit subject to Uniform Guidance may include hundreds of entities (departments, agencies, component units) reporting federal program expenditures on a reporting entity’s SEFA. Federal program expenditures on the SEFA could total over $1 billion.” This example is unclear and fails to illustrate how there could be multiple compliance audit attest clients with amounts on a SEFA.
CL 7	CliftonLarsonAllen LLP (CLA)	**Yes**
CL 8	Grant Thornton LLP	**Yes** Grant Thornton agrees with items a. through g. noted as specific request for comment in the Exposure Draft and does not have any specific comments to share as a response to these questions.
CL 9	Texas Society of CPAs (TXCPA)	**Yes** The PSC [Professional Standards Committee of the Texas Society of CPAs] believes the revised definitions are adequate and assist in clarifying applicability of independence rules. The revised definitions appear to accurately carve out exceptions to the existing rules.
CL 10	Auditor of Public Accounts (Virginia APA)	**Yes** We support the proposed new definition of “compliance audit,” which provides an appropriate categorization for evaluating independence to meet the needs of applicable report users. We further believe the clarity of the definition and related examples will result in consistent application.
CL 11	Crowe LLP	**Yes**

CL 12	KPMG LLP	**Yes** We concur with PEEC's position regarding the questions presented for specific comment, so we did not respond to each question individually.
CL 13	RSM US LLP	**No** We recommend that the second sentence of the first paragraph be revised to read, "For example, the member may report on compliance under governmental audit requirements, such as the Uniform Guidance in accordance with AU-C section 935" (i.e., remove the reference to AU-C section 806 as explained above). In the second paragraph of the definition, we also recommend that "attest engagement" not be included when using the term "compliance audit": "A *compliance audit* ~~attest engagement~~ may include multiple…"
CL 14	PricewaterhouseCoopers LLP (PwC)	**No** According to AU-C section 806, Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements, "the objective of the auditor is to report appropriately on an entity's compliance with aspects of contractual agreements or regulatory requirements in connection with the audit of financial statements" [emphasis added]. AU-C 806.01 "addresses the auditor's responsibility when the auditor is requested to report on an entity's compliance with aspects of contractual agreements or regulatory requirements, insofar as they relate to relate to accounting matters, in connection with an audit of the financial statements" and that "[s]uch a report is commonly referred to as a by-product report." Additionally, AU-C 806.07 and .12-.13 describe the required elements of the auditor's report on compliance with aspects of contractual agreements or regulatory requirements. The auditor is only required to provide negative assurance on the compliance matter that is the subject of the report.

		The auditor's report on an entity's compliance issued pursuant to AU-C section 806 is not the result of a standalone engagement; rather, the report is a communication provided in connection with the audit of financial statements as a by-product of the audit. Therefore, the entity is considered a "financial statement attest client" as defined in ET section 0.400.16 (0.400.18 of the proposed revisions) of the Code of Conduct and the auditor would be required to be independent of that entity pursuant to the Independence Rule and all of its applicable interpretations, including the "Client Affiliates"' interpretation (ET section 1.224.010) and (when relevant) the "State and Local Government Client Affiliates" interpretation (ET section 1.224.010 and 1.224.020 of the proposed revisions). The limited independence exceptions established under the proposed revisions would not apply because the compliance report is a report prepared as part of an engagement to audit financial statements. We recommend that references to AU-C section 806 be removed from the definition of a "compliance audit." In contrast to AU-C section 806, AU-C section 935 provides for an auditor to express a standalone report and opinion on an entity's compliance with the subject of the compliance audit, such as an entity's compliance with Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* ("Uniform Guidance") applicable to federal awards. AU-C section 935 "does not apply to the financial statement audit component of [compliance audits]" (AU-C 935.02) and the auditor's compliance report issued pursuant to AU-C 935 is not a by-product of the financial statement audit. When the auditor is engaged or required by law or regulation to provide an opinion about whether, in all material respects, an entity has "complied" with the requirements of specified laws, statutes, regulations, rules, and provisions of contracts or grant agreements or whether management's assertion about the entity's "compliance" with specified requirements is fairly stated, that engagement would be performed in accordance with either AU-C section 935 or AT-C section 315, *Compliance Attestation*. Beyond the proposed definition of a "compliance audit," paragraph 6 of the

		exposure draft's explanatory memo also explains that, in addition to reporting under AU-C section 806 or 935, for example, a compliance audit engagement may also require reporting on the accuracy of a schedule, such as a schedule of expenditure of federal awards, or statement, under AU-C section 725 or 805. Engagements to report on compliance matters under AU-C section 935 are required to include an auditor's report on a schedule of expenditures of federal awards (SEFA). The SEFA is a supplemental schedule to the audited financial statements that determines the applicability and scope of the single audit under Uniform Guidance. The auditor's report on an entity's SEFA is prepared in accordance with AU-C section 725, *Supplementary Information in Relation to the Financial Statements as a Whole*. AU-C 725.03 states that "[t]he objective of the auditor, when engaged to report on supplementary information in relation to the financial statements as a whole, is to (a) evaluate the presentation of the supplementary information in relation to the financial statements as a whole and (b) report on whether the supplementary information is fairly stated, in all material respects, in relation to the financial statements as a whole." As it relates to the SEFA, the objective of the auditor is to report on the expenditures of federal awards included in the schedule as being fairly presented in relation to the entity's financial statements. The report under AU-C 725 does not specifically address whether the SEFA is presented in compliance with the elements required by Uniform Guidance. Similarly, the auditor's report on a schedule prepared in accordance with AU-C section 805, Special Considerations — Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement, does not specifically address compliance with any set of preparation guidelines. Paragraph 6 of the exposure draft's explanatory memo could be interpreted to mean that a "compliance audit" extends to the accompanying schedules reported on under either AU-C section 725 or AU-C section 805. We suggest that the Committee clarify that, similar to the by-product report provided pursuant to AU-C 806, AU-C 725 and AU-C 805 audits are not considered a "compliance audit" for the purposes

		of applying the proposed independence exceptions. As an overarching recommendation in light of the comments described above, we suggest that, in lieu of the first paragraph of the proposed "compliance audit" definition, the Committee either adopt the same language of the definition of a "compliance audit" in AU-C section 935.11 or incorporate the definition in AU-C section 935.11 by reference. This approach would eliminate the risk that the proposed independence exceptions are inappropriately applied to audits of financial statements performed under AU-C section 725 or AU-C section 806 or to engagements performed under AU-C section 805. *Nonattest services for compliance audit attest clients* The "Engagements, Other Than AUPs, Performed in Accordance With SSAEs" interpretation (ET section 1.297.030) establishes certain independence exceptions for engagements to issue reports in accordance with the AICPA Statements on Standards for Attestation Engagements (SSAEs). One of those exceptions relates to the member's performance of nonattest services that do not relate to the specific subject matter of the SSAE engagement. Specifically, the interpretation states that, when providing nonattest services that would otherwise impair independence under the interpretations of the "Nonattest Services" subtopic (ET section 1.295), threats would be at an acceptable level and independence would not be impaired if (1) the nonattest services do not relate to the specific subject matter of the SSAE engagement, and (2) the "General Requirements for Performing Nonattest Services" interpretation (ET section 1.295.040) of the Independence Rule are met when providing the nonattest service. We recommend that the PEEC consider adopting a similar approach for compliance audits. That is, the PEEC should consider amending the Code of Conduct to establish that a member's independence would not be considered impaired due to the provision of otherwise prohibited nonattest services to a compliance audit attest client provided that the services do not relate to the specific compliance matter that is the subject of the compliance audit and the member complies with the "General

		Requirements for Performing Nonattest Services" interpretation. Given that the primary objective of a compliance audit is to report on an entity's compliance with specific requirements, nonattest services that do not relate to the specific compliance matter that is the subject of the compliance audit are unlikely, in our view, to pose threats to independence. Additionally, such an exception for nonattest services would create further consistency between the independence approach for compliance audits performed under AU-C 935 and the approach for compliance examinations performed under AT-C 315.
CL 15	National Association of State Boards of Accountancy (NASBA)	**No** We do not believe that AU-C 806 engagements should be included in the scope of the Exposure Draft. In an AU-C 806 engagement, the primary focus is an opinion on the financial statements and any reporting on compliance is a "by-product" (to use the terms in AU-C 806) of the financial statement audit. In other words, while there may be reporting on compliance, it is inseparable from the financial statement audit and independence in the financial audit context must be applied. Conversely, in an AU-C 935 engagement, the primary focus of the compliance audit is to report on the entity's compliance and it may be possible to separate consideration of independence for entities within the compliance audit client (assuming that they meet the criteria). As a result, we believe that AU-C 806 engagements should not be subject to the proposed revisions in this Exposure Draft. NASBA believes that additional clarity could be achieved if the definition of compliance audit was expanded to include non-governmental examples of what might constitute a compliance audit, such as a large, multi-location commercial publicly traded company; a real estate developer subject to a compliance audit in connection with the terms of lease agreements (if AU-C 806 engagements are retained in the scope of the Exposure Draft) and government grants; and for-profit entities required to undergo compliance audits as a result of the receipt of federal pandemic loans and/or grants.

CL 16	BDO, USA LLP	**No response**
CL 17	Deloitte LLP	**No** The proposed definition of "compliance audit" is not clear due to: • inconsistency with the definition of a "compliance audit" in AU-C 935 *Compliance Audits* ("AU-C 935"), potentially broadening the proposed definition to include engagements that are not compliance audits as defined by AU-C 935 • inclusion of other examples in the exposure draft background narrative that may create confusion and misinterpretation of the proposed definition Please see our detailed response at Appendix 1. (From Appendix 1 about the definition of "compliance audit") Inconsistency with AU-C 935 definition of "compliance audit" The primary inconsistency between the proposed definition and AU-C 935 is that the proposed definition goes beyond the population of engagements that are subject to AU-C 935. Specifically, compared to the proposed definition, the extant definition and text of AU-C 935: 1) does not include engagements performed under AU-C sections other than AU-C 935 in the scope of the AU-C 935 definition of compliance audits, 2) limits the scope of AU-C 935 to governmental audit engagements, and 3) explicitly states that AU-C 806 does not apply to compliance audits as defined in AU-C 935. As explained below, we believe the proposed definition of a compliance audit should be consistent with the extant definition in AU-C 935 and should not include AU-C 806 engagements. • First, the proposed definition of "compliance audit" includes reports on

		compliance under AU-C 806 Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements (“AU-C 806”), while the extant AU-C 935 definition does not include AU-C 806 engagements. The AU-C 935 definition is shown below: **Compliance audit.** A program-specific audit or an organization wide audit of an entity's compliance with applicable compliance requirements. By including AU-C 806 engagements, the proposed definition goes beyond the scope of the extant AU-C 935 definition and creates two different definitions of “compliance audits” in the professional standards. This may cause the reader to interpret the proposed definition as expanding the population of compliance audits to non-governmental compliance audit engagements, which may relate to for-profit commercial entities and be subject to rules of other regulators. • Secondly, AU-C 935 stipulates in paragraphs .01-.02 (see below) that the scope of AU-C 935 is limited to governmental audit engagements (i.e., Single Audits). In addition, the AU-C Appendix explicitly indicates all paragraphs of AU-C 806 are not applicable to compliance audits as defined in AU-C 935 (see below). The addition of a diverging definition of a compliance audit that has a broader scope than the extant professional standards will amplify complexity and cause confusion and misapplication for readers. The specific relevant excerpts from AU-C 935 are presented below. **AU-C 935 paragraphs .01-.02** *.01 Governments frequently establish governmental audit requirements for entities to undergo an audit of their compliance with applicable compliance requirements. This section is applicable when an auditor is engaged, or required by law or regulation, to perform a*

compliance audit in accordance with all the following:

- *Generally accepted auditing standards (GAAS)*
- *The standards for financial audits under Government Auditing Standards*
- *A governmental audit requirement that requires an auditor to express an opinion on compliance (Ref: par. .A1–.A2)*

.02 This section addresses the application of GAAS to a compliance audit. Compliance audits usually are performed in conjunction with a financial statement audit. This section does not apply to the financial statement audit component of such engagements. Although certain AU-C sections are not applicable to a compliance audit, as identified in the appendix "AU-C Sections That Are Not Applicable to Compliance Audits," all AU-C sections other than this section are applicable to the audit of financial statements performed in conjunction with a compliance audit.

AU-C 935 Appendix excerpt:

AU-C Section	Paragraphs Not Applicable to Compliance Audits
806, *Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements*	All

- Lastly, in addition to the primary inconsistencies discussed above, there are other notable distinctions between AU-C 935 and AU-C 806 that are not addressed in the exposure draft:
  - Reports on compliance under AU-C 806 offer *negative assurance* (i.e., “nothing came to the auditor's attention that caused the auditor

		to believe that the entity failed to comply with specified aspects of the contractual agreements or regulatory requirements, insofar as they relate to accounting matters" (AU-C 806.07). In comparison, AU-C 935 engagements require the auditor to express an opinion on compliance (AU-C 935.01). ○ AU-C 806 engagements are in connection with audited financial statements (a byproduct report) and explicitly distinguished from compliance audits in the extant professional standards as noted above. These additional distinctions further highlight the importance clarity and consistency between the proposal and the extant professional standards. In summary, as noted above we believe the proposed definition of compliance audits should be consistent with the extant definition in AU-C 935 and should not include AU-C 806 engagements. However, if PEEC decides to remain inconsistent with AU-C 935, we suggest adding a statement as shown below indicating the definition should not be applied outside the Independence Rule (ET 1.200). Suggested additions appear in ***bold italicized*** text below. **0.400. Definitions** **.09** Compliance audit. An attest engagement that is performed under the Statements on Auditing Standards when the member is requested to report on an entity's compliance with specific requirements. For example, the member may report on compliance requirements of a contractual agreement or regulatory requirements in accordance with AU-C section 806, or report on compliance under governmental audit requirements, such as the Uniform Guidance, in accordance with AU-C section 935. ***This definition is solely for the purpose of applying the "Independence Rule" [1.200.001] and its interpretations and should not be used or***

relied upon in any other context.

A compliance audit attest engagement may include multiple compliance audit attest clients. For example, multiple compliance audit attest clients may have amounts included in a schedule of expenditures of federal awards in a compliance audit performed in accordance with the Uniform Guidance.

There is precedent for such qualifying language elsewhere in the AICPA Code, specifically in the definition of "partner equivalents" (ET 0.400.38), which contains a statement that the definition is not to be relied upon for non-independence purposes. Our understanding is this language was included to avoid confusion and misapplication of the definition in contexts outside the AICPA Code.

Inclusion of other examples in the exposure draft narrative:

Paragraph 6 of the exposure draft explanatory material cites AU-C Section 725 *Supplementary Information in Relation to the Financial Statements as a Whole* ("AU-C 725") and AU-C Section 805 *Special Considerations — Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement* ("AU-C 805") as examples of additional reporting as part of a compliance audit engagement, but there are no citations of these examples included in the proposed definition of compliance audit. The purpose of these examples is not clear, given there was no substantive discussion in the background and the examples were not included in the proposed definition. We agree with the omission, as AU-C 935 explicitly excludes AU-C 725 and AU-C 805 from applicability to compliance audits:

AU-C Section	Paragraphs Not Applicable to Compliance Audits
725 *Supplementary Information in Relation to the Financial Statements as a Whole*	All
805 *Special Considerations — Audits of Single Financial*	All

		Statements and Specific Elements, Accounts, or Items of a Financial Statement However, if PEEC does not make any clarifying edits to the proposed definition of compliance audits and intends to include such engagements in the scope of the proposed definition, we believe PEEC should address the connection between the proposal and the examples in background for conclusions documents or non-authoritative guidance with robust examples and scenarios illustrating the application of the standard.

Question b: Is the definition of "compliance audit attest client" clear? If not, please explain how it should be clarified.		
Yes: 8 No: 8 No response: 1		
CL 1	Terrill W. Ramsey	**No** Phrase "trivial and clearly inconsequential" – From a search of current Code of Professional Conduct "Code" I only find where this phrase is used once. I do not find where the word "trivial" is used other than in this phrase. I find twice where the term "clearly inconsequential" is used other than in this phrase (1.180.101 paragraph 10 and 2.180.010 paragraph .10) and both times without the word trivial. Use of the term "clearly inconsequential" without "trivial in one place in the Code and use of it in the proposed new definition in the phrase trivial and clearly inconsequential implies "trivial" and "clearly inconsequential" have different meanings or else why would both be needed one place and not the other. Also, if both have same meaning, why would both be needed? Based on web searches and Word thesaurus I find the words trivial and inconsequential to be synonyms. In the proposed definition of compliance audit attest client, the phrase "trivial and clearly inconsequential" becomes more important and should be clearly defined and consistently used. I believe the Code using concept intended by this phrase increases the chance of it

		being used as a precedent later in other places for compliance audits standards/guidance making it more important to be clear in the proposed change. The Yellow Book in 6.48 allows the auditor to use judgment in how to report noncompliance which is clearly inconsequential, however based upon the $1,000 federal expenditure example in item 30, it appears intention in ED is for a much lower level than current "management letter comment" threshold. Suggestions: • If intention is that trivial and clearly inconsequential have different meanings, then add definition of each in way to show difference. • If intention is they mean the same, pick one of the terms or a new term and define. Using two terms with intention they have same meaning is both redundant and confusing. • The definition of term used in compliance audit attest client definition for trivial and clearly inconsequential concept needs to be clear to convey the intention shown by the $1,000 out of $1 billion example in paragraphs 28 through 30. Such clarity is key to promoting consistency of practice. I believe this example is good and the definition needs to convey a much lower threshold than in the Yellow Book 6.48.
CL 2	National State Auditors Association	**Yes**
CL 3	Office of the Washington State Auditor	**Yes** Staff note: Provided comments on trivial and inconsequential as part of their response to question c. below, and not as part this question.
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**No** Again, the term "attest" is redundant and so the definition should be changed to "compliance audit client." All audit engagements are attest engagements. The definition is not entirely clear because the client is defined by what traits the engagement does not have rather than what traits it does have. We believe that

		when a firm has been engaged to perform a compliance audit in accordance with AU-C 806 or 935, then the firm has a compliance audit client. This definition does not address situations where the member firm is engaged by someone other than the entity upon which compliance audit procedures will be applied. For example, a school district hires a firm to perform compliance audits on charter schools in their district on compliance with the terms of the schools' charter agreements. In a charter school audit, the types of issues that one tests include whether the charter school had the requisite number of fire drills during the year, did they submit the requisite attendance records to the district for the school year, or does the charter school use only non-toxic art supplies. Under this scenario, the school district would not meet the definition of the "compliance audit attest client" because no procedures are performed on the district and there are no amounts in the report material, trivial or otherwise. And yet, these types of compliance audits are common.
CL 5	Tennessee Comptroller of the Treasury	**Yes**
CL 6	U.S. Government Accountability Office (GAO)	**No** The compliance audit attest client definition paragraph .10 states that "an entity with respect to which a compliance audit is performed, unless the entity (a) is not subject to compliance audit procedures and (b) reports amounts that are trivial and clearly inconsequential. When an entity meets this definition, it is not considered a financial statement attest client." The underlying rationale for including paragraph .10 (a) "unless the entity is not subject to compliance audit procedures" in the proposed definition is unclear. We believe the definition could be improved by incorporating additional explanatory

		information to make it more clear and understandable. The compliance audit attest client definition paragraph .10 (b) states that unless the entity reports amounts that are "trivial and clearly inconsequential" the entity would not be a compliance audit attest client if both (a) and (b) are met. However, the context and the basis for which the auditor is to determine trivial and clearly inconsequential is undefined. We suggest that trivial and clearly inconsequential be defined within the context of the proposed paragraph.[2] [2]"Trivial" is similar to "clearly trivial" defined in AU-C 450, *Evaluation of Misstatements Identified During the Audit*, para. .05, for financial statement audits.
CL 7	CliftonLarsonAllen LLP (CLA)	**No** CLA believes that the definition of "compliance audit attest client" would be clearer if it was emphasized that the exception applies when there are multiple entities and that both conditions must be met in order for a client to not meet the definition of a compliance audit attest client. Proposed wording: "~~An~~ **A reporting** entity with respect to which a compliance audit is performed. ~~unless the entity~~ **To the extent the reporting entity contains multiple entities, an individual entity would not be considered a compliance audit attest client if that particular entity**: a. is not **likely to be** subject to compliance audit procedures and b. reports amounts that are trivial and clearly inconsequential. When an entity meets this definition, it is not considered a financial statement attest client."
CL 8	Grant Thornton LLP	**Yes** Grant Thornton agrees with items a. through g. noted as specific request for comment in the Exposure Draft and does not have any specific comments to share as a response to these questions.

CL 9	Texas Society of CPAs (TXCPA)	**No** The definition appears to explain what is not a compliance audit attest client rather than what is a compliance audit attest client. However, the definition does provide helpful guidance for compliance audits not performed in conjunction with financial statement audits.
CL 10	Auditor of Public Accounts (Virginia APA)	**Yes**
CL 11	Crowe LLP	**Yes**
CL 12	KPMG LLP	**Yes** We concur with PEEC's position regarding the questions presented for specific comment, so we did not respond to each question individually.
CL 13	RSM US LLP	**No** We believe the definition should be revised to exclude entities that are also financial statement attest clients as follows: "An entity, other than a financial statement attest client, with respect to which a compliance audit is performed, unless …" We also do not believe the final sentence should be included within the definition as a compliance audit attest client could also be financial statement attest client. We recommend "clearly" precede "trivial" in order that it modify both trivial and inconsequential to be consistent with how similar concepts are articulated in other standards, and consequentially remove "clearly" that precedes inconsequential (i.e., would be articulated as "clearly trivial and inconsequential").
CL 14	PricewaterhouseCoopers LLP (PwC)	**Yes**

CL 15	National Association of State Boards of Accountancy (NASBA)	**No** NASBA believes that the definition of "compliance audit attest client" would be enhanced if the phrase "trivial and clearly inconsequential" were replaced with the term "clearly trivial." The term "clearly trivial" is defined in AU-C Section 450.A2. In many circumstances, the independent auditor performing a financial statement audit will also be engaged to perform a compliance audit for the same client. Greater clarity and consistency would be achieved if the extant term as defined in Generally Accepted Auditing Standards were used in the Code.
CL 16	BDO, USA LLP	**No response**
CL 17	Deloitte LLP	**No** See comments in response to Q2a above regarding revisions to the proposed "compliance audit attest client" definition. While we agree with the notion of applying a trivial and clearly inconsequential ("TCI") test, we have several concerns and requests for clarification regarding its application as outlined in Appendix 1. These concerns may be best addressed through non-authoritative guidance for members, which should include robust examples. (From Appendix 1 about the definition of "compliance audit attest client") • There is no reasonable third-party test or guidance regarding the viewpoint from which the amounts should be TCI. AU-C 935 notes that in a compliance audit, materiality is influenced by the needs of grantors (AU-C 935.A8). It is not clear from whose viewpoint amounts should be considered TCI. • There is no point of reference for determining whether an amount is TCI. Without specific application guidance, there is a risk that the reader will assess TCI in a vacuum without considering other amounts or factors, such as the compliance audit attest client's financial statements or the program itself.

		○ Compare this to the approach to materiality in AU-C 935.A7, which states that materiality is in relation to the government program as a whole and can be specified by the governmental audit requirement. It is not clear whether the same applies to evaluation of TCI under the proposal. ○ The term TCI also appears in the *State and Local Government Client Affiliates* interpretation (ET 1.224.020) and is accompanied by a statement that TCI is in relation to the financial statements as a whole. However, the proposal remains silent on what amounts should be compared to when evaluating whether an amount is TCI. We suggest either including such guidance in the proposed revisions or providing non-authoritative guidance to clarify this important aspect of evaluating whether amounts are TCI. • The terms immaterial and TCI may be viewed as having the same meaning in practice, and additional guidance would facilitate members' compliance and understanding. For example, are there qualitative factors that would make an entity more than TCI, as qualitative factors would also impact the evaluation of materiality? We suggest nonauthoritative guidance to assist members' understanding of how applying the concept of TCI is different from evaluating materiality. • We suggest guidance regarding inadvertent breaches due to subsequent changes in TCI amounts. What should a member do if amounts are TCI at a point in time, but circumstances change after the report is issued making those amounts more than TCI? The possibility of inadvertent breaches increases in these scenarios and warrant additional guidance to avoid unintended consequences for members and clients.

Question c: Do you agree that there should be an exception to the independence requirements in a compliance audit for entities that are not subject to compliance audit procedures and report amounts that are trivial and clearly inconsequential? If you disagree, please explain why.		
Yes: 13 No: 1 No response: 3		
CL 1	Terrill W. Ramsey	**No response**
CL 2	National State Auditors Association	**Yes** We agree with this exception. Multiple entities reporting amounts on the reporting entity's schedule of state or federal awards could report trivial or inconsequential amounts. Relationships with these types of entities are unlikely to create significant independence threats, and absent an exception, the cost of compliance would outweigh the benefits. Although we agree with the exception, the example of $1,000 out of $1 billion in paragraph 30 (of the exposure draft) is excessively conservative and could diminish its use if auditors perceive this as a guideline for applying the exception.
CL 3	Office of the Washington State Auditor	**Yes** However, we noticed the exposure draft uses the term "trivial and clearly inconsequential." We would suggest the term "clearly trivial" be used instead, since this is the term used and defined in AU-C 450.05. We see no conceptual reason for auditors to calculate different thresholds for purposes of determining applicability of this independence requirement and for actually conducting the audit. If the threshold is intended to be the same – which we presume to be the case – then the same term should be used. Alternatively, we also think it would be appropriate for this threshold to be raised to "immaterial." If the entity is not subject to audit procedures and amounts reported are also immaterial to the schedule, it would – by definition – neither have an impact

		on the audit nor on users.
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**No** Because compliance audits often do not report on **any** amounts, we do not believe that trivial or inconsequential amounts are an appropriate exemption criterion.
CL 5	Tennessee Comptroller of the Treasury	**Yes** We agree exceptions should exist to the independence requirements in a compliance audit for entities not subject to compliance audit procedures and report amounts that are trivial and clearly inconsequential.
CL 6	U.S. Government Accountability Office (GAO)	**No response**
CL 7	CliftonLarsonAllen LLP (CLA)	**Yes**
CL 8	Grant Thornton LLP	**Yes** Grant Thornton agrees with items a. through g. noted as specific request for comment in the Exposure Draft and does not have any specific comments to share as a response to these questions.
CL 9	Texas Society of CPAs (TXCPA)	**Yes** The PSC agrees that exceptions to the independence rules as explained in the exposure draft are logical and adequate.
CL 10	Auditor of Public Accounts (Virginia APA)	**Yes** We agree there should be an exception to the independence requirements in a compliance audit for entities that are not subject to compliance audit procedures and

		report amounts that are trivial and clearly inconsequential. Specifically, we agree with the explanations of the objectives of a compliance audit in paragraphs nine through 16 as supporting basis for applying different independence requirements to a compliance audit attest client than a financial statement attest client, including the two exceptions proposed in the request for comment.
CL 11	Crowe LLP	**Yes**
CL 12	KPMG LLP	**Yes** We concur with PEEC's position regarding the questions presented for specific comment, so we did not respond to each question individually.
CL 13	RSM US LLP	**Yes** We agree that there should be an exception to the independence requirements in a compliance audit for entities that are not subject to compliance audit procedures and report amounts that are trivial and clearly inconsequential (see our prior comment regarding the second condition (reports amounts that are trivial and clearly inconsequential)).
CL 14	PricewaterhouseCoopers LLP (PwC)	**Yes**
CL 15	National Association of State Boards of Accountancy (NASBA)	**Yes** NASBA agrees that there should be an exception to the independence requirements in a compliance audit for entities that are not subject to compliance audit procedures and report amounts that are trivial and clearly inconsequential. See b. above concerning the use of the term "trivial and clearly inconsequential."
CL 16	BDO, USA LLP	**No response**

CL 17	Deloitte LLP	**Yes** Notwithstanding our comments above and our concerns regarding the application of a TCI test, we agree there should be an exception for such entities in a compliance audit, given that threats are unlikely to be significant as it relates to such entities and their affiliates.

Question d: Do you agree that the affiliates interpretations should not apply in a compliance audit? If you disagree, please explain why.		
Yes: 13 No: 1 No response: 3		
CL 1	Terrill W. Ramsey	**No response**
CL 2	National State Auditors Association	**Yes**
CL 3	Office of the Washington State Auditor	**Yes** Since a compliance audit is different in nature from a financial audit.
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**No** We believe that this issue is already adequately addressed in the affiliates interpretations which specifically state that they apply to financial statement attest clients.
CL 5	Tennessee Comptroller of the Treasury	**Yes**
CL 6	U.S. GAO	**No response**

CL 7	CliftonLarsonAllen LLP (CLA)	**Yes**
CL 8	Grant Thornton LLP	**Yes** Grant Thornton agrees with items a. through g. noted as specific request for comment in the Exposure Draft and does not have any specific comments to share as a response to these questions.
CL 9	Texas Society of CPAs (TXCPA)	**Yes**
CL 10	Auditor of Public Accounts (Virginia APA)	**Yes** We strongly agree that affiliates interpretations should not apply in a compliance audit on the basis that significant threats to independence generally do not exist for relationships and circumstances with affiliates of a compliance audit attest client, as described in paragraph 36.
CL 11	Crowe LLP	**Yes**
CL 12	KPMG LLP	**Yes** We concur with PEEC's position regarding the questions presented for specific comment, so we did not respond to each question individually.
CL 13	RSM US LLP	**Yes**
CL 14	PricewaterhouseCoopers LLP (PwC)	**Yes**
CL 15	National Association of State Boards of	**Yes** Assuming that the guidance relates solely to AU-C 935 engagements, NASBA

	Accountancy (NASBA)	agrees that the affiliates interpretations should not apply in a compliance audit.
CL 16	BDO, USA LLP	**No response**
CL 17	Deloitte LLP	**Yes** Notwithstanding our comments and concerns noted above regarding the application of a TCI test, we agree the affiliates interpretation should not apply in a compliance audit when amounts are not subject to compliance audit procedures and are TCI.

Question e: Do you agree that the revision in each of the affiliates interpretations serves as a useful reminder that these interpretations do not apply to specific attest engagements (e.g. compliance audits and engagements performed under the SSAEs)? If you disagree, please explain why.		
Yes: 13 No: 1 No response: 3		
CL 1	Terrill W. Ramsey	**No response**
CL 2	National State Auditors Association	**Yes**
CL 3	Office of the Washington State Auditor	**Yes** This is helpful to alert practitioners to the exception when looking at the affiliates interpretation.
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**No** ET sec.1.224.010.01-.04 already makes clear that the interpretation applies to financial statement attest clients. Therefore, we believe that a specific reminder than the section does not apply to specific attest engagements may be useful, but not required.

CL 5	Tennessee Comptroller of the Treasury	**Yes**
CL 6	U.S. Government Accountability Office (GAO)	**No response**
CL 7	CliftonLarsonAllen LLP (CLA)	**Yes** CLA does agree if the auditor is performing only the compliance audit.
CL 8	Grant Thornton LLP	**Yes** Grant Thornton agrees with items a. through g. noted as specific request for comment in the Exposure Draft and does not have any specific comments to share as a response to these questions.
CL 9	Texas Society of CPAs (TXCPA)	**Yes** The PSC agrees that the revisions in the affiliates' interpretations provide clarification on what does and does not constitute a financial statement audit. The proposed guidance should eliminate confusion in this determination.
CL 10	Auditor of Public Accounts (Virginia APA)	**Yes**
CL 11	Crowe LLP	**Yes**
CL 12	KPMG LLP	**Yes** We concur with PEEC's position regarding the questions presented for specific comment, so we did not respond to each question individually.
CL 13	RSM US LLP	**Yes**

		Since the existing interpretations apply to financial statement attest clients rather than financial statement audits, we believe the proposed additions in each of the affiliates interpretations should be revised to state, “This interpretation does not apply to a compliance audit attest client or …”
CL 14	PricewaterhouseCoopers LLP (PwC)	**Yes** We agree that proposed paragraph .05 in the “Client Affiliates” interpretation and proposed paragraph .07 in the “State and Local Government Client Affiliates” interpretation serve as a necessary clarification that those interpretations do not apply to compliance audits and engagements performed in accordance with the AICPA Statements on Standards for Attestation Engagements.
CL 15	National Association of State Boards of Accountancy (NASBA)	**Yes**
CL 16	BDO, USA LLP	**No response**
CL 17	Deloitte LLP	**Yes**

Question f: Do you agree that entities that are not subject to compliance attestation procedures in an engagement performed under the SSAEs are not considered responsible parties and therefore are not subject to the "Independence Standards for engagements Performed in Accordance with Statements on Standards for Attestation Engagements" subtopic (ET section 1.297)? If you disagree, please explain why.		
Yes: 13 No: 1 No response: 3		
CL 1	Terrill W. Ramsey	**No response**
CL 2	National State Auditors Association	**Yes**
CL 3	Office of the Washington State Auditor	**Yes**
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**No** We do not necessarily agree. As with any attest or assurance engagement, the engaging party is not necessarily the responsible party. However, one would want to be independent with respect to the engaging party in such a situation. So, while it is true that if the entity that is not subject to the compliance attestation procedures is not the responsible party, the member should still be independent with respect to them. This is the underlying problem with the proposed definition of compliance audit attest client which relies on the client being the entity upon which compliance procedures are performed.
CL 5	Tennessee Comptroller of the Treasury	**Yes**
CL 6	U.S. Government Accountability Office (GAO)	**No response**

CL 7	CliftonLarsonAllen LLP (CLA)	**Yes**
CL 8	Grant Thornton LLP	**Yes** Grant Thornton agrees with items a. through g. noted as specific request for comment in the Exposure Draft and does not have any specific comments to share as a response to these questions.
CL 9	Texas Society of CPAs (TXCPA)	**Yes**
CL 10	Auditor of Public Accounts (Virginia APA)	**Yes**
CL 11	Crowe LLP	**Yes**
CL 12	KPMG LLP	**Yes** We concur with PEEC's position regarding the questions presented for specific comment, so we did not respond to each question individually.
CL 13	RSM US LLP	**Yes**
CL 14	PricewaterhouseCoopers LLP (PwC)	**Yes**
CL 15	National Association of State Boards of Accountancy (NASBA)	**Yes**
CL 16	BDO, USA LLP	**No response**

CL 17	Deloitte LLP	**Yes**

Question g: Do you agree that the effective date provides adequate time to implement the proposals? If you disagree, please explain why.		
Yes: 14 No: 0 No response: 3		
CL 1	Terrill W. Ramsey	**No response**
CL 2	National State Auditors Association	**Yes**
CL 3	Office of the Washington State Auditor	**Yes**
CL 4	New York State Society of Certified Public Accountants (NYSSCPA)	**Yes** We believe the effective date provides adequate time to implement the proposals.
CL 5	Tennessee Comptroller of the Treasury	**Yes**
CL 6	U.S. Government Accountability Office (GAO)	**No response**
CL 7	CliftonLarsonAllen LLP (CLA)	**Yes**
CL 8	Grant Thornton LLP	**Yes**

		Grant Thornton agrees with items a. through g. noted as specific request for comment in the Exposure Draft and does not have any specific comments to share as a response to these questions.
CL 9	Texas Society of CPAs (TXCPA)	**Yes** The effective date provides adequate time to implement the proposed guidance. We think that early implementation would be beneficial to smaller entities.
CL 10	Auditor of Public Accounts (Virginia APA)	**Yes**
CL 11	Crowe LLP	**Yes** We believe the effective date, with early implementation allowed, provides sufficient time and flexibility for firms to develop policies or modify existing policies and provide training as necessary to implement the proposal.
CL 12	KPMG LLP	**Yes** We concur with PEEC's position regarding the questions presented for specific comment, so we did not respond to each question individually.
CL 13	RSM US LLP	**Yes**
CL 14	PricewaterhouseCoopers LLP (PwC)	**Yes**
CL 15	National Association of State Boards of Accountancy (NASBA)	**Yes**
CL 16	BDO, USA LLP	**No response**

CL 17	Deloitte LLP	**Yes** We agree with the proposed effective date. In conjunction with the proposed timing, we suggest any non-authoritative guidance be finalized ahead of the effective date so that it is useful for members in implementing the changes into their policies and procedures.

