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Ethically Speaking

U.S. Government

Accountability Office (GAO)

The AICPA issued a [comment letter](#) responding to the proposals contained in the [August 2010 GAO Exposure Draft](#).

The division prepared a [comparative analysis](#) of the AICPA's and IESBA's independence rules to the August 2010 GAO exposure draft to assist members in understanding the proposal.

The GAO received more than 80 comment letters on the exposure draft and expects to have an Advisory Council meeting on May 11, 2011. Should all go as planned; the Yellow Book will be finalized in June 2011 but will likely not be effective until periods beginning after December 15, 2012, which would coincide with the ASB's clarity project. Based on the comments received, the final standards will likely differ in some respects from the exposure draft.

Ethical Tax Standards

An [exposure draft](#) has been released with respect to proposed revisions to Statements on Standards for Tax Services (SSTS) Interpretation Nos. 1-1 and 1-2. The interpretations are being revised to reflect revisions made to SSTS No. 1, *Tax Return Positions* (AICPA, *Professional Standards*, TS sec. 100), which became effective January 1, 2010, and to provide members with additional guidance on the application of SSTS No. 1.

A preface to the revised interpretations provides an overview of the most common tax return reporting standards and issues to be considered in determining if the applicable reporting standards and disclosure requirements have been satisfied.

The revised Interpretation No. 1-1, "Reporting and Disclosure Standards," contains illustrations

Ethically Speaking

Exposure Drafts

The Ethics Division has two exposure drafts outstanding. The exposure draft dated [February 28, 2011](#), contains a number of proposals that affect *members in the practice of public accounting*, and the exposure draft dated [April 4, 2011](#), contains one proposal that affects *all members* and three proposals that affect *members in business and industry*. Comments are requested by May 31, 2011, and June 5, 2011, respectively.

Members in Business and Industry

The first of the three proposals in the [April 4, 2011](#), exposure draft that affects members in business and industry is a proposed definition of a member in business and industry. The definition specifies that these members would include members employed or engaged on a contractual or volunteer basis in an executive, a staff, or an administrative capacity in such areas as industry, the public sector, education, the not-for-profit sector, regulatory bodies, or professional bodies.

The next is proposed Interpretation No. 501-10, "Financial Interests" This interpretation addresses threats to integrity and objectivity that a member in business and industry may face due to the member or his or her family member's financial interest in, or other relationship with, the employer. The proposed interpretation is not intended to create new requirements or bar members in business and industry from having financial interests in an employer but, rather, to provide guidance to members in business and industry on evaluating potential threats to their integrity and objectivity and applying appropriate safeguards, when necessary.

The other proposed interpretation is Interpretation No. 501-11, "False, Misleading, or Deceptive Acts in Promoting or Marketing Professional Services," which addresses false, misleading, or deceptive claims that a member in business and industry may make about the member's qualifications. The interpretation states that a member in business and industry would be considered to have committed an act discreditable if the member promotes or markets his or her abilities to provide professional services or makes claims about his or her experience or qualifications in a manner that is false, misleading, or deceptive.

All Members

The [April 4, 2011](#), exposure draft also contains a proposed interpretation that is applicable to all members. Specifically, proposed Interpretation No. 501-9, "Confidential Information Obtained From Employment," provides guidance to all members on maintaining confidentiality of an employer's confidential information and, therefore, would apply to a member in public practice relative to confidential information of their firm. The proposed interpretation states that a member would be considered to have committed an act discreditable if the member uses any confidential information acquired as a result of employment relationships without the proper authority or specific consent of the employer, unless a legal or professional responsibility exists to use or disclose such information.

Members in the Practice of Public Accounting**Client Affiliates**

The [February 28, 2011](#), exposure draft contains proposed interpretation No. 101-18 "Application of the Independence Rules to Affiliates." The proposed new interpretation provides guidance on when and how the independence requirements should be applied to interests and relationships that a member and firm have with entities that are affiliated with an attest client. Current guidance concerning application of the independence requirements to entities that are affiliated with an attest client is limited, and the Ethics Division receives a significant number of inquiries on this topic.

