



**AICPA Interpretation 101-3, *Performance of Nonattest Services*
Requirement to Document Understanding With an Attest Client**

In September 2003, the AICPA’s Professional Ethics Executive Committee (PEEC) issued revisions to Interpretation 101-3 to ensure its continued effectiveness in promoting independence when a member renders nonattest services to an attest client¹. The new rules became effective for new engagements on January 1, 2004.

One of the requirements of the new rules is that, prior to performing nonattest services for an attest client, the member should establish and *document in writing* his or her understanding with the client regarding the:

- Objectives of the engagement
- Services to be performed
- Client's acceptance of its responsibilities
- Member's responsibilities; and
- Any limitations of the engagement

To provide members with additional time to update their firm policies and procedures and further educate firm personnel, the Committee deferred the effective date of the new documentation requirement until January 1, 2005. Accordingly, the documentation requirement is effective for any nonattest services performed for an attest client on or after January 1, 2005, including services already in progress at that date.

What clients are affected by the documentation requirement?

The documentation requirement applies to any nonattest services (e.g., bookkeeping, tax or consulting services) performed by the member for an attest client. For purposes of this rule, an “attest client” is any client for which the member performs any service for which independence is required. Accordingly, for purposes of this rule, a client for which a member performs a compilation, would

¹ Other regulators may have more restrictive rules regarding independence when performing nonattest services for an attest client. Accordingly the member should be aware of and comply with all rules and regulations applicable to specific clients.



only be considered an attest client if the member's compilation report does not disclose a lack of independence.

In cases where a member only provides nonattest services to a client, the general requirements of the interpretation, including the documentation requirement, are not effective until the client becomes an attest client. For example, if a member provides only tax planning and bookkeeping services for a client and is subsequently asked to perform a review of the client's financial statements, that member could perform such services if, upon acceptance of the review engagement, he or she prepares the required documentation and can demonstrate that he or she has complied with the other general requirements of the interpretation during the period covered by the financial statements, including the requirement to *establish* an understanding with the client regarding the matters identified above.

What form of documentation is required?

While the rule requires that the understanding with the client must be in writing, the form of documentation is left to the member's discretion. The method of documentation is not as important as the content of the documentation. For example, if the member performs a consulting engagement for an audit client, the member may decide to document the required elements with respect to the consulting engagement in the audit engagement letter, but the understanding could also be documented, for example, in a separate engagement letter specific to the consulting service engagement, in a memo to the audit files, or in a checklist that the member completes as part of the audit. If a client engages the member to perform tax services, the understanding could be documented in a tax organizer or in a memo contained in the tax working papers. Other methods of documentation such as a memo of understanding maintained in the member's billing or correspondence files (i.e., separate from the client work paper files) would also satisfy this requirement. Illustrative sample language that can be incorporated into an audit, review or compilation engagement letter, a "stand alone" nonattest services engagement letter, a tax organizer letter, or other documentation method preferred by the member is provided below.

Are there any activities that are excluded from the documentation requirement?

The documentation requirement does not apply to routine activities performed by the member, such as providing advice and responding to the client's technical questions as part of the normal client-member



relationship.

Would independence be impaired where a member fails to document the understanding with the client?

No. A failure to prepare the required documentation would not impair the member's independence provided the understanding with the client had been established. However, the failure to document the understanding with the client would be considered a violation of Rule 202 – *Compliance With Standards* [ET section 202].

General requirements no. 2 and no. 3 under Interpretation 101-3 do not apply to certain routine activities performed by the member. What are considered to be routine activities for purposes of the Interpretation?

Whether an activity is routine should be determined considering all of the facts and circumstances surrounding the activity. Routine activities generally involve providing advice or assistance to the client on an informal basis as part of the normal client-member relationship. Routine activities typically are insignificant in terms of time incurred or resources expended and generally do not result in a specific project or engagement or in the member producing a formal report or other formal work product. Examples of routine activities may include:

- Providing advice to the client on an accounting matter as an ancillary part of the overall attest engagement;
- Researching and responding to the client's technical questions on relevant tax laws as an ancillary part of providing tax services;
- Providing advice to the client on routine business matters;
- Educating the client on matters within the technical expertise of the member; and
- Providing information that is readily available to the member, such as best practices and benchmarking studies to the client.

**SAMPLE LANGUAGE TO DOCUMENT UNDERSTANDING WITH CLIENT FOR
THE PROVISION OF BOOKKEEPING AND TAX SERVICES
[For Illustrative Purposes Only]**



Objectives of the Engagement and Services to be Performed

We provide the bookkeeping and tax services outlined below.

At the end of each month, CPA Firm agrees to perform the following functions:

- Post coded transactions to ABC Co.'s general ledger
- Propose adjusting or correcting journal entries to be reviewed and approved by ABC Co.
- Prepare a trial balance based on the adjusted general ledger
- Prepare monthly sales and payroll tax returns [insert applicable tax jurisdictions]

At the end of the year, CPA Firm agrees to perform the following functions:

- Propose adjusting or correcting journal entries to be reviewed and approved by ABC Co.
- Prepare federal and state income tax returns [insert applicable tax jurisdictions]
- Prepare year-end sales and payroll tax returns [insert applicable tax jurisdictions]
- Answer inquiries on specific tax matters

CPA Firm will not perform management functions or make management decisions on behalf of ABC Co. However, we will provide advice and recommendations to assist management of ABC Co. in performing its functions and making decisions.

ABC Co.'s Responsibilities

ABC Co. agrees to perform the following functions in connection with CPA Firm's provision of the bookkeeping and tax services:

- Make all management decisions and perform all management functions, including determining account codings and approving all proposed journal entries;
- Assign [name of competent client employee] to oversee the bookkeeping and tax services and evaluate the adequacy and results of the services;
- Accept responsibility for the results of the bookkeeping and tax services, including the journal entries, general ledger, trial balance, and tax returns; and
- Establish and maintain internal controls over the bookkeeping and tax return preparation

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processes.

CPA Firm's Responsibilities and Limitations of the Engagement

CPA Firm will perform the services in accordance with applicable professional standards, including the Statements on Standards for Tax Services issued by the American Institute of Certified Public Accountants.

This engagement is limited to the bookkeeping and tax services outlined above. CPA Firm, in its sole professional judgment, reserves the right to refuse to do any procedure or take any action that could be construed as making management decisions or performing management functions, including determining account codings and approving journal entries. CPA Firm will advise ABC Co. with regard to tax positions taken in the preparation of the tax return, but ABC Co. must make all decisions with regard to those matters.

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