Question h: What independence requirements applicable to compliance audits would you like further explained through nonauthoritative guidance?		
CL 1	Terrill W. Ramsey	**No response**
CL 2	National State Auditors Association	We believe additional guidance surrounding the trivial and clearly inconsequential description is needed so that auditors do not base their assessments on the $1,000 out of $1 billion example in the current draft without considering additional context and factors when exercising their professional judgement to determine what is trivial and clearly inconsequential.
CL 3	Office of the Washington State Auditor	We found the triviality example used in paragraphs 27-31 of the exposure draft to be unrealistic and therefore unhelpful. In future explanations of this exception, we would suggest a more realistic amount of $500,000 as an example of clearly trivial for a Schedule of Expenditures of Federal Awards (SEFA) that reports $1 billion. $500,000 is 5% of 1% of $1 billion, which is generally accepted as a quantitative triviality threshold. $500,000 is also well below the threshold for even a type B risk assessment on a $1 billion SEFA and thus clearly inconsequential to single audit planning.
CL 4	New York State Society of Certified Public	We suggest clarification as to the requirements for compliance with these rules by engaging parties versus responsible parties.

	Accountants (NYSSCPA)	
CL 5	Tennessee Comptroller of the Treasury	We believe the PEEC should consider defining or describing what constitutes a "compliance audit procedure" in situations other than a Single Audit using the Unform Guidance and its Compliance Supplement.
CL 6	U.S. Government Accountability Office (GAO)	**No response**
CL 7	CliftonLarsonAllen LLP (CLA)	**No response**
CL 8	Grant Thornton LLP	We suggest the nonauthoritative guidance incorporate the supporting analysis and examples provided in the Exposure Draft as well as highlight other scenarios and examples to address the following: • clarifying the scope of the revisions and definitions apply regardless of whether the compliance auditor also performs the financial statement audit but do not impact the independence requirements for attest engagements that are not considered compliance audits • reporting on a grant award or schedule of expenditures or other similar scope of services that may also be considered a compliance audit as opposed to a financial statement audit or other attestation engagement • the differences between the reporting objectives of a compliance audit versus a financial statement audit • the evaluation of the subject to audit and trivial and clearly inconsequential or the affiliate exception, including the application of professional judgment when determining what amounts are considered trivial and clearly inconsequential. For example, the following scenarios can be considered:

		- the evaluation of entities that meet the compliance audit attest client definition when the entities are determined to be subject to the compliance audit procedures without consideration of reporting trivial and clearly inconsequential amounts - scenarios when entities perform activities to support the compliance audit attest client, or the subject matter included in the compliance audit, that may result in such entities being considered a compliance audit attest client and are subject to the requirements under the "Independence Rule" as well as services for and relationships with such entities that may create independence threats - scenarios when entities do not meet the not subject to audit and trivial and clearly inconsequential exception as the entity is not subject to the compliance audit procedures but is reporting amounts that are not trivial and clearly inconsequential and services for and relationships with such entities that may create independence threats • other situations and related examples of other relationships or circumstances that may create threats to independence and the application of the "Conceptual Framework for Independence" (ET sec. 1.210.010) • scenarios when entities perform activities to support the compliance audit attest client, or the subject matter included in the compliance audit, that may result in such entities not being considered a compliance audit attest client and are subject to evaluation under the "Conceptual Framework for Independence" as well as services for and relationships with such entities that may create an independence threat.
CL 9	Texas Society of CPAs (TXCPA)	The independence requirements applicable to compliance audits have been adequately explained in the proposed guidance. The PSC believes that the independence rules should remain principal based and not rule based. Additionally, specific examples would be helpful in assisting audit firms that do not perform a lot

		of these types of engagements to determine applicability of the requirements since single audits may be newly required for some clients due to COVID relief money received.
CL 10	Auditor of Public Accounts (Virginia APA)	Define Compliance Audit Procedures We believe there is an opportunity to include further guidance on what constitutes a "compliance audit procedure" in paragraph 8. While we agree with the proposed definition of "compliance audit attest client", we believe the proposed guidance, as read currently, is not clear as to the nature or extent of procedures that would meet the definition of a "compliance audit procedure." For example, when performing a single audit of a state, an auditor may perform analytical procedures over the entirety of the state's federal awards to assist in determining Type A and B federal programs subject to single audit. Our presumption is that such procedures would not constitute compliance audit procedures for the purposes of evaluating exceptions discussed in paragraph 8. Expand Guidance over Establishing 'Trivial' Thresholds The example described in paragraph 30 provides $1,000 out of $1 billion as an appropriate threshold for determining whether amounts are trivial and clearly inconsequential. We believe this level of conservatism would negate virtually any meaningful benefit of the exception. While we understand that this is only one example, the example is the primary starting point for an auditor's considerations in the absence of additional considerations or guidance. PEEC should include in nonauthoritative guidance factors auditors may consider in exercising professional judgement to determine the amounts to be considered trivial, as discussed in paragraph 21. As an example, the guidance may address whether it is appropriate for an auditor to consider the actions or requests of intended users of a compliance audit report, for example, that an auditor must report known questioned costs when likely questioned costs are greater than $25,000 and is not required to risk assess "relatively small" programs as defined by the entity requiring the compliance audit.

CL 11	Crowe LLP	We do not believe the independence requirements applicable to compliance audits needs to be further explained through nonauthoritative guidance.
CL 12	KPMG LLP	We offer the following considerations on #18 of the Exposure Draft #18 notes, “A compliance audit may include multiple entities in the reporting entity’s schedule or statement. For example, in a compliance audit performed in accordance with Uniform Guidance for a state and local government, there may be multiple entities (departments, agencies, component units) that include amounts in the reporting entity’s schedule of expenditures of federal awards (SEFA).” This seems to indicate that an entity does not need to be a legally separate entity and can instead be a department within a legal entity. Consideration of independence at the legal entity level is standard, but we are unsure how this would work at a department level. In other words, how would a department which rolls up into an agency or component unit be considered? We recommend clarifying whether there is a legal entity concept here associated with “entity.”
CL 13	RSM US LLP	Examples of how to apply the Conceptual Framework for Independence to the new and revised definitions and revised interpretations in the circumstances described in paragraphs 41–44 of the Exposure Draft would be helpful. We find it difficult to understand how an entity responsible for compliance requirements would not be considered a compliance audit attest client.
CL 14	PricewaterhouseCoopers LLP (PwC)	We have no suggestions for the development of non-authoritative guidance beyond those topics already under consideration by the PEEC as described in the agenda materials for the Committee’s open meeting held on May 17, 2022.
CL 15	National Association of State Boards of Accountancy (NASBA)	No additional comments.

CL 16	BDO, USA LLP	No response
CL 17	Deloitte LLP	See responses to questions 2a-2g above.

Proposed revisions (redline)

Proposed additions appear in ***boldface italic***. Deletions appear in ~~strikethrough~~. Proposed revisions to the exposure draft since the August meeting are highlighted in yellow.

Text of proposed new definition "compliance audit"

0.400 Definitions

.09 **Compliance audit**. An *attest engagement* that is performed ~~under the Statements on Auditing Standards when the *member* is requested to report on an entity's compliance with specific requirements . For example, the *member* may report on compliance requirements of a contractual agreement or regulatory requirements in accordance with AU-C section 806, or report on compliance under governmental audit requirements, such as the Uniform Guidance,~~ in accordance with AU-C section 935***, including any reporting on a related schedule or statement in accordance with AU-C section 725 or 805***.

A *compliance audit* ~~*attest engagement*~~ may include multiple *compliance audit* ~~*attest*~~ *clients*. For example, multiple *compliance audit* ~~*attest*~~ *clients* may have amounts included in a schedule of expenditures of federal awards in a *compliance audit* performed in accordance with the Uniform Guidance.

Nonauthoritative questions and answers regarding *compliance audits* are available in Q&A section 10, Definitions.

Text of proposed new definition “compliance audit ~~attest~~ client”

0.400 Definitions

.10 **Compliance audit ~~attest~~ client.** An entity with respect to which a *compliance audit* is performed~~., unless the entity~~ **Members *should apply the “Independence Rule” [1.200.001] and related* interpretations *applicable to an* attest client *to the* compliance audit client.**

To the extent the* compliance audit *includes amounts from multiple entities in a schedule or statement, an entity would not be considered a* compliance audit client*, and, therefore, the “Independence Rule” [1.200.001] and related* interpretations *would not apply with respect to an entity, if that entity:

a. is not subject to compliance audit procedures and

b. ***includes*** ~~reports~~ amounts ***in the schedule or statement*** that are trivial and clearly inconsequential ***to the schedule or statement as a whole***.

When an entity meets ***the*** ~~this~~ definition ***of a* compliance audit client**, it is not considered a *financial statement attest client* ***and, therefore, the “Client Affiliates” interpretation [1.224.010] and the “State and Local Government Client Affiliates” interpretation [1.224.020] would not apply***.

Nonauthoritative questions and answers regarding *compliance audit clients* are available in Q&A section 10, Definitions.

Text of proposed revised definition “financial statement attest client”

0.400 Definitions

~~.16~~***.18*** **Financial statement attest client.** An entity whose *financial statements* are audited, reviewed, or compiled when the ***member's*** compilation report does not disclose a lack of *independence*.

This definition does not include a **compliance audit** ~~**attest**~~ **client*****. Therefore, the “Client Affiliates” interpretation [1.224.010] and the “State and Local Government Client Affiliates” interpretation [1.224.020] would not apply.***

Text of proposed revised interpretation “Client Affiliates”

~~1.224.010 Client Affiliates~~

~~[Paragraphs .01–.04 are unchanged]~~

~~***.05 This interpretation does not apply to a compliance audit or an engagement subject to the “Independence Standards for Engagements Performed in Accordance with Statements on Standards for Attestation Engagements” subtopic [1.297] of the “Independence Rule” [1.200.001].***~~

~~[Paragraphs .05–.14 are renumbered as .06–.15 but are otherwise unchanged]~~

Text of proposed revised interpretation “State and Local Government Client Affiliates”

~~1.224.020 State and Local Government Client Affiliates~~

~~[Paragraphs .01–.06 are unchanged]~~

~~**Exceptions**~~

~~***.07 This interpretation does not apply to a compliance audit or an engagement subject to the “Independence Standards for Engagements Performed in Accordance with Statements on Standards for Attestation Engagements” subtopic [1.297] of the “Independence Rule” [1.200.001].***~~

~~[Paragraphs .07–.11 are renumbered as .08–.12 but are otherwise unchanged.]~~

Proposed revisions (clean)

Text of proposed new definition “compliance audit”

0.400 Definitions

.09 **Compliance audit**. An *attest engagement* that is performed in accordance with AU-C section 935, including any reporting on a related schedule or statement in accordance with AU-C section 725 or 805.

A *compliance audit* may include multiple *compliance audit clients*. For example, multiple *compliance audit clients* may have amounts included in a schedule of expenditures of federal awards in a *compliance audit* performed in accordance with the Uniform Guidance.

Nonauthoritative questions and answers regarding *compliance audits* are available in Q&A section 10, Definitions.

Text of proposed new definition “compliance audit client”

0.400 Definitions

.10 **Compliance audit client.** An entity with respect to which a *compliance audit* is performed. *Members* should apply the “Independence Rule” [1.200.001] and related *interpretations* applicable to an *attest client* to the *compliance audit client*.

To the extent the *compliance audit* includes amounts from multiple entities in a schedule or statement, an entity would not be considered a *compliance audit client*, and, therefore, the “Independence Rule” [1.200.001] and related *interpretations* would not apply with respect to an entity, if that entity:

a. is not subject to compliance audit procedures and

b. includes amounts in the schedule or statement that are trivial and clearly inconsequential to the schedule or statement as a whole.

When an entity meets the definition of a *compliance audit client*, it is not considered a *financial statement attest client* and, therefore, the “Client Affiliates” interpretation [1.224.010] and the “State and Local Government Client Affiliates” interpretation [1.224.020] would not apply.

Nonauthoritative questions and answers regarding *compliance audit clients* are available in Q&A section 10, Definitions.

Text of proposed revised definition “financial statement attest client”

0.400 Definitions

.18 **Financial statement attest client.** An entity whose *financial statements* are audited, reviewed, or compiled when the *member's* compilation report does not disclose a lack of *independence*.

This definition does not include a *compliance audit client*. Therefore, the “Client Affiliates” interpretation [1.224.010] and the “State and Local Government Client Affiliates” interpretation [1.224.020] would not apply.

Proposed Q&As for compliance audits

Q&A section 10, Definitions, .01–.06

You can find these and other Q&As here:

- Ethics Online Library — Look for *Ethics Questions and Answers* to discover a range of topics from independence to records requests and more.
- AICPA *Technical Questions and Answers* — In addition to ethics Q&As, this resource has an array of technical content for auditing and accounting, financial reporting, compilation, and review standards.

Terms defined in the AICPA Code of Professional Conduct are italicized in this document. If you'd like to see the definitions, you can find them in "Definitions" (ET sec. 0.400)

.01 Examples of a compliance audit

Inquiry — What are some examples of a *compliance audit*?

Reply — A *compliance audit* is an *attest engagement* performed in accordance with AU-C section 935, including any reporting on a related schedule or statement in accordance with AU-C section 725 or 805. Examples of *compliance audits* may include the following:

a. *Compliance audits* performed in accordance with the U.S. Department of Housing and Urban Development *Consolidated Audit Guide*

b. *Compliance audits* subject to the U.S. Department of Education Office of Inspector General's *Guide For Audits of Proprietary Schools and For Compliance Attest Engagements of Third-Party Services Administering Title IV Programs*

c. *Compliance audits* performed under Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), including program specific audits.

When the *attest engagement* is not performed in accordance with AU-C section 935, the engagement does not meet the definition of a *compliance audit*. Examples of engagements that are not *compliance audits* include the following:

a. Engagements performed in accordance with the Statements on Standards for Attestation Engagements (For these engagements, the *member* should refer to the requirements in the "Independence Standards for Engagements Performed in Accordance With

Statements on Standards for Attestation Engagements" subtopic [ET sec. 1.297]).

b. *Financial statement attest engagements*

c. Audits performed in accordance with AU-C sections 725 or 805, when such audit is not performed in conjunction with an AU-C section 935 compliance audit

d. Compliance attest engagements subject to the U.S. Department of Education Office of Inspector General's *Guide For Audits of Proprietary Schools and For Compliance Attest Engagements of Third-Party Services Administering Title IV Programs* performed in accordance with the Statements on Standards for Attestation Engagements

.02 Multiple compliance audit clients

Inquiry — When could there be multiple *compliance audit clients* in a *compliance audit*?

Reply — When a *compliance audit* includes amounts from multiple entities in a schedule or statement, each entity is considered a *compliance audit client* unless the entity is not subject to compliance audit procedures and also includes amounts in the schedule or statement that are trivial and clearly inconsequential to the schedule or statement as a whole as described in the definition of *compliance audit client*.

For example, in a *compliance audit* performed in accordance with Uniform Guidance for a state and local government, multiple agencies, departments, or component units within the state and local government may include amounts in the schedule of expenditures of federal awards (SEFA). Each entity reporting amounts in the reporting entity's SEFA is a *compliance audit client* unless it is not subject to compliance audit procedures and also includes amounts in the schedule or statement that are trivial and clearly inconsequential to the schedule or statement as a whole.

.03 Trivial and clearly inconsequential

Inquiry — How should a *member* determine what is "trivial and clearly inconsequential" when identifying the *compliance audit client(s)*?

Reply — Determining whether an entity in a *compliance audit* includes amounts in the schedule or statement that are trivial and clearly inconsequential to the schedule or statement as a whole is a matter of professional judgment, considering both quantitative and qualitative factors. The *member* may look to the Statement on Auditing Standards for additional guidance on what may be relevant when considering what is trivial and clearly inconsequential.

.04 Changes in the entities that are the compliance audit clients

Inquiry — Could the entities that are *compliance audit clients* change during the *period of professional engagement*?

Reply — Yes. The *member* should be alert to changes to the determination of the *compliance audit client(s)* throughout the *period of the professional engagement*. An entity that was excluded from the definition of *compliance audit client* may become a *compliance audit client* either because it becomes subject to the compliance audit procedures, or it includes amounts in the schedule or statement that are no longer trivial and clearly inconsequential to the schedule or statement as a whole. In other words, the entity is no longer excluded from being considered a *compliance audit client* because it no longer meets both criteria described in the definition of *compliance audit client*.

.05 Using the conceptual framework in a compliance audit

Inquiry — In a *compliance audit*, when should a *member* apply the "Conceptual Framework for Independence" (ET sec. 1.210.010)?

Reply — Upon encountering other relationships or circumstances that may create *threats* to *independence*, the *member* should apply the "Conceptual Framework for Independence" (ET sec. 1.210.010) to evaluate whether *threats* are at an *acceptable level*.

For example, when an entity does not include amounts in the schedule or statement (and therefore does not meet the definition of a *compliance audit client*) but supports a *compliance audit client* in a way that results in that entity being subject to compliance audit procedures, the *member* should use the "Conceptual Framework for Independence" to evaluate *threats* to *independence* related to any relationships or circumstances that exist with such entity.

In a *compliance audit* subject to the Uniform Guidance, there may be an entity that does not include amounts in the schedule of expenditures of federal awards but provides support activities for a *compliance audit client*. Those activities, such as providing accounting and financial reporting support for the client, may be subject to compliance audit procedures.

If the *member* is considering providing financial information system design services, for example, to an entity that is providing accounting and financial reporting support to the *compliance audit client*, the *member* should use the "Conceptual Framework for Independence" to evaluate whether *threats* (specifically, the self-review *threat*) are at an *acceptable level* or whether *threats* can be reduced to an *acceptable level* by applying appropriate *safeguards*.

.06 Evaluating independence when performing a financial statement audit and a compliance audit for the same client

Inquiry — When performing a *financial statement* audit and a *compliance audit* for the same *client*, how should the *independence* requirements be applied?

Reply — When performing a *financial statement* audit and a *compliance audit* for the same *client*, *members* should comply with the *independence* requirements for each *attest engagement*. The entities requiring *independence* in each *attest engagement* may be the same

but may also be different. Therefore, an evaluation of each *attest engagement* should be performed to identify all entities requiring *independence*.

IESBA convergence: Fees

Task force members
Alan Long (chair), Anika Heard, Randy Milligan, Kathy Savage, Peggy Ullmann

Observers
Sonia Araujo, Brandon Mercer, Jan Neal

AICPA staff
Sarah Brack, Ellen Goria

Task force charge
To develop a principles-based framework for members to determine when the level of fees and fee dependency impair independence.

Reason for agenda item
To obtain committee input on the proposed revised approach for converging with IESBA's fees guidance and the proposed authoritative and nonauthoritative guidance.

Task force activities
At the August PEEC meeting, the task force requested the committee's input on proposed authoritative guidance developed as an IESBA convergence project.

Engagements covered
The committee was split in its recommendations on scope:

- Some recommended that the two new interpretations scope in all attest engagements.
- Some recommended that the scope align with IESBA's scope which extends only to audits and reviews.

Additional observations included these:

- If threats are significant, the type of engagement is irrelevant.
- If the firm is small, a compilation can be a significant engagement.

The task force considered limiting the engagements subject to the new fees requirements, but determined that the relevant threats could be present in any attest engagement. Therefore, applying the requirements to all attest engagements is in the public interest. As a result, the task force did not change the scope of either the proposed "Determining Fees for an Attest Client" interpretation or the "Fee Dependency" interpretation.

Covered members

The proposed interpretations at the August meeting extended the provisions to all covered members. Committee members from the largest firms indicated that extending the provisions to all covered members is too expansive and should be limited to the firm and engagement partner.

The task force agrees that some provisions should extend to only those covered members with the authority to determine fees. Accordingly, the proposed "Determining fees for an Attest Client" interpretation includes a modifier in paragraph .03 to limit the requirement to the "covered member involved with determining the fees." See agenda item 2B.

Application guidance

The previous draft of the "Determining Fees for an Attest Client" and "Fee Dependency" interpretations included IESBA's application guidance relating to

- how to determine whether an attest client's fees constitute a large proportion of fees;
- ways to mitigate the threats when an attest client's fees constitute a large proportion of fees in years prior to the fifth year; and
- how to determine if fees from nonattest services create significant threats to independence.

Much of this information would be better as nonauthoritative guidance as it provides information on how and why a threat may exist and allows for more brevity and clarity in the interpretations. This content is now in the proposed Q&As in agenda item 2C.

Threats

The task force discussed whether the Conceptual Framework for Independence (ET sec. 1.210.010) is sufficient to ensure that members will identify and evaluate the threats identified by IESBA's fees standard (self-interest and undue influence) without additional authoritative guidance.

Though use of only the Conceptual Framework for Independence can help members determine that threats do exist, in practice these threats may not be apparent. Therefore, the task force proposes the following revisions to the conceptual framework to highlight that it can assist members with fee-related threats:

- Revising the existing example in item (*c*) under the self-interest threat of the conceptual framework in paragraph .16 as follows

  > A *member* or his or her *firm* relies excessively on ~~revenue~~ ***fees from attest and nonattest services*** from a single *attest client*.

- Adding a new item (*d*) under the undue influence threat in paragraph .18 to align with the new fees guidance, as follows

> ***A large proportion of fees charged by the firm to an attest client is generated by providing nonattest services.***

Q&A visibility

The "Cumulative Effect on Independence When Providing Multiple Nonattest Services" interpretation (ET sec. 1.295.020) requires members to evaluate whether the performance of multiple nonattest services create a significant threat to independence.

The "Determining Fees for an Attest Client" proposed interpretation may be important to consider when a member is providing multiple nonattest services. Because the "Cumulative Effect on Independence When Providing Multiple Nonattest Services" interpretation doesn't specifically mention the self-interest and undue influence threats, the task force proposes adding at the end of the interpretation a link to the proposed Q&As in agenda item 2C to alert members to these other potential threats.

Finally, the task force proposes adding links to the proposed Q&As at the end of each new and revised section of the code that relates to this project. This will spur members to consider this new guidance in their assessment of fee-related threats.

Questions for the committee

1. Can you think of a specific reason that it is not in the public interest for fees requirements to apply to all attest engagements?
2. Do you have any other concerns with or comments on the task force's proposals?

Materials presented

- Agenda item 2B: Preliminary draft new and revised interpretations related to fees convergence
- Agenda item 2C: Preliminary draft Q&As related to fees convergence

Preliminary draft new and revised interpretations related to fees convergence

1.230.030 Determining Fees for an Attest Client

.01 For the purposes of this interpretation, fees comprise fees or other types of remuneration for an attest engagement.

.02 Determining the fees to be charged to an attest client, whether for attest or other services, is a business decision taking into account the facts and circumstances relevant to that specific engagement, including the requirements of technical and professional standards.

.03 The provision of other services to an attest client is not an appropriate consideration in determining the attest engagement fee, except as provided for in paragraph .04. If a covered member involved with determining the fees allows the attest engagement fee to be influenced by the firm's provision of nonattest services to an attest client, the self-interest and undue influence threats to the covered member's compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and could not be reduced to an acceptable level by the application of safeguards.

For additional guidance on factors to consider when determining fees, nonauthoritative questions and answers are available in* Ethics Questions and Answers *section 125 at [link to Q&A section 125].

Accordingly, independence would be impaired.

.04 When determining the attest engagement fee, the firm may take into consideration the cost savings achieved as a result of experience derived from the provision of nonattest services to an attest client.

1.230.040 Fee Dependency

.01 When the total fees generated from an attest client by the firm represent a large proportion of the total fees of that firm, the dependence on, and concern about the potential loss of, fees from attest and other services from that client impact the level of the self-interest threat and create an undue influence threat to a covered member's independence.

.02 In calculating the total fees of the firm, the covered member should include fees from attest and nonattest services and might use financial information available from the previous financial year and estimate the proportion based on that information if appropriate.

.03 When for each of five consecutive years total fees from an attest client represent, or are likely to represent, a large proportion of the total fees received by the firm, threats to the covered member's compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and independence would be impaired unless one of the following safeguards is applied:

a. Prior to the attest report being issued for the fifth year, an appropriate reviewer who is not a member of the firm issuing the report, reviews the fifth year's work; or

b. After the attest report on the fifth year has been issued, and before the attest report is issued on the sixth year's attest engagement, an appropriate reviewer who is not a member of the firm issuing the report or a professional body, reviews the fifth year's attest work.

.04 If the total fees described in paragraph .05 continue to represent a large proportion, the covered member shall, each year, apply one of the safeguards .05*a* or .05*b*.

.05 When two or more firms are engaged to conduct an attest engagement, the involvement of the other firm in the attest engagement may be regarded each year as an action equivalent to that in paragraph .05*a*, if:

a. The circumstances addressed by paragraph .05 apply to only one of the firms performing the attest engagement; and

b. Each firm performs sufficient work to take full individual responsibility for the report.

For additional guidance on factors to consider when determining fees, nonauthoritative questions and answers are available in* Ethics Questions and Answers *section 125 at [link to Q&A section 125].

1.210.010 Conceptual Framework for Independence

[Paragraphs .01–.15, .17, and .19–.23 are unchanged.]

.16 *Self-interest threat.* The *threat* that a *member* could benefit, financially or otherwise, from an interest in, or relationship with, an *attest client* or persons associated with the *attest client*. Examples of self-interest *threats* include the following:

a. A *member* has a *direct financial interest* or material *indirect financial interest* in the *attest client*. [1.240.010]

b. A *member* has a *loan* from the *attest client*, an officer or a director of the *attest client* with 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 the *attest client*. [1.260.010]

c. A *member* or his or her *firm* relies excessively on ~~revenue~~ ***fees from attest and nonattest services*** from a single *attest client*.

d. A *member* or *member's firm* has a material joint venture or other material joint business arrangement with the *attest client*. [1.265]

.18 *Undue influence threat.* The *threat* that a *member* will subordinate his or her judgment to that of an individual associated with an *attest client* or any relevant third party due to that individual's reputation or expertise, aggressive or dominant personality, or attempts to coerce or exercise excessive influence over the *member*. Examples of undue influence *threats* include the following:

a. Management threatens to replace the *member* or *member's firm* over a disagreement on the application of an accounting principle.

b. Management pressures the *member* to reduce necessary audit procedures in order to reduce audit fees.

c. The *member* receives a gift from the *attest client*, its management, or its significant shareholders. [1.285.010]

d. ***A large proportion of fees charged by the firm to an attest client is generated by providing nonattest services.***

For additional guidance on factors to consider when determining fees, nonauthoritative questions and answers are available in **Ethics Questions and Answers** ***section 125 at [link to Q&A section 125].***

Preliminary draft Q&As related to fees convergence

Q&A section 125, Fees, .01–.03

You can find these and other Q&As here:

- Ethics Online Library — Look for *Ethics Questions and Answers* to discover a range of topics from independence to records requests and more.
- AICPA *Technical Questions and Answers* — In addition to ethics Q&As, this resource has an array of technical content for auditing and accounting, financial reporting, compilation, and review standards.

Terms defined in the AICPA Code of Professional Conduct are italicized in this document. If you'd like to see the definitions, you can find them in "Definitions" (ET sec. 0.400)

.01 Factors that may help determine whether an attest client generates a large proportion of the firm's fees.

Inquiry —The "Fee Dependency" interpretation (ET sec. 1.230.040) of the "Independence Rule" (ET sec. 1.200.001), says "when the total fees generated from an attest client by the firm represent a large proportion of the total fees of that firm . . . the level of the self-interest threat [is impacted] and create[s] an undue influence threat to a covered member's independence." What are some factors to consider in determining whether the fees from an *attest client* constitute a large proportion of total fees charged by the *firm*?

Reply — Each situation is unique, so it is important to use professional judgment to determine what qualitative and quantitative factors are appropriate considerations. Following are examples of some factors:

a. The size of the *attest client*, in terms of the percentage of fees or the dollar amount of fees versus total revenue of the *firm*, engagement *partner*, *office*, or practice unit of the *firm*.

b. The significance of the *attest client* to the *firm*, engagement *partner*, *office*, or practice unit of the *firm* in light of the following:

i. The amount of time the *firm*, *partner*, *office*, or practice unit devotes to the *attest client*

ii. The effect on the *partner*'s stature within the *firm* due to the *partner*'s relationships with the *attest client*

iii. The manner in which the *partner, office*, or practice unit is compensated

iv. The effect that losing the *attest client* would have on the *firm*, *partner*, *office*, or practice unit

c. The importance of the *attest client* to the *firm*'s growth strategies (for example, the *firm* is trying to enter a particular industry)

d. The stature of the *attest client*, which may enhance the *firm*'s eminence in the marketplace

e. Whether the *firm* also provides services to related parties (for example, also provides professional services to *affiliates* or owners of the *attest client*)

f. Whether the engagement is recurring

g. The operating structure of the *firm*

h. Whether the *firm* is expected to diversify such that any dependence on the *attest client* is reduced

When the factors indicate that an *attest client* may represent a large proportion of the *firm*'s fees, the following are examples of actions that might reduce the proportion:

a. Reducing the extent of nonattest services provided to the *attest client*

b. Increasing the client base of the firm to reduce dependence on the *attest client*

c. Increasing the extent of services provided to other *clients*

See Q&A section 125.02 for guidance on what to do if there are no actions a *member* can take to reduce the proportion.

.02 Actions that may mitigate threats when an attest client generates a large proportion of the firm's fees.

Inquiry — A *member* has considered factors such as those in Q&A section 125.01 and has determined that an *attest client* generated a large proportion of the *firm*'s fees. What can the *member* do to mitigate threats to independence?

Reply — These are a few actions that may be taken to mitigate threats:

a. Having an appropriate reviewer who has not provided attest or nonattest services to the *attest client* review the attest work performed before the current-year attest report is

issued

b. Ensuring that the compensation of the *partner* is not significantly influenced by the fees generated from the *attest client*

c. Implementing policies and procedures for identifying and monitoring significant *client* relationships, including the following:

i. Consider *client* significance in the planning stage of the engagement.

ii. Base the consideration of *client* significance on *firm*-specific criteria or factors that are applied on a facts and circumstances basis.

iii. Periodically monitor the relationship. What constitutes periodic is a matter of judgment, but assessments of *client* significance that are performed at least annually can be effective in monitoring the relationship. During the course of such a review, a *client* previously deemed to be significant may cease to be significant. Likewise, *clients* not identified as significant could become significant whenever factors the *firm* considers relevant for identifying significant *clients* arise. (For example, additional services are contemplated.)

d. Assigning a second (or concurring) review *partner* who is not otherwise associated with the *attest engagement* and who practices in an *office* other than those who perform the *attest engagement*

e. Subjecting the assignment of engagement personnel to approval by another *partner* or manager

f. Periodically rotating engagement *partners*

g. Subjecting significant *client attest engagements* to internal firm monitoring procedures

.03 Large proportion of fees for an attest client generated by nonattest services.

Inquiry — The "Conceptual Framework for Independence" (ET sec. 1.210.010) indicates that the undue influence *threat* may exist when a large proportion of fees charged by the *firm* to an *attest client* is generated from nonattest services. Is that the only *threat* that exists and what should a *member* do to determine whether fees from nonattest services create significant *threats* to independence?

Reply — The undue influence and self-interest *threats* may exist when a large proportion of fees charged by the *firm* to an *attest client* is generated by providing nonattest services to the *attest client* (Q&A section 125.01, "Factors that may help determine whether an attest client generates a large proportion of the firm's fees" can help determine what constitutes a large proportion).

This is due to concerns about the potential loss of either the *attest engagement* or other services and the perception that the *firm* will focus on the nonattest relationship.

Because each situation is unique, it is important to use professional judgment to determine when these *threats* exist and when *threats* are not at an acceptable level. Following are some considerations that may help you determine if *threats* exist and how significant the *threats* are to your independence:

a. The ratio of fees for nonattest services to the *attest engagement* fee

b. The length of time during which a large proportion of fees for nonattest services to the *attest engagement* fee has existed

c. The nature, scope and purposes of the nonattest services, including:

    i. Whether they are recurring services

    ii. Whether law or regulation mandates the services to be performed by the *firm*

If you conclude that *threats* are not at an acceptable level, following are examples of actions that might help reduce the level of *threats*:

a. Having an appropriate reviewer who does not take part in the *attest engagement* assess the reasonableness of the fee proposed

b. Having an appropriate reviewer who did not take part in the *attest engagement* review the work performed on the *attest engagement*

Solicitation or disclosure of CPA examination questions and answers

AICPA staff

Summer Young

Reason for agenda item

To revise the AICPA Code of Professional Conduct (code) to address recent continuing professional education (CPE) course cheating issues.

