

Members in Small Local Accounting Firms

April 2004

AICPA

What CPAs Are Talking About: An Update on Jim Metzler's Listening Tour

In the Feb. issue, we interviewed James C. Metzler, CPA, the AICPA's new Vice President—Small Firm Interests. When he took office on Aug. 1 of last year, Metzler began a listening tour designed to help him learn more about small firm needs and how the AICPA can help address them. To his new position, Metzler brought 32 years of experience with the Buffalo, N.Y., CPA firm of Gaines, Metzler, Kriner and Company, along with three years spent coaching CPA firms as co-founder of Convergence Coaching LLC.

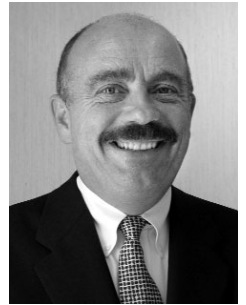
During his first few months on the job, Metzler has visited roughly 20 cities nationwide. This article will describe some of what he learned on this first leg of the listening tour and his insights into possible solutions.

Coping with New Standards

New and ever-more-complicated standards are an important concern for small firms and their clients. "The increasing complexity of accounting and auditing standards has become a big issue," Metzler says.

To make sure that financial statements remain relevant and practical for their clients, many smaller firms find themselves using other comprehensive bases of accounting or limited scope assurances. Although this is an imperfect solution, they are not necessarily eager for a new set of differentiated standards for private companies, Metzler says, because that would only add a new layer of requirements to learn. As one step in ensuring that these concerns are heard and addressed, Metzler is a member of the AICPA's new Special Task Force on Private Companies Financial Reporting, a group that is examining the challenges in this area. In his meetings with members around the country, "most CPAs who consider this an important issue were pleased to learn of this new AICPA task

force, which has appropriate small firm representation," he says. "After an extensive research effort, if the task force decides there's a problem, it's charged with defining it and proposing a solution on behalf of the profession."



AICPA Commitment to Small Firms

Metzler believes that the AICPA has shown its commitment to small firms in part by creating his job last summer. Another example is representation by small firm members on virtually every AICPA committee and task force, including those recently formed on private companies and the enhanced reporting model, and on the board of directors.

In his travels, Metzler discovered that many CPAs were unaware of all the AICPA has to offer them. "There are numerous deliverables offered by the AICPA aimed specifically at small firms," he says. "But many CPAs working in small firms are unaware of either the existence of these deliverables or of the recent emphasis on making certain their interests are well represented within the AICPA."

Strong communications is one way to remind CPAs of what the Institute is doing for them. "Through aggressive outreach I intend to make certain small firm AICPA members know they have powerful friends within the Institute and that a host of deliverables are available now that they will find useful." The deliverables he mentions include everything from small firm networking groups, to information on best practices culled from the MAP 2004 survey, to succession planning aids and niche practice

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opportunities. "I hope to help create a small firm catalog that pulls together all these available resources," he says.

The Listening Tour Continues

The biggest surprise he has encountered, Metzler says, has been this disconnect between perception and reality—between

what CPAs believe is being done for them at the Institute and what is actually available or under way. "I see my job as twofold. I intend to be an advocate for small firms at every conference table within the AICPA. I also want to make certain small firms are aware of the many deliverables already available that can have a posi-

tive impact on their practice."

To better inform CPAs about Institute initiatives—and to receive ongoing updates on their needs—Metzler plans to continue his listening tour indefinitely. He welcomes input from members. His e-mail address is:

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Navigating the General Requirements of the Nonattest Services Rules of the AICPA Code of Professional Conduct, Interpretation 101-3—Performance of Nonattest Services

Revisions to the AICPA rules that apply when nonattest services are provided to attest clients (Interpretation 101-3—*Performance of nonattest services*) became effective on Dec. 31, 2003.¹ The revised interpretation clarifies existing guidance with respect to bookkeeping and internal audit services, places further restrictions on valuation, appraisal and actuarial services and information systems design and development, and strengthens the general requirements of Interpretation 101-3 by requiring that a member² document his or her understanding with the client regarding the services to be performed. The revisions also reinforce the long-standing AICPA position that the member's attest client must designate a competent employee to oversee nonattest services provided by the member, including making all management decisions related to the services.