The Professional Ethics Executive Committee (PEEC) proposes that the independence requirements should be applied to interests and relationships that a member and firm have with affiliates of a *financial statement attest client*, a term defined in this interpretation. For all other attest clients, PEEC believes that a threats and safeguards approach is appropriate to determine when a relationship with an entity affiliated with such attest client poses an independence threat.

The proposed interpretation identifies 10 types of entities that should be considered affiliates of a financial statement attest client. These affiliates can be broken up into two main groups: traditional entities, such as subsidiaries and parents, and nontraditional entities, such as unregistered investment companies and benefit plan sponsors. The proposed interpretation requires that when a client is a financial statement attest client, members should apply to its affiliates the independence provisions of the AICPA code that are applicable to the financial statement attest client. However the proposal contains four exceptions to this requirement.

regarding the determination of which standards apply, as well as illustrations of whether the realistic possibility of success and reasonable basis standards have been satisfied. The revised Interpretation No. 1-2, "Tax Planning," includes references to nonsigning preparers and clarifications to the illustrations. Also, numerous language clarifications are reflected in these two revised interpretations. Comments on the exposure draft are due by May 15, 2011, and can be submitted at SSTComments@aicpa.org.

Ethics Hotline

The AICPA Ethics Hotline provides non-authoritative guidance to members on questions related to ethics, including independence. Each year, staff members respond to more than 4,000 inquiries. The Ethics Hotline is open from 9 a.m. to 5 p.m. ET on weekdays. A staff member can be reached via email at ethics@aicpa.org or via phone at (888) 777-7077, option 5 followed by option 2.

Other Resources

The [Ethics Division Website](#) has been redesigned and new content is added regularly. Information regarding the activities of the Professional Ethics Executive Committee can be found under [Community](#) and numerous tools and aids issued by the division or others can be found under [Resources](#). Articles, past copies of this newsletter, recently issued division documents and disciplinary reports can be found under [News and Publications](#).

The [2010-2011 Ethics Risk Alert](#) is now available. This publication focuses on recent developments in independence and ethics for accountants and auditors.

Two review tools are available to assist members in achieving compliance with the AICPA, U.S., SEC, and the Public Company Accounting Oversight Board (PCAOB) and GAO independence rules.

- [Independence Compliance: Checklists and Tools for Complying With AICPA, SEC, and PCAOB Independence Requirements](#)
- [Independence Compliance: Checklists and Tools for Complying With AICPA and GAO Independence Requirements, Second Edition](#)

From an international converging perspective, the proposal goes beyond the International Ethics Standards Board for Accountant's (IESBA's) related entity requirements for private entities that only extend to entities over which an audit or review client has direct or indirect control. PEEC believed it was appropriate to provide guidance beyond that provided by the IESBA because of the diverse and sometimes complex organizational structures that exist in the United States. The proposed interpretation also extends the independence requirements for clients whose financial statements are compiled by a member when the member's compilation report does not disclose a lack of independence.

Interpretation No. 101-3: Establishing or Maintaining Internal Control

The [February 28, 2011](#), exposure draft also contains a revision to interpretation 101-3, "Performance of Nonattest Services," under Rule 101, *Independence* (AICPA, *Professional Standards*, ET sec. 101 par. .05). One of the proposed revisions to this interpretation relates to a general activity that would impair a member's independence: establishing or maintaining internal controls, including performing ongoing monitoring activities for a client. PEEC recognized that an inconsistency existed within the current interpretation in that certain bookkeeping and other nonattest services permitted under the interpretation could be viewed as maintaining internal controls for the client and, as such, may appear to be prohibited by the general activity.