Background

Several firms have been sanctioned by the SEC for employees sharing answer keys to various CPE courses; consequently, several state boards of accountancy have taken action against individuals identified in these instances. As the extant code prohibits question and answer sharing only for the CPA exam, staff proposes the attached revisions to the three "Solicitation or Disclosure of CPA Examination Questions and Answers" interpretations (ET sec. 1.400.020, 2.400.020, and 3.400.020).

Questions for the committee

1. Does the committee agree with staff's recommended edits to the interpretations?
2. Does the committee approve the proposed revisions to the "Solicitation or Disclosure of CPA Examination Questions and Answers" interpretations for exposure?
3. Does the committee agree that the exposure period can be limited to 60 days?
4. Does the committee agree with the proposal to make the revisions effective as soon as possible (that is, as soon as notice appears in the *Journal of Accountancy*)?

Action needed

The committee is asked to approve the proposed revised interpretations for exposure with a 60-day comment period and the recommended effective date.

Materials presented

Agenda item 3B: Proposed revisions to the "Solicitation or Disclosure of CPA Examination Questions and Answers" interpretations

Proposed revisions to the "Solicitation or Disclosure of CPA Examination Questions and Answers" interpretations

Additions appear in ***boldface italic***. Deletions appear in ~~strikethrough~~.

Terms defined in the AICPA Code of Professional Conduct are italicized in this document. If you'd like to see the definitions, you can find them in "Definitions" (ET sec. 0.400)

1.400.020 Solicitation or Disclosure of ~~CPA~~ Examination Questions and Answers

.01 A member who solicits or knowingly discloses the Uniform CPA Examination question~~(s)~~ or answer~~(s)~~, or both, without the AICPA's written authorization shall be considered to have committed an act discreditable to the profession, in violation of the "Acts Discreditable Rule" [1.400.001]. [Prior reference: paragraph .07 of ET section 501]

.02 A member who solicits or knowingly discloses questions or answers, or both, of any continuing professional education course shall be considered to have committed an act discreditable to the profession, in violation of the "Acts Discreditable Rule" [1.400.001] when the course is used by the member to meet the member's

a. state licensure requirements;

b. AICPA membership requirements; or

c. state CPA society membership requirements.

2.400.020 Solicitation or Disclosure of ~~CPA~~ Examination Questions and Answers

.01 A member who solicits or knowingly discloses the Uniform CPA Examination question~~(s)~~ or answer~~(s)~~, or both, without the AICPA's written authorization shall be considered to have committed an act discreditable to the profession, in violation of the "Acts Discreditable Rule" [2.400.001]. [Prior reference: paragraph .07 of ET section 501]

.02 A member who solicits or knowingly discloses questions or answers, or both, of any continuing professional education course shall be considered to have committed an act discreditable to the profession, in violation of the "Acts Discreditable Rule" [2.400.001] when the course is used by the member to meet the member's

- ***a. state licensure requirements;***
- ***b. AICPA membership requirements; or***
- ***c. state CPA society membership requirements.***

3.400.020 Solicitation or Disclosure of ~~CPA~~ Examination Questions and Answers

.01 A member who solicits or knowingly discloses the Uniform CPA Examination question~~(s)~~ or answer~~(s)~~, or both, without the AICPA's written authorization shall be considered to have committed an act discreditable to the profession, in violation of the "Acts Discreditable Rule" [3.400.001]. [Prior reference: paragraph .07 of ET section 501]

.02 A member who solicits or knowingly discloses questions or answers, or both, of any continuing professional education course shall be considered to have committed an act discreditable to the profession, in violation of the "Acts Discreditable Rule" [3.400.001] when the course is used by the member to meet the member's

- ***a. state licensure requirements;***
- ***b. AICPA membership requirements; or***
- ***c. state CPA society membership requirements.***

Information systems services

Task force members

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

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Task force charge

To develop nonauthoritative guidance to assist members with implementing the "Information Systems Services" interpretation (ET sec. 1.295.145), which is effective January 1, 2023.

Reason for agenda item

To provide the committee with an overview of the recently issued nonauthoritative guidance and to seek input on additional Q&As.

Task force activities

Since the August 2022 PEEC meeting, division staff has released three *Ethically Speaking* episodes (57, 58 and 59) that cover the education provided during the information system services roundtable workshops and address some of the major issues attendees brought up during the breakout sessions.

Three Q&As went into the Online Ethics Library provide guidance on these issues identified during the roundtable workshops:

a. IT Help Desk: Provide examples of activities that indicate that the member may or may not be operating or managing an IT help desk for an attest client.

b. Hypercare: Explain that hypercare is part of an implementation engagement.

c. Network Maintenance and Updates: Provide examples of activities that indicate that the member's professional services related to performing network maintenance will or will not result in the member assuming a management responsibility.

The task force developed additional Q&As to address the remaining issues identified during the roundtable workshops:

a. Explain what a data-gathering system is.

b. Provide some factors to consider in determining whether designing or developing a data-gathering system is related to an FIS.

c. Clarify what the phrase “could significantly affect” means in item (c) of paragraph .06.

d. Add cross references in Q&A section 250 “Nonattest services – Information systems services” to Q&As on cybersecurity services.

e. Explain that a member can apply the exception in paragraph .03 of the "Scope and Applicability of Nonattest Services" interpretation (ET sec. 1.295.010) if the financial information system designed by the member is in use.

The task force recommends the artificial intelligence (AI) task force develop nonauthoritative guidance to raise awareness that a management participation threat exists if members design or develop information systems, such as AI, which perform management responsibilities (for example, a system generates a specific action for the attest client’s management to take).

As the feedback received from the three roundtable workshops has been addressed in nonauthoritative guidance, when the proposed Q&As in agenda item 4B are published, the information systems services member enrichment project will conclude.

Questions for the committee

1. Does the committee have any suggestions on the proposed Q&As?
2. Are there any other issues you would like the task force to consider?

Materials presented

- Agenda item 4B: Q&A section 250, Nonattest services – Information Systems Services (proposed .05–.09)

Q&A section 250, Nonattest Services – Information Systems Services (proposed .05–.09)

You can find these and other Q&As here:

- Ethics Online Library — Look for *Ethics Questions and Answers* to discover a range of topics from independence to records requests and more.
- AICPA *Technical Questions and Answers* — In addition to ethics Q&As, this resource has an array of technical content for auditing and accounting, financial reporting, compilation, and review standards.

Terms defined in the AICPA Code of Professional Conduct are italicized in this document. If you'd like to see the definitions, you can find them in "Definitions" (ET sec. 0.400).

.05 Description of a data-gathering system

Inquiry — Paragraph .06 of the "Information Systems Services" interpretation (ET sec. 1.295.145) points out how to determine whether a nonattest service is related to a financial information system (FIS). Item (*c*) of that paragraph says that a service is related to an FIS if it "affects a data-gathering system, such as an analytical or reporting tool, that is used in management's decision-making about matters that could significantly affect financial reporting."

What is a data-gathering system?

Reply — A data-gathering system ingests data from one or multiple sources and performs certain functions or processes on that data, such as displaying information in a dashboard or performing analytical algorithms and producing outputs.

.06 Factors to help determine whether designing or developing a data-gathering system is related to a financial information system

Inquiry — What are some factors a *member* may consider in determining whether designing or developing a data-gathering system is related to a financial information system (FIS) in accordance with item *(c)* of paragraph .06 of the "Information Systems Services" interpretation (ET sec. 1.295.145)?

Reply — A *member* may consider whether a data-gathering system:

- Meets the discrete tool exception
- Feeds the altered data back into a financial reporting system, and the data is significant

to the financial statements or financial processes as a whole

- Generates data for *client* management to analyze and make a management decision.

For example, a *member* considers designing or developing a dashboard for an *attest client*. The dashboard will provide alternative views of existing data from an *attest client*'s financial systems. Assume the dashboard does not feed the altered data into a financial reporting system and the dashboard does not generate a specific action for *client* management to take but rather provides information to consider. In this situation, a *member* may conclude that designing or developing the data-generating system is not related to an FIS.

However, if the dashboard feeds the altered data back into a financial reporting system or generates specific actions for *client* management to take, *members* should use their professional judgement to determine if the nonattest service is related to an FIS, and whether self-review, management participation or other *threats* exist.

As a reminder, for more information about the discrete tool, see item (*a*) of paragraph .03 of the "Information Systems Services" interpretation (ET sec. 1.295.145) and step 1 of the practice aid *Independence considerations for information systems services* for more information on the exception.

.07 Determining whether a data-gathering system could significantly affect financial reporting

Inquiry — Paragraph .06 of the "Information Systems Services" interpretation (ET sec. 1.295.145) points out how to determine whether a nonattest service is related to a financial information system (FIS).

Item (*c*) of that paragraph indicates that a service is related to a financial information system (FIS) if it "affects a data-gathering system, such as an analytical or reporting tool, that is used in management's decision-making about matters that could significantly affect financial reporting." What does the phrase "could significantly affect" mean?

Reply — The phrasing in the interpretation means that, during the *independence* evaluation for an engagement, the *member* has a responsibility to consider whether the information systems services are related to a tool that is considered an FIS in accordance with item (*c*) of paragraph .06. This evaluation does not need to include whether the client may modify the tool the *member* designed and provided to the *client* to perform functions that will significantly affect financial reporting. Whether a matter could significantly affect financial reporting is a matter of professional judgment and is based upon the specific facts and circumstances of each *client* and engagement.

.08 Cybersecurity services

Inquiry — Does the AICPA have ethics-related Q&As on cybersecurity services?

Reply — Yes. The AICPA has published the following nonauthoritative ethics Q&As regarding cybersecurity:

- Q&A section 205.01, “Accepting responsibility for design, development, or implementation of policies and procedures for cybersecurity threats and practices”
- Q&A section 217.01, “General training on cybersecurity issues”
- Q&A section 217.02, “General training on cybersecurity issues”
- Q&A section 217.03, “Advice and recommendations on improving cybersecurity practices”
- Q&A section 217.04, “Attack and penetration testing related to cybersecurity”

.09 Period of impairment for prohibited information system services

Inquiry —The *member* is engaged by a nonattest client to design and implement a financial information system (FIS) as defined in paragraph .03*(a)* of the “Information Systems Services” interpretation (ET sec. 1.295.145). In a subsequent period, the *member* is asked to perform an *attest engagement*.

Can the *member* apply the exception found in paragraph .03 of the "Scope and Applicability of Nonattest Services" interpretation (ET sec. 1.295.010) even if the FIS is still in use?

Reply — Yes, the *member* may still apply the exception in paragraph .03. The *member* should exercise professional judgment and consider all facts and circumstances of the specific situation when assessing whether the exception in paragraph .03. can be satisfied.

For example, if an FIS is implemented prior to the period covered by the *financial statements* and with sufficient time to produce financial information that will be audited by another *firm*, the exception in paragraph .03 is likely to be met. However, if an FIS is implemented after the start of the period covered by the *financial statements*, the exception in paragraph .03 is not likely to be met.

Refer to Q&A section 200.02 for an example of how to apply the exception found in paragraph .03 of the "Scope and Applicability of Nonattest Services" interpretation (ET sec. 1.295.010).

Agenda item 5A

Assisting attest clients with implementing accounting standards

Task force members

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

Observers

Vincent DiBlanda, John Ford, Erik Lange, Brandon Mercer

AICPA staff

Liese Faircloth

Task force charge

To provide guidance on how members may assist attest clients with implementing an accounting standard without impairing independence.

Reason for agenda item

To obtain committee input on the proposed update to the nonattest services Q&A.

Task force activities

The task force met after the August 2022 PEEC meeting to consider committee feedback on the proposed addition to a Q&A. The overall topic of the Q&A is the "skill, knowledge, and/or experience" requirement in the nonattest services interpretation of the "Independence Rule" (ET sec.1.200.001) and specifically covers examples of client understanding for particular nonattest services.

An existing Q&A (Q&A sec. 201.02) addresses the meaning of suitable skill, knowledge, and/or experience and another existing Q&A (Q&A sec. 210.05) provides some factors for determining suitable skill, knowledge, and/or experience.

The task force discussed whether to add an example of skill to the proposed revision to the Q&A and felt that knowledge and experience were the more important to include as the Q&A is providing examples of nonattest services and client understanding.

Questions for the committee

1. Does the committee agree that the three examples of ways a member may assist a client should be included at the end of the assisting clients section of the reply in the Q&A?
2. Does the committee have any other input regarding the Q&A?

Materials presented

Agenda item 5B: Proposed revised Q&A — Examples of nonattest services and client understanding

Proposed revisions to Q&A section 210 Nonattest Services — General Requirements, paragraph.10, Examples of nonattest services and client understanding

You can find these and other Q&As here:

- Ethics Online Library — Look for *Ethics Questions and Answers* to discover a range of topics from independence to records requests and more.
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Proposed additions appear in ***boldface italic***. Deletions appear in ~~strikethrough~~.

.10 Examples of nonattest services and client understanding

Inquiry —- ***The "General Requirements for Performing Nonattest Services" interpretation (ET sec. 1295.030) explains that the member needs to determine whether the attest client has "designated an individual with suitable skill, knowledge and/or experience to oversee the service being provided."***

What are some examples of nonattest services and the level of understanding that ~~the individual designated by the attest client to oversee the nonattest services~~ ***this person*** should possess in order to comply with the "General Requirements for Performing Nonattest Services" interpretation?

Reply — Following are four examples along with the level of understanding required by each:

In the "Assisting clients with implementing accounting standards" section of this response, only changes made since the August meeting are tracked. However, the entire section is being added to the Q&A.

- *Assisting clients with implementing accounting standards* — When a *member* assists an attest client with implementing an accounting standard, the *member* should be satisfied

that the individual designated by the *attest client* **to oversee the service** has ~~appropriate~~ **suitable** skill, knowledge, and/or experience.

Some considerations ~~Factors~~ that may help a member determine whether this individual has ~~appropriate~~ **suitable skill, knowledge, and/or experience** include whether the individual has experience ~~implementing~~ ***applying*** accounting standards, ~~and the individuals' understanding~~ knowledge of the company's accounting processes and controls, **and an understanding of the accounting standard being implemented**.

If the member believes the individual does not sufficiently understand the standard ***and*** the potential impact on the financial statements, ~~and~~ ***including*** the related processes and controls, the member may provide training ***that will help the individual who will oversee the implementation service attain the appropriate understanding.*** ~~and research to help that individual achieve the necessary understanding. The member should also be satisfied that the individual has the appropriate knowledge and experience to evaluate how best to implement the standard.~~ ***Generally, t***his training should occur prior to ~~assisting the client with implementation~~ ***beginning the service***. After the training **and before beginning the service**, the member should assess whether the individual ~~has sufficient knowledge~~ ***is able to oversee the member's service including determining the reasonableness of the member's recommendations and evaluating the results of the implementation service.*** ~~*to evaluate how best to implement the standard.*~~

After the *member* is satisfied that the individual has suitable skill, knowledge and/or experience, the *member* may assist with evaluating the effects of adopting a new standard. Following are examples from the interpretation of ~~activities that~~ **ways** ~~a~~ **the** member **may assist**. **It's important that you apply professional judgment when assisting a client**:

- — Analysis of the potential impact of implementing the accounting standard
- — Recommendations of possible revisions to existing policies, procedures, and internal controls
- — Preparation of transition-related calculations to illustrate the impact of the application of the accounting standard for management's consideration and selection

[Added X 2022]

- *Bookkeeping* — When the member performs routine bookkeeping services for an attest client, the *member* should be satisfied that the individual designated by the *attest client*

understands the basis for the proposed journal entries and how the posting of the journal entries will affect the *financial statements*. For recurring or standard journal entries (for example, depreciation), the individual designated by the *attest client* may require no explanation regarding the reason for the entry (for example, when the member has previously discussed these entries with the *attest client*), whereas for more complex journal entries (for example, deferred taxes), the member may need to have further discussions with the individual designated by the *attest client* discussing the underlying requirements and the basis for the entry and how the entry will affect the *financial statements*. For such services, the individual designated by the *attest client* must have the skills, knowledge, and experience to approve the proposed journal entries and accept responsibility for the company's individual designated by the *attest client*. ***[Added prior to June 2005]***

- *Tax compliance services* — For tax return preparation engagements, the individual designated by the *attest client* need not have an in-depth understanding of the applicable tax laws. However, the individual designated by the *attest client* should review the tax return, understand and approve key tax positions taken or disclosed in the return, and approve the filing of the return. The *member* also should be satisfied that the individual understands the company's tax situation, has a general understanding of how the amounts on the tax return were determined, and make all decisions regarding significant tax positions taken in the return. ***[Added prior to June 2005]***

- *Valuation services* — For more complex engagements, such as permitted valuation services, the *member* may need to explain to the individual designated by the attest client the valuation methodologies used as well as all significant assumptions. The individual then should be in a position to approve all significant assumptions and accept responsibility for the resulting valuation. [Added prior to June 2005]

Engagement quality reviewer

Task force members
Alan Long (chair), Michael Brand, Dan Dodson, Anna Dourdourekas, Randy Milligan

Observers
Ahava Goldman, Brandon Mercer

AICPA staff
Jennifer Kappler

Task force charge
To determine convergence needs with and recommend changes to the AICPA code related to IESBA's (International Ethics Standards Board for Accountants') final pronouncement addressing the objectivity of an engagement quality reviewer or other reviewer.

Reason for agenda item
To obtain committee input regarding nonauthoritative guidance to assist members in addressing threats to objectivity arising from the use of an engagement quality reviewer who previously served as the lead attest engagement partner.

Task force activities
The task force has met twice since the August 2022 PEEC meeting. At the August meeting, PEEC agreed with the task force's proposal to move forward with nonauthoritative guidance to accomplish convergence.

The task force agrees with IESBA's conclusion that if a former lead partner on an attest engagement becomes a quality reviewer for the same client, there could be a threat that the judgments made or services performed or supervised by individuals in the member's firm are not appropriately evaluated. The task force also agrees that examples of potential safeguards will be helpful if the lead attest engagement partner concludes this threat is not at an acceptable level.

However, instead of stipulating additional threats and safeguards like IESBA, the task force recommends the lead attest engagement partner use the "Conceptual Framework for Members in Public Practice" interpretation (ET sec. 1.000.010) as a guide for evaluation.

Using the conceptual framework would be a more effective approach because AICPA nonauthoritative guidance is not appropriate for the following:

- Quantifying as a safeguard a cooling-off period between the time an individual serves as the lead attest engagement partner and the engagement quality reviewer.

International Standard on Quality Management (ISQM) 2 requires a two-year cooling-off period before the engagement partner can serve as the engagement quality reviewer. No such cooling-off period is required by the Auditing Standards Board's (ASB) Statement on Quality Management Standards (SQMS) No. 2.

- Identifying as a threat to objectivity a relationship that may exist between the engagement quality reviewer and a member of the engagement team.

  This example was added to IESBA's conceptual framework under the familiarity threat. The task force does not agree that such relationships create a familiarity threat with respect to a member's objectivity.

- Identifying a threat to objectivity when two engagement partners serve as the engagement quality reviewers for each other's engagements.

  This threat is identified in IESBA's application guidance as a self-interest threat. However, the risk of an engagement quality reviewer's objectivity being compromised to conclude in favor of the engagement partner would be offset by the potential repercussions of failing to comply with professional standards.

- Addressing the situation where an engagement quality reviewer has a direct reporting line to the lead attest engagement partner.

  This threat is identified in IESBA's application guidance as an intimidation threat. However, the requirement in ASB's SQMS No. 2 for an engagement quality reviewer to have the appropriate authority to perform the review adequately addresses this issue. Specifically, the application guidance states that the engagement quality reviewer's authority could be diminished by having a direct reporting line to the engagement partner. A member's compliance with SQMS No. 2 should preclude such a threat.

Questions for the committee

1. Does the committee believe the lead attest engagement partner should be identified as the individual responsible for concluding that the self-review threat is significant? If not, should this be both the lead attest engagement partner and the engagement quality reviewer?
2. Does the committee have any suggested revisions to Agenda Item A: Q&A .01?
3. Does the committee have any suggested revisions to Agenda Item A: Q&A .02?
4. Does the committee have any suggested revisions to Agenda Item B: Q&A .06?

Materials presented

- Agenda item 6B: Q&A section 50, Objectivity, .01–.02
- Agenda item 6C: Q&A section 100, Independence. .06

Q&A section 50, Objectivity (.01–.02)

You can find these new and other Q&As here:

- Ethics Online Library — Look for *Ethics Questions and Answers* to discover a range of topics from independence to records requests and more.
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.01 Possible factors to consider when evaluating the objectivity of an engagement quality reviewer

Inquiry — Is there a self-review *threat* to a *member's* objectivity if that member serves as the engagement quality reviewer (EQR) after previously being the lead *attest engagement partner*?

Reply — Yes and the lead *attest engagement partner* will need to determine the significance of the *threat*.

The lead *attest engagement partner* likely has specialized knowledge of the client and related industry, including the regulatory environment, which contribute to an EQR's competence. However, there is a *threat* that the engagement quality reviewer would not appropriately evaluate the results of previous judgments made or services performed or supervised by individuals in the *member's firm*. This would include when the engagement quality reviewer previously served as the lead *attest engagement partner*.

The following factors may assist the lead *attest engagement partner* in determining the significance of the *threat*:

- The *member's* current role and seniority within the *firm*, including the *firm's* reporting structure
- The length of time the *member* was previously involved with the *attest engagement* and the *member's* role
- When the *member* last served on the *attest engagement team* prior to being appointed as engagement quality reviewer

- Any relevant changes to the circumstances of the engagement subsequent to the *member's* participation on the *attest engagement team*

- The nature and complexity of issues that required significant judgment during the period the *member* served on *the attest engagement team* and the level of involvement in the conclusions reached

.02 Potential safeguards when a significant self-review threat to an engagement quality reviewer's objectivity is identified

Inquiry — If the lead *attest engagement partner* concluded that the self-review *threat* to the *member's* objectivity was significant, can the *member* still serve as the engagement quality reviewer (EQR)?

Reply — Yes, if *safeguards* can be applied to eliminate the *threat* or reduce it to an *acceptable level*. Though not all-inclusive, the following list provides examples of such *safeguards*:

- An individual within the *firm* possessing highly specialized knowledge, skills, or expertise assists the EQR in evaluating significant judgments

- An individual from outside the *firm*, or someone from within the *firm* who is not otherwise associated with the *attest engagement*, assesses the conclusions reached by the EQR

- Consultation with a third party, a professional regulatory body, or an external professional accountant

- Incentives and disincentives within the *firm* structure to encourage the objectivity of the EQR

- The extent of changes in the matters on which significant judgments were made and the facts and circumstances around those significant judgments compared to the period or periods in which the EQR was the lead *attest engagement partner*

If there are no *safeguards* that can eliminate the *threat* or reduce it to an *acceptable level*, *independence* will be *impaired* if this *member* serves as the EQR on this engagement.

When *safeguards* are applied to eliminate or reduce significant *threats* to an *acceptable level*, the *member* should document the identified *threats* and *safeguards*.

Q&A section 100, Independence, .06

You can find these new and other Q&As here:

- Ethics Online Library — Look for *Ethics Questions and Answers* to discover a range of topics from independence to records requests and more.
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.06 An engagement quality reviewer is considered a member of the engagement team for independence purposes

Inquiry — In accordance with professional standards, the purpose of an engagement quality review is to provide an objective evaluation of the significant judgments made by the engagement team and the conclusions reached. The AICPA Statements on Quality Management Standards state that the engagement quality reviewer (EQR) is not a member of the engagement team. However, the definition of *attest engagement team* in the AICPA Code of Professional Conduct (code) includes concurring and engagement quality reviewers. How do I reconcile this apparent conflict?

Reply — The code uses the term *attest engagement team* to identify members who are subject to the "Independence Rule" (ET sec. 1.200.001) and its related interpretations. Accordingly, by including concurring and engagement quality reviewers in this definition, the code requires they maintain the same high level of independence as those on the engagement team.

Simultaneous employment or association with an attest client

Task force members

Cathy Allen (chair), Andy Bonner, Jeff Lewis, Nancy Miller, Dan Vuckovich

Observers

Robin Donaldson, Nicole Anderson McLean, Brandon Mercer, Bella Rivshin

AICPA staff

Jennifer Kappler

Task force charge

To consider whether to add an exception to the "Simultaneous Employment or Association With an Attest Client" interpretation (ET sec. 1.275.005) for individuals employed by the armed services and whether other modifications to the subtopic "Current Employment or Association with an Attest Client" (ET sec. 1.275) are warranted.

Reason for agenda item

To obtain committee approval to explore potential revisions to the code.

Task force activities

The task force previously concluded that there should be an exception to the "Simultaneous Employment or Association with an Attest Client" interpretation for individuals employed by the armed services.

Since the August 2022 PEEC meeting the task force has focused on whether there should be other modifications to the subtopic "Current Employment or Association with an Attest Client" or the "Simultaneous Employment or Association with an Attest Client" interpretation under this subtopic. Specifically, the task force reviewed the scope of individuals at the firm (partners and professional employees) who are prohibited from having employment relationships with an attest client and which roles at the client they are prohibited from having to prepare the following gap analysis.

Gap analysis

A gap analysis compared the code's "Simultaneous Employment or Association with an Attest Client" interpretation to equivalent rules of IESBA, SEC, PCAOB, GAO, and DOL. The results of this analysis led the task force to believe that the scope of the "Simultaneous Employment or Association with an Attest Client" interpretation may be too broad.

IESBA and GAO do not specifically address simultaneous employment and so the conceptual framework would be applied. The current SEC and PCAOB guidance are consistent with the extant code. DOL prohibition on employment extends to members, not all professionals, so to

the extent a firm's professional employees are not members, they may be permitted to be employed by the plan or plan's sponsor.

Boundaries for proposed modifications

The task force did not want to create unintended consequences so looked to the following interpretations to help establish boundaries for any proposed modifications.

What are the boundaries at the firm?	
Covered member[1]	Partner or professional employee
Former employment or association with an attest client (ET sec. 1.277.010) Considering employment or association at an attest client (ET sec. 1.279.010) Plan is an attest client or is sponsored by an attest client (ET sec. 1.250.010) Family relationships with attest client subtopic (ET sec. 1.270)	Subsequent employment or association with an attest client (ET sec. 1.279.20) Former partner and professional employees' participation in a firm sponsored plan (ET sec. 1.250.020)

[1] See agenda item 7B for definition of "covered member".

What are the boundaries at the client?	
Key position[2] or similar[3]	Employee
Former employment or association with an attest client (ET sec. 1.277.010) Subsequent employment or association with an attest client (ET sec. 1.279.20) Family relationships with attest client subtopic (ET sec. 1.270) Former partner and professional employees' participation in a firm sponsored plan (ET sec. 1.250.020)	Considering employment or association at an attest client (ET sec. 1.279.010) Plan is an attest client or is sponsored by an attest client (ET sec. 1.250.010)

Additionally, just two[4] of the eight interpretations in the "Current Employment or Association with an Attest Client" subtopic do not limit the role to a key position at the attest client.

Therefore, the task force recommends the boundaries for any scope modification not be decreased beyond "covered member" at the firm and "key position" at the client. Modifying the scope of the "Simultaneous Employment or Association with an Attest Client" interpretation could result in more consistency with other provisions in the code. Further discussion and analysis of the "Staff Augmentation Arrangements" interpretation (ET sec. 1.275.007) is warranted.

Preliminary threats analysis

The task force prepared a threats analysis to determine whether narrowing the scope of the limitations — concerning both the type of employment at the client and of a professional's role in the firm — created significant threats to independence. The task force considered the ability of the client's employee to affect the subject matter of the engagement, the ability of the professional employee to affect the engagement, and what a reasonable and informed third party who is aware of this information would conclude regarding whether there is a significant threat to independence in fact or appearance.

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[2] See agenda item 7B for definition of "key position"

[3] Officer, director, promoter, underwriter, voting trustee or trustee of the entity's pension or profit sharing trust.

[4] The prohibitions in the "Simultaneous Employment or Association with an Attest Client" interpretation and the "Staff Augmentation Arrangements" interpretation.

The preliminary analysis indicates that narrowing the scope will not create significant threats to independence.

Task force's preliminary recommendation

The results of the gap analysis, scope comparisons, and threats analysis support narrowing the scope of the limitations imposed by the "Simultaneous Employment or Association with an Attest Client" interpretation and will result in consistency with other provisions in the code that address employment.

This will make the AICPA code less restrictive than the SEC, PCAOB, and DOL. It will also have boundaries not currently included in IESBA and GAO standards that employ the conceptual framework for these situations. The task force believes that modifying the scope of the interpretation would facilitate compliance with independence while maintaining threats at an acceptable level.

Questions for the committee

1. Does the committee approve the task force exploring narrowing the scope of the limitations imposed by the "Simultaneous Employment or Association with an Attest Client" interpretation?
2. The task force plans to review the comment letters received related to the Staff Augmentation Arrangement exposure draft to identify stakeholders who may have concerns with narrowing the scope. Once identified, the task force will determine whether outreach to those stakeholders is needed. Does the committee have any concerns with this approach?

Definitions relevant to simultaneous employment or association with an attest client

Definitions

Key position. A position in which an individual has

a. primary responsibility for significant accounting functions that support material components of the *financial statements*;

b. primary responsibility for the preparation of the *financial statements*; or

c. the ability to exercise influence over the contents of the *financial statements*, including when the individual is a member of the board of directors or similar governing body, chief executive officer, president, chief financial officer, chief operating officer, general counsel, chief accounting officer, controller, director of internal audit, director of financial reporting, treasurer, or any equivalent position.

For purposes of *attest engagements* not involving *financial statements*, a key position is one in which an individual is primarily responsible for, or able to influence, the subject matter of the *attest engagement*, as previously described.

Covered member. All of the following:

a. an individual on the *attest engagement team*.

b. an *individual in a position to influence the attest engagement*.

c. a *partner*, *partner equivalent*, or *manager* who provides 10 or more hours of nonattest services to the *attest client* within any fiscal year. Designation as *covered member* ends on the later of (i) the date that the *firm* signs the report on the *financial statements* for the fiscal year during which those services were provided or (ii) the date he or she no longer expects to provide 10 or more hours of nonattest services to the *attest client* on a recurring basis.

d. a *partner* or *partner equivalent* in the *office* in which the lead *attest engagement partner* or *partner equivalent* primarily practices in connection with the *attest engagement*.

e. the *firm*, including the *firm's* employee benefit plans.

f. an entity whose operating, financial, or accounting policies can be *controlled* by any of the individuals or entities described in items *a*–*e* or two or more such individuals or entities if they act together.

Public interest entities

Task force members

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Jennifer Clayton, Ellen Goria

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Jason Brodmerkel, Misty Brown, Mary Foelster, Ahava Goldman, Sue Hicks, Kim Kushmerick, Melinda Nolan, Ian MacKay, Ashley Whitaker, Brian Wilson

Task force charge

To determine convergence needs related to the International Ethics Standards Board for Accountants (IESBA) revisions to their *Definitions of Listed Entity and Public Interest Entity*.

The revised definitions and related standard are effective for audits of financial statements for periods beginning on or after December 15, 2024, and early adoption is permitted. IESBA also issued a related basis for conclusion document and brought draft Q&As to their June 2022 meeting for input.

Reason for agenda item

To obtain input on the AICPA task force's proposed approach for converging with IESBA public interest entity (PIE) guidance.

Background

The IESBA code includes more restrictive independence requirements for PIEs. For example, the IESBA code prohibits the provision of non-assurance (or nonattest, in the AICPA code) services to a PIE audit or review client if that service might create a self-review threat in relation to the audit or review of the financial statements on which the firm will express an opinion.

IESBA's new PIE definition contains 3 mandatory categories of PIEs:

a. A publicly traded entity

b. An entity one of whose main functions is to take deposits from the public

c. An entity one of whose main functions is to provide insurance to the public

It also contains a general category:

> *d. An entity specified as such by law, regulation or professional standards to meet the purpose described in paragraph 400.10[1].*

The application guidance explains that bodies responsible for setting ethics standards are expected to define these categories more explicitly (that is, refine) to fit their jurisdictions. The application guidance also

a. indicates that bodies responsible for setting ethics standards are expected to add categories but are *not* expected to remove any.

b. encourages firms to consider whether to treat additional entities as PIEs.

The application guidance provides ethics standards-setting bodies with a list of factors to consider when refining these categories (that is, determining what entities should be considered PIEs because there is significant public interest in the entity's financial condition). Additional factors are also provided to help firms with their evaluation of whether additional entities should be treated as PIEs.

The factors provided for ethics standards-setting bodies to consider are as follows:

1. Nature of the business or activities, such as the holding of assets in a fiduciary capacity for a large number of stakeholders taking on financial obligations to the public as part of the entity's primary business. Examples might include financial institutions, such as banks and insurance companies, and pension funds

2. Whether the entity is subject to regulatory supervision designed to provide confidence that the entity will meet its financial obligations

3. Size of the entity

4. Importance of the entity to the sector in which it operates including how easily replaceable it is in the event of financial failure

5. Number and nature of stakeholders including investors, customers, creditors and

[1] Paragraph 400.10 states *"Stakeholders have heightened expectations regarding the independence of a firm performing an audit engagement for a public interest entity because of the significance of the public interest in the financial condition of the entity. The purpose of the requirements and application material for public interest entities as described in paragraph 400.8 is to meet these expectations, thereby enhancing stakeholders' confidence in the entity's financial statements that can be used when assessing the entity's financial condition."*

employees

6. Potential systemic impact on other sectors and the economy as a whole in the event of financial failure of the entity

These are the additional factors IESBA provided for *firms* to consider:

7. Whether the entity is likely to become a PIE in the near future

8. Whether in similar circumstances, a predecessor firm has applied independence requirements for PIEs to the entity

9. Whether in similar circumstances, the firm has applied independence requirements for PIEs to other entities

10. Whether the entity has been specified as not being a PIE by law, regulation, or professional standards

11. Whether the entity or other stakeholders requested the firm to apply independence requirements for PIEs to the entity and, if so, whether there are any reasons for not meeting this request

12. The entity's corporate governance arrangements, for example, whether those charged with governance are distinct from the owners or management

During the August 2022 meeting, PEEC agreed that a set of independence interpretations specific to PIEs *not* be added to the AICPA code. This is because the three mandatory categories covered by the new PIE definition are already heavily regulated in the United States by the SEC,[2] PCAOB, NAIC,[3] and FDIC[4] and these regulators have independence requirements that are generally as restrictive as the IESBA PIE requirements.