Some members, particularly those affiliated with smaller firms, have expressed concerns regarding the practical application of certain general requirements outlined in the Interpretation, such as whether the level of competence that the designated client employee should possess to be a "competent employee" (General Requirement No. 2b.) and effectively oversee the nonattest service should be equivalent to that of the member. This is not the case.

In meeting the competency requirement, it is not intended that the client employee possess a level of technical expertise commen-

surate with that of the member. Rather, the client employee should understand the nonattest services sufficiently to be able to understand the key issues involved, make any required management decisions and evaluate the adequacy of the resulting work product.

The requirement for a competent client employee to oversee the member's service was explicitly stated in the AICPA's previous version of Interpretation 101-3, which called for the client to be in a position to make an informed judgment on the results of the services and for the client designee to be "a management-level individual" and "be responsible for overseeing the services being provided." In addition, the requirement was implicit to the independence rule on internal audit assistance services (Interpretation 101-13—*Extended audit services*). The management oversight requirement was included in both the previous and current interpretations to ensure that the member does not perform management functions or make decisions on management's behalf.

In general, "oversight" is not intended to mean that client management must "supervise" the member in his or her day-to-day rendering of the service. Rather, the Interpretation contemplates that client management will agree to the nature and timing of the delivery of the service, provide general direction to the member regarding the tasks the member is asked to undertake, monitor the service as it progresses as appropriate, understand the key issues involved and make all management decisions related to the service.

However, the Interpretation does not preclude greater involvement with the service on the part of the designated client employee. The level of oversight could therefore go beyond what is contemplated by the Interpretation depending on the nature of the service and the designated client employee's level of understanding of the subject matter and perceived need to be more involved in the service in order to, for example, become better versed on the key

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¹ In order to provide members with additional time to update their firm policies and procedures and further educate firm personnel, the Professional Ethics Executive Committee (PEEC) has deferred until Dec. 31, 2004, the effective date of the new requirement in Interpretation 101-3 to *document in writing* the understanding that members have been required to establish with the attest client under Interpretation 101-3 since the late 1990s. The documentation requirement will apply to all nonattest services (e.g., bookkeeping, tax, consulting, internal audit services, etc.) performed for an attest client after Dec. 31, 2004, (i.e., nonattest services engagements in process at or commencing after Dec. 31, 2004). All other requirements of Interpretation 101-3 remain effective Dec. 31, 2003, subject to the transition provisions of the Interpretation.

² The term "member" means an individual who is a member of the AICPA. However, anyone who performs an audit of an entity's financial statements under U.S. generally accepted auditing standards would be required to be independent under the AICPA's independence rules (refer to AU Section 220). Accordingly, those individuals would be equivalent to a "member" for purposes of complying with Interpretation 101-3.

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issues and make the necessary decisions, evaluate the adequacy and results of the service and accept responsibility for its results.

Consider the analogy whereby a homeowner hires an electrician to install new electrical wiring in his or her home. The homeowner hires the electrician because he or she does not possess the necessary technical skills to perform the work him- or herself. However, the homeowner knows the result he or she is seeking and has been advised by the electrician regarding the key issues that will be involved in the rewiring job, including the requirements of the local building code and the tasks that are necessary to accomplish the desired result. When overseeing the service, the homeowner may then observe the electrician at work as appropriate, ask questions as the work progresses if they are important to ensure a continued understanding of the service and make all necessary decisions, and evaluate the finished work product. In the end, the homeowner's oversight of the work enables him or her to accept responsibility for the results of the service, even though he or she was unable to perform the actual wiring installation him- or herself.

A similar approach would be followed when a member provides permitted nonattest services to an attest client. For example, competent client employees are likely to be able to evaluate the adequacy and results of routine bookkeeping services and accept responsibility for those results by performing the level of oversight contemplated by the Interpretation. Accordingly, competent client employees might rely on providing general direction to the member upfront, monitoring the service as it progresses, understanding and approving proposed journal entries and making management decisions as needed. The member, on the other hand, could ensure compliance with the requirements of the rules by reviewing the proposed journal entries with client management and explaining how each entry (in general terms) affects the financial statements. The client should then be in a position to approve the journal entries and accept responsibility for the financial statements.

