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Dear Ms. Hazel:

On behalf of the Tennessee Department of Audit, Division of State Audit, we thank you for the opportunity to comment on the PEEC Exposure Draft (ED), *Proposed Revised Definitions of Client and Attest Client As Well As Related Definitions, and Other Guidance*. We generally agree with the amendments proposed in the ED.

Our responses to the issue for consideration and other comments are as follows:

Issue 1

We agree with the committee that the inclusion in the “Attest Client” definition of the requirement to comply with the “Integrity and Objectivity Rule” and its interpretations is the correct location to minimize a member overlooking this requirement because it will appear each time the definition is viewed.

General Comments:

For ¶1.224.020 (page 13), we believe the last sentence needs to clarify the conclusion that the covered member and the covered member’s immediate family would not be considered “employed” by the primary government. We agree with the government auditor exception in part 1 (1.000.02) but are not quite sure how this conclusion fits within the logic in the part 1 requirement.

In regard to ¶1.400.200 (page 15), we believe the ¶.01d examples including adjusting, closing, combining, or consolidating journal entries that are member-prepared records, not from client records or the client explicitly agreeing to take responsibility), create a potential independence impairment based on similar guidance in the generally accepted government

auditing standards (GAGAS or the GAO Yellow Book). We suggest providing similar guidance as in the Yellow Book.

On page 17 (last sentence of ¶2), the guidance indicates there is a “presumption” there would be an agreement between the engaging party and the subject entity. That might be the case, but verification also should be part of the equation.

For 1.290.010 ¶.07 (page 21), the materiality concept appears limited to the covered member’s firm or the attest client. However, there is not mention about materiality to the attest client engagement. Should engagement materiality also be included in this actual or threatened litigation section? In addition, we assume “disputes” is referring to litigation filed by either the firm or client. Was that the intended interpretation? For ¶.11, what is meant by “other” attest clients? In addition, we believe the paragraph would be clearer if reworded as follows: “If only the underwriter, officers, or directors of the covered member’s other attest clients file cross-claims against the covered member,…”

In regard to 1.295.040 ¶.02 (page 21), the rule discusses the “attest client-member relationship.” We suggest that attest client-member engagement is more appropriate.

For 1.295.120 ¶.01a (page 21), we suggest the following modification: “... determined or approved the **transaction details** and account classifications...” For ¶.01c, the new GAO Yellow Book exposure draft defines preparing financial statements based on information in the attest client’s trial balance as a significant threat. We believe this might create an unnecessary inconsistency in the frameworks.

For 1.295.140 ¶.02 (page 22), we suggest replacing the phrase “with respect to which” to “for whom” throughout the proposed amendments. The current proposed phrase results in an awkward sentence.

In regard to 1.295.150 ¶.10 (page 22), we have serious concerns with allowing members to perform internal audit functions and then also performing the attest engagement, especially if management can control the results of the internal audit services performed for the client (e.g., demand findings are not written).

For 1.510.040 – 1.520.050 (pages 23-24), we believe it would be difficult for members to perform these services without impacting independence. At the very least, we do not believe government auditors should perform these services and likely would not to begin with. These types of services appear to open the door to audit failures of the past when the lines between audit and non-audit services (and resultant revenues) led to independence failures. We believe any safeguards allowed should establish a high threshold to meet.

Should you have questions or need clarification on any of our comments, please contact Gerry Boaz (615) 747-5262 (Gerry.Boaz@cot.tn.gov) or me at (615) 747-5251.

Sincerely,

Deborah V. Loveless, CPA
Director, Division of State Audit