A better approach is for the AICPA code to direct members to those regulators' independence guidance. This would avoid adding a separate set of independence standards to the code that could be inconsistent with a particular regulator. The committee agreed with this approach.

Task force activities

The task force's discussions since August have focused mainly on how to refine the mandatory categories and some discussions on the other components of the project.

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[2] See IESBA's benchmarking reports.

[3] National Association of Insurance Commissioners.

[4] Federal Deposit Insurance Corporation.

In evaluating the potential refinements to the mandatory categories and any potential additional categories, the task force considered the SEC independence rules, which apply to issuers and certain non-issuers. The SEC independence rules that apply to issuer audits are the rules the task force considered to be substantially equivalent to the IESBA PIE requirements.

In this memo, when we acknowledge these additional rules are applicable, we will refer to them as the SEC issuer independence rules.

SEC independence rules	Additional SEC independence rules that apply to issuer audits
• General standard of auditor independence (Rule 2-01(b)) • Financial relationships (Rule 2-01(c)(1)) • Employment relationships (Rule 2-01(c)(2)(i)-(iii)(A) and (c)(2)(iv)) • Business relationships (Rule 2-01(c)(3)) • Non-audit services (Rule 2-01(c)(4)) • Contingent fees/commissions (Rule 2-01(c)(5))	• Employment cooling-off for former members of the audit engagement team (Rule 2-01(c)(2)(iii)(B)-(C)) • Partner rotation (Rule 2-01(c)(6) • Audit committee administration of the engagement (i.e., audit committee pre-approval) (Rule 2-01(c)(7) • Audit partner compensation (Rule 2-01(c)(8))

Preliminary refinement of mandatory categories

IESBA's application guidance indicates that bodies responsible for setting ethics standards are *not* expected to remove any of the mandatory categories, only refine them.

In considering the factors provided for ethics standards-setting bodies when refining the categories, an important factor is whether the entity is "subject to regulatory supervision designed to provide confidence that the entity will meet its financial obligations." Accordingly, the task force reviewed each of the three mandatory categories to determine how to refine them so that each category would include those entities that are subject to one of the above noted regulators.

Publicly traded entity — Definition and refined mandatory category

Definition

The first mandatory category of PIE is a "publicly traded entity." To help users understand what would be included in this category, IESBA adopted the following definition of publicly traded entity:

> *An entity that issues financial instruments that are transferrable and traded through a publicly accessible market mechanism, including through listing on a stock exchange.*
>
> *A listed entity as defined by relevant securities law or regulation is an example of a publicly traded entity.*

In addition, paragraph 66 of the basis for conclusion document explains that the new definition is not intended to include only entities having shares, stock or debt traded on formal exchanges but encompasses those on second-tier markets or over-the-counter (OTC) trading platforms.

The task force recommends IESBA's "publicly traded entity" definition be proposed as a new definition to the AICPA code with one revision: eliminating the example from the definition. The example is not necessary because the term "listed entity" is not common terminology in the U.S. but rather an international term. The common term in the U.S. is "issuer."

The broad definition will include financial instruments that are not subject to the SEC's independence rules (for example, governmental bonds, certain entities listed on the OTC trading platforms). However, the proposed refined scope of this PIE category in the next section clarifies that such financial instruments are not included.

Refined mandatory category

The task force recommends refining this category to include only entities that are "subject to Regulation SX, SEC Rule 2-01 (that is, SEC independence rules)."

> A publicly traded entity ***that is subject to Regulation S-X, SEC Rule 2-01, "Qualifications of Accountants"***

This refinement covers issuers, publicly traded mutual funds, and entities traded on the OTC trading platforms that are subject to the SEC issuer independence rules. This is consistent with IESBA's goal that the new definition is not intended to include only entities having shares, stock, or debt traded on formal exchanges but encompasses those on second-tier markets or OTC trading platforms.

The refinement excludes entities traded on the OTC trading platforms that have only informational filing requirements with the SEC but are not subject to SEC Rule 2-01.

The scope of the AICPA's extant PIE definition includes an entity that is listed on a foreign exchange.[5] The suggested refinement eliminates these entities. This is appropriate because the auditor will apply the foreign jurisdiction's PIE definition and related standards.

As drafted, the refined category excludes certain entities whose auditors are subject only to the

[5] Excerpt from extant AICPA definition of PIE "All listed entities, including entities that are outside the United States whose shares, stock, or debt are quoted or listed on a recognized stock exchange or marketed under the regulations of a recognized stock exchange or other equivalent body."

non-issuer SEC independence rules (but not subject to the SEC issuer independence rules). The section “Additional PIE categories being considered” addresses these entities.

An auditor of an issuer is required to disclose in their auditor’s report that they are independent in accordance with the U.S. federal securities laws and the applicable rules and regulations of the SEC and the PCAOB.

Questions for the committee

1. Does the committee agree with the proposed definition of “publicly traded entity”?
2. Does the committee agree with refining the publicly traded entity category to include only those entities that are subject to Regulation SX, SEC Rule 2-01?

Deposits from the public — Refined mandatory category

The second mandatory category of PIE is “an entity one of whose main functions is to take deposits from the public.”

The task force recommends refining this category to include only entities “that meet the annual audit requirement imposed by Sections 363.1(a) and 363.2(a) of Part 363 of the FDIC’s regulations (12 CFR 363 – Annual Independent Audits and Reporting Requirements)”.

> An entity one of whose main functions is to take deposits from the public ***that meets the annual audit requirement imposed by Sections 363.1(a) and 363.2(a) of Part 363 of the FDIC’s regulations (12 CFR 363 – “Annual Independent Audits and Reporting Requirements”)***

This will capture those financial institutions with assets of $500 million or more that are already subject to SEC issuer independence rules. This refinement also places significant importance on the size of the entity (factor 3 in the list of considerations), as the audit requirement becomes applicable when the bank has more than $500 million in assets.

Financial institutions that are publicly traded will also be considered a PIE under mandatory category 1, publicly traded entities.

The auditor’s independence in accordance with the U.S. federal securities laws and the applicable rules and regulations of the SEC and the PCAOB must be disclosed in the auditor’s report.

Credit unions are not captured by this category as they are not subject to SEC issuer independence rules. However, they are regulated by the National Credit Union Administration (NCUA) which protects the interests of credit union members. Auditors of credit unions are subject to AICPA independence rules.

Question for the committee

3. Does the committee agree with refining this category to include only those entities that meet the annual audit requirement imposed by Sections 363.1(a) and 363.2(a) of Part 363 of the FDIC's regulations (12 CFR 363)?

Insurance — Refined mandatory category

The third mandatory category of PIE is "an entity one of whose main functions is to provide insurance to the public."

The task force recommends refining this category to include only entities that are subject to the National Association of Insurance Commissioners (NAIC) Annual Financial Reporting Model Regulation (Model Audit Rule), and whose auditor is required to follow independence requirements included in Section 7 (Qualifications of Independent Certified Public Accountant) of the Model Audit Rule.

> An entity one of whose main functions is to provide insurance to the public ***that is subject to the NAIC Annual Financial Reporting Model Regulation (Model Audit Rule), and whose auditor is required to follow independence requirements included in Section 7 (Qualifications of Independent Certified Public Accountant) of the Model Audit Rule***

This requirement excludes small insurance entities that aren't currently subject to the NAIC audit requirement. Currently, insurers are exempt from the Model Audit Rule if they have direct premiums of less than $1,000,000 written in a state in any calendar year and less than 1,000 policyholders or certificate holders of direct written policies nationwide at the end of the calendar year.

This suggested refinement places significant importance on factors 2 and 3 (whether the entity is subject to regulatory supervision designed to provide confidence that the entity will meet its financial obligations and size of the entity, respectively).

Section 7 of the Model Audit Rule has independence requirements for auditors of insurers that are subject to the Model Audit Rule. These independence requirements are comparable to those of the SEC issuer independence rules as they contain provisions related to the following:

- Partner rotation
- Prohibited nonaudit services

- Cooling off period for employment
- Audit committee approval
- Good standing with the standards of the profession

Auditors of these insurance companies are required to include with their audited financial report a letter representing that they are in compliance with the requirements of Section 7 of the Model Audit Rule in accordance with Model Audit Rule Section 12: *Accountant's Letter of Qualifications.*

Insurance entities that are publicly traded are PIEs under category 1, publicly traded entities.

Other identified insurance entities that do not have uniform application of the Model Audit Rule specific requirements or regulations vary by state and include these:

- Health maintenance organization, managed care organization, health care
- Warranty companies structured as insurance entities
- Captives
- Risk retention groups

Regulators in the states, through either the departments of health or departments of insurance, determine the appropriate rules these additional entity types should follow; therefore, these insurance entities should not fall into this PIE category. The public is sufficiently protected with the existing independence standards required for auditors.

Question for the committee

4. Does the committee agree with refining this category to include only those entities that are subject to the National Association of Insurance Commissioners (NAIC) Annual Financial Reporting Model Regulation (Model Audit Rule), and whose auditors are required to follow independence requirements included in Section 7 (Qualifications of Independent Certified Public Accountant) of the Model Audit Rule?

Additional categories recommended

IESBA's application guidance indicates that ethics standards-setting bodies are expected to add categories. The application guidance identifies the following possible additional categories:

- Pension funds
- Collective investment vehicles

- Private entities with large numbers of stakeholders (other than investors)
- Not-for-profit organizations or governmental entities
- Public utilities

Following are the additional categories the task force recommends adding as PIEs.

Pension funds

The task force recommends adding a category to the definition that would capture Form 11-K filers (Annual Report of Employee Stock Purchase, Savings, and Similar Plans Pursuant to Section 15(d) of the Securities Exchange Act of 1934).

> ***Employee benefit plans that are required to file Form 11-K with the SEC under Section 15(d) of the Exchange Act***

This category is necessary because the plan has a company stock fund component, where participants can invest in the sponsor company's publicly traded stock and auditors must comply with the SEC issuer independence rules.

The auditor's report must include a disclosure that the auditor is independent in accordance with the U.S. federal securities laws and the applicable rules and regulations of the SEC and the PCAOB.

Other types of employee benefit plans in the U.S. include plans subject to Title 1 of ERISA (besides 11-K plans), governmental employee benefit plans, church plans and other plans established and maintained solely for the purpose of complying with applicable workers' compensation, unemployment compensation, or disability insurance laws.

Plans subject to Title 1 of ERISA are required to file a Form 5500 with the Department of Labor (DOL). Plans with more than 100 eligible participants are required to have a financial statement audit performed by an independent qualified public accountant. The DOL is the regulator of these plans and recently updated their independence rules, which in some respects are more restrictive than the AICPA independence rules but are not as extensive as the SEC's issuer independence rules.

These other plans regulated by the DOL are subject to regulatory supervision designed to provide confidence that the entity will meet its financial obligations (factor 2). It is not necessary to treat these other employee benefit plans as PIEs. The public is sufficiently protected with the existing independence standards required for auditors.

Collective investment vehicles

The task force recommends adding a category to the PIE definition that will capture investment companies (including mutual funds) that are registered with the SEC.

Included in this new category are “similar products” such as, real estate investment trusts (REIT), unit investment trusts (UIT), and business development companies (BDC). These additional entities, similar to registered investment companies, are subject to the SEC’s issuer independence requirements, as outlined in Regulation S-X Rule 2-01 Qualifications of Accountants. The task force recommends adding a category to capture these entities.

An investment company or similar product that is registered with the SEC

The auditor’s report must include a disclosure that the auditor is independent in accordance with the U.S. federal securities laws and the applicable rules and regulations of the SEC and the PCAOB.

General category

IESBA’s new PIE definition also includes a general category to capture any additional entities where stakeholders would have heightened expectations because of the significance of the public interest in the financial condition of the entity. The task force recommends adding a general category related to entities whose audits are subject to the SEC issuer independence rules but will not be captured by one of the other proposed categories.

Any entity for which an audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to an audit of an issuer, as defined in Section 10A(f) of the Securities Act of 1934

An example of such an entity is a financial market utility that is registered with the Securities Clearing Agency and is subject to SEC issuer independence rules. Discussions are ongoing about whether to include this as an example of an entity in the general category or as an example in a Q&A. The task force expects to bring a recommendation to the committee at its meeting in February 2023.

Questions for the committee

5. Does the committee agree an additional PIE category should be added for employee benefit plans that are required to file Form 11-K with the SEC under Section 15(d) of the Exchange Act?

6. Does the committee agree an additional PIE category should be added for investment companies or similar products that are registered with the SEC?

7. Does the committee agree the general category should be included in the PIE definition?

Additional PIE categories being considered

Non-issuer broker-dealers registered with the SEC

Non-issuer broker-dealers would *not* be captured by the refined category "publicly traded entity" or general category as these entities are not publicly traded, and the auditor would not be subject to the SEC issuer independence rules.[6] The auditors of these entities would be subject to SEC non-issuer independence rules as well as certain PCAOB independence rules.

The task force has discussed this potential category extensively. The task force has not yet reached a consensus on a recommendation about whether these entities should be added as a new category of PIE and is therefore seeking committee input. Because the SEC has not explicitly required the auditors of these entities to be subject to the SEC issuer independence rules under Rule 2-01[7], if these entities end up categorized as PIEs, the AICPA code will need revisions to add the additional independence requirements will.

Question for the committee

8. Do committee members have views on the inclusion or exclusion of non-issuer broker-dealers as a PIE?

Funds that are advised by an investment advisor registered with the SEC where the advisor chooses to rely on the audit of the fund to meet the exemption in SEC Rule 206(4)-2, Custody of funds or securities of clients by investment advisers, under the Investment Advisers Act of 1940 (the custody rule)

Private equity funds and hedge funds with an advisor who is registered with the SEC and relies upon the private audit opinion to meet the custody rule exception of Rule 206 will not be included in the general category because these entities are not subject to the SEC issuer independence rules.[6]

Most members of the task force believe these funds should not be included as a category of PIE. These are a few observations that support not adding these entities as a new category:

- The SEC has already determined that the public is protected without requiring the

[6] CAQ alert "SEC/PCAOB Independence Rules for Non-Issuer Audit and Attestation Engagements."

[7] In August 2003 the SEC issued a Q&A that clarified "…for brokers and dealers or investment advisors that are not issuers as defined in the Act, the auditors would not be subject to the rotation requirements, or the compensation requirements of the Commission's independence rules…"

auditors of these entities to be subject to the issuer independence rules.

- These entities are private funds and not publicly traded.
- Unlike issuers and non-issuer broker-dealers, the auditors of these funds are not subject to the PCAOB's jurisdiction and standards.

Question for the committee

9. Do committee members have views on the inclusion or exclusion of private equity funds and hedge funds as a PIE?

Category not being recommended

Not-for-profit and governmental entities

In 2018 the U.S. Government Accountability Office (GAO) considered what independence rules should apply to entities subject to the "Yellow Book" and revised the Government Auditing Standards to incorporate more robust independence requirements.

The revised independence standards are in some respects more restrictive than those of the AICPA (for example, the preparation of accounting records and financial statement services are considered to create significant threats to independence).

Because of the enhanced independence requirements established by the GAO and the fact that the regulator did not believe it was necessary to adopt the more restrictive SEC independence rules, the task force does not recommend not-for-profit and governmental entities be added as an additional category of PIE.

Question for the committee

10. Does the committee agree that not-for-profit and governmental entities should not be included in the PIE definition?

Firm provision

IESBA's application guidance also encourages firms to consider whether to treat additional entities as PIEs.

The AICPA's extant PIE definition contains a similar encouragement:

Members may wish to consider whether additional entities should also be treated as public interest entities because they have a large number and wide range of stakeholders. Factors to be considered may include

- the nature of the business, such as the holding of assets in a fiduciary capacity for a large number of stakeholders;
- size; and
- number of employees.

The task force recommends that only the beginning of the first sentence in the extant definition be included in the revised PIE definition.

Members may wish to consider whether additional entities should also be treated as public interest entities~~. because they have a large number and wide range of stakeholders. Factors to be considered may include~~

- ~~the nature of the business, such as the holding of assets in a fiduciary capacity for a large number of stakeholders;~~
- ~~size; and~~
- ~~number of employees.~~

The task force recommends that the staff draft a Q&A that provides factors a member may wish to consider when deciding whether to treat an entity as a PIE that has not been captured by the refined categories. The task force will consider those factors that IESBA believes firms should consider as described in 7–12 above under "Background."

Question for the committee

11. Does the committee agree with the task force's recommendation of a Q&A?

Transparency requirement

IESBA's standard also includes the following transparency requirement.

Public Disclosure – Application of Independence Requirements for Public Interest Entities

R400.20 Subject to paragraph R400.21, when a firm has applied the independence requirements for public interest entities as described in

paragraph 400.8 in performing an audit of the financial statements of an entity, the firm shall publicly disclose that fact in a manner deemed appropriate, taking into account the timing and accessibility of the information to stakeholders.

R400.21 As an exception to paragraph R400.20, a firm may not make such a disclosure if doing so will result in disclosing confidential future plans of the entity.

Because the requirement doesn't stipulate where the disclosure is made, the International Auditing and Assurance Standards Board (IAASB) has a project underway to determine where the disclosure should be made. As part of this project, IAASB issued an exposure draft. Comments were due October 4, 2022.

Based on the proposed refinements to date, the AICPA will not need to incorporate the transparency requirement into the code. The goal of transparency will be achieved by the regulator that is specified in the refined definition because the regulations of these regulators require disclosure in their auditor's report or in the case of the NAIC, a letter attached to the auditor's report.

The task force is still evaluating potential categories that may include entities that would not require disclosure of compliance with enhanced independence rules. Discussions on the requirement for transparency are ongoing.

Materials presented

Agenda item 8B: Preliminary draft revised public interest entity (PIE) definition

Preliminary draft revised public interest entity (PIE) definition

Text in green font is from the IESBA code.

Text in regular black font is from the extant AICPA code.

Text in ***bold italic font*** are additions the task force recommends adding to the preliminary draft revised definition.

Text in strikethrough are deletions the task force recommends not be included in the preliminary draft revised definition.

Publicly traded entity

An entity that issues financial instruments that are transferrable and traded through a publicly accessible market mechanism, including through listing on a stock exchange.

~~***A listed entity as defined by relevant securities law or regulation is an example of a publicly traded entity.***~~

Public interest entity

~~For the purposes of Part 4A, a~~***A***n entity is a public interest entity when it falls within any of the following categories:

a. ~~All listed entities, including entities that are outside the United States whose shares, stock, or debt are quoted or listed on a recognized stock exchange or marketed under the regulations of a recognized stock exchange or other equivalent body.~~ ***A publicly traded entity that is subject to Regulation S-X, SEC Rule 2-01, "Qualifications of Accountants";***

b. ***An entity one of whose main functions is to take deposits from the public that meets the annual audit requirement imposed by Sections 363.1(a) and 363.2(a) of Part 363 of the FDIC's regulations (12 CFR 363 – "Annual Independent Audits and Reporting Requirements");***

c. ***An entity one of whose main functions is to provide insurance to the public that is subject to the NAIC Annual Financial Reporting Model Regulation (Model Audit Rule), and whose auditor is required to follow independence requirements included in Section 7 (Qualifications of Independent Certified Public Accountant) of the Model Audit Rule***; ~~or~~

d. ***An employee benefit plan that is required to file Form 11-K with the SEC under Section 15(d) of the Exchange Act;***

e. ***An investment company or similar product that is registered with the SEC; or***

~~b.~~ ***f.*** ~~An entity specified as such by law, regulation or professional standards to meet the purpose described in paragraph 400.10.~~ Any entity***, other than those set forth in a. – e. above,*** for which an audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to an audit of ***an issuer, as defined in Section 10A(f) of the Securities Act of 1934*** ~~listed entities (for example, requirements of the SEC, the PCAOB, or other similar regulators or standard setters).~~

Members may wish to consider whether additional entities should also be treated as public interest entities ~~because they have a large number and wide range of stakeholders~~. ~~Factors to be considered may include~~

- ~~the nature of the business, such as the holding of assets in a fiduciary capacity for a large number of stakeholders;~~
- ~~size; and~~
- ~~number of employees.~~

Members should refer to the independence regulations of applicable authoritative regulatory bodies when a member performs attest services and is required to be independent of the attest client under such regulations.

If a member decides to consider whether additional entities should be treated as PIEs, a nonauthoritative question and answer is available in **Ethics Questions and Answers** ***section 100 at [link to Q&A] that provides examples of factors that may assist the member.***

IESBA update

Reason for agenda item

To provide project summaries for IESBA's key projects and task forces.

Division staff welcomes input on any of the projects.

Materials presented

- Agenda item 9B: Tax planning and related services
- Agenda item 9C: PIE rollout
- Agenda item 9D: Technology
- Agenda item 9E: Engagement team
- Agenda item 9F: Strategy and work plan
- Agenda item 9G: Sustainability

Tax planning and related services

Convergence considerations

It is too early to determine convergence considerations; however, division staff is keeping the AICPA tax division abreast of the project.

Project description

The objective of the project is to develop a principles-based framework, leveraging the fundamental principles and the conceptual framework, to guide professional accountants' ethical conduct when providing tax planning and related services to employing organizations and clients, thereby maintaining the International Ethics Standards Board for Accountants (IESBA) code's robustness and relevance as a cornerstone of public trust in the global accountancy profession.

At a high level, the approved project proposal explains that the framework will do the following:

- Provide guidance to assist the professional accountant (PA) in identifying what might be deemed acceptable or unacceptable tax planning behavior in the context of the fundamental principles. The project will explore the following approach:
  - — Understand the applicable tax laws and regulations, including as far as possible the legislative intent, and comply with them.
  - — Obtain an understanding of the rationale for the particular tax scheme, structure, or transaction, considering a reasonable and informed third party's perceptions. In this regard, the project will develop guidance on indicators of what might be deemed acceptable versus unacceptable tax planning in the light of understanding that rationale, drawing on the work done by other organizations.
  - — If there is no intent to promote indication or perception of unacceptable tax planning, provide guidance on applying the conceptual framework to the tax planning facts and circumstances, that is, what types of threats might be created and what actions, including safeguards, might address the threats. This might include guidance to navigate situations where the legislative intent behind tax laws and regulations is uncertain.
- Address circumstances where there might be undue pressure, whether from management or from a client, to skirt the boundaries of what might be deemed acceptable tax planning. Linking to the provisions of the code addressing pressure to breach the fundamental principles might be appropriate in this regard.
- Recognize that an inducement might be offered to achieve certain tax outcomes in strict

noncompliance with tax legislation. Linking to the provisions of the code addressing inducements might be appropriate in this regard.

- Provide guidance for when communication with management or those charged with governance is appropriate, including as part of an escalation process, the matters or concerns that might be communicated. In this regard, professional accountants in business (PAIBs) might be guided to consider internal protocols, policies, or procedures for referring matters.

- Provide guidance on when and with whom to consult (internally or externally), which might be a part of specific actions to address identified threats.

- Address considerations relating to transparency balanced against the PA's duty of confidentiality under the code, including

    — the circumstances in which transparency will be appropriate or justified (for example, as a safeguard to address threats, to disclose risks from uncertainties, or to disclose the rationale for a particular tax scheme, structure or transaction intent);

    — when informed consent for disclosure should be obtained in the case of clients;

    — to whom disclosure might be made and when; and

    — the matters that might be disclosed.

- Address any documentation expectations for the PA.

AICPA input on the project

Ethics and tax division staff provided input to IESBA's Tax Planning and Related Services Task Force (TPRS) on the proposals included in IESBA's September 2022 agenda papers. In addition, staff provided input to a member of TPRS after the September meeting based on updates from TPRS during IESBA's September meeting. Staff is closely monitoring whether TPRS gets involved with matters outside of its purview, such as tax morality.[1]

PEEC itself has not yet provided input.

AICPA staff welcomes PEEC's comments on the project including any concerns the committee believes should be monitored or conveyed to the project task force or IESBA.

[1] The project proposal asserted that the guidance developed will "respect and not undermine national sovereignty to enact and promulgate" not only "tax laws and regulations as each jurisdiction sees fit" but ethical tax standards.

Status

The task force recommended that two new sections be added to the IESBA code to provide guidance on tax planning and related services. Proposed new section 280 applies to professional accountants in business and proposed new section 380 applies to professional accountants in public practice. Though the proposals provide a significant amount of application guidance, at a high level, both proposals require the following about of the PA:

- Must obtain an understanding of the tax laws and regulations in their jurisdiction that prohibit certain tax planning arrangements.
- Must obtain an understanding of the tax planning service requested including the goals of the tax planning and the relevant tax laws and regulations. When the PA is in public practice, they are also required to obtain an understanding of the client, its owners, management and those charged with governance, and its business activities.
- Must explain the basis on which the PA advised or recommended a tax planning arrangement.
- Should advise on a tax planning arrangement only if the PA has established a credible basis[2] in laws and regulations for the arrangement.
- Must consider the reputational, commercial, and wider economic risks and consequences arising from the way stakeholders might view the arrangement before providing advice that has a credible basis. This is referred to in the agenda paper as "the stand-back test."
- Must discuss the nature of uncertainty[3] with the client, management, and those charged with governance (where appropriate).
- Must communicate that a tax planning arrangement that the PA does not believe has a credible basis should not be pursued and what the risks are if it is. If the arrangement is pursued, the PA is also required to take steps to dissociate from a tax planning arrangement. When this disagreement occurs for a PA in business, the requirement is scalable based upon the PA's role at the organization.

IESBA provided input on the proposals and the task force is expected to revise the proposals and seek approval to expose them during IESBA's December 2022 meeting.

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[2] It was reported that the term "creditable basis" was used since it seemed jurisdictionally neutral, that is, the task force had not identified any jurisdictions that used that threshold.

[3] Uncertainty as to whether a proposed tax planning arrangement will comply with the relevant tax laws and regulations.

PIE rollout

Project description

In April 2022, IESBA released the *Final Pronouncement: Revisions to the Definitions of Listed Entity and Public Interest in the Code* (PIE final pronouncement) along with a staff-prepared Basis for Conclusions document.

This project involves rollout activities to raise awareness and promote adoption and implementation of IESBA's revisions to the definitions of "listed entity" and "public interest entity" (PIE) in the code.

PEEC input on the project

Staff shared the draft Q&As with PEEC's PIE task force during its kickoff meeting in June 2022.

Status

Key activities reported at the September 2022 IESBA meeting include the following:

- Panel discussion co-hosted by IFAC and ASEAN Federation of Accountants – October
- Panel discussion co-hosted by the Pan African Federation of Accountants – October
- Meeting with Accountancy Europe's Ethics and Competence Working Party – October
- Q&As – Expected issuance in 4Q 2022
- Updated jurisdictional PIE definitions database project – Expected initiation in 4Q 2022

Technology

Convergence considerations

Convergence steps may be necessary if IESBA adopts the proposal.

Project description

To propose technology-related revisions to the IESBA code and to develop nonauthoritative material.

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

The fact finding[1] and development of nonauthoritative material[2] is being conducted by the Technology Working Group (TWG). During the September 2022 meeting the TWG presented its draft final phase 2 report. The final report will be released by the end of 2022.

PEEC input on the project

PEEC submitted a comment letter on the exposure draft.

Status

Following is a summary of the components of the TTF's exposure draft. Staff has noted where PEEC's comment letter expressed concern. In addition, staff included updates from the September 2022 IESBA meeting. For detailed information from the September 2022 meeting, refer to the memo that outlines the significant issues raised by respondents, the marked text from the exposure draft and the presentation material from the meeting.

> NOTE: For context, history and background from previous PEEC meeting agendas are included in the following sections. Updates since the August meeting are highlighted.

Professional competence and due care

The proposal includes revisions to the *Professional Competence and Due Care* subsection.

[1] The TWG will conduct fact-finding and information gathering on disruptive technologies and related issues, including blockchain (e.g., cryptocurrencies and initial coin and security token offerings), cyber-security, cloud-based services, internet of things (IoT), and data governance.

[2] The TWG plans to develop nonauthoritative materials related to ethical leadership in an era of complexity and digital change; confidentiality and privacy; auditor independence; and accountability and transparency.

One addition emphasizes that serving clients and employing organizations with professional competence and due care involves the application of interpersonal, communication, and organizational skills. The TTF acknowledges that these skills are not necessarily limited to technology; however, they are increasingly regarded as critical skills for the future-ready accountant.

In the comment letter, PEEC expressed disagreement that interpersonal, communication, and organizational skills should be required for professional competence. Professional accountants have varying levels of soft skills and abilities and, as drafted, the proposal could be taken to imply that neurodiverse individuals are not competent.

PEEC also noted that application paragraphs should not contain requirements and offered a suggested revision to the proposal. The other addition to this subsection is a requirement that when professional accountants believe it is appropriate to make users aware of the limitations inherent in their services or activities, they provide sufficient information to enable the recipient to understand the implications of such limitations. Though the TTF acknowledges this communication is not limited to technology, they believe this addition is in line with increasing public demand for transparency.

During the September 2022 meeting the TTF reported that there was “reserved support” for this provision. One suggestion made by a commenter that the TTF agreed to consider was to rephase the following sentence. Staff believes this rephasing would address PEEC’s concern.

> For example, interpersonal, communication and organizational skills may facilitate interactions with entities and individuals with which the professional accountant, the firm or the employing organization has a professional or business relationship.

Confidentiality

The proposal includes an addition to the *Confidentiality* subsection to emphasize the professional accountant’s role in more actively protecting confidential information given changes in public expectations.

> Maintaining the confidentiality of information acquired in the course of professional and business relationships involves the professional accountant taking appropriate action to secure such information in the course of its collection, use, transfer, storage, dissemination, and lawful destruction.

The proposal also includes a definition of confidential information.

> Confidential information: Any information, data, or other material in whatever form or medium (including written, electronic, visual, or oral) that is not in the public domain.

The proposal includes refinements to paragraph 114.A3 to enhance the flow of the

Confidentiality subsection and to modernize the characterization of means of communications. The proposed refinements to this paragraph are:

> In deciding whether to disclose confidential information, factors to consider, depending on the circumstances, include:
>
> - Whether the interests of any parties, including third parties whose interests might be affected, could be harmed if the client or employing organization consents to the disclosure of information by the professional accountant.
> - Whether all the relevant information is known and substantiated, to the extent practicable. Factors affecting the decision to disclose include:
>   - — Unsubstantiated facts
>   - — Incomplete information
>   - — Unsubstantiated conclusions
> - The proposed means ~~type~~ of communicat***ing***~~on,~~ ***the information*** ~~and to whom it is addressed~~.
> - Whether the parties to whom the ***information*** ~~communication~~ is ***to be*** addressed ***or access is to be granted*** are appropriate recipients.

PEEC's Protecting Client Confidentiality and Data Security Task Force discussions

The task force met to discuss the confidentiality additions. Their feedback on the confidentiality topics follows and was included in PEEC's comment letter:

- The definition of confidential information seems broad enough to accommodate for changes in technology without having to revise.
- With respect to the addition to the *Confidentiality* subsection to emphasize the professional accountant's role in more actively protecting confidential information given changes in public expectations
  - — Encourage IESBA to retain the phrase "appropriate action." The task force believes this will allow jurisdictions to adopt the necessary clarity needed to align with their laws and regulations.[3]
  - — Request that IESBA provide clarity into why they used both professional and business relationships. The task force believes that when a professional accountant has a business relationship with an entity or individual, a professional

[3] The task force noted that if this phrase is adopted by IESBA, PEEC might consider using the reasonable third-party test when converging with the standard.

relationship also exists. Perhaps clarifying what relationships are covered by each would help provide guidance about what the appropriate guardrails are.

During the September 2022 meeting the TTF reported that there was “broad support” for this provision along with suggestions and clarifications. The TTF proposed an edit to clarify that confidentiality should still be maintained even when the public accountant is aware that improper disclosure of that information has occurred.

The TTF also proposed adding the following application guidance about what information to provide when seeking consent to disclose confidential information:

- The nature of the information to be used;
- The purpose for which the information is to be used by the individual or entity obtaining consent (for example, training, development of technology, research or benchmarking data or studies);
- The individual or entity who will undertake the purpose for which the information is to be used;
- Whether the identity of the individual or entity that provided such information or any individuals or entities to which such information relates will be identifiable from the output of the purpose for which the information is to be used.

Additionally, the TTF proposed this revision to the definition of “confidential information”:

> Any information, data or other material in whatever form or medium (including written, electronic, visual or oral) ***that is not publicly available*** ~~is not in the public domain~~.

Complex circumstances and applying the conceptual framework

The proposal recognizes that complex circumstances might increase the challenges of applying the conceptual framework but is not a new threat per se. It describes the facts and circumstances that increase the challenges in applying the conceptual framework in complex circumstances and provides examples of actions that might help professional accountants manage and mitigate the challenges arising from such circumstances.

The proposal explains that complex circumstances arise where the relevant facts and circumstances involve (*a*) elements that are uncertain and (*b*) multiple variables and assumptions, which are interconnected or interdependent. The proposal also acknowledges that these facts and circumstances might also be rapidly changing.

Following are examples of possible actions included in the proposal:

- Consulting with others, including experts, to ensure appropriate challenge and additional input as part of the evaluation process
- Using technology to analyze relevant data to better inform the accountant's judgement
- Making the firm or employing organization and, if appropriate, relevant stakeholders aware of inherent uncertainties or difficulties arising from the facts and circumstances
- Monitoring any developments or changes in facts and circumstances and assessing whether they might impact any judgments the accountant has made

PEEC expressed concern with the clarity of the guidance and therefore, the potential for inconsistent application. PEEC recommended addressing this topic in nonauthoritative materials so that examples or scenarios could be used to demonstrate how complexity can play a role when applying the conceptual framework.

During the September 2022 meeting the TTF reported that there were "mixed views" for this provision. Some of the reservations expressed nclude these:

- Lack of clarity
- Content too vague
- Whether the application material was really needed in the code
- Whether the guidance is consistent with the IAASB's guidance

To address some of these reservations, the TTF proposed relocating the content to the Conceptual Framework as part of the "Exercising Professional Judgment" discussion.

The TTF also proposed simplifying the drafting for understanding and applicability as follows.