Because it was never PEEC's intent to have the permitted activities listed in the interpretation be considered as impairing independence, PEEC agreed to revise the general activity to state, "Accepting responsibility for designing, implementing or maintaining internal control." PEEC believes that the phrase *designing and implementing* is not only clearer than *establishing* but is more reflective of the language used in the professional standards (for example, auditing standards) and the *Code of Ethics for Professional Accountants* (Code) issued by the IESBA. The addition of the phrase *accepting responsibility* for is intended to clarify that practitioners are able to assist their clients by performing services to design, implement, or maintain certain aspects of internal control when management accepts responsibility for such services, and the other general requirements of the interpretation are met.

In addition, the proposal replaces the term *management functions* with *management responsibilities* because PEEC believes that it is clearer, and PEEC proposes certain revisions to reflect this change, such as incorporating a description of the term *management responsibilities*, as well as additional examples of management responsibilities.

One proposed revision to the interpretation may be viewed as more restrictive. Specifically, PEEC is proposing to include a requirement that members evaluate the significance of the management participation threat created by performing separate evaluations on the client's internal control system. PEEC believes that an inconsistency in the interpretation exists by prohibiting a member from performing ongoing monitoring procedures for a client while permitting separate evaluations because, depending on the scope or extent of the controls being tested and the frequency of the separate evaluations, the member may be performing services equivalent to ongoing monitoring procedures. Accordingly, PEEC is proposing that the significance of the threat created by performing separate evaluations should be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level.

Confidential Client Information

The [February 28, 2011](#), exposure draft contains a proposed definition of *confidential client information* that is substantially the same as that exposed in the [September 2009 exposure draft](#). The proposed definition explains that *confidential client information* is information that is not known to be in the public domain or available to the public. The definition provides examples of information that would not be considered confidential because it would be considered to be in the public domain or available to the public (for example, information obtained from commercially available databases).

The exposure draft also contains an updated proposed revision to a related ethics ruling. The ruling requires that a member obtain the client's written consent before disclosing confidential client information to a third party or using such information for the member's own purposes when such information results in disclosure to others.

To facilitate members' and other users' understanding of the revised proposals, PEEC developed a table that summarizes and provides examples of (a) three categories of information that a member may be asked to provide to third parties or that the member may wish to use for his or her own purposes and (b) how to handle such information. These categories are: (1) client information that is in the public domain, (2) client information not in the public domain, and (3) other information in the member's possession. Although this table is not authoritative guidance (that is, not an enforceable standard), it is included in the exposure draft and would be posted on the division's website with other nonauthoritative guidance issued by the division.

Other Proposals

The [February 28, 2011](#), exposure draft also contains a number of other proposals, including (1) a new interpretation that would permit certain

Future Meetings

May 12-13, 2011
August 4-5, 2011
November 2-3, 2011

Interested parties are encouraged to attend the open meetings in person. Furthermore, the Professional Ethics Division maintains an open phone line so that interested parties can observe the PEEC's public meetings via telephone. Anyone interested in attending a meeting in person or via conference call should contact Ellen Gorla at egoria@aicpa.org.

- [Agenda](#) materials are available online approximately one week before the meeting.
- [Minutes](#) of past meetings are also available online.

individuals to be employed as an adjunct faculty member of a client educational institution, provided that certain safeguards are met; (2) a clarified definition of *public interest entities*; (3) a proposed revision to an interpretation that would allow members to apply a modified approach to independence to all SSAE engagements that require independence or when the compilation report does not disclose a lack of independence; and (4) a provision that would recognize the IESBA Code as a minimum standard in certain circumstances.

Ethics Codification

PEEC continues to make progress on its codification of the AICPA ethics standards. The primary focus of this initiative is to improve the AICPA Code, so that members and others can apply the rules and reach the right conclusions more easily. To achieve this, PEEC will restructure the Code into topical areas, edit the Code using consistent drafting and style conventions, and revise certain provisions (primarily independence) to reflect the conceptual framework approach.

A conceptual framework helps members comply with certain ethics requirements. For example, ET section 100-1, [Conceptual Framework for AICPA Independence Standards](#) (AICPA, *Professional Standards*), defines several concepts and terms (for example, *independence*, *threat*, *safeguard*, *acceptable level*) and provides examples of different types of threats and safeguards. A member may identify a threat to his or her compliance with the independence standard and, using the framework, evaluate the threat and determine whether safeguards could be applied to eliminate or reduce the threat to an acceptable level.