For more complex engagements, however, some clients may want a more active role in the service to ensure that they understand the key issues involved and can effectively carry out their oversight responsibilities. This may be the case in the preparation of tax returns. The client may perceive a greater need to be more extensively involved in overseeing the preparation of a complicated tax return than would be necessary if the return were routine and uncomplicated. In either instance, the client employee would need to review the tax return, understand the company's tax situation, understand how the amounts were determined, make decisions regarding tax positions taken in the return and conduct sufficient oversight to be able to evaluate and accept responsibility for the results of the service. In addition, if the member were required to make adjustments to the client's financial information to prepare the returns (such as cash to accrual adjustments in a small company environment), the member would need to perform procedures similar to those discussed above for bookkeeping services.

Although the assessment of client competency can be difficult, the AICPA's Professional Ethics Executive Committee believes that members are capable of making such an assessment and do so already in meeting other requirements of generally accepted auditing standards (e.g., assessing the competency of a specialist brought in to assist in an audit engagement).

In some situations, however, the member may conclude that

For more information...

The AICPA *Code of Professional Conduct* is available at:



www.aicpa.org/about/code/index.htm

A PDF version of Interpretation 101-3—*Performance of nonattest services* can be viewed at:



www.aicpa.org/download/ethics/interp_revisions_Sept03.pdf

Members and other interested parties who need additional guidance on the rules can call the AICPA Ethics Hotline at 888/777-7077 (menu option 5, followed by option 2) or contact the ethics division by e-mail at ethics@aicpa.org. Additionally, members and other interested parties are encouraged to review the following documents available on our Web site which will explain the concepts underlying the rules and provide more detailed guidance:

1. **Background and Basis for Conclusions**, dated: Dec. 31, 2003. Explains the revisions to Interpretation 101-3 and the rationale behind the new rules and offers insight into comments received and the deliberations that took place prior to the rules' adoption.



www.aicpa.org/members/div/ethics/index/bfc1.htm

2. **A Conceptual Framework for AICPA Independence Standards**, dated: Jan. 22, 2004. Describes the risk-based approach to analyzing independence matters as used by the Professional Ethics Executive Committee of the AICPA.



www.aicpa.org/download/ethics/AICPA_Draft_Conceptual_Framework_FINAL.pdf

3. **AICPA Plain English Guide to Independence**, updated Jan. 1, 2004. This guide is designed to assist in understanding the independence requirements under the AICPA *Code of Professional Conduct* and, if applicable, other rule-making and standard-setting bodies.



www.aicpa.org/download/ethics/plainenglish.doc

the client is unable (or perhaps unwilling) to oversee the nonattest services and evaluate the adequacy and results of the services performed. In such instances, the Interpretation makes it clear that the member would be unable to perform both attest and nonattest services. Accordingly, the client would need to determine in which capacity it wanted the member to function; as an attest service provider or as a nonattest service provider. The member would be permitted to assist the client in an assessment of their needs, which would allow the client to make an informed decision.

For example, if the member believes the client is best served by having available timely and accurate financial statements, the member may recommend the client engage him or her to provide nonattest services that do not comply with the general requirements of the Interpretation, at which point the member would be limited to issuing a compilation report on the client's financial statements that discloses his or her lack of independence and the client would need to engage another accounting firm to perform the attest

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engagement. On the other hand, if the member's performance of the audit or review is of paramount importance to the client, the member should recommend the client hire another service provider to perform the required bookkeeping (or other nonattest) service.

As our profession enters a new era of scrutiny by the public and regulators, it is imperative that we, as CPAs, remain mindful of

our responsibilities to both our clients and the public, and take all steps necessary to maintain our independence when performing nonattest services for attest clients. By remaining faithful to our dual responsibilities, while following the provisions of Interpretation 101-3, we will continue to live up to the high standards we have traditionally set for ourselves.

Resources, CPE Products on Fraud Prevention and Detection

An important tool for members is the **AICPA Antifraud and Corporate Responsibility Resource Center**, an online resource devoted to the prevention, detection and investigation of fraud (www.aicpa.org/antifraud).