> The circumstances in which professional accountants carry out professional activities and the factors involved vary considerably in their range and complexity. The professional judgment exercised by accountants might need to take into account the complexity arising from the compounding effect of the interaction between, and changes in, elements of the facts and circumstances that are uncertain and variables and assumptions that are interconnected or interdependent.
>
> Managing complexity might include:
>
> - Analyzing, and investigating, as relevant, any uncertain elements, the multiple variables and assumptions and how they are interconnected or interdependent.
> - Using technology to analyze relevant data to better inform the professional

accountant's judgment.

- Consulting with others, including experts, to ensure appropriate challenge and additional input as part of the evaluation process.

- Being alert to any developments or changes in the facts and circumstances and assessing whether they might impact any judgments the accountant has made. (Ref: Para. R120.9 and 120.9 A1).

- Making the firm or employing organization and, if appropriate, relevant stakeholders aware of the inherent uncertainties or difficulties arising from the facts and circumstances.

Organizational culture

The proposal includes application guidance to the conceptual framework that explains professional accountants are expected to demonstrate ethical behavior in dealings with business organizations and individuals with which the accountant or the firm or employing organization has a professional or business relationship.

During the September 2022 meeting the TTF proposed the discussion on ethical leadership from extant 200.5 A3 be mirrored in the part 3, for professional accountant in public practice.

In addition, the TTF proposed a clarifying edit to address questions about whether the term "demonstrate" in the following bullet imposed a documentation requirement.

> ***Exhibit*** ~~Demonstrate~~ ethical behavior in dealings with ~~business organizations and~~ individuals with which the accountant, the firm or the employing organization has a professional or business relationship.

Factors that affect the application of the conceptual framework when technology is used

The proposal explains that when a professional accountant (in business or in public practice) relies on output from technology, the following factors may help identify threats to the fundamental principles:

- Whether the information about how the technology functions is available to the accountant
- Whether the technology is appropriate for the purpose in which it is to be used
- Whether the accountant has the professional competence to understand, use and explain the output from the technology
- Whether the technology incorporates expertise or judgments of the accountant or the employing organization/firm

- Whether the technology was designed or developed by the accountant or employing organization/firm and therefore might create a self-interest or self-review threat

PEEC recommended that IESBA specify which threats relate to each consideration as done in the final bullet above.

During the September 2022 meeting the TTF reported that comments were “generally supportive” for this provision.

Input included clarification regarding whether technology incorporates expertise or judgements of the accountant or the employing organization/firm and whether the accountant has the professional competence to understand, use and explain the output from the technology.

In addition, suggestions were made including linking the considerations to specific threats, adding a subheading, safeguards and considerations as well as including specific issues related to artificial intelligence systems.

To address some of this feedback, the TTF proposed the discussion be revised as follows

> *Identifying Threats Associated with the Use of Technology*
> The following are examples of facts and circumstances relating to the use of technology that might create threats for a professional accountant when undertaking a professional activity:
>
> - Self-interest threats
>
> - The data available is not sufficient for the effective deployment of the technology.
>
> - Information about how the technology functions is not available to the accountant.
>
> - The technology is not appropriate for the purpose for which it is to be used.
>
> - The accountant does not have sufficient expertise, or access to an expert with sufficient understanding, to use and explain the output from the technology, for the purpose intended. (Ref: Para. 230.2).
>
> - Self-interest or Self-review threats
>
> - Use of the technology requires the knowledge, expertise or judgment of the accountant or the employing organization.
>
> - The technology was designed or developed using the knowledge,

expertise or judgment of the accountant or employing organization.

The TTF also recommended adding a new discussion to address

> The professional accountant's evaluation of the level of a threat associated with the use of technology might also be impacted by the work environment within the employing organization and its operating environment. For example:
>
> - Level of corporate oversight and internal controls over the technology.
> - Assessments of the quality and functionality of technology are undertaken by a third-party.
> - Training is provided regularly to all relevant employees so they obtain the professional competence to sufficiently understand, use and explain the output from the technology.

Using or relying on the work of others or on the output of technology

The proposal adds explicit references to technology relating to using or relying on the work of others and provides factors to consider when determining whether reliance on technology is reasonable. The proposal also highlights that the professional accountant's position may be a factor to consider because the position could affect the opportunity and ability to obtain the needed information.

The factors included in the proposal are as follows:

- The nature of the activity to be performed by the technology
- The expected use of, or extent of reliance on the output from the technology
- The professional accountant's ability to understand the output from the technology for the context in which it is to be used
- Whether the technology is established and effective for the purpose intended
- Whether the technology has been appropriately tested and evaluated for the purpose intended
- The reputation of the developer of the technology if acquired from or developed by an external vendor
- The employing organization's or firm's oversight of the design, development, implementation, operation, maintenance, monitoring or updating of the technology
- The appropriateness of the inputs to the technology, including data and any related decisions

PEEC recommended that this content not be combined with the discussion about relying on the work of others, rather appear as its own discussion. In addition, PEEC recommended IESBA explain why the scope of the guidance in part 2 and part 3 differs (reliance on versus use of the output of technology). PEEC also requested that IESBA provide additional guidance on how professional accountants should apply the factors, including practical examples.

During the September 2022 meeting the TTF reported that comments were "generally supportive" for this provision. The reservations were including the discussion within the same section as using the work of an expert and focusing on just the output of technology as opposed to the whole process.

These were some of the suggestions for resolving the issues:

- Clarify how the reputation of the software developer is assessed.
- Add factors such as controls over user access.
- Emphasize the accountant's accountability such as when decision-making is automated.

In response to this feedback the TTF moved the guidance related to using the output of technology from the section "Using the Work of an Expert or the Output of Technology" into its own section.

Prohibition on assuming management responsibilities

The proposal includes a reminder that when technology is used in performing a professional activity for an attest client, the prohibition on assuming a management responsibility applies regardless of the nature or extent of such use.

Business relationships

The proposal expands one of the examples and adds an additional example of what could constitute a close business relationship to the *General* subsection of the *Business Relationships* section of the IISs.

The example that explains a close business relationship would include situations where a firm or client distributes or markets the other's products was expanded to include situations where the products or services or sold or resold. The new example of a close business relationship involves arrangements under which the firm or a network firm develops jointly with the client, products or solutions which one or both parties sell or license to third parties.

In response to the 24 percent of survey respondents who indicated that they did not think that nonassurance services (NAS) provisions are relevant when a firm licenses technology that performs NAS to the audit client, the proposal adds a reminder to the Business Relationship section (section 520) that the NAS provisions in fact do apply. The reminder also clarifies that

this not only applies when a firm licenses technology but when a firm provides, sells, or resells such technology. This reminder was also added to the introduction discussion of the NAS provision (section 600). PEEC was not supportive of adding either of these reminders.

During the September 2022 meeting the TTF reported that there was “broad support” for the provisions. It was suggested that examples and a general principle for identifying and assessing “close business relationships” be added.

The TTF reported that they believe developing a general principle for identifying and assessing close business relationships is outside of their scope. They did recommend a new application paragraph to highlight “arrangements under which the firm or a network firm licenses products or solutions to or from a client might create a close business relationship.”

The TTF also reported that they *would* clarify in the basis for conclusion that the NAS provision would not be applicable when an accountant just passes through the license to a client as a reseller.

Threats when providing nonassurance services

The proposal includes an additional technology-related factor that is relevant in identifying the different threats that might be created by providing NAS to an audit client and evaluating the level of such threats.

> The client’s dependency on the service, including the frequency with which the service will be provided.

Accounting and bookkeeping services

The proposal adds application guidance to the *Accounting and Bookkeeping Services* subsection of the IISs to highlight that automated nonattest services are not necessarily routine and mechanical.

> Accounting and bookkeeping services can either be manual or automated. In determining whether an automated service is routine or mechanical, factors to be considered include how the technology functions and whether the technology is based on expertise or judgment attributable to the firm or the network firm.

PEEC requested clarification about the relevance of how the technology functions when determining whether an automated service is routine and mechanical. If IESBA chooses not to add the clarification, PEEC recommended the phrase “factors to be considered include how the technology functions and” be replaced by “a firm may consider.”

During the September 2022 meeting the TTF proposed the following clarifying revisions.

> Accounting and bookkeeping services can either be manual or automated. In

determining whether an automated service is routine or mechanical, factors to be considered include ***the activities performed by, and the output of, the technology, and*** ~~how the technology functions and~~ whether the technology ~~is based on~~ ***provides an automated service that is based on or*** requires the expertise or judgment~~s~~ of the firm or ~~a~~ network firm

Information technology system services

The proposal adds the following application guidance to the *Information Technology System Services* subsection of the IISs:

- Provides an expanded description of information technology (IT) systems services to highlight that the services related to IT systems extend beyond the design, or implementation of hardware or software systems. The expanded description includes
    - — Designing or developing hardware or software IT systems
    - — Implementing IT systems, including installation, configuration, interfacing, or customization
    - — Operating, maintaining, monitoring, or updating IT systems
    - — Collecting or storing data or managing (directly or indirectly) the hosting of data on behalf of the audit client
- Clarifies what the client is required to do to ensure the firm does not assume a management responsibility and adds two examples of services that would involve assuming a management responsibility. One example added is when a firm or network firm operates the audit client's network security, business continuity or disaster recovery function. The other example added is when the firm or network firm provides services in relation to the hosting (directly or indirectly) of an audit client's data. With respect to the hosting services example, it is clarified that collection, receipt and retention of data provided by the audit client to enable the provision of a permissible service would not result in assuming a management responsibility.
- Incorporates examples of IT systems services that might create a self-review threat when they form part of or affect an audit client's accounting records or system of internal control over financial reporting:
    - — Designing, developing, implementing, operating, maintaining, monitoring, or updating IT systems
    - — Supporting an audit client's IT systems, including network and software applications
    - — Implementing accounting or financial information reporting software whether or not it was developed by the firm or a network firm

PEEC expressed several concerns with these elements of the exposure draft, including the following:

- The proposal should clarify that an IT system does not include a tool that performs only discrete calculations when the audit client evaluates and accepts responsibility for the input and assumptions and the audit client has sufficient information to understand the calculation and the results.

- With respect to hosting services, the parenthetical text "(directly or indirectly)" should be clarified using the discussion from the explanatory material. If such clarification is not added, then the parenthetical text should not be included in the code and should be addressed as a Q&A.

- The examples of services that do not create self-review threats should remain in the code and be expanded to include examples of commercial-off-the-shelf implementation services.

During the September 2022 meeting the TTF reported that there was "broad support" for the provisions. With respect to hosting, requests for clarification were received along with concern that as drafted it was too broad and unclear. In response the TTF clarified that the use of portals for providing permissible services was not prohibited and proposed the following revisions to address the concerns noted above.

> Examples of IT systems services that result in the assumption of a management responsibility include where a firm or a network firm:
>
> - ***Stores data or manages (directly or indirectly) the hosting of data on behalf of the audit client***. ~~Provides services in relation to the hosting (directly or indirectly) of an audit client's data.~~ ***Such hosting includes:***
>
> ***(a) Acting as the only access to a financial or non-financial information system of the audit client;***
>
> ***(b) Taking custody of or storing the audit client's data or records such that the audit client's data or records are otherwise incomplete; or***
>
> ***(c) Providing electronic security or back-up services, such as business continuity or a disaster recovery function, for the audit client's data or records.***
>
> - ***Operates, maintains, or monitors the audit client's IT systems or website.***
>
> - ~~Operates an audit client's network security, business continuity or disaster recovery~~

~~function~~.

Engagement team

Convergence considerations

Professional Ethics Division staff is currently performing the preliminary assessment of convergence needs. Staff notes that the AICPA Code of Professional Conduct (code) does not provide guidance related to component auditors who are outside of the network firm. Therefore, PEEC may need a convergence project to provide specific guidance for these auditors.

However, PEEC may not need a convergence project for engagement quality reviewers (EQRs) as the definition of *attest engagement team* in the AICPA code seems to be drafted broadly enough to include EQRs.

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

Project description

To ensure that the International Independence Standards (IISs) provide clear and consistent guidance on independence.

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

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

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

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

If the component auditor does not meet the independence requirements relevant to the group

[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).

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 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).

PEEC input on the project

PEEC submitted a comment letter on the exposure draft.

Following is a summary of the components of the exposure draft. Staff has noted where PEEC's comment letter expressed concern.

In addition, staff has included updates from the September 2022 IESBA meeting. For detailed information from the September 2022 meeting, refer to the memo that outlines the significant issues raised by respondents and the marked text from the exposure draft.

> NOTE: For context, history and background from previous PEEC meeting agendas are included in the following sections. Updates since the August meeting are highlighted.

[2] ED-ISA 600, paragraph 22.

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

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

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 proposal revises these definitions to scope in EQRs from outside of the firm or network.

To do this, the proposal adds to all three definitions that individuals who can directly influence the outcome of the engagement include those who are engaged by the firm. The proposal also revises item (b) (iii) in each definition as follows (excerpted from the "Glossary, Including Lists of Abbreviations" section of the IESBA code):

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

During the September 2022 meeting the task force reported that there was "broad support" for these revisions and that the board did not recommend any edits on these specific points.

Definition of engagement team

The proposal

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

The proposal revises the definition of *engagement team* as follows

> 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*** external experts~~engaged by the firm or by a network firm~~ ***and internal auditors*** ~~The term "engagement team" also excludes~~

~~individuals within the client's internal audit function~~ who provide direct assistance on ***the*** ~~an audit~~ engagement ~~when the external auditor complies with the requirements of ISA 610 (Revised 2013),~~ *~~Using the Work of Internal Auditors~~*. ~~This excludes external experts engaged by the firm or by a network firm.~~

In Part 4A, the term "engagement team" refers to individuals performing audit or review procedures on the audit or review engagement, respectively. This term is further described in paragraph 400.A.

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

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

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

In Part 4B, the term "engagement team" refers to individuals performing assurance procedures on the assurance engagement.

PEEC recommended the definition of an "engagement team" also exclude other individuals that the group auditor does not direct, supervise, or assume responsibility for (for example, component auditors referred to in a group auditor's report). PEEC suggested that if IESBA does not include this in the definition, clarification could be done through nonauthoritative means.

During the September 2022 meeting the task force reported that commenters "generally supported" the proposed approach for aligning the engagement team definition of the IESBA code to the revisions to the definition of the same term in the ISQM 1 and ISA 220 (Revised).

To address requests to more clearly align the text related to ISA 620 to the standard and to clarify the auditor's responsibility, the task force recommended the following revisions

ISA 620 ~~deals with the auditor's responsibilities relating to the work of~~ ***defines an auditor's expert as*** an individual or organization ***possessing expertise*** in a field ~~of expertise~~ other than accounting or auditing, ~~when that~~ ***whose*** work ***in that field*** is used ***by the auditor*** to assist the auditor in obtaining sufficient appropriate audit evidence. ***ISA 620 deals with the auditor's responsibilities relating to the work of such experts.***

Notwithstanding the general support for the definition, commenters expressed concerns (1) related to service providers and experts; (2) with the application material; and (3) with the complexity of including engagement team members as audit team members.

The task force did not recommend any revisions to the proposals to address these concerns. However, to address the concerns related to the complexity of including engagement team members as audit team members the task force developed a diagram to help users. The diagram is found on page 36 of the memo that outlines the significant issues raised by respondents.

Individual independence

IESBA believes 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.

IESBA 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 independence standards should also require independence of the individuals involved in the group audit engagement of any components that are not related entities.

The requirement that members of the group audit team be required to be independent of the group audit client was clarified through the following addition:

> **R405.4** All members of the audit team for the group audit shall be independent of the group audit client in accordance with the requirements of this Part that are applicable to the audit team.

PEEC indicated that it will be challenging for individuals (and firms) from a component audit firm

[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 way 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."

outside of the group audit firm's network (non-network) to maintain independence with respect to related entities of the group audit client. PEEC recommended a threats and safeguard approach be applied to non-network firms and individuals from those firms versus what is currently being proposed. PEEC recommended that if IESBA adopts the strict requirement that either IESBA or IAASB provide guidance that would address matters such as what the group auditor should communicate to these non-network component audit firms.

It would be helpful to clarify that when an entity undergoes a standalone audit, the auditor will not need to comply with Section 405 when the group engagement partner concludes that the entity is not a component audit client for purposes of the group audit.

During the September 2022 meeting the task force reported that commenters "generally supported" the proposed approach for individuals. One concern expressed was that a more balanced approach that focuses only on relationships with entities more likely to threaten the individual's independence be considered.

The cost of implementing a system that could support compliance with such independence requirements at a component auditor firm level, especially for SMPs, could be disproportionate relative to the likelihood of threats created. Besides the cost factor, the task force recognized that this could become a significant compliance task that would take resources and time away from the component auditor firm's focus on the audit work, potentially adversely impacting audit quality. The task force also acknowledged that monitoring compliance with respect to all relevant related entities of the group audit client could raise some client confidentiality issues at the component auditor firm outside the group auditor firm's network.

Consequently, irrespective of whether the group audit client is a publicly traded entity, the task force proposed that the code should not require an individual from, or engaged by, a component auditor firm outside the group auditor firm's network who is involved in a group audit to be independent of the following related entities of the group audit client or other components in the group:

- Any entity that has direct or indirect control over the group audit client.
- Any sister entities of the group audit client.
- Any entities in which the group audit client, or its controlled entity, has a direct financial interest that gives it significant influence over such entities and the interest is material to the group audit client and its controlled entity.
- Any components in the group that are not related entities.

As a proportionate approach, the task force believes that audit team members within, or engaged by, a component auditor firm outside the group auditor firm's network need to be

independent of the component audit client, and the entity on whose group financial statements the group auditor firm expresses an opinion. The task force believes that those are the entities where the greatest threat to independence lies with respect to these audit team members. This proposal was referred to as option 3 in the marked text.

The task force explained that in addition to this option, they also considered the following approaches for scoping in any controlled entities of the group audit client:

- Independence would also be required in relation to all entities that are directly or indirectly controlled by the group audit client. This was referred to as option 1 in the marked text.

- The scope should additionally capture only the controlled entities connected with the component audit client, i.e., entities that also have direct or indirect control over the component audit client. This was referred to as option 2 in the marked text.

IESBA favored option 3 during its discussion of this issue at the September 2022 meeting.

Firm independence of component auditor outside of network

When a component auditor is within the group auditor's network the IESBA code already requires network firms to be independent. Accordingly, the proposal focuses 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 using the PIE or non-PIE standard that is applicable to the group audit client. To help firms apply this general rule, the proposal includes in paragraphs 405.12 A1 and 405.12 A2 three examples of how firms should apply the nonassurance services provisions.

In addition, the proposal requires the component firm *not* have a financial interest in the entity on whose group financial statements the group auditor firm expresses an opinion (R405.6 (b)). While initially this prohibition was drafted to only apply to PIEs, after feedback, the prohibition was expanded to be applicable for *all* group audit clients. IESBA does not believe that the level of the threats to independence warrant going beyond this entity (e.g., ultimate parent entity that is above the group audit client or sister entity to the component entity). This prohibition, however, would not extend to the component firm's network firms[6].

[6] This less restrictive position is not applicable to the firm issuing the audit opinion on the group financial statements and its network firms. These entities would need to be independent of the group audit client, its related entities and any other components scoped in under proposed ISA 600 (Revised).

The proposal extends the requirements and application material related to loans and guarantees (Section 511) to component firms that are outside of the network (paragraph R405.6 (c)).

The proposal requires that when a component auditor firm outside the group auditor firm's network knows, or has reason to believe, that a relationship or circumstance:

- involving the group audit client is relevant to the evaluation of the component auditor firm's independence from the component audit client, the component auditor firm shall include that relationship or circumstance when identifying, evaluating, and addressing threats to independence (R405.7).
- of a firm within the component auditor firm's network with the component audit client or the group audit client creates a threat to the component auditor firm's independence, the component auditor firm shall evaluate and address any such threat (R405.8).

The proposal also clarifies when the component audit partner is required to apply the provisions applicable to key audit partners. This is required when the group engagement partner communicates to the component audit partner that they are considered a key audit partner because they make key decisions or judgements on significant matters with respect to the group audit client.

PEEC's comments above related to individuals are also applicable to firms. In addition, PEEC recommended clarification about which PIE requirements the component audit team should apply with respect to the group audit when the component entity and group audit client are both PIEs but reside in different jurisdictions. This is important because the PIE definition may be refined differently by the jurisdictions.

During the September 2022 meeting the task force reported commenters "generally supported" the proposed approach but raised some issues to be considered.

In response to the comment about which refined PIE definition should be applied (PEEC's comment above) the task force noted that if the group audit client (the entity under group audit) is a PIE or non-PIE based on national laws, that distinction at the group level should flow to the component level for group audit purposes, regardless of whether the entity at the component level would be regarded as a PIE by national laws in that entity's jurisdiction. In addition, for group audit purposes, a component auditor firm is required to be independent of the component audit client following the code's relevant provisions, along with national requirements applicable to the group audit client (the entity under the group audit).

To address concerns related to clarifying responsibility, the task force recommended adding a new sub-section to Section 405 on communication between the group auditor firm and component auditor firms to better emphasize the group auditor firm's responsibility. This sub-

section includes a requirement that calls on the group auditor firm to communicate the necessary information at appropriate times to enable the component auditor firm to meet its responsibilities under Section 405. Furthermore, it includes application material to provide specific examples of matters the group auditor firm might communicate as well as a requirement that the component auditor firm communicate its compliance with the relevant ethical requirements to the group auditor firm. (See paragraphs R405.3, 405.3 A1 and R405.4 in the marked text.)

The task force clarified that when the group audit client is a PIE, a component auditor firm outside the group auditor firm's network must comply with the nonassurance provisions (i.e., Section 600) that are applicable to PIEs with respect to the component audit client, except paragraphs R600.21 to R600.24.The task force also proposed the following clarifications regarding "key audit partners at component level"

- Elevate the application material to a requirement and explicitly state that determining a key audit partner at a component level for group audit purposes, and communicating that determination to the relevant individual, are the engagement partner's responsibility. (See paragraph R405.15(a) in the marked text.)

- Require the group engagement partner to indicate the specific independence requirements applicable to the key audit partner at a component auditor firm for the purposes of the group audit. (See paragraph R405.15(b) in the marked text.)

Changes in component audit firms

The proposal reminds component auditors to consider relationships it had (or has) with the component auditor prior to agreeing to perform audit work. The reminder not only highlights nonattest services the component auditor firm may have provided (or is providing) but financial or business relationships (405.13 A1 and A2).

PEEC recommended that IESBA address situations that could change the independence requirements of the component auditor as it applies to mergers or acquisitions by the group audit client. An example is when a PIE group audit client acquires a non-PIE entity during or after the period covered by the group financial statements.

During the September 2022 meeting the task force reported commenters "generally supported" the proposed application material relating to changes in component auditor firms during or after the period covered by the group financial statements. The task force noted that commenters raised a few more scenarios for IESBA's consideration that they believe the code should also explicitly address. To address these suggestions the task force proposed additional guidance regarding how to apply the provisions in Section 400 in the context of a group audit when:

- A firm has provided a NAS to a component audit client prior to the period covered by the

group financial statements. (See paragraph 405 .17 A3 in the marked text.)

- A firm has provided a NAS to a component audit client prior to becoming the component auditor firm in a PIE group. (See paragraph 405.18 A1 in the marked text.)

- The group audit client later becomes a PIE. (See paragraph 405 .18 A2 in the marked text.)

The task force clarified that the process outlined in the code to address mergers or acquisitions should be followed when the group auditor firm determines – after the period during which independence is required has commenced – that audit procedures are required to be performed at a component that is not a related entity. (See paragraph R405.16 in the marked text.)

Breaches of an independence requirement by a component auditor outside of network

The general approach for a breach of independence by a component auditor that is outside of the network is the same as the process that should be followed by a component auditor that is in the network except, the component auditor outside of the network would not need to communicate with those charged with governance (TCWG).

At a high level, the process for a component auditor outside of the network would be as follows:

- Evaluate the significance of the breach and its impact on the firm's objectivity and ability to express an opinion on the component audit client's financial information for group reporting purposes.
- Determine whether it is possible to take action that satisfactorily addresses the consequences of the breach and whether such action can be taken and is appropriate in the circumstances.
- Promptly report the breach to the group audit partner and include the assessment of the significance of the breach and any actions proposed or taken to address the consequences of the breach.

Upon receiving notification of a breach by a component auditor outside of the firm, the group audit partner should do the following:

- Review the assessment of the significance of the breach and any actions proposed or taken to address the consequences of the breach.
- Evaluate whether the breach would prohibit them from relying on the component auditor.
- Determine if any further action is necessary.
- Discuss with TCWG the details of the breach, whether the action proposed or taken addresses the breach, and the firm's rational for how the breach impacts its objectivity.

If TCWG do not concur that the actions proposed or taken by the component auditor firm

satisfactorily address the consequences of the breach at the component auditor firm, the group auditor firm should not use the work for the group audit. In addition, the group audit firm should determine whether to perform further or alternative procedures or perform itself the necessary audit work procedures on the component audit client, to obtain such concurrence.

During the September 2022 meeting the task force reported many respondents supported the proposals on breaches and agreed that it is appropriate to address a breach of independence by a component auditor firm. The comments on the proposed subsection mainly highlight practical challenges regarding the application of the provisions.

To address some of the practical challenges, the task force proposed

- amendments to the introductory paragraph of the subsection to clarify that the focus of the component auditor firm's and the group auditor firm's assessment is to determine the significance and the impact of the breach on the component auditor firm's objectivity and not to reassess or review the group auditor firm's objectivity or ability to issue the group audit report. (See paragraphs 405.19 A1 and A2 in the marked text.)
- component auditor firms within the group auditor firm's network apply the same process to address a breach of an independence provision as a component auditor firm outside of the group auditor firm’s network.(See paragraph R405.20 in the marked text.)
- additional application material in line with the extant code's provisions to help a component auditor firm evaluate the significance and the impact of the breach. (See paragraph 405.20 A1 in the marked text.)
- including a requirement for component auditor firms to communicate their assessment of the significance of the breach and any actions proposed or taken to the group engagement partner in writing. (See paragraph R405.20(d) in the marked text.)
- adding application material, in line with the extant code's relevant provisions, to assist a component auditor firm in considering any actions that might be taken to address the breach. (See paragraph 405.20 A1 in the marked text.)
- clarifying that when the group engagement partner receives communication from a component auditor firm about a breach, the group engagement partner cannot evaluate the impact of the breach on the component auditor firm's objectivity. Rather, based on the available information, the group engagement partner would only be able to review the component auditor firm's assessment of the significance of the breach and its impact on the component auditor firm's objectivity. (See paragraph R405.21 in the marked text.)
- clarifying that when a breach occurs at a component auditor firm within the group auditor’s firm’s network, TCWG must be informed since the policies and procedures of the group auditor firm’s network are relevant to the considerations of TCWG regarding the group auditor firm’s independence. (See paragraph 405.23 A1 in Agenda Item 5-B.)

Strategy and work plan

Project description

To seek stakeholder input what key trends, developments, or issues IESBA should consider as it begins the process of developing its Strategy and Work Plan (SWP) 2024–2027. The IESBA Strategy Survey 2022 is open to the public and responses were requested by July 8, 2022.

AICPA staff input on the project

The AICPA Professional Ethics Division submitted a response to question 2 of the survey in July 2022.

Status

Using the results of the survey, IESBA will develop and issue for public comment a consultation paper. IESBA expects to finalize the SWP by the end of 2023 for release in early 2024.

During the September 2022 meeting, a memo summarizing the responses received, and the planning committee's (PC) initial analysis was shared. Staff encourages reading the memo summarizing the responses received as the following is a high-level summary.

Proposed strategic focus: Sustainability reporting and assurance

Questions 1 through 3 in the survey covered this focus area. These questions asked

> What level of importance do you believe the IESBA should place on dedicating strategic focus to responding through standard-setting action to the developments in sustainability reporting and assurance in its next strategy period (2024-2027)?
>
> Do you believe the IESBA should explore the concept of expanding the scope of the code to cover assurance service providers other than professional accountant's in public practice? What preconditions would need to be in place and what potential challenges, or drawbacks do you foresee if the code's provisions were scoped to the nature of the assurance services provided as opposed to who is providing the assurance services?
>
> Are there other matters the IESBA should consider with regards to this strategic focus area?

During the September 2022 IESBA meeting, the PC reported that respondents "strongly supported" IESBA's proposed strategic focus on standards-setting work in relation to sustainability reporting and assurance in light of the market demand for reliable and comparable sustainability-related information and the pace of regulatory and standards developments across the globe.

In addition, respondents also agreed that IESBA should explore the concept of expanding the

scope of the code to cover sustainability assurance providers other than professional accountants in public practice (PAPPs). Many respondents pointed out that for a scope enlargement for the code to be effective, there will be a need for a comprehensive framework of monitoring and enforcement, a system of quality management effectively designed and implemented by the service providers, as well as requirements for professional competence such as those that govern the work of the audit profession.

Proposed strategic focus: Raising the bar for PAIB ethical behavior

Question 4 in the survey covered this focus area. This question asked

> Beyond sustainability reporting which is covered under the first strategic focus area above, do you believe the IESBA should dedicate strategic focus on further raising the bar of ethical behavior for PAIBs in its next strategy period (2024-2027)?

During the September 2022 IESBA meeting, the PC reported that there was “general support” for the proposed strategic focus on raising the bar of ethical behavior for professional accountants in business (PAIBs). Respondents agreed that PAIBs play a significant role in the financial and non-financial information supply chains, and that it is important that they adhere to a high standard of ethical behavior. Some respondents suggested IESBA gain a better understanding of the expanding roles of PAIBs in senior roles such as CFOs and assess if the code sufficiently addresses the ethical challenges they face.

Proposed strategic focus: Strengthening independence standards for audit engagements

Question 5 in the survey covered this focus area. This question asked

> Do you believe the IESBA should continue to dedicate strategic focus on strengthening the IIS for audit engagements in its next strategy period (2024-2027)? If so, what specific developments or issues do you believe the IESBA should focus on beyond the matters outlined above and in Section C?

During the September 2022 IESBA meeting, the PC reported that respondents acknowledged that IESBA has significantly enhanced the International Independence Standards (IIS) in recent years. A number of respondents, including two monitoring group (MG) members, supported the proposed strategic focus on strengthening independence standards for audit engagements and have suggested additional potential projects for the SWP. Other respondents recommended that the Board slow down the pace of change in the standards. They suggested instead that the Board focus its resources on post-implementation reviews (PIRs) and research to identify new environmental issues and opportunities for further enhancement.

Proposed strategic focus: Promoting timely adoption and effective implementation of the code

Questions 6 and 7 in the survey covered this focus area. These questions asked

> Do you believe the IESBA should devote strategic focus on promoting timely adoption and effective implementation of the Code in its next strategy period (2024-2027)?
>
> Are there specific operability issues or concerns with respect to the Code you believe the IESBA should be made aware of?

During the September 2022 IESBA meeting, the PC reported that there was "strong support" from respondents for the proposed strategic focus on promoting timely adoption and effective implementation of the code. Respondents highlighted the importance of conducting PIRs on key changes to the code such as those already pre-committed by IESBA to assess the effectiveness of the revisions as well as to identify potential opportunities for further enhancement.

Other key environment trends or developments

The survey also asked respondents whether there were other key environmental trends or developments that IESBA should focus on during its next strategy period (2024-2027).

A member of the MG encouraged IESBA to be agile in resource allocations and be able to properly respond to emerging public interest issues as they arise. The member further encouraged IESBA to consider in its standards-setting toolkit an expedited process when the nature of the project (e.g., those with narrower scopes) can be completed through proper due process in a more expedited timeline to achieve the public interest objective.

Another MG member noted that:

- The code should be clear and enforceable and allow for audits to be performed on a consistent basis. The MG member suggested IESBA articulate clear ethics principles and supporting ethics provisions, along with clearly linked requirements, to promote better ethical behavior and outcomes.
- It continues to support the coordination efforts among standards-setting organizations relevant to auditing.
- Regarding the proposed projects and initiatives to be included in the consultation paper, it is important to focus on the expected outcomes associated with those projects and initiatives.

Other comments from respondents include the following:

- Some jurisdictions are experiencing difficulty in attracting and retaining talent to the profession, which in part may be due to the pace and volume of regulatory changes. On the other hand, a respondent noted that the code plays a key role in reinforcing the value

of the profession and thus will help to attract talent for firms.

- The impact of the pandemic created many changes in the work environment, for example, working from home and an inability to travel to client premises.

- There is an increasing possibility that PAPPs may split into two categories in the coming years: assurance providers and consultants. In this regard, a respondent explained that its network remains committed to the multi-disciplinary practice (MDP) model on the basis that it provides the best opportunity for career development and stimulating work for its employees and allows the network to provide the best quality of work for its clients.

- Sustainability reporting and assurance will result in an increasing focus on the integration of financial and non-financial reporting.

- The rapid developments seen in the metaverse, crypto assets and non-fungible tokens have implications, particularly for accountants in business and issues surrounding valuation.

- Technology and AI are areas that are constantly evolving. Therefore, it would be helpful to have some capacity to deal with emerging technologies in the next strategy period.

- Recent examples of significant ethical failures in large firms across G20 jurisdictions indicate leadership and cultural issues. It was suggested that IESBA, in collaboration with the IAASB, consider thought leadership activities or developing guidance material emphasizing the firm culture and leadership requirements in the IESBA Code and the IAASB's quality management standards.

- Applicability of the code to SMPs and whether the Board should take a similar approach to the IAASB's Audits of Less Complex Entities (LCE) project.

- A suggestion for IESBA to allow for some flexibility in its work plan for unforeseen issues that, if addressed on a timely basis, would benefit stakeholders more than some of the other planned projects.

Sustainability

Project description

The Sustainability Working Group will, among other matters

- undertake fact finding to better understand the sustainability, environmental, social and governance (ESG) landscape and to inform potential future standards-setting work.
- advise IESBA staff on the development of guidance to highlight existing provisions in the International Code of Ethics for Professional Accountants (IESBA code — including International Independence Standards) that are relevant to addressing ethical concerns relating to sustainability reporting and assurance, especially the issue of “greenwashing.”
- review the code to identify potential areas for enhancement to maintain its robustness and relevance to sustainability reporting and assurance.