Revising or recasting independence provisions to reflect the conceptual framework approach represents a significant change. PEEC believes that this will enhance understanding of the Code by providing additional context for the rules and guidance on the application of the framework. However, recasting will not change the substance of the existing rules by allowing members to apply judgment where none is permitted today. For example, if a covered member holds stock in an audit client, the only safeguard that would eliminate or sufficiently mitigate the financial self-interest threat to independence would be to eliminate the interest or cease being a covered member, which is the same requirement as under today's rule. Some rules in the Code, such as those for acts discreditable, false advertising, and confidentiality, will likely not lend themselves to a conceptual framework approach and not be recast. For those rules, PEEC will apply only drafting and style conventions.

Since initiation of the project, PEEC representatives have spoken to numerous groups, such as state board members and AICPA committees, to keep its constituents informed and obtain their input. Of particular concern are challenges that the state accountancy boards that incorporate by reference the AICPA ethics standards may face in updating their rules. Thus, PEEC assembled a State Board Advisory Group to act as a sounding board to PEEC as it develops the codification. That group comprises the following state board members and executive directors: Dan Sweetwood, executive director of the Nebraska Board of Public Accountancy; Susan Harris, executive director of the Mississippi State Board of Public Accountancy; Edith Steele, retired executive director of the Oklahoma Accountancy Board; Mark Crocker, executive director of the Tennessee State Board of Accountancy; Rona Shor Chernoff, member of the New York State Board of Public Accountancy; and Kent Bailey, member of the Oregon Board of Accountancy. Wes Williams, chairman of PEEC and Lisa Snyder, director, AICPA Professional Ethics Division spoke about the codification project at NASBA's 2011 Executive Directors Conference on March 7 in San Diego, and presentations will be made at the upcoming NASBA regional meetings.

The codification will also be pilot tested prior to exposure by a broad group of users, including state CPA society representatives, various regulators, and AICPA members.

If you have a question or comment about the codification project, please e-mail PEEC staff member Ellen Gorla at egoria@aicpa.org.

Other Projects

A task force has been charged with reviewing Interpretation No. 501-1, "Response to Requests by Clients and Former Clients for Records," under Rule 501, *Acts Discreditable* (AICPA, *Professional Standards*, ET sec. 501 par. .02), to consider whether additional guidance is needed with regard to electronic records and files and whether the provisions on withholding certain records due to unpaid client fees is still appropriate. In studying the issue, the task force will consider the rules of the state boards of accountancy, as well as Section 19 "Licensees' Working Papers; Clients' Records" of the *Uniform Accountancy Act*.

A complete list of the [projects](#) that PEEC plans to undertake during the next three years and a list of all PEEC [exposure drafts](#) are available online.

International Focus

At its February 2011 meeting, the IESBA discussed its proposed strategic plan. In addition to pursuing current projects on conflicts of interest and responding to fraud and illegal acts, the IESBA is considering a project to reassess its inadvertent violations guidance that currently exists in the IESBA Code. The IESBA also discussed not pursuing a project on independence and collective investment vehicles.

[Agenda materials and minutes](#) for past IESBA meetings are available on the

Faces of PEEC

Edwin A. Rommel, III, CPA



Ed joined PEEC in 2010 and is a partner and cofounder of Twilley, Rommel & Stephens, P.A., where he advises business and tax clients. While a member of PEEC, he is serving as a member of the Codification State Board Advisory Group and the Retention of Records Task Force. Ed graduated from Loyola College and, in addition to being a CPA, is a Certified Valuation Analyst (CVA) and Accredited in Business Valuation (ABV). Ed is an active member of the profession, having served as an elected member of the AICPA Council and

Member Advisory Panel, as well as the past president of the Maryland Association of CPAs (MACPA) and current member of MACPA's ethics committee. Ed is also a director of Bay National Bank and the chairman of its audit committee.

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