Here are other helpful products and CPE courses pertaining to fraud.

SAS No. 99: Consideration of Fraud in a Financial Statement Audit (No. 060701CPA04). Price: \$15 member/\$18.75 non-member.

Corporate Ethics for Financial Managers: Navigating with Case Studies and Practical Solutions (No. 029880CPA04). A series of nine case studies that illustrate real-world ethical dilemmas and application of values consistent with the high standards of the profession. Price: \$49 member/\$61.25 non-member.

Financial Reporting Fraud: A Practical Guide to Detection and Internal Control (No. 029879CPA04). This guide provides illustrations and examples of fraud concepts in addition to referencing research findings and authoritative literature. Price: \$49 member/\$61.25 non-member.

now available

Revenue Recognition: Guidance, Implementation, and Fraud Concerns (No. 181200CPA04) provides guidance in identifying the differences between aggressive accounting and financial fraud and the point at which aggressive accounting practices become fraudulent. Prerequisite: Basic knowledge of accounting principles related to revenue recognition. Recommended CPE credit: 6. Level: Intermediate; Format: 100-min. VHS tape/manual. Price:

\$128 member/\$160 non-member.

Fraud Detection in a GAAS Audit—SAS No. 99 Implementation Guide (No. 006613CPA04) provides detailed information, examples and best practices for implementing SAS No. 99. Price: \$69 member/\$86.25 non-member.

Fraud and the Financial Statement Audit: Auditor Responsibilities Under New SAS (No. 731811CPA04, text; No. 181811CPA04, videocourse; No. 181820CPA04, DVD). Recognize how the new fraud standard differs from the prior standard and the effect on your audit experience. Prerequisite: None. Estimated CPE Credit: 8, text; 9, videocourse. Level: Intermediate. Format: Text or 120-min VHS tape/manual. Price: \$119 member/\$148.75 non-member, text; \$148.80/\$186, videocourse. Recommended CPE Credit: 9; Format: 135-min. DVD/manual. Price: \$149 member/\$186.25 non-member.

Fraud and the CPA (No. 731730HSCPA04). This interactive self-study course from the AICPA and the Association of Certified Fraud Examiners will help CPAs deepen their fraud knowledge, enhance professional skepticism and improve decision processes. Prerequisite: None. Estimated CPE Credit: 8. Level: Basic. Format: CD-ROM. Price: \$119 member/\$148.75 non-member.

The CPA's Handbook of Fraud and Commercial Crime Prevention (No. 056504CPA04) is designed to help CPAs manage the risk of fraud. Price: \$180 member/\$225 non-member.

How Fraud Hurts You and Your Organization is a free one-hour corporate governance training program developed by the AICPA and the Association of Certified Fraud Examiners. View the program from www.aicpa.org/antifraud. Or, order the program on CD-ROM (No. 056513HSCPA04; \$8 shipping & handling fee for first copy applies).

To order, write: AICPA Service Center, CPA04, Harborside Financial Center, 201 Plaza Three, P.O. Box 2209, Jersey City, N.J. 07303-2209; fax 800/362-5066; call 888/777-7077 (8:00 a.m. to 8:00 p.m., ET); shop online at www.cpa2biz.com/store; or e-mail service@aicpa.org. Orders totaling \$300 or less must be prepaid by check or credit card. Prices do not include shipping and handling, or sales tax if applicable. Have membership number ready.



IRS Tax Forums

The IRS Nationwide Tax Forums offer updates from the IRS on tax law, compliance and tax practice and procedure. The offerings include seminar presentations and workshops, as well as focus groups with subjects from ethics and professional conduct to how to enroll and participate in e-file and the new e-services. Those in attendance include representatives from software vendors, tax service providers and professional associations.

Locations for the 2004 forums include:

- Atlantic City, N.J., July 6-8.
- Orlando, July 20-22.
- Minneapolis, Aug. 3-5.
- New Orleans, Aug. 17-19.
- San Antonio, Tex., Aug. 31-Sept. 2.
- Las Vegas, Sept. 14-16.

For more information:



www.irs.gov/taxpros/article/0,,id=97192,00.html