Status

Due to the urgency of the topic, it was agreed that the working group should not produce a report to the board on its fact finding, rather should develop a project plan or plans on how to revise the IESBA code to address the ethical issues related to sustainability.

Preliminary review

During the September 2022 meeting the working group shared its observations from a preliminary review of the code and the International Independence Standards (IIS). The objective of the review was to consider whether the provisions in the code could be applied as is for sustainability information (preparation or assurance) and by persons/firms who are not accountants or whether some adaption may be necessary. Some of the observations included these:

- The current focus of the terminology. For example, references to financial statements versus subject matter/subject matter information and audit versus assurance. Also, the term professional accountant (PA) is used throughout the code instead of a general term that could encompass non-PAs who may provide preparation or assurance services related to sustainability.
- Part 2 of the code that is applicable to professional accountants in business (PAIB) includes sections on preparing and presenting information, pressure, or acting with sufficient expertise, while Part 3 of the code that is applicable to professional accountants in public practice (PAPP) does not.
- Coordination with IAASB might be necessary to address areas such as

- Applicability of ISQM standards if extending code to persons/firms who are not accountants.
- Application of the concept of network firms if a decision is made to extend scope for firms that are not PAs.
- How to apply the provisions in Part 4A in firms that are not partnerships.
- Consider revising certain provisions to address materiality in relation to sustainability engagements.
- Consider explicit reference to IAASB's forthcoming sustainability-related standards and whether the reference to ISAE 3000 (Revised) remain appropriate.

- The code has two sets of independence provisions. Those in Part 4A apply to audits and reviews, and those part 4B apply to other assurance engagements. Part 4A has significantly more requirements than part 4B and under the current scopes of part 4A and part 4B, assurance engagements on sustainability information would appear to fall under part 4B. Given this difference, is part 4B nonetheless sufficiently stringent and "fit for purpose," particularly for recurring assurance engagements and where the firms undertaking them may be part of a network that also provides other services?

Independence

The working group believes that due to the public interest nature of sustainability reports, part 4B is no longer an appropriate set of independence provisions that should apply when providing assurance. Given that stakeholders, including regulators are calling for profession agnostic standards, the working group requested input on how it should proceed with developing profession agnostic independence provisions to address sustainability assurance engagements.

The working group presented IESBA with two options on how to proceed.

Option A

Under option A revisions would be made to the existing ISS which would clarify whether part 4A or part 4B applies to the engagement. It was explained that this approach would likely result in extensive changes, would take more than nine months and would still be focused on the profession so an addition would be needed to indicate that it is applicable to non-PAs.

This option seems consistent with the direction taken by the European Commission (EC) and SEC in that they concluded that the same independence rules applicable to financial statement audits should be applicable to sustainability assurance engagements.

Some of the possible questions this option might raise are:

- Since sustainability covers a broad range of matters, whether only certain sustainability engagements should impose the more stringent independence provisions.
- Whether the sustainability engagements covered by the more stringent independence provisions should be limited to a subset of these engagements such as “assurance engagements of significant public interest.”
- The need for an analysis of scenarios for all situations (for example, when auditor of a financial statement also provides assurance on sustainability information versus when they do not).

Option B

Under option B a new set of independence provisions would be developed for sustainability assurance engagements (that is, part 4C). This approach is simpler as it will not alter the existing content and will allow sustainability assurance providers, PAs or non-PAs, to refer to the same set of dedicated standards. The planning committee believes this approach could be achieved faster than the approach outlined in option A and could be drafted so that it is not focused on just the profession.

This approach will differ from the European Commission’s final Corporate Sustainability Reporting Directive text and SEC proposals and could create the wrong impression that the existing independence provisions aren’t sufficiently robust for sustainability assurance. The approach could also present a risk to the timely adoption of nonassurance services, fees, and public interest entities related enhancements to the code, will have a limited shelf life and will result in duplication.

Twelve board members preferred option A. In addition, IESBA agreed to meet on November 1, 2022 to further discuss.

Questionnaire

The working group issued a sustainability stakeholder questionnaire. If bandwidth permits, AICPA staff will submit a response.

Staff publication

IESBA issued a staff publication explaining how the code addresses concerns about misleading sustainability information (that is, greenwashing).

Noncompliance with laws and regulations

Task force members

Bob Denham (chair), Tom Campbell, Elizabeth Pittelkow Kittner, Lisa Snyder, Dan Vuckovich

Observers

Mike Glynn, Tom Neill

AICPA staff

Emily Daly, Kelly Hnatt, Toni Lee-Andrews, Justin Long

Task force charge

To develop nonauthoritative implementation guidance for noncompliance with laws and regulations (NOCLAR).

Reason for agenda item

To update the committee on the nonauthoritative guidance developed since the August meeting and to obtain input on the proposed Q&As.

Task force activities

Since the August PEEC meeting, the task force has met twice to discuss nonauthoritative guidance.

Online *Journal of Accountancy* articles

Two NOCLAR articles will be published in November in the *Journal of Accountancy*. Elizabeth Pittelkow Kittner authored an article outlining the responsibilities for members in business. The publication date for this is yet to be determined. Cathy Allen authored an article intended for members in public practice, which is projected to be published in November 2022.

Decision tree animation

Staff created an animated decision tree to walk members through their responsibilities when they encounter suspected or actual noncompliance. The animation is structured as a “build your own adventure.” Participants will initially select whether they are in public practice or business and they will be further segmented by the types of professional services they provide or role within an employing organization.

Questions and answers

Kelly Hnatt drafted questions and answers, included as agenda item 9B, to help members implement the new interpretations.

Questions for the committee

1. Does the committee have additional questions or topics to include in the Q&As?
2. Should the Q&As include references to other professional standards, such as the auditing standards?

Webcast

Staff has scheduled a NOCLAR webcast for December 2, 2022 at 2 p.m. ET. It will be free to all members with one hour of CPE credit. The webcast will focus on the MIB interpretation because this is the first new guidance in the code for MIBs since 2017. The task force is still seeking a subject matter expert to participate.

Materials presented

Agenda item 10B: Q&A section 90, Responding to noncompliance with laws and regulations, .01–.27

Q&A section 90, Responding to noncompliance with laws and regulations, .01–.27

You can find these and other Q&As here:

- Ethics Online Library — Look for *Ethics Questions and Answers* to discover a range of topics from independence to records requests and more.
- AICPA *Technical Questions and Answers* — In addition to ethics Q&As, this resource has an array of technical content for auditing and accounting, financial reporting, compilation, and review standards.

Terms defined in the AICPA Code of Professional Conduct are italicized in this document. If you'd like to see the definitions, you can find them in "Definitions" (ET sec. 0.400)

.01 Level of guidance in the new interpretations

Inquiry — Are the new "Responding to Noncompliance With Laws and Regulations" interpretations (ET sec. 1.180.010 and 2.180.010) general guidance or do they impose specific responsibilities when a member becomes aware of noncompliance with laws and regulations (NOCLAR) or suspected NOCLAR?

Reply — The interpretations for members in business and members in public practice contain requirements with which a *member* must comply. These requirements (designated by the word "should") vary depending on whether the *member* is performing an audit or review of *financial statements*, is providing another *professional service*, or is a *member* in business.

.02 Interaction with other laws and regulations

Inquiry — If a *member* has complied with applicable legal or regulatory provisions for how to address a particular type of NOCLAR, does this mean that the *member* does not need to comply with the applicable NOCLAR interpretation?

Reply — No. The NOCLAR interpretations for members in public practice and members in business may contain other applicable provisions that laws or regulations do not require. Here are some examples:

- Provisions addressing escalation of the matter within the entity
- In the case of an audit of group *financial statements*, communication with the relevant *member* involved in the group audit
- Advice to management or *those charged with governance* regarding mitigation or

remediation of the consequences of NOCLAR or the deterrence of NOCLAR

- Determination of the need for further action (including withdrawal from the *client* relationship) in appropriate circumstances

- Documentation

.03 Addressing noncompliance before the effective date of the interpretations

Inquiry — The NOCLAR interpretations become effective on June 30, 2023. If a *member* becomes or is aware of an act or suspected act of NOCLAR prior to that time, is there any obligation to address it?

Reply — No. However, as early adoption is permitted, the provisions may be applied with respect to any NOCLAR or suspected NOCLAR of which the *member* becomes or is aware prior to that date.

.04 Acts of noncompliance that occur before the effective date of the interpretations

Inquiry — The NOCLAR interpretations become effective on June 30, 2023. If an act of NOCLAR was committed before, then and the *member* became aware of it subsequent to June 30, 2023, is there any obligation for the *member* to address it?

Reply — Yes. The interpretations for members in public practice and members in business require a response to any instance of NOCLAR a *member* learns about after June 30, 2023.

.05 Clearly inconsequential matters

Inquiry — Paragraph .10 of the interpretations for members in business and members in public practice scopes out clearly inconsequential matters. Why does paragraph .07 indicate that the only laws and regulations covered are those that directly affect the determination of material amounts and disclosures in the *financial statements*, and those for which compliance may be fundamental to the *client's* or *employing organization's* business?

Reply — The phrases "material amounts and disclosures" and "fundamental to the operating aspects of the business" refer to the kind of laws and regulations covered by the NOCLAR interpretations.

These phrases do not refer to the actual or suspected instances of NOCLAR. For example, laws and regulations addressing corporate taxation are within the scope of the interpretations. However, if an entity narrowly misses a deadline for filing its tax return, this could be a clearly inconsequential matter and the interpretations would require nothing further from the *member*.

.06 Noncompliance by an entity other than client or employer

Inquiry — A *member* becomes aware of a breach of a law by an entity that is not the *member's client* or employer. Do the interpretations for members in business and members in public

practice impose a responsibility to respond to the matter?

Reply — No. As the *member* had no professional relationship with the entity, the interpretations do not apply.

.07 Noncompliance by contractors, agents, or non-executive directors of a client or employer

Inquiry — Does the code require a *member* to respond to acts of NOCLAR committed by contractors or agents working for the *client* or *employing organization*, or by non-executive directors of the *client* or *employing organization*?

Reply — Yes. The definition of NOCLAR in the interpretations for members in business and members in public practice includes acts committed by anyone working for or under the direction of a *client* or the *employing organization* if such acts are related to the business activities of the *client* or *employing organization*.

Contractors, agents, and non-executive directors are examples of parties who work for or under the direction of a *client* or *employing organization*. In the context of responding to NOCLAR, a formal employment relationship does not need to exist between the party that has committed the act of NOCLAR and the *client* or *employing organization*.

.08 Responsibility for detecting noncompliance

Inquiry — Do the interpretations for members in business and members in public practice require *members* to detect acts of NOCLAR at their *client* or *employing organization*?

Reply — No. The interpretations do not require *members* to perform specific procedures to identify acts of NOCLAR when providing *professional services*. The interpretations for members in business and members in public practice merely require a response from *members* when they become aware of NOCLAR or suspected NOCLAR.

Members performing financial statement audit or review services do have certain requirements regarding the *member's* consideration of a company's possible illegal acts., however, and must comply with any applicable professional standards, in addition to the interpretation for members in public practice.

.09 Encountering noncompliance versus being made aware of noncompliance

Inquiry — Paragraph .07 of the interpretation for members in public practice indicates that a *member* may encounter or be made aware of an identified or suspected NOCLAR while providing a *professional service* to a *client*. Is there a difference in responsibility when a *member* encounters an instance of NOCLAR and when a *member* is made aware of one by someone else?

Reply — No. The *member's* required approach is the same whether a *member* encounters an

identified or suspected NOCLAR unexpectedly or another party brings such a matter to the *member's* attention.

.10 Discovery of noncompliance during audit and review engagements

Inquiry — If a *member* providing financial statement audit or review services becomes aware of an actual or suspected NOCLAR committed by a *client* in circumstances other than through performing *professional services*, for example by coming across the matter on the internet or hearing about it from someone at a social event, is the *member* required to discuss the matter with management or *those charged with governance*?

Reply — The interpretation for members in public practice is applicable regardless of the source or whether the information was obtained as a result of audit procedures. The *member*, however, should consider whether the information is credible (see paragraph .13) and whether the matter is within the scope or is clearly inconsequential.

.11 Noncompliance with no direct effect on the amounts and disclosures in financial statements

Inquiry — Is there any expectation that a *member* be able to identify NOCLAR that does not have a direct effect on the determination of the amounts and disclosures in the *financial statements*—for example, in relation to food safety or vehicle emissions requirements?

Reply — No. There is no expectation in the interpretations for members in business and members in public practice to have a level of knowledge of laws and regulations greater than what is needed to perform an engagement for a *client* or perform a role within the *employing organization*.

Members who specialize in a particular field (for example, corporate taxation or greenhouse gas emissions) need a sufficient understanding of the laws and regulations applicable to that field to competently undertake engagements related to the relevant subject matter.

Members are expected to be able to recognize NOCLAR or suspected NOCLAR related to their subject matter expertise if information concerning the matter comes to their attention. For example, if a *member* has been engaged to provide an assurance report regarding a food manufacturer's controls relating to compliance with licensing regulations, the *member* is expected to be able to recognize noncompliance with those regulations.

The *member* is not expected to recognize NOCLAR or suspected NOCLAR in areas beyond the *member's* training or beyond which the *member* has been engaged to apply specialized skills. See paragraphs .13 and .14 of the interpretations for members in business and members in public practice. It is understood that instances of NOCLAR might be concealed, and the interpretations do not require *members* to search for NOCLAR.

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.12 Examples of NOCLAR fundamental to an organization's business

Inquiry —The interpretations for members in business and members in public practice explain the required approach when a *member* encounters or is made aware of suspected or actual NOCLAR that does not have a direct effect on the determination of the amounts and disclosures in the *client's* or *employing organization's financial statements*, but compliance with which may be fundamental to the operating aspects of the *client's* or *employing organization's* business, to its ability to continue its business, or to avoid material penalties. What are some examples of these types of NOCLAR?

Reply — Fraud, corruption and bribery are some examples. Other laws and regulations in this category might be relevant only to certain entities because of the nature of their business. Here are some additional examples that may apply:

- Environmental protection regulations for an entity operating in the fossil fuels industry
- Regulatory capital requirements for a bank
- Laws and regulations against money laundering and terrorist financing for financial institutions
- Vehicle emissions regulations for a car manufacturer
- Licensing regulations for a pharmaceutical company or a food manufacturer

In sum, *members* who provide *professional services* that require an understanding of those laws and regulations to an extent sufficient to competently perform such *professional services* are expected to be able to recognize NOCLAR or suspected NOCLAR in relation to those laws and regulations.

.13 An organization's response to noncompliance

Inquiry — If management and *those charged with governance* (TCWG) are unwilling to address an identified or suspected NOCLAR, does this mean that the *member* has no further responsibilities with respect to the matter under the code?

Reply — No. Part of the response framework in the interpretation for members in public practice involves assessing the appropriateness of the response of management and, where applicable, the response to the matter by TCWG. If management and TCWG do not address the matter, this would be grounds for the *member* to conclude that their response is not appropriate.

If this happens, paragraph .24 of the members in public practice interpretation requires the *member* to determine whether the public interest requires further action. Paragraph .25 sets out various factors for the *member* to consider in making this determination, including the nature and extent of any such further action.

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.14 A member's responsibility regarding adverse consequences or deterrence of noncompliance

Inquiry — Does the code impose any responsibility on the *member* to rectify, remediate, or mitigate the adverse consequences of identified or suspected NOCLAR or to deter the commission of NOCLAR?

Reply — No. Rectifying, remediating, or mitigating adverse consequences of identified or suspected NOCLAR or deterring the commission of NOCLAR are the sole responsibility of management, with oversight from *those charged with governance*. Paragraph .19 of the interpretation for members in public practice requires the auditor to only advise management to take appropriate and timely actions, if they have not already done so.

.15 Documentation related to noncompliance

Inquiry — What is the purpose of the documentation provisions in the interpretations for members in business and members in public practice?

Reply — Documentation provides several benefits, including facilitating review of team members' work, enhancing the quality of the professional judgments made through documentation of the thought process, and retaining a record of matters of continuing significance to future *professional services*.

Importantly, the requirement to document the matter helps the *member* demonstrate compliance with the interpretations, including retaining a record of the *member's* professional judgments and actions given the information available to the *member* at the time. The documentation requirement is set out in paragraph .30 of the members in public practice interpretation. Paragraph .29 of the members in business interpretation and paragraph .44 of the members in public practice interpretation encourage documentation.

.16 Contractually negotiated confidentiality clause relating to noncompliance

Inquiry — How should *members* in public practice resolve interactions between a contractually negotiated confidentiality clause in contracts for *professional services* and clauses in such contracts that require compliance with applicable laws and regulations and professional standards when providing the services?

Reply — *Members* should first determine whether the *professional service* is one that would be excluded from the interpretation for members in public practice (see paragraph .06). If the engagement is not specifically excluded, then the *member* should discuss the professional obligation to abide by the code with the *client*, which includes the obligation to respond to actual or suspected NOCLAR (see BL section 2.3.2, requiring compliance with the rules of the Code of Professional Conduct [code] as a condition of membership).

If there is a contractually negotiated confidentiality clause (as opposed to confidentiality

imposed by law or regulation), it would be advisable to include a clause making it clear that such a confidentiality clause is subject to the *member's* obligation to comply with the code. For contracts signed before the effective date of the NOCLAR provisions, *members* should consider whether amendments are advisable or practicable.

.17 Implementation of noncompliance requirements in firm policies and methodologies

Inquiry — To what extent is the process of responding to NOCLAR or suspected NOCLAR under the members in public practice interpretation expected to be explicitly addressed in *firm* policies and methodologies?

Reply — Approaches to implementation of and changes to the code vary among *firms*. For clarity and consistency, however, *firms* may find it useful to articulate the following in their policies and methodologies:

- The scope of the interpretation
- The escalation process within an engagement team and within the *firm*, including when to escalate the matter and to which level within the engagement team and within the *firm*
- When to consult with legal counsel or other external parties
- Who within the *firm* should be involved in discussions with management and *those charged with governance*
- The protocols for communication within a group engagement team, with a *network firm* and, if not within the *firm* or a *network*, with the external auditor of a *client*
- Determination of the need for further action, including withdrawal from the engagement and *client* relationship

Regardless of the approach or extent to which the NOCLAR response process is encompassed in *firm* policies and methodologies, *members* remain responsible for compliance with the code.

.18 Laws and regulations addressed by the interpretation for members in public practice

Inquiry — What is the relationship between the laws and regulations addressed by the interpretation for members in public practice and the laws and regulations addressed by other professional standards?

Reply —This interpretation does not expand the range of laws and regulations of which a *member* must have knowledge for purposes of performing an engagement. However, if a *member* becomes aware of identified or suspected NOCLAR that is within the scope of laws and regulations addressed by the interpretation, the code requires the *member* to respond to it

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in accordance with the interpretation, regardless of whether the matter falls within the scope of laws and regulations addressed by specific applicable professional standards.

.19 Relationship of NOCLAR guidance with applicable professional standards

Inquiry — Does the interpretation for members in public practice in any way extend *members'* obligations under professional standards with respect to the performance of an audit or review?

Reply — No. The interpretation is not intended to modify or interpret any applicable professional standards. However, the interpretation does impose requirements on *members* beyond applicable professional standards for purposes of fulfilling their ethical obligations under the code.

Though the scope of laws and regulations covered by the interpretation is the same as applicable professional standards, the application of the interpretation differs from the application of professional standards in light of the different objectives of the code.

Specifically, under professional standards, *members* are concerned with whether the consequences of identified or suspected NOCLAR have a material effect on the *financial statements*. This concern will apply equally for purposes of the code, given the need for *members* to have regard to the consequences for the entity.

However, where the interpretation goes beyond is in alerting *members* to give attention to possible wider public interest implications that could substantially harm stakeholders, whether in financial or non-financial terms. See paragraph .12 and note the need to take into consideration potential harm to the interests of the entity, investors, creditors, employees, or the general public.

.20 Timing related to finalization of an auditor's report and becoming aware of noncompliance

Inquiry — A *member* becomes aware of an instance of NOCLAR shortly before the *member* is expected to sign the auditor's report on the entity's *financial statements*. How does the timing of finalization of the auditor's report affect the ***member's*** responsibilities under the interpretation for members in public practice?

Reply — The ***member's*** responsibilities under the interpretation are separate and distinct from the ***member's*** responsibilities under applicable auditing standards. The timing of finalization of the auditor's report therefore does not affect the ***member's*** responsibilities under the NOCLAR interpretation. The *member* must still respond to the instance of NOCLAR according to the interpretation's provisions.

.21 When management disagrees with the assessment of noncompliance

Inquiry — During the audit of an entity's *financial statements*, a *member* becomes aware of

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suspected NOCLAR committed by the entity. Management, however, disagrees with the *member* regarding the information and conclusion concerning the matter. Does the interpretation for members in public practice require the *member* to do anything further?

Reply — It depends. The *member* may have obligations to go beyond the interactions with *those charged with governance* (TCWG). Management's disagreement with the *member* is not sufficient grounds for the *member* to stop pursuing the matter.

The *member* needs to be satisfied that management's explanations adequately dispel the *member's* suspicion. If not, the *member* may consider other courses of action.

Some possible courses of action include consulting with others within the *firm*, obtaining advice from the *member's* legal counsel, consulting on a confidential basis with a regulator or professional body, or escalating the matter to TCWG. The *member* should also consult applicable professional standards.[1]

.22 Group engagement partner's required action in response to noncompliance

Inquiry —Under the interpretation for members in public practice, is the group engagement partner always required to take action to address any identified or suspected NOCLAR, including when the components are based in other jurisdictions?

Reply — Yes. The interpretation for members in public practice requires the group engagement *partner* to always respond, consistent with the *member's* responsibility to act in the public interest.

.23 Assessing the effects of noncompliance on components

Inquiry — A group engagement *partner* has become aware of an instance of NOCLAR at a component during an audit of group *financial statements*. In considering whether to communicate the matter to those performing work at other components where the matter may be relevant, is the group engagement *partner* expected to assess the possible effects of the NOCLAR on such components?

Reply — No. Paragraph .23 of the interpretation for members in public practice requires only that the group engagement *partner* take steps to have the matter communicated to those performing work at components where the matter may be relevant, unless prohibited from doing so by law or regulation. Responsibility for assessing the possible impact of the NOCLAR on the components rests with the *members* performing work at those components.

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[1] See paragraphs .17-20 of AU-C Section 250 *Consideration of Laws and Regulations in an Audit of Financial Statements* for the auditor's GAAS responsibilities when noncompliance is identified or suspected.

.24 Disclosure of noncompliance to an appropriate authority before an entity has addressed the matter

Inquiry — Do the interpretations for members in business and members in public practice permit disclosure of NOCLAR or suspected NOCLAR to an appropriate authority if management, the *member's* superiors, and those charged with governance (TCWG) have not yet appropriately addressed the matter?

Reply — *Members* should consult the "Confidential Client Information Rule" (ET sec 1.700.001) and the "Confidential Information Obtained From Employment or Volunteer Activities" interpretation (ET sec. 2.400.070) of the "Acts Discreditable Rule" (ET sec. 2.400.001) to determine whether any disclosure can be made. As consideration of the matter may involve complex analysis and judgments, a *member* may want to consider consulting internally or externally, including obtaining legal or other advice to understand the *member's* options.

.25 Communication of noncompliance after a change of auditor

Inquiry — When an auditor withdraws from the *client* relationship as a result of identified or suspected NOCLAR, is that auditor expected to identify the proposed new auditor in order to communicate information about the NOCLAR?

Reply — No, the predecessor auditor is not expected to seek out the proposed new auditor in order to provide this information. *Members* should consult the applicable professional standards regarding communications between successor and predecessor auditors.

.26 Responsibility to address noncompliance when performing professional services other than audit or review services

Inquiry — Does a *member* who is engaged to provide a *professional service* other than an audit or review of an entity's *financial statements* have the same level of responsibility to address identified or suspected NOCLAR under the interpretation for members in public practice as a *member* who is engaged to perform an audit or review of the entity's *financial statements*?

Reply — No. The requirements for responding to identified or suspected NOCLAR for a *member* engaged to provide a service other than an audit or review of *financial statements* is significantly less than that expected of a *member* engaged to perform an audit or review of *financial statements*.

For example, paragraph .31 of the interpretation for members in public practice requires the former only to seek to obtain an understanding of the matter, that is, to make an attempt at gathering such an understanding, recognizing that limitations on access to information may preclude obtaining that understanding.

In contrast, paragraph .13 of the interpretation requires the latter to obtain an understanding of the matter. This provision recognizes that there is a greater public expectation of *members*

providing financial statement audit or review services compared with *members* providing other services, and that *members* providing financial statement audit or review services have greater access to information compared with those who provide other *professional services*.

.27 Suspected noncompliance that a member cannot substantiate

Inquiry — If a *member* who is engaged to provide a *professional service* other than an audit or review of the entity's *financial statements* becomes aware of a suspected NOCLAR within the entity but is unable to substantiate the suspicion, does this mean that the *member* has not complied with the interpretation for members in public practice?

Reply — No. The interpretation recognizes that for *members* providing services other than audits or reviews of *financial statements*, there may be limitations on access to information. The *member's* ethical responsibilities will be fulfilled if the member makes an attempt to obtain relevant information to substantiate the suspicion.

Statements on Standards for Tax Services

Reason for agenda item

To provide an overview of recent activities and seek input on the exposure draft and invitation to comment.

Background

The AICPA Tax Executive Committee (TEC) issued its exposure draft (ED) of the revised Statements on Standards for Tax Services (SSTSs) that, if adopted, will be effective January 1, 2024, as well as an invitation to comment (ITC) on potential approaches to effectively introduce quality management in tax. The ED and ITC request feedback from stakeholders by the end of 2022.

In September 2018, the SSTS Revision Task Force began its project to update the SSTSs to

- better reflect the issues and needs of members and the tax practices of today and in the future and
- ensure the highest ethical standards for members who support the public's view that CPAs are the premier providers of tax services.

As part of those efforts, the task force

- developed a new structure to organize the SSTSs by type of tax work performed;
- updated the existing standards to better reflect the current and possible future state of the tax profession; and
- drafted three new standards on data protection, reliance on tools, and the representation of clients before taxing authorities.

In addition, the task force explored items that will require more research and investigation and held extensive discussions among its members and multiple committees to explore what, if any, revisions to the SSTSs should address issues of quality management in tax.

Action needed

The committee is asked to provide any feedback on the ED and ITC and to invite their firms, and observers to review and comment.

Materials presented

- Agenda item 11B: Revised Statements on Standards for Tax Services: An Exposure Draft and Invitation to Comment

AICPA

Revised Statements on Standards for Tax Services

An Exposure Draft and Invitation to Comment

Contents

Explanatory memorandum

Introduction

Statements on Standards for Tax Services (SSTSs) are issued by the AICPA Tax Executive Committee (TEC), the senior technical body of the AICPA designated to promulgate standards of tax practice. The General Standards Rule (AICPA, Professional Standards, ET secs. 1.300.001 and 2.300.001) and the *Compliance With Standards Rule* (AICPA, Professional Standards, ET secs. 1.310.001 and 2.310.001) of the AICPA Code of Professional Conduct require compliance with these standards. Many state boards of accountancy also incorporate the SSTSs as part of their professional rules of conduct for CPAs.

The purpose of this combined document is to solicit feedback, respectively, on:

1. **Part 1: Exposure Draft (ED)** of proposed revisions to the AICPA's SSTSs that, if adopted, will become effective on Jan. 1, 2024, and
2. **Part 2: Invitation to Comment (ITC)** on potential approaches to effectively introduce quality management in tax.

In September of 2018, the AICPA TEC approved formation of the SSTS Revision Task Force to update the SSTSs to (1) better reflect the issues and needs of members and the tax practices of today and in the future and (2) ensure the highest ethical standards for members who support the public's view that CPAs are the premier providers of tax services.

As part of those efforts, the task force:

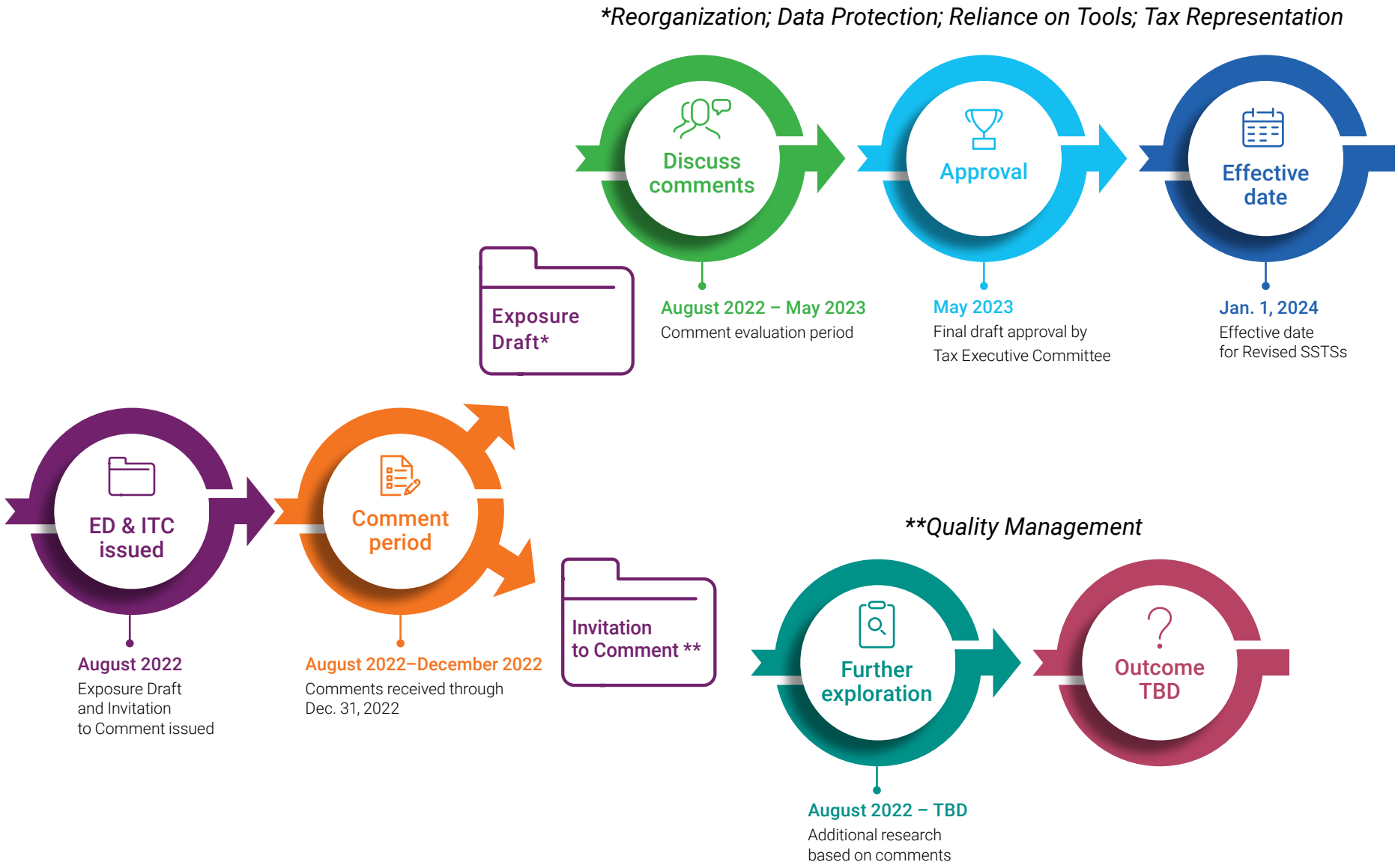
- Developed a new structure to organize the SSTSs by type of tax work performed,
- Updated the existing standards to better reflect the current and possible future state of the tax profession and
- Drafted three new standards surrounding data protection, reliance on tools and the representation of clients before taxing authorities.

In addition, the task force explored items that will require additional research and investigation and held extensive discussions among its members and multiple committees to explore what, if any, revisions to the SSTSs should be made to address issues of quality management in tax.

Stakeholders are invited to comment on all matters in this ED and ITC. Specific questions related to the ED and ITC are included at the ends of Part 1 and Part 2, respectively.

SSTS revision timeline

The following graphic demonstrates the anticipated timing of the SSTSs updates and the research and exploration period on quality management in tax.



Description of combined document

This combined ED and ITC presents the findings and conclusions of the SSTS Revision Task Force as approved by the TEC. The document is divided into two separate sections: Part 1: ED and Part 2: ITC.

The ED presents changes the AICPA proposes to make to the SSTSs. Following consideration of comments received, the changes outlined in the ED, if adopted, are expected to be included in a revised SSTSs document to be approved no later than May 31, 2023, and effective Jan. 1, 2024.

The ITC presents items for consideration that will require additional research and investigation regarding the concept of quality management in tax. Depending on the nature of the comments received in response to the ITC, the AICPA will pursue additional research to determine how and when the SSTSs and/or other guidance may be provided on quality management in tax. At this time, it is not known if and when any changes resulting from the ITC will be implemented.

All comments, whether related to the ED or the ITC, are due no later than Dec. 31, 2022. See further discussion below under request for comments.

Request for comments

Respondents are asked to provide comments on the proposed changes and questions listed in the ED and the ITC. Comments are most helpful when they refer to specific questions asked and include the reasons supporting the respondent's view.

> When a respondent agrees with proposals in the ED or ITC, it will be helpful for the AICPA to be made aware of this view.

Written comments on the ED and ITC will become part of the public record of the AICPA and will be available on the AICPA's website after Dec. 31, 2022. The AICPA will consider all responses received on or before Dec. 31, 2022.

Please submit comments via our online form. Alternatively, you may email your submission to: SSTScomments@aicpa-cima.com.

Reponses may be submitted in Word format or directly in the body of the email with an appropriate signature (name, firm). Unless the respondent explicitly permits otherwise, comments will be posted without the sender's email address. Respondents may also submit a PDF version of their response for posting to the AICPA website.

Comment period

The comment period for this ED and ITC ends Dec. 31, 2022.

Part 1:
Exposure draft of proposed revisions to the SSTSs

Background

The SSTSs have their origin in the Statements on Responsibilities in Tax Practice (SRTPs), which provided a body of advisory opinions on good tax practice. The guidelines as originally set forth in the SRTPs became more important than many members had anticipated when the guidelines were issued. The courts, the IRS, state accountancy boards and other professional organizations recognized and relied on the SRTPs as the appropriate articulation of professional conduct in a CPA's tax practice. The SRTPs became de facto enforceable standards of professional practice because state disciplinary organizations and courts regularly held CPAs accountable for failure to follow the guidelines set forth in the SRTPs.

The SRTPs were originally issued between 1964 and 1977. The first nine SRTPs and an introduction were combined and promulgated in 1976; the tenth SRTP was issued in 1977. The original SRTPs concerning the CPA's responsibility to sign the tax return (SRTP No. 1, *Signature of Preparers*, and No. 2, *Signature of Reviewer: Assumption of Preparer's Responsibility*) were withdrawn in 1982 after Treasury Department regulations were issued adopting substantially the same standards for all tax return preparers. The sixth and seventh SRTPs, concerning the responsibility of a CPA who becomes aware of an error, were revised in 1991. The first interpretation of the SRTPs, Interpretation No. 1-1, *Realistic Possibility Standard*, was approved in December 1990.

Given the level of reliance on the SRTPs by state disciplinary organizations and courts, the AICPA's TEC concluded it was appropriate to issue tax practice standards that would become a part of the AICPA's Professional Standards. At its July 1999 meeting, the AICPA Board of Directors approved support of the executive committee's initiative and placed the matter on the agenda of the October 1999 meeting of the AICPA's governing Council. On Oct. 19, 1999, Council approved designating the TEC as a standard-setting body, thus authorizing that committee to promulgate standards of tax practice. As a result, the original SSTSs, largely mirroring the SRTPs, were issued in August 2000. The SSTSs and Interpretation No. 1-1, *Realistic Possibility Standard*, of SSTS No. 1, *Tax Return Positions*, superseded and replaced the SRTPs and their Interpretation No. 1-1, effective Oct. 31, 2000.

Although the number and names of the SSTSs, and the substance of the rules contained in each of them, remained the same as in the SRTPs, the language was revised to both clarify and reflect the enforceable nature of the SSTSs. In addition, because the applicability of these standards is not limited to federal income tax practice (as was the case with the SRTPs), the language was changed to indicate the broader scope. In 2003, in connection with the tax shelter debate, SSTS Interpretation No. 1-2, *Tax Planning*, of SSTS No. 1 was issued to clarify a member's responsibilities in connection with tax planning; that interpretation became effective Dec. 31, 2003. These two interpretations were initially updated in 2010. On Aug. 15, 2011, the TEC adopted the updated Interpretation 1-1, now titled, *Reporting and Disclosure Standards*, and 1-2, *Tax Planning*, effective Jan. 31, 2012.

When the original SSTSs were issued, an effort was made to keep to a minimum any changes in the language of the SSTSs from that of the predecessor SRTPs. This was done to alleviate concerns regarding the enforceability of standards that differed from the SRTPs under which members had been practicing. Since the issuance of the original SSTSs, members have asked for clarification on certain matters, such as the duplication of the language in SSTS No. 6, *Knowledge of Error: Return Preparation*, and No. 7, *Knowledge of Error: Administrative Proceedings*. Also, certain changes in federal and state tax laws have raised concerns regarding the need to revise SSTS No. 1. As a result, in 2008, the original SSTS Nos. 1–8 were updated, effective Jan. 1, 2010. The original SSTS Nos. 6–7 were combined into the revised SSTS No. 6, *Knowledge of Error: Return Preparation and Administrative Proceedings*. The original SSTS No. 8, *Form and Content of Advice to Taxpayers*, was renumbered SSTS No. 7. In addition, various revisions were made to the language of the original SSTSs. The last significant updates to the content of the SSTSs were effective Jan. 1, 2010.

In 2018, changes were made to the SSTSs to bring the references to the AICPA Code of Professional Conduct into conformity with the AICPA ethics codification.

In September of 2018, the TEC approved the formation of a task force to update the SSTSs. The task force is composed of AICPA Tax Section members representing diverse interests including small and sole practitioner firms, Private Company Practice Section ("PCPS") members, medium and large CPA firms and academia. The task force developed and presented the updated SSTSs to the TEC for their approval.

Explanation of proposed revisions to the SSTSs

The goals of the revisions of the SSTSs are to ensure that the standards are better aligned to reflect the current state of the tax profession and to address the emerging needs of today's members. Proposed updates to the standards include:

- Reorganization of the SSTSs by type of tax work performed; and
- Promulgation of three new standards surrounding data protection, reliance on tools and the representation of tax clients before taxing authorities.

Reorganization

Included in its efforts to update the SSTSs, the task force developed a new practice-based organizational structure for the standards. Under the new organizational framework:

- Standard 1 includes general tax guidance with broad applicability (includes new standards on data protection and reliance on tools)
- Standard 2 includes tax return preparation guidance
- Standard 3 includes guidance specific to providing tax advice
- Standard 4 includes guidance for members providing tax representation services (new standard)

The task force believed that the existing standards were largely applicable to all types of tax services and were drafted to be general in nature, to allow for their use, no matter what type of tax service was being delivered. At the time of the drafting of the original standards, most of the tax services being provided were compliance-oriented and involved tax return preparation.

This revision project has reorganized the standards so that most of the existing standards have been incorporated into either general standards (Standard 1) or compliance standards (Standard 2). Because the proposed new standards around data protection and reliance on tools are applicable to different types of tax services, they were also included with the general standards. The existing standard as related to tax advisory services (Standard 3) and the new standard related to representation services (Standard 4) were determined to be unique and have been separately stated. This alignment is intended to assist members in applying standards to specific tax practice situations and to help them understand the scope and expectations of these standards.

Data protection

The subject of the protection of taxpayer data has exponentially grown over time and has gained global importance as technology now allows for the transfer and storage of large amounts of confidential financial information with the simple press of a button. In many cases, this data is never seen in a hard copy format. The task force believed it was important to implement a standard which ensures members adopt reasonable safeguards to protect taxpayer data, both in electronic format and otherwise.

The task force also recognized that constant advances in technology make it challenging to identify any one set of standards with broad applicability across all tax practices. The purpose of the new standard is to expressly state a member's responsibility to make a reasonable effort to safeguard confidential client information. It was broadly written to consider the variability among member practices as well as continuingly changing privacy laws and technology.

Reliance on tools

Tax is not a static subject, given regular changes resulting from various legislative and regulatory amendments, and judicial decisions. However, over time, these changes have become more frequent, extensive and complex, with related authoritative guidance from the taxing authorities often delayed or incomplete. This situation often leaves members struggling to (1) provide clients or firm departments the necessary information to allow the correct and accurate preparation and filing of their respective tax returns and (2) plan for future events to efficiently manage potential tax liabilities.

Members have long relied on tools of various types to allow them to accurately interpret a particular provision of the tax code. However, in today's tax practice environment, members rely on technology to provide services more than at any point in history. That trend will continue with the introduction of artificial intelligence, data science, quantum computers and other developing technologies.

Currently, tax professionals do not have a professional standard relating specifically to reliance on these tools when providing services. The task force identified the need for a standard which protects members by defining when they may reasonably rely on tools of all types used in the performance of tax services.

Tax representation

As previously noted, the best practices that were the forerunner of the existing SSTSs were written over fifty years ago. At that time, tax preparation was the overwhelming service that was provided by tax professionals. Since then, tax practices have expanded to provide a wide variety of services including tax representation services. The task force believed the continuing growth in the number of CPA firms providing tax representation services, in various venues, involving different types of taxes, obligated the development of this proposed standard.

Another goal of the task force was to avoid proposing standards which might appear duplicative of other existing standards in effect today. While it is true that CPAs who provide tax services are bound by existing standards related to representation, including Circular 230, such rules may be limited in scope (e.g., Circular 230 only governs representation before the Internal Revenue Service).

Mapping of current standards to proposed standards

The following table maps the current SSTSs to the reorganized SSTSs and provides additional details related to the proposed revisions.

Table Mapping: Current SSTSs to Proposed SSTSs

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
Preface	Preface (modified)	This now includes extant ongoing process section with revisions.
History		The existing history and updates have been relocated and included in the background section of the combined ED/ITC document.
Ongoing process		This content is revised and relocated into the preface section.
	Definitions (NEW)	The definitions section was added at the beginning as these terms are used throughout the standards. There is no change to the existing definition of "taxpayer" or "tax position" from extant standards. The definition of "member" is added to reinforce the applicability of standards.
SSTS No. 1, *Tax Return Positions*	SSTS No. 1, *General Standards for Members Providing Tax Services* (NEW)	This is a new standard specifically addressing general matters applicable to all tax services. It consolidates into a single standard guidance from extant SSTS Nos. 1 and 5 along with adding proposed new standards on data protection and reliance on tools.
	1.1. Advising on Tax Positions	
Introduction	Introduction	
No. 1 Introduction – ¶1	1.1.1. (modified)	This adds reference to tax positions mentioned in the new SSTS No. 2. The definition of tax return position and taxpayer is relocated to the definitions section.

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
No. 1 Introduction – ¶2	1.1.2.	
No. 1 Introduction – ¶3	1.1.3. (modified)	This deletes reference to signing tax returns since this is now covered in the new SSTS No. 2.
Statement	Statement	
No. 1 Statement – ¶4		This is relocated to proposed 1.1.5.
	1.1.4. (NEW)	This expands on the definition of tax position as stated in the definitions section.
No. 1 Statement – ¶5	1.1.5. (modified)	This includes extant ¶4 and adds a new reference to written standards of other taxing authorities. If the position's likelihood exceeds the "realistic possibility of success" standard, then these other standards should be followed.
No. 1 Statement – ¶6		This is relocated to proposed 2.1.7.
No. 1 Statement – ¶7		This is relocated to proposed 2.1.8.
	1.1.6. (NEW)	This adds reference to due diligence and professional judgement when advising on tax positions.
No. 1 Statement – ¶8	1.1.7. (modified)	This deletes reference indicating that the member has a responsibility to be an advocate for a taxpayer.
Explanation	Explanation	
No. 1 Explanation – ¶9	1.1.8. (modified)	This deletes reference to signing returns but keeps the rest of extant paragraph. This also relocates extant paragraph with reference to signing returns to proposed 2.1.10.
No. 1 Explanation – ¶10		This is relocated to proposed 2.1.11.

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
No. 1 Explanation – ¶11	1.1.9.	
No. 1 Explanation – ¶12	1.1.10.	
No. 1 Explanation – ¶13	1.1.11.	
No. 1 Explanation – ¶14		This is relocated to proposed 2.1.14.
No. 1 Explanation – ¶15	1.1.12.	
No. 1 Explanation – ¶16		This is relocated to proposed 2.1.3.
SSTS No. 2, *Answers to Questions on Returns*	2.2. Tax Return Questions	
Introduction	Introduction	
No. 2 Introduction – ¶1	2.2.1.	
Statement	Statement	
No. 2 Statement – ¶2	2.2.2. (modified)	This adds reference to acts required before signing as a preparer.
Explanation	Explanation	
No. 2 Explanation – ¶3	2.2.3.	
No. 2 Explanation – ¶4	2.2.4.	
No. 2 Explanation – ¶5	2.2.5.	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
No. 2 Explanation – ¶6	2.2.6. (modified)	This adds the requirement to advise a client if an omission of an answer may cause the return to be incomplete or result in penalty assessment.
No. 2 Explanation – ¶7	2.2.7.	
SSTS No. 3, *Certain Procedural Aspects of Preparing Returns*	2.3. Reliance on Information from Others	
Introduction	Introduction	
No. 3 Introduction – ¶1	2.3.1.	
Statement	Statement	
No. 3 Statement – ¶2	2.3.2.	
No. 3 Statement – ¶3	2.3.3. (modified)	This deleted the reference to the example, "such as taxpayer maintenance of books and records or substantiating documentation to support the reported deduction or tax treatment."
No. 3 Statement – ¶4	2.3.4. (modified)	This adds reference to other sources including, but not limited to, the tax return of another taxpayer.
Explanation	Explanation	
No. 3 Explanation – ¶5	2.3.5.	
No. 3 Explanation – ¶6	2.3.6.	
No. 3 Explanation – ¶7	2.3.7.	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
No. 3 Explanation – ¶8	2.3.8.	
No. 3 Explanation – ¶9	2.3.9.	
SSTS No. 4, *Use of Estimates*	2.4. Use of Estimates	
Introduction	Introduction	
No. 4 Introduction – ¶1	2.4.1. (modified)	This added that responsibility of the data lies with the taxpayer.
Statement	Statement	
No. 4 Statement - ¶2	2.4.2. (modified)	This added reference to estimates provided by others but authorized by the taxpayer.
Explanation	Explanation	
No. 4 Explanation - ¶3	2.4.3.	
No. 4 Explanation - ¶4	2.4.4.	
No. 4 Explanation - ¶5	2.4.5. (modified)	This adds reference that a member should inform a taxpayer of his or her duty to maintain records that support the return.
No. 4 Explanation – ¶6	2.4.6.	
No. 4 Explanation – ¶7	2.4.7.	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
SSTS No. 5, *Departure from a Position Previously Concluded in an Administrative Proceeding for Court Decisions*	2.5. Departure from Previous Positions	
Introduction	Introduction	
No. 5 Introduction – ¶1	2.5.1.	
No. 5 Introduction – ¶2	2.5.2.	
No. 5 Introduction – ¶3	2.5.3.	
Statement	Statement	
No. 5 Statement – ¶4	2.5.4. (modified)	This added reference to tax return positions in proposed 2.1.
Explanation	Explanation	
No. 5 Explanation – ¶5	2.3.5. (modified)	This added a statement regarding "unless the taxpayer is contractually bound to a particular tax treatment."
No. 5 Explanation – ¶6	2.5.6.	
SSTS No. 6, *Knowledge of Error: Return Preparation and Administrative Proceedings*	1.2. Knowledge of Errors	
Introduction	Introduction	
No. 6 Introduction – ¶1	1.2.1.	
No. 6 Introduction – ¶1	1.2.2.	
No. 6 Introduction – ¶2	1.2.3.	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
	1.2.4. (NEW)	This references that taxing authorities may impose specific standards in connection with errors discovered during tax engagements.
No. 6 Introduction – ¶3	1.2.5.	
Statement	Statement	
No. 6 Statement – ¶4	1.2.6. (modified)	This adds reference to errors in an administrative filing. This formally references proposed 3.1.2. related to form advice to be provided.
No. 6 Statement – ¶5	1.2.7. (modified)	This adds reference to prior year returns.
No. 6 Statement – ¶6		This is relocated to proposed 1.2.9.
	1.2.8.	This repeats extant ¶4 and reinforces the need to review the continuance of the client relationship if the client refuses to correct a previously discovered error.
	1.2.9.	This is relocated from extant ¶6.
Explanation	Explanation	
No. 6 Explanation – ¶7	1.2.10.	This formally references proposed 3.1.2. related to form advice to be provided and adds extant ¶14.
No. 6 Explanation – ¶8	1.2.11.	
No. 6 Explanation – ¶9	1.2.12.	
	1.2.13. (NEW)	This references a member's responsibility to both the taxpayer and tax system.

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
No. 6 Explanation – ¶10	1.2.14.	
No. 6 Explanation – ¶11	1.2.15.	
No. 6 Explanation – ¶12	1.2.16.	
No. 6 Explanation – ¶13	1.2.17.	
No. 6 Explanation – ¶14		This is relocated to proposed 1.2.10.
	1.3. Data Protection (NEW)	This is a new standard regarding making reasonable efforts to safeguard taxpayer data.
	Introduction	This states responsibilities for data protection while performing taxpayer services.
	1.3.1.	
	1.3.2.	
	1.3.3.	
	Statement	Efforts were made to have statements as limited as possible to make them reasonable but still enforceable.
	1.3.4.	
	1.3.5.	
	Explanation	Multiple examples are provided to explain reasonable efforts to safeguard taxpayer data.
	1.3.6.	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
	1.3.7.	
	1.3.8.	
	1.3.9.	
	1.3.10.	
	1.3.11.	
	1.3.12.	
	1.3.13.	
	1.4. Reliance On Tools (NEW)	This is a new standard regarding the allowance of members to rely on multiple types of resources in providing tax services.
	Introduction	The definition of tools is provided.
	1.4.1.	
	1.4.2.	
	Statement	Professional judgement must be used in reliance on tools. The guidance is intentionally broad in scope.
	1.4.3.	
	1.4.4.	
	Explanation	Tools should be used to improve efficiency and enhance a member's understanding of an issue; tools cannot supplant professional judgement.

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
	1.4.5.	
	1.4.6.	
	1.4.7.	
	1.4.8.	
	SSTS No. 2, *Standards for Members Providing Tax Compliance Services, Including Tax Return Positions*	This new standard specifically addresses tax compliance services and consolidates into a single standard guidance from extant SSTS Nos. 1–5.
	2.1. Tax Return Positions (NEW)	
	Introduction	
	2.1.1.	This replicates extant SSTS No. 1, ¶1 but removes definitions of tax return position and taxpayer, since these have been relocated to the definitions section.
	2.1.2. (NEW)	This adds reference to tax positions mentioned in proposed SSTS No. 1 and proposed SSTS No. 2.3.
	2.1.3.	This replicates extant SSTS No. 1, ¶16.
	2.1.4.	This replicates extant SSTS No. 1, ¶2.
	Statement	
	2.1.5. (NEW)	This adds reference to the definition of tax position in proposed 1.1.4.

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
	2.1.6.	This includes extant SSTS No. 1, ¶4 and ¶5 and adds reference to written standards of other taxing authorities. If they exceed the "realistic possibility of success" standard, then these other standards should be followed.
	2.1.7.	This replicates extant SSTS No. 1, ¶6.
	2.1.8.	This replicates extant SSTS No. 1, ¶7.
	2.1.9. (NEW)	This adds guidance related to tax positions proposed by other parties, as referenced in proposed 2.3.
	Explanation	
	2.1.10.	This replicates extant SSTS No. 1,¶9.
	2.1.11. (modified)	This replicates extant SSTS No. 1, ¶10 but deletes the statement referencing the fact that the standards that apply to a taxpayer may differ from those that apply to a member.
	2.1.12.	This replicates extant SSTS No. 1, ¶12.
	2.1.13.	This replicates extant SSTS No. 1, ¶13.
	2.1.14.	This replicates extant SSTS No. 1, ¶14.
	2.1.15.	This replicates extant SSTS No. 1, ¶15.
SSTS No. 7, *Form and Content of Advice to Taxpayers*	SSTS No. 3, *Standards for Members Providing Tax Consulting Services*	
Introduction	Introduction	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
No. 7 Introduction – ¶1	3.1.1. (modified)	This sentence was deleted: "The statement does not, however, cover a member's responsibilities when the expectation is that the advice rendered is likely to be relied on by parties other than the taxpayer."
Statement	Statement	
No. 7 Statement – ¶2	3.1.2. (modified)	This added reference to the definition of competence under Circular 230, Section 10.35.
No. 7 Statement – ¶3	3.1.3. (modified)	This added reference to tax return positions in proposed 2.1.
No. 7 Statement – ¶4	3.1.4. (modified)	This adds reference to the requirement of a member to communicate subsequent developments if he or she was engaged to implement tax advice previously provided or is engaged to specifically do so.
Explanation	Explanation	
No. 7 Explanation – ¶5	3.1.5.	
No. 7 Explanation – ¶6	3.1.6.	
No. 7 Explanation – ¶7	3.1.7.	
No. 7 Explanation – ¶8	3.1.8.	
No. 7 Explanation – ¶9	3.1.9.	
No. 7 Explanation – ¶10	3.1.10.	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
No. 7 Explanation – ¶11		Deleted.
	3.1.11. (NEW)	This adds guidance about if a member is advising on a position but is not engaged to prepare or sign a tax return, then as long as the member advises the taxpayer on the appropriate disclosure, the standard is satisfied.
	3.1.12. (NEW)	This adds guidance about if a member believes that a taxpayer penalty may be assessed, the member should advise the taxpayer about the possible penalty and opportunities for penalty avoidance with appropriate disclosure. This also states that it is the taxpayer's responsibility to decide whether and how to disclose.
No. 7 Introduction – ¶1	3.1.13.	This added a sentence that was deleted in proposed 3.1.1. related to advice likely to be relied on by parties other than the taxpayer.
	SSTS No. 4, *Standards for Members Providing Tax Representation Services* (NEW)	This is a new standard on taxpayer representation which focuses on the representation relationship.
	Introduction	This limits the standard to representations which require a power of attorney. It also references guidance from other sources that must be adhered to.
	4.1.1.	
	4.1.2.	
	Statement	This provides guidance on the steps a member needs to address throughout the course of the representational relationship.
	4.1.3.	
	4.1.4.	

SSTSs Nos. 1–7 (Effective Jan. 1, 2010, and updated April 30, 2018, to include revised AICPA Code of Professional Conduct citations)	Proposed SSTSs No. 1–4 (Effective no earlier than Jan. 1, 2024)	Notes related to proposed changes
	4.1.5.	
	4.1.6.	
	4.1.7.	
	4.1.8.	
	Explanation	This addresses competency and other subject areas that members need to be familiar with during the representation engagement, including those imposed by the taxing authorities as well as those included in the AICPA's Code of Professional Conduct.
	4.1.9.	
	4.1.10.	
	4.1.11.	
	Contributors	Members of the TEC, Tax Practice Responsibilities Committee, SSTS Revision Task Force and AICPA staff who participated in the issuance of the ED and the ITC are listed. Similar information was provided in the extant standards without a separate heading.

Effective date

If issued as final, the effective date for these finalized SSTSs will be no earlier than Jan. 1, 2024.

Exposure draft

Proposed Statements on Standards for Tax Services

PREFACE

Introduction

Standards are the foundation of a profession. The AICPA aids its members in fulfilling their ethical responsibilities by instituting and maintaining standards against which their professional performance can be measured. Compliance with professional standards of tax practice also reaffirms the public's awareness of the professionalism that is associated with CPAs as well as the AICPA.

This publication sets forth enforceable tax practice standards for members of the AICPA, known as the Statements on Standards for Tax Services (SSTSs or statements). These statements apply to all members providing tax services regardless of the jurisdictions in which they practice. Interpretations of these statements may be issued as guidance to assist in understanding and applying the statements. Any such interpretations have the same authority as defined in the AICPA Code of Professional Conduct, ET sec. 0.100.020, *Interpretations and Other Guidance*.

The SSTSs and their interpretations are intended to complement other standards of tax practice, such as Treasury Department Circular No. 230, *Regulations Governing Practice before the Internal Revenue Service* (Circular 230), penalty provisions of the Internal Revenue Code and state boards of accountancy rules.

The SSTSs are written in as simple and objective a manner as possible. However, by their nature, practice standards provide for an appropriate range of behavior and need to be interpreted to address a broad range of personal and professional situations. The SSTSs recognize this need by, in some sections, providing relatively subjective rules and by leaving certain terms undefined. These terms are generally rooted in tax concepts and, therefore, should be readily understood by tax practitioners. Accordingly, enforcement of the SSTSs is under the *General Standards Rule* (AICPA, Professional Standards, ET secs. 1.300.001 and 2.300.001), and the *Compliance with Standards Rule* (AICPA, Professional Standards, ET secs. 1.310.001 and 2.310.001) of the AICPA Code of Professional Conduct, and will be undertaken on a case-by-case basis. Members are expected to comply with these standards.

Ongoing process

The following SSTSs and any interpretations issued thereunder reflect the AICPA's standards of tax practice and delineate members' responsibilities to taxpayers, the public, the government and the profession. The statements are intended to be part of an ongoing process of articulating standards of tax practice for members. These standards are subject to change as necessary or appropriate to address changes in the tax law or other developments in the tax practice environment.

To accommodate the complexity and rapid change inherent in the tax practice environment, the AICPA issues supplementary guidance to the SSTSs and interpretations in various forms, such as frequently asked questions (FAQs) and practice guides. Such documents are not rules, regulations or official guidance of the Tax Executive Committee (TEC) issued pursuant to its rule-making authority and, therefore, are not authoritative guidance.

Members are encouraged to assess the adequacy of their practices and procedures for providing tax services in conformity with these standards. This process will vary according to the size of the practice and the nature of tax services performed.

The TEC promulgates the SSTSs and their interpretations. Acknowledgment is also due to the many members who have devoted their time and efforts over the years to developing and revising the AICPA's standards.

Form of standards

Each statement is divided into subsections that address a variety of aspects related to tax services. Although some statements have several subsections that address different aspects of tax services, the subsections should be applied as essential elements of the entire statement generally related to all tax services.

- For ease of analysis, each subsection contains an introduction and an explanation section.
- In addition to the AICPA, applicable tax authorities may impose specific reporting and disclosure standards with regard to advising on tax return positions or preparing or signing tax returns. These standards can vary between taxing authorities and by type of tax.
- A member should refer to the current version of Internal Revenue Code Sec. 6694, *Understatement of taxpayer's liability by tax return preparer*, the most recent version of Circular 230 and other applicable tax authority guidance to determine the reporting and disclosure standards that are applicable to the service being provided.

Definitions

All terms herein are as defined in the AICPA Code of Professional Conduct except as noted below.

- **Taxpayer:** A taxpayer is a client, a member's employer or any other third-party recipient of tax services.
- **Tax position:** A tax position is (i) a position reflected on a tax return on which a member has specifically advised a taxpayer or (ii) a position about which a member has knowledge of all materials facts and, on the basis of those facts, has concluded whether the position is appropriate.
- **Member:** Consistent with the AICPA Code of Professional Conduct, ET sec. 0.100; unless otherwise noted, the SSTSs apply to all members providing tax services.

1.1. Advising on tax positions

Introduction

1.1.1. This statement defines tax positions and sets forth the general standards for members advising on tax positions. Standards related to tax return positions are contained in Statement on Standards for Tax Services No. 2, *Standards for Members Providing Tax Compliance Services, Including Tax Return Positions*.

1.1.2. This statement also addresses a member's obligation to advise a taxpayer of relevant tax disclosure responsibilities and potential penalties.

1.1.3. In addition to the AICPA, applicable taxing authorities may impose specific reporting and disclosure standards with regard to advising on tax positions. These standards can vary between taxing authorities and by type of tax.

Statement

1.1.4. A tax position is a conclusion reached when applicable tax law, regulations, case law or other regulatory or recognized guidance is applied to a particular transaction, a specific set of facts and circumstances or a controversy.

1.1.5. A member should determine and comply with the standards, if any, that are imposed by the applicable taxing authority with respect to advising on tax positions.

a. If the applicable taxing authority has no promulgated standards with respect to advising on tax positions, a member should not advise a taxpayer to take a tax position unless the member has a good-faith belief that the position has at least a realistic possibility of being sustained administratively or judicially on its merits if challenged.

b. If the applicable taxing authority has written standards that exceed the realistic possibility standard described in 1.1.5.a. above, the member should comply with those taxing authority standards.

c. Notwithstanding section 1.1.5.a. and b., a member may, as permitted by a taxing authority, advise a taxpayer to take a tax position where the member (i) concludes that there is a reasonable basis for the position and (ii) advises the taxpayer to appropriately disclose that position.

1.1.6. A member should exercise due diligence and professional judgment when advising on tax positions for a particular situation. Such diligence and judgment should inform the scope of the member's inquiry undertaken in the authoritative pronouncements for the particular tax in question and, where appropriate, in professional and other literature related to the issues in question.

1.1.7. When advising on a tax position, a member has the right to be an advocate for the taxpayer with respect to a position satisfying the aforementioned standards.

Explanation

1.1.8. The AICPA and various taxing authorities impose specific standards with respect to tax positions. In a given situation, the standards, if any, imposed by the applicable taxing authority may be higher or lower than the standards set forth in section 1.1.5. A member is to comply with the standards, if any, of the applicable taxing authority; if the applicable taxing authority has no standards or if its standards are lower than the standards set forth in section 1.1.5., the standards set forth in section 1.1.5. will apply.

1.1.9. In addition to a duty to the taxpayer, a member has a duty to the tax system. However, it is well established that the taxpayer has no obligation to pay more taxes than are legally owed, and a member has a duty to the taxpayer to assist in achieving that result or any other legally valid tax outcome the taxpayer desires. The standards contained in section 1.1.5. recognize a member's responsibilities to both the taxpayer and the tax system.

1.1.10. In reaching a conclusion concerning whether a given standard in section 1.1.5. has been satisfied with respect to a particular jurisdiction, a member may consider a well-reasoned construction of the applicable statute and related regulations of that jurisdiction, if any, well-reasoned articles or treatises or guidance issued by the applicable taxing authority, regardless of whether such sources would be treated as authority under Internal Revenue Code Section 6662, *Imposition of accuracy-related penalty on underpayments*, and the regulations thereunder. A position would not fail to meet these standards merely because the position is later abandoned for practical or procedural considerations during an administrative hearing or in the litigation process.

1.1.11. If a member has a good-faith belief that more than one tax position meets the standards set forth in section 1.1.5., a member's advice concerning alternative acceptable positions may include a discussion of the likelihood that each such position might or might not be challenged by the taxing authority.

1.1.12. If particular facts and circumstances lead a member to believe that a taxpayer penalty might be asserted, the member should so advise the taxpayer and should discuss with the taxpayer the opportunity, if any, to avoid such penalty by appropriate disclosure to the taxing authority. A member should also advise the taxpayer it is their responsibility to decide whether and how to disclose.

1.2. Knowledge of errors

Introduction

1.2.1. This statement sets forth the applicable standards for a member who becomes aware of (a) an error in a taxpayer's previously filed tax return; (b) an error in a return that is the subject of an administrative proceeding, such as an examination by a taxing authority or an appeals conference; or (c) a taxpayer's failure to file a required tax return.

1.2.2. As used herein, the term error includes any position, omission or method of accounting that, at the time a position is advised or a return is filed, fails to meet the standards set out in 1.1, *Advising on Tax Positions*, or 2.1, *Tax Return Positions*. The term error also includes a position taken on a prior year's return that no longer meets these standards due to legislation, judicial decisions or administrative pronouncements having retroactive effect. However, an error does not include an item that has an insignificant effect on the taxpayer's tax liability. The term administrative proceeding does not include a criminal proceeding.

1.2.3. This statement applies whether or not the member prepared or signed a return that contains the error.

1.2.4. In addition to the AICPA, applicable taxing authorities may impose specific standards with regard to errors discovered during the provision of tax services by a member. These standards can vary between taxing authorities and by type of tax.

1.2.5. Special considerations may apply when a member has been engaged by legal counsel to provide assistance in a matter relating to a taxpayer.

Statement

1.2.6. A member should inform a taxpayer promptly upon becoming aware of the taxpayer's failure to file a required return, an error in a previously filed return, an error in a return that is the subject of an administrative proceeding, an error in an

administrative filing (such as a ruling request, accounting method change, etc.) or an error in advice provided. A member also should advise the taxpayer of the potential consequences of the error and advise on corrective measures to be taken. Such advice may be given orally. See also section 3.1.2. regarding the documentation of advice.

1.2.7. If a member prepares a tax return for the current or a prior tax year, and the taxpayer has not taken appropriate action to correct an error related to a tax return position in a tax return for a prior year, the member should consider whether to withdraw from preparing the current return and whether to continue a professional or employment relationship with the taxpayer. If the member does prepare the current year return, the member should take reasonable steps to ensure that the error is not repeated.

1.2.8. A member is not allowed to inform a taxing authority of an error without the taxpayer's permission, except when required by law. Members also should consider whether they can continue a professional relationship with a taxpayer who refuses to properly mitigate a discovered error.

1.2.9. If a member is representing a taxpayer in an administrative proceeding with respect to a return that contains an error of which the member is aware, the member should request the taxpayer's agreement to disclose the error to the taxing authority. Lacking such agreement, the member should consider whether to withdraw from representing the taxpayer in the administrative proceeding and whether to continue a professional or employment relationship with the taxpayer.

Explanation

1.2.10. If a member becomes aware of an error while performing tax services, the member's responsibility is to advise the taxpayer of the existence of the error. The member should advise the taxpayer of the error and the potential consequences, and advise on corrective measures to be taken, if any. If the member does not prepare the taxpayer's tax return or was not the provider of the advice, the member may instead advise that the error be discussed with the taxpayer's tax return preparer or advisor. Similarly, when representing the taxpayer before a taxing authority in an administrative proceeding with respect to a return containing an error of which the member is aware, the member should advise the taxpayer to disclose the error to the taxing authority and of the potential consequences of not disclosing the error. Refer to section 3.1.2. for considerations regarding the decision to provide such advice in oral or written form.

1.2.11. It is the taxpayer's responsibility to decide whether to correct an error. If the taxpayer does not correct an error, a member should consider whether to withdraw from the engagement and whether to continue a professional or employment relationship with the taxpayer. Although recognizing that the taxpayer may not be required by statute to correct an error by filing an amended return, a member should consider whether a taxpayer's decision not to file an amended return or otherwise correct an error may predict future behavior that might require termination of the relationship.

1.2.12. Once the member has obtained the taxpayer's consent to disclose an error in an administrative proceeding, the disclosure should not be delayed to such a degree that the taxpayer or member might be considered to have failed to act in good faith or to have, in effect, provided misleading information. In any event, disclosure should be made before the conclusion of the administrative proceeding.

1.2.13. Members have a responsibility to both the taxpayer and the tax system. Discovery of an error in an administrative proceeding or filing, such as a ruling request, might negate the effect of the ruling if not disclosed to the authority. Failure to comply with statutory or regulatory compliance requirements impact not only the taxpayer, but also the integrity of the entire tax system.

1.2.14. A conflict between the member's interests and those of the taxpayer may be created by, for example, the potential for violating Code of Professional Conduct, *Confidential Client Information Rule* (AICPA, Professional Standards, ET sec. 1.700.001) (relating to the member's confidential client relationship); the tax law and regulations; or laws on privileged communications, as well as by the potential adverse impact on a taxpayer of a member's withdrawal. Therefore, a member should consider consulting with his or her own legal counsel before deciding upon providing advice to the taxpayer and whether to continue a professional or employment relationship with the taxpayer.

1.2.15. If a member believes that a taxpayer may face possible exposure to allegations of fraud or other criminal misconduct, the member should advise the taxpayer to consult with an attorney before the taxpayer takes any action.

1.2.16. If a member decides to continue a professional or employment relationship with the taxpayer and is requested to prepare a tax return for a year subsequent to that in which an error occurred, the member should take reasonable steps to ensure that the error is not repeated. If the subsequent year's tax return cannot be prepared without perpetuating the error, the member should consider withdrawal from the return preparation. If a member learns that the taxpayer is using an erroneous method of accounting and it is past the due date to request permission to change to a method meeting the standards of section 2.1.1., the member may sign a tax return for the current year, providing the tax return includes appropriate disclosure of the use of the erroneous method.

1.2.17. Whether an error has no more than an insignificant effect on the taxpayer's tax liability is left to the professional judgment of the member based on all the facts and circumstances known to the member. In judging whether an erroneous method of accounting has more than an insignificant effect, a member should consider the method's cumulative effect, as well as its effect on the tax advice provided, current year's tax return or the tax return that is the subject of the administrative proceeding.

1.3. Data protection

Introduction

1.3.1. This statement sets forth the applicable standards for a member's responsibilities related to the protection of taxpayer data obtained in the course of rendering services for a taxpayer.

1.3.2. A member's responsibility to protect taxpayer information is a well-established professional responsibility. The increasing use of technology by individuals and businesses, together with a growing awareness and attention of data breaches and identity theft, has resulted in a growing sensitivity towards and need for a focus on the protection of taxpayer data, including electronic data.

1.3.3. This standard complements, and does not alter or replace, the confidentiality standards established in the AICPA Code of Professional Conduct 1.700.001, *Confidential Information Rule* and the Interpretations thereunder.

Statement

1.3.4. A member should make reasonable efforts to safeguard taxpayer data, including data transmitted or stored electronically.

1.3.5. A member should consider applicable privacy laws when collecting and storing taxpayer data.

Explanation

1.3.6. The statement uses the term "reasonable," knowing that actions or behaviors considered "reasonable" may differ over time, among members and from firm to firm based on size and resources. The absence of any bright-line rules was purposeful, allowing for changing technology, laws, guidance and practice.

1.3.7. Appropriate safeguards should be implemented to protect both member and taxpayer data stored within the member's information systems platform. Appropriate safeguards should be based on current recommended practices, and may, for example, include the installation and use of commercial security software to prevent unwanted or unauthorized access to information, encryption of data that is sent between multiple parties over the internet, the use of secure networks, strong password policies, use of firewalls and use of secure data sharing/collaboration platforms.

a. A member should consider other industry standards, such as the AICPA's Privacy Management Framework and Trust Services Criteria when developing a privacy program.

1.3.8. Members may use electronic tools owned and hosted by others, such as tax return preparation software, or may outsource certain tasks, such as converting paper documents to electronic information. Members should take reasonable efforts to confirm that taxpayer information properly shared with others in the course of providing a service is appropriately protected.

1.3.9. A member should take reasonable steps to limit the amount of taxpayer confidential information in the member's files. For example, the member should collect only the information necessary to perform the services for which the member is being engaged or otherwise approved to perform by the taxpayer, returning or redacting any confidential taxpayer information unnecessary to complete the services. This may also include insisting that any personally identifiable information (PII) or personal health information (PHI) be masked/anonymized prior to receipt by the member. Additionally, adherence to appropriate document retention and destruction policies can help to ensure that taxpayer data is properly removed from a member's information systems once it is no longer needed under the respective statute of limitations or the member's document retention policies.

1.3.10. In developing safeguards, members should also consider steps to be taken in the event of a data breach, including compliance with notification obligations. For example, the Federal Trade Commission (FTC) provides recommendations that include securing systems and fixing issues that are attributed to the breach. Consider forming a plan to quickly respond to those affected by the breach. Notify appropriate authorities of the breach as required by law.

1.3.11. Members should consider applicable privacy laws. For example, the Financial Services Modernization Act of 1999 (also referred to as the Gramm-Leach-Bliley Act (GLBA)), requires professional tax return preparers to ensure the security and confidentiality of customer (i.e., taxpayer) financial information. As part of the implementation of the GLBA, the FTC issued the Safeguards Rule, requiring the development of a written information security plan that describes the program put in place to protect taxpayer information commensurate with relative firm size of the member and complexity of services provided. Additionally, under these rules, return preparers are responsible for taking steps to ensure that their affiliates and service providers safeguard taxpayer information in their care. As with many privacy laws, the FTC has subsequently updated the rule to keep pace with technology and members should periodically review applicable privacy laws to keep abreast of applicable rules.

1.3.12. A member should have general knowledge of the current security expectations of taxing authorities and taxpayers. Data security is a topic addressed in the tax press and by taxing authorities. For example, at the time of this writing, the IRS has a webpage with links to various publications and other information related to data protection. Members are not expected to become experts in this area, but it is reasonable that a member avail himself or herself of the information made generally available to tax professionals on the subject, including those referenced in section 1.3.7.1.

1.3.13. Training is a vital component of any data protection plan. A member should make reasonable efforts to ensure all non-member personnel who the member supervises should be trained and informed about data protection. For example, staff should be informed how to recognize phishing emails and the dangers of opening or downloading attachments from unknown senders.

1.4. Reliance on tools

Introduction

1.4.1. This statement sets forth the applicable standards for members when relying on tools in the provision of tax services including, but not limited to, the preparation of a tax return, tax consulting services and tax representation.

1.4.2. For purposes of this section, a tool is a resource used in the provision of tax services. Tools include, but are not limited to, tax preparation software, tax research publications (paper or electronic), tax-related calculation aides, tax planning software, state and local tax aids, online data search engines, data analytics, statistical models, artificial intelligence and relevant professional publications and resources.

Statement

1.4.3. A member should exercise appropriate professional judgement and professional care when relying on a tool.

1.4.4. A member may reasonably rely on tools used in providing tax services to a taxpayer. Use of the tool does not absolve the member of his or her professional obligations under AICPA or other applicable ethical standards.

Explanations

1.4.5. Tools developed for use in the provision of tax services provide significant benefits to members. It is generally a best practice of a member to rely on such tools to a certain extent to improve efficiency and client service.

1.4.6. The source of the tools must be considered when determining the appropriate level of reliance on that tool. For example, subscription-based tax research tools and resources may have more weight than opinion articles from independent internet sources.

1.4.7. A member who employs tools in providing tax services remains responsible for the completed work product in accordance with the various other standards contained in the statements. Accordingly, members should take reasonable steps to satisfy themselves that the results presented by the use of various tools are reliable. For example, a member should confirm that the calculation of taxable income and tax liability for an income tax return that is completed using professional tax return preparation software is accurate and meets the standards for tax return positions established in 2.1, *Tax Return Positions*.

1.4.8. Tools should be used to enhance or improve the member's understanding of a tax issue, not to supplant the member's professional judgement. For example, when preparing a Federal Form 1040, *U.S. Individual Income Tax Return*, a member must still attest under penalties of perjury that, to the best of the preparer's knowledge and belief, the return and accompanying schedules are true, correct and complete. That responsibility cannot be transferred entirely to reliance on a tool.

2.1. Tax return positions

Introduction

2.1.1. This statement sets forth the applicable standards for members preparing or signing tax returns (including amended returns, claims for refund and information returns) filed with any taxing authority.

2.1.2. Additional standards apply to tax positions which a member advises on. Refer to 1.1, *Advising on Tax Positions*. When signing or preparing a tax return that includes a tax position which a third party advised on, also refer to 2.3, *Reliance on Information from Others*.

2.1.3. For purposes of this statement, preparation of a tax return includes giving advice on events that have occurred at the time the advice is given if the advice is directly relevant to determining the existence, character or amount of a schedule, entry or other portion of a tax return.

2.1.4. This statement also addresses a member's obligation to advise a taxpayer of relevant tax return disclosure responsibilities and potential penalties.

Statement

2.1.5. A tax return position is a tax position (as defined in section 1.1.4) that is reflected on a tax return prepared by a member or for which a member signs as preparer.

2.1.6. A member should determine and comply with the standards, if any, that are imposed by the applicable taxing authority with respect to preparing or signing a tax return.

a. If the applicable taxing authority has no written standards with respect to preparing or signing a tax return, a member should not prepare or sign the tax return unless the member has a good-faith belief that the tax return position has at least a realistic possibility of being sustained administratively or judicially on its merits if challenged.

b. If the applicable taxing authority has written standards that exceed the realistic possibility standard described in section 2.1.6.a. above, the member should comply with those taxing authority standards.

c. Notwithstanding section 2.1.6.a. and b., a member may, as permitted by a taxing authority, prepare or sign a tax return which includes a tax return position where (i) the member concludes there is a reasonable basis for the tax return position and (ii) the position is appropriately disclosed.

2.1.7. When preparing or signing a tax return on which a tax return position is taken, a member should, when relevant, advise the taxpayer regarding potential penalty consequences of such tax return position and the opportunity, if any, to avoid such penalties through disclosure.

2.1.8. A member should not advise a taxpayer to take a tax return position or prepare or sign a tax return reflecting a tax return position that the member knows:

a. exploits the audit selection process of a taxing authority, or

b. serves as a mere arguing position advanced solely to obtain leverage in a negotiation with a taxing authority.

2.1.9. A member may rely, in good faith, on the tax positions proposed by others regarding the issues being considered, provided the member is satisfied that the standards in 2.3, Reliance on Information from Others, are satisfied.

Explanation

2.1.10. The AICPA and various taxing authorities impose specific reporting and disclosure standards with respect to tax return positions and preparing or signing tax returns. In a given situation, the standards, if any, imposed by the applicable taxing authority may be higher or lower than the standards set forth in section 2.1.6. A member is to comply with the standards, if any, of the applicable taxing authority. If the applicable taxing authority has no standards or if its standards are lower than the standards set forth in section 2.1.6, the standards set forth in section 2.1.6. will apply.

2.1.11. Our self-assessment tax system can function effectively only if taxpayers file tax returns that are true, correct and complete. A tax return is prepared based on a taxpayer's representation of facts, and the taxpayer has the final responsibility for positions taken on the return.

2.1.12. In reaching a conclusion concerning whether a given standard in 2.1.6. has been satisfied, a member may consider a well-reasoned construction of the applicable statute and related regulations, if any, well-reasoned articles or treatises or pronouncements issued by the applicable taxing authority, regardless of whether such sources would be treated as authority under Internal Revenue Code Section 6662, *Imposition of accuracy-related penalty on underpayments*, and the regulations thereunder. A position would not fail to meet these standards merely because it is later abandoned for practical or procedural considerations during an administrative hearing or in the litigation process.

2.1.13. If a member has a good-faith belief that more than one tax return position meets the standards set forth in section 2.1.6., a member's advice concerning alternative acceptable positions may include a discussion of the likelihood that each such position might or might not cause the taxpayer's tax return to be examined and whether the position would be challenged in an examination. In such circumstances, such advice is not a violation of section 2.1.6.

2.1.14. A member's advising on whether information is appropriately disclosed by the taxpayer should be based on the facts and circumstances of the particular case and the disclosure requirements of the applicable taxing authority. If a member advising on a tax position, but not engaged to prepare or sign the related tax return, advises the taxpayer concerning appropriate disclosure of the position, then the member shall be deemed to meet the disclosure requirements of these standards.

2.1.15. If particular facts and circumstances lead a member to believe that a taxpayer penalty might be asserted, the member should so advise the taxpayer and should discuss with the taxpayer the opportunity, if any, to avoid such penalty by disclosing the position on the tax return. A member should also advise the taxpayer it is their responsibility to decide whether and how to disclose.

2.2. Tax return questions

Introduction

2.2.1. This statement sets forth the applicable standards for members when signing the preparer's declaration on a tax return if one or more questions on the return have not been answered. The term questions include requests for information on the return, in the instructions or in the regulations, whether or not stated in the form of a question.

Statement

2.2.2. Before signing as preparer, a member should take reasonable steps to obtain from the taxpayer the information necessary to provide appropriate answers to all required questions on a tax return.

Explanation

2.2.3. It is recognized that the questions on tax returns are not of uniform importance, and often they are not applicable to the particular taxpayer. Nevertheless, there are at least three reasons why a member should be satisfied that a reasonable effort has been made to obtain information to provide appropriate answers to the questions on the return that are applicable to a taxpayer:

a. A question or other information may be of importance in determining taxable income or loss, or the tax liability shown on the return, in which circumstance an omission may detract from the completeness of the return.

b. A request for information may require a disclosure necessary for a complete return or to avoid penalties.

c. A member often must sign a preparer's declaration stating that the return is true, correct and complete. Additionally, this may be stipulated as being signed under penalties of perjury.

2.2.4. Reasonable grounds may exist for omitting an answer to a question applicable to a taxpayer. For example, reasonable grounds may include the following:

a. The information is not readily available and the answer is not significant in terms of its impact on taxable income or loss, or the tax liability shown on the return.

b. Genuine uncertainty exists regarding the meaning of a question in relation to the particular return.

c. The information requested is voluminous; in such cases, a statement should be made on the return that the information will be supplied upon request.

2.2.5. A member should not omit an answer merely because it might prove disadvantageous to a taxpayer.

2.2.6. A member should consider whether the omission of an answer to a question may cause the return to be deemed incomplete or result in penalties, and advise the taxpayer accordingly.

2.2.7. If reasonable grounds exist for omission of an answer to an applicable question, a taxpayer is not required to provide on the return an explanation of the reason for the omission.

2.3. Reliance on information from others

Introduction

2.3.1. This statement sets forth the applicable standards for members concerning the obligation to examine or verify certain supporting data or to consider information related to another taxpayer when preparing a taxpayer's tax return.

Statement

2.3.2. In preparing or signing a return, or a portion of a return, a member may in good faith rely, without verification, on information furnished by the taxpayer or by third parties. However, a member should not ignore the implications of information furnished and should make reasonable inquiries if the information furnished appears to be incorrect, incomplete or inconsistent either on its face or on the basis of other facts known to the member. A member should consider one or more of the taxpayer's prior year tax returns, or a portion of a return, whenever feasible.

2.3.3. If the tax law or regulations impose a condition with respect to deductibility or other tax treatment of an item, a member should make reasonable inquiries to determine to the member's satisfaction whether such condition has been met.

2.3.4. When preparing a tax return, a member should consider relevant information actually known by that member from other sources, including the tax return of another taxpayer. In using such information, a member should consider any limitations imposed by any law or rule relating to confidentiality.

Explanation

2.3.5. The preparer's declaration on a tax return often states that the information contained therein is true, correct and complete to the best of the preparer's knowledge and belief based on all information known by the preparer. This type of reference should be understood to include information furnished by the taxpayer or by third parties to a member in connection with the preparation of the return.

2.3.6. The preparer's declaration does not require a member to examine or verify supporting data; a member may rely on information furnished by the taxpayer unless it appears to be incorrect, incomplete or inconsistent. However, there is a need to determine by inquiry that a specifically required condition, such as maintaining books and records or substantiating documentation, has been satisfied and to obtain information when the material furnished appears to be incorrect, incomplete or inconsistent. Although a member has certain responsibilities in exercising due diligence in preparing a return, the taxpayer has the ultimate responsibility for the contents of the return. Thus, if the taxpayer presents unsupported data in the form of lists of tax information, such as dividends and interest received, charitable contributions and medical expenses, such information may be used in the preparation of a tax return without verification unless it appears to be incorrect, incomplete or inconsistent either on its face or on the basis of other facts known to a member.

2.3.7. Even though there is no requirement to examine underlying documentation, a member should encourage the taxpayer to provide supporting data where appropriate. For example, a member should encourage the taxpayer to submit underlying documents for use in tax return preparation to permit full consideration of income and deductions arising from security transactions and from pass-through entities, such as estates, trusts, partnerships and S corporations.

2.3.8. The source of information provided to a member by a taxpayer for use in preparing the return is often a pass-through entity, such as a limited partnership, in which the taxpayer has an interest but is not involved in management. A member may accept the information provided by the pass-through entity without further inquiry, unless there is reason to believe it is incorrect, incomplete or inconsistent, either on its face or on the basis of other facts known to the member. In some instances, it may be appropriate for a member to advise the taxpayer to ascertain the nature and amount of possible exposure to tax deficiencies, interest and penalties by taxpayer contact with management of the pass-through entity.

2.3.9. A member should make use of a taxpayer's returns for one or more prior years in preparing the current return whenever feasible. Reference to prior returns and discussion of prior-year tax determinations with the taxpayer often provides information to determine the taxpayer's general tax status, avoid the omission or duplication of items and afford a basis for the treatment of similar or related transactions. As with the examination of information supplied for the current year's return, the extent of comparison of the details of income and deduction between years depends on the particular circumstances.

2.4. Use of estimates

Introduction

2.4.1. This statement sets forth the applicable standards for members when using the taxpayer's estimates in the preparation of a tax return. Appraisals or valuations are not considered estimates for purposes of this statement. The accuracy of the estimate is the responsibility of the taxpayer.

Statement

2.4.2. Unless prohibited by statute, administrative rule or judicial holdings, a member may use estimates, whether from the taxpayer or other sources authorized by the taxpayer as permitted in 2.3, *Reliance on Information from Others*, in the preparation of a tax return if it is not practical to obtain exact data and if the member determines that the estimates are reasonable based on the facts and circumstances known to the member. Estimates should be presented in a manner that does not imply greater accuracy than exists.

Explanation

2.4.3. Accounting requires the exercise of professional judgment and, in many instances, the use of approximations based on judgment. The application of such accounting judgments, as long as not in conflict with rules set forth by a taxing authority, is acceptable. These judgments are not estimates within the purview of this statement. For example, a federal income tax regulation provides that if all other conditions for accrual are met, the exact amount of income or expense need not be known or ascertained at year end if the amount can be determined with reasonable accuracy.

2.4.4. When the taxpayer's records do not accurately reflect information related to small expenditures, accuracy in recording some data may be difficult to achieve. Therefore, the use of estimates by a taxpayer in determining the amount to be deducted for such items may be appropriate.

2.4.5. When records are missing or precise information about a transaction is not available at the time the return must be filed, a member may prepare a tax return using a taxpayer's estimates of the missing data. The member should inform the taxpayer of the taxpayer duty to maintain records that support the return.

2.4.6. Estimated amounts should not be presented in a manner that provides a misleading impression about the degree of factual accuracy.

2.4.7. Specific disclosure that an estimate is used for an item in the return is not generally required; however, such disclosure should be made in unusual circumstances where nondisclosure might mislead the taxing authority regarding the degree of accuracy of the return as a whole. Some examples of unusual circumstances include the following:

a. A taxpayer has died or is ill at the time the return must be filed.

b. A taxpayer has not received a Schedule K-1 for a pass-through entity at the time the tax return is to be filed.

c. There is litigation pending (for example, a bankruptcy proceeding) that bears on the return.

d. Fire, technology issues or natural disaster has destroyed the relevant records.

2.5. Departure from previous positions

Introduction

2.5.1. This statement sets forth the applicable standards for members in advising on a tax return position that departs from the position determined in an administrative proceeding or in a court decision with respect to the taxpayer's prior return.

2.5.2. For purposes of this statement, administrative proceeding includes an examination by a taxing authority or an appeals conference relating to a return or a claim for refund.

2.5.3. For purposes of this statement, court decision means a decision by any court having jurisdiction over tax matters.

Statement

2.5.4. Unless the taxpayer is bound to a specified treatment of a tax return position in a later tax year, the member may advise on a tax return position or prepare or sign a tax return that departs from the treatment of an item as concluded in an administrative proceeding or court decision with respect to a prior return of the taxpayer, provided the requirements of 2.1, *Tax Return Positions*, are satisfied.

Explanation

2.5.5. If an administrative proceeding or court decision has resulted in a determination concerning a specific tax treatment of an item in a prior year's return, a member will usually advise this same tax treatment in subsequent years. However, unless the taxpayer is contractually bound to a particular tax treatment, departures from consistent treatment may be justified under such circumstances as the following:

a. Taxing authorities tend to act consistently in the disposition of an item that was the subject of a prior administrative proceeding but generally are not bound to do so. Similarly, a taxpayer is not bound to follow the tax treatment of an item as consented to in an earlier administrative proceeding.

b. The determination in the administrative proceeding or the court's decision may have been caused by a lack of documentation. Supporting data for the later year may be appropriate.

c. A taxpayer may have yielded in the administrative proceeding for settlement purposes or not appealed the court decision, even though the position met the standards in 2.1, *Tax Return Positions*.

d. Court decisions, rulings or other authorities that are more favorable to a taxpayer's current position may have developed since the prior administrative proceeding was concluded or the prior court decision was rendered.

2.5.6. The consent in an earlier administrative proceeding and the existence of an unfavorable court decision are factors that the member should consider in evaluating whether the standards in 2.1, *Tax Return Positions*, are met.

Statement on Standards for Tax Services No. 3, *Standards for Members Providing Tax Consulting Services*

Introduction

3.1.1. This statement sets forth the applicable standards for members concerning certain aspects of providing tax advice to a taxpayer and considers the circumstances in which a member has a responsibility to communicate with a taxpayer when subsequent developments affect advice previously provided.

Statement

3.1.2. A member should use professional judgment to ensure that tax advice provided in a tax consulting engagement reflects competence and is based on applicable standards. For this purpose, competence follows the definition established in Section 10.35 of Circular 230. A member may communicate tax advice in writing or orally. When communicating tax advice in writing, a member should comply with relevant taxing authorities' standards, if any, applicable to written tax advice. A member should use professional judgment about any need to document oral advice. A member is not required to follow a standard format when communicating or documenting oral and written advice.

3.1.3. A member should assume that tax advice provided to a taxpayer will affect the manner in which the matters or transactions considered would be reported or disclosed on the taxpayer's tax returns. Therefore, for tax advice given to a taxpayer, a member should consider, when relevant (a) return reporting and disclosure standards applicable to the related tax position and (b) the potential penalty consequences of the return position. In ascertaining applicable return reporting and disclosure standards, a member should follow the standards in 2.1, *Tax Return Positions*.

3.1.4. A member has no professional obligation to communicate the impact of subsequent developments that affect advice previously provided to taxpayers, whether current clients or not. Members should communicate the impact of subsequent developments when they are assisting in implementing procedures or plans associated with the tax advice previously provided, or are specifically engaged to report on such developments by specific agreement.

Explanation

3.1.5. Tax advice is recognized as a valuable service provided by members. The form of advice may be oral or written and the subject matter may range from routine to complex. Because the range of advice is so extensive and because advice should meet the specific needs of a taxpayer, neither a standard format nor guidelines for communicating or documenting advice to the taxpayer can be established to cover all situations.

3.1.6. Although oral advice may serve a taxpayer's needs appropriately in routine matters or in well-defined areas, written communications are recommended in important, unusual, substantial dollar value or complicated transactions. The member may use professional judgment about whether, subsequently, to document oral advice.

3.1.7. In deciding on the form of advice provided to a taxpayer, a member should exercise professional judgment and consider such factors as the following:

a. The importance of the transaction and amounts involved
b. The specific or general nature of the taxpayer's inquiry
c. The time available for development and submission of the advice
d. The technical complexity involved

e. The existence of authorities and precedents

f. The tax sophistication of the taxpayer

g. The need to seek other professional advice

h. The type of transaction and whether it is subject to heightened reporting or disclosure requirements

i. The potential penalty consequences of the tax position for which the advice is rendered

j. Whether any potential applicable penalties can be avoided through disclosure

k. Whether the member intends for the taxpayer to rely upon the advice to avoid potential penalties

3.1.8. A member may assist a taxpayer in implementing procedures or plans associated with the advice offered. When providing such assistance, the member should review and revise such advice as warranted by new developments and factors affecting the transaction.

3.1.9. Sometimes a member is requested to provide tax advice but does not assist in implementing the plans adopted. Although such developments as legislative or administrative changes or future judicial interpretations may affect the advice previously provided, a member cannot be expected to communicate subsequent developments that affect such advice unless the member undertakes this obligation by specific agreement with the taxpayer.

3.1.10. Taxpayers should be informed that (a) the advice reflects professional judgment based upon the member's understanding of the facts, and the law existing as of the date the advice is rendered and (b) subsequent developments could affect previously rendered professional advice. Members may use precautionary language to the effect that their advice is based on facts as stated and authorities that are subject to change.

3.1.11. If a member advising on a position, but not engaged to prepare or sign the related tax return, advises the taxpayer concerning appropriate disclosure of the position, then the member shall be deemed to meet the disclosure requirements of these standards.

3.1.12. If particular facts and circumstances lead a member to believe that a taxpayer penalty might be asserted, the member should so advise the taxpayer and should discuss with the taxpayer the opportunity, if any, to avoid such penalty by disclosing the position on the tax return. Although a member should advise the taxpayer with respect to disclosure, it is the taxpayer's responsibility to decide whether and how to disclose.

3.1.13. This standard does not address situations in which consulting services may be relied on by parties other than the taxpayer.

Statement on Standards for Tax Services No. 4, *Standards for Members Providing Tax Representation Services*

Introduction

4.1.1. This statement sets forth the applicable standards for a member representing a taxpayer with a power of attorney before an applicable taxing authority. Representing a taxpayer in various tax matters could involve application of other standards. The focus of this statement is on the representation relationship itself.

4.1.2. In addition to the AICPA, applicable taxing authorities may impose specific guidance related to the representation of taxpayers, such as Circular 230. These standards can vary between taxing authorities and by type of tax.

Statement

4.1.3. The member, and any individuals working with or for the member, should have or take steps to obtain technical competence in the subject matter involved. This includes competence in the technical tax area involved as well as the tax practice and procedures of the taxing authority. For this purpose, competence follows the definition established in Section 10.35 of Circular 230.

4.1.4. The member should take appropriate steps to ensure compliance with all relevant professional and regulatory obligations when representing a taxpayer.

4.1.5. The member should act with integrity and professionalism in all dealings with the taxing authority. This includes not unduly delaying or impeding the taxing authority.

4.1.6. Information requested by the taxing authority should, with taxpayer approval, be provided by the member on a timely basis unless there is a good-faith belief that the information is privileged.

4.1.7. The member should consider if the taxpayer's conduct may be fraudulent or criminal in nature. If so, the member should advise the taxpayer to retain legal counsel and refrain from further representation.

4.1.8. Upon completion of the examination by the taxing authority, the member should review any documents or computations detailing the results of the examination for correctness and discuss with the taxpayer the consequences of agreeing to these conclusions.

Explanation

4.1.9. Competency is an important issue for professionals who provide tax representation services. While continuing professional education tends to focus on tax law updates or more complex technical tax issues, members often overlook the complicated rules of tax practice and procedure that go hand in hand with representation of taxpayers. Members dealing with tax agencies should be knowledgeable about the procedural issues they may encounter while representing taxpayers.

4.1.10. Members should consider multiple areas which could impact a taxpayer representation engagement. Among other items, this may include:

a. Consulting with a local law firm to determine whether the representation would constitute the unauthorized practice of law;

b. Determining whether CPA licensure in another jurisdiction may be required;

c. Executing any taxpayer authorizations required by the taxing authority such as powers of attorney;

d. Determining whether the member may be facing a conflict of interest such as representing other taxpayers who are taking a contrary position;

e. Establishing and documenting in writing an understanding with the taxpayer regarding objectives of the engagement, services to be performed, taxpayer's acceptance of its responsibilities, member's responsibilities and any limitations of the engagement.

4.1.11. When representing taxpayers, members are required to comply with all conflict-of-interest standards, such as Section 1.000.020, *Ethical Conflicts of the Code of Professional Conduct*.

Questions for respondents

The goal of the revisions of the SSTSs is to ensure that the standards are still relevant in today's tax environment, address the current and emerging needs of today's members and to serve the public. In addition, the standards were reorganized to enhance their understanding and use.

The AICPA values the views of all stakeholders and is seeking comments. We encourage you to provide us your thoughts on any or all of the revisions and have provided specific questions to help you provide us feedback.

Please advise if your response is on behalf of a firm, business or other stakeholder or whether it represents your individual views. Additionally, please include what your role and title is and details of your firm or organization size.

Please submit comments via our online form. Alternatively, you may email your submission to: SSTScomments@aicpa-cima.com.

ED1. Do you agree with the reorganization of the current SSTSs, and will it enhance their use and understanding? Please explain the rationale behind your response.

ED2. Based on review of the proposed changes to the SSTSs, is there any other subject matter which you believe should be revised or deleted from the SSTSs? If so, please provide the rationale.

ED3. Are the proposed new standards (data protection, reliance on tools and tax representation services) clear and understandable? If you believe more specificity would be helpful, what recommendations would you suggest?

ED4. What other subjects impact your tax practice or the tax function you perform and should be considered in future revisions to the SSTSs? Please provide details of the recommended additions, together with your reasoning for the proposed changes.

ED5. What additional guidance is needed to help you understand, effectively implement and apply the proposed standards to your working environment?

Part 2:
Invitation to Comment

This ITC is separate and independent from the preceding ED and presents items for consideration that require additional research and investigation and thus will require additional time to define and potentially implement. Depending on the nature of the comments received in response to this ITC, the AICPA will pursue additional research to determine the appropriateness of future modifications to the SSTSs or other guidance. At this time, it is not known if or when any changes resulting from the ITC will be implemented.

Introduction

As part of the process to update the SSTSs, the SSTS Revision Task Force held extensive discussions around the importance of additional concepts with the potential to significantly impact the tax practice of the future. A resonating theme emerged in many discussions related to quality management in tax, defined as a proactive, risk-based, scalable approach to ensure that an individual or firm possesses the necessary competence to practice. Based on the discussions, members agreed that quality is a key market differentiator in their practices; however, its implementation is inconsistent and the environment in which members operate is dynamic.

Given the importance of this topic, the AICPA is inviting members and stakeholders to comment on the questions raised in this ITC. The task force and the TEC will consider all comments in determining the best approach to address quality within the tax function.

Issue description

One of the aims of the AICPA's Code of Professional Conduct is to protect the public interest. The public interest principle states that "... members should accept the obligation to act in a way that will serve the public interest, honor the public trust and demonstrate a commitment to professionalism." Members are expected to provide quality services in a manner that demonstrates a level of professionalism consistent with these goals. These are the expectations that members are held to and, when asked, it is recognized that high quality work products are a defining feature of CPAs.

The CPA brand is consistently associated with numerous characteristics including trust, integrity, honesty and quality. Many professions aspire to be associated with these traits, yet few achieve the reputation CPAs have maintained for over 125 years. Thus, members have an opportunity to continue to be perceived as the premier providers of tax services by demonstrating adherence to quality principles in the delivery of their services. By investing in systems that will help them develop a strong approach to quality management and making sure that such concepts are embraced by all individuals who are part of the firm or department, members can enhance the services they provide and can better position themselves in the event of an investigation by the IRS Office of Professional Responsibility or other government agency.

State of quality management in tax

CPAs have benefited from practicing in a self-regulated profession due to the strong reputation of the AICPA's professional standards. However, in December of 2009, the IRS released a 57-page document outlining a plan to regulate all tax return preparers. Although CPAs, attorneys and enrolled agents were exempted from most of the requirements imposed on "unenrolled" tax return preparers, the IRS indicated a plan to assess the quality of tax return preparation by exempted tax professionals. Despite the judicial determination in *Loving v. Commissioner* that the IRS did not have the authority to regulate tax return preparers, discussions regarding both the regulation of tax return preparers and the quality of professionally prepared tax returns have continued. For example, the IRS requires individuals

representing taxpayers before the IRS to have adequate procedures in place to comply with ethical and quality guidelines established in Circular 230 (refer to Section 10.36).

The IRS has since publicly announced that it is reviewing the provisions of Circular 230 with the intent of updating them. Although unknown if such revisions will encompass mandatory enhancements to quality, it is widely believed that greater scrutiny, by both the taxing authorities and the public at large, will be placed on members.

Some members have expressed that initiating an approach to quality management in tax may be perceived as a step towards peer review. The TEC and the AICPA consider the concept of quality management and peer review to be independent and distinct from one another.

Implementation

With more focus on quality management in tax comes the perception that implementing such procedures could present a burden or put members at a competitive disadvantage against other tax practitioners. In reality, most members already have quality management procedures in place. While some may believe that such an approach could mandate the use of checklists or other such documents to prove procedures are being adhered to in the performance of tax services, alternative simpler approaches could be used. For example, a member could periodically discuss how they adhere to the six elements of a tax practice quality control system identified in the Tax Practice Quality Control Guide and Template. This resource is offered by the AICPA Tax Section to members who are looking to develop a more robust system in areas such as:

- Leadership responsibilities for quality within a firm,
- Relevant ethical requirements,
- Acceptance and continuance of client relationships and specific engagements,
- Human resources,
- Engagement performance, and
- Monitoring.

In general, members have expressed support for initiatives to improve the quality of tax services. Though the implications related to the cost and effort necessary to implement such initiatives may be deemed too burdensome by some members, many recognize the benefits. The process of implementing a system that encompasses the firm's organizational structure, along with the policies and procedures established to provide a level of confidence that the tax practice complies with applicable professional, statutory and regulatory requirements (e.g., SSTSs and Circular 230), demonstrates good business practice.

Embracing quality principles will demonstrate to regulators, clients, organizations and the public that members are the premier providers of tax services. There is not a "one-size-fits-all" solution, simply the desire to consistently produce a quality product in a manner that works best for a member's particular circumstances. With this in mind, the TEC and the task force seek the input of members and stakeholders on the optimal approach to improve quality management in tax.

We appreciate your responses to the questions below, along with any other thoughts you have around the concept of quality management and how it can best be implemented by all members, irrespective of the tax services they provide or the type of client or organization they serve.

Please submit comments via our online form. Alternatively, you may email your submission to: SSTScomments@aicpa-cima.com.

Questions for respondents

Please advise if your response is on behalf of a firm, business or other stakeholder or whether it represents your individual views. Additionally, include what your role and title is, details of your firm or organization size and details about your processes and procedures.

ITC1. How do you define quality management in tax? Please be as specific as possible.

ITC2. What role do you think the AICPA should undertake regarding quality management in tax? Please explain your rationale.

ITC3. To preserve the ability to self-regulate, do you believe the AICPA should consider quality management in tax for potential inclusion in future SSTSs? If "no," how should quality management in tax be addressed? Please provide your reasoning.

ITC4. How do you currently approach and ensure adherence to quality management within your tax function?

- What challenges do you experience?
- What type of application material would be helpful from the AICPA?

Contributors

The TEC promulgates the SSTSs and their interpretations. The Tax Practice Responsibilities Committee and SSTS Revision Task Force report to the TEC and were responsible for the overall project.

Below lists the members of the TEC, Tax Practice Responsibilities Committee and SSTS Revision Task Force at the time of this exposure.

Acknowledgment is also due to the many members who have devoted their time and efforts over the years to developing and revising the AICPA's standards.

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