
EXPOSURE DRAFT

OMNIBUS PROPOSAL

AICPA PROFESSIONAL ETHICS DIVISION

INTERPRETATIONS AND RULINGS

August 13, 2012

Comments are requested by September 14, 2012

Prepared by the AICPA Professional Ethics Executive Committee for comments from persons interested in independence, behavioral, and technical standards matters.

Comments should be addressed to Lisa A. Snyder, director of the Professional Ethics Division, at lsnyder@aicpa.org.

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August 13, 2012

This exposure draft contains important proposals for review and comment by the AICPA's membership and other interested parties regarding pronouncements for possible adoption by the Professional Ethics Executive Committee (PEEC). The text and an explanation of the proposed pronouncements are included in this exposure draft.

After the exposure period is concluded, and PEEC has evaluated the comments, PEEC may decide to publish one or more of the proposed pronouncements. Once published, the pronouncements become effective on the last day of the month in which they are published in the *Journal of Accountancy*, except if otherwise stated in the pronouncements.

Your comments are an important part of the standard-setting process; please take this opportunity to comment. Responses must be received at the AICPA by September 14, 2012. All written replies to this exposure draft will become part of the public record of the AICPA.

All comments received will be considered by PEEC at its next open meeting.

Please send comments to Lisa A. Snyder, director of the Professional Ethics Division, via e-mail at lsnyder@aicpa.org.

Sincerely,

Wes Williams, *Chair*
AICPA Professional Ethics Executive Committee

Lisa A. Snyder, *Director*
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Explanation for Reestablishment of Client Affiliate Related Guidance Under Rule 101

The Professional Ethics Executive Committee (PEEC) adopted Interpretation No. 101-18, “Application of the Independence Rules to Affiliates,” under Rule 101, *Independence* (AICPA, *Professional Standards*, ET sec. 101 par. .20), at its August 2011 meeting. In order to allow members adequate time to implement this guidance, PEEC approved a delayed effective date of January 1, 2014, but allowed for early adoption.

Also, at the August 2011 meeting, PEEC voted to delete a number of ethics rulings and Interpretation No. 101-8, “Effect on Independence of Financial Interests in Nonclients Having Investor or Investee Relationships With a Covered Member’s Client,” because PEEC believed adequate guidance would exist in either Interpretation No. 101-18 (once effective or implemented) or ET section 100-1, *Conceptual Framework for AICPA Independence Standards* (AICPA, *Professional Standards*).

Because Interpretation No. 101-18 could be implemented early by members, the interpretation was added to the Code of Professional Conduct (AICPA Code) effective November 30, 2011. On the same date, the deleted ethics rulings and Interpretation No. 101-8 were deleted from the AICPA Code.

PEEC has become aware that by deleting the ethics rulings and Interpretation No. 101-8, some members believed they did not have adequate guidance if they chose not to early implement the new interpretation, and this caused some members to spend more time analyzing situations under ET section 100-1 than if the deleted material was still available for use in applicable situations prior to adoption of Interpretation No. 101-18.

To alleviate these issues and provide guidance to members during this transition period, PEEC is proposing that the deleted ethics rulings providing client affiliate related guidance and Interpretation No. 101-8 be reestablished effective October 31, 2012, and remain effective until the earlier of

- January 1, 2014, the effective date of Interpretation 101-18, or
- the date of adoption of Interpretation No. 101-18 by a member who adopts Interpretation No. 101-18 early as permitted.

The guidance being exposed for reestablishment is

- Interpretation No. 101-8.
- Ethics Ruling No. 21, “Member as Director and Auditor of an Entity’s Profit Sharing and Retirement Trust,” of ET section 191, *Ethics Rulings on Independence, Integrity, and Objectivity*.
- Ethics Ruling No. 38, “Member as Co-Fiduciary With Client Bank,” of ET section 191.
- Ethics Ruling No. 60, “Employee Benefit Plans—Member’s Relationships With Participating Employer,” of ET section 191.

- Ethics Ruling No. 69, “Investment With a General Partner,” of ET section 191.
- Ethics Ruling No. 81, “Member’s Investment in a Limited Partnership,” of ET section 191.
- Ethics Ruling No. 98, “Member’s Loan From a Nonclient Subsidiary or Parent of an Attest Client,” of ET section 191.
- Ethics Ruling No. 106, “Member Has Significant Influence Over an Entity That Has Significant Influence Over a Client,” of ET section 191.
- Ethics Ruling No. 111, “Employee Benefit Plan Sponsored by Client,” of ET section 191.

The guidance, once reestablished, could not be applied by a member once Interpretation No. 101-18 is adopted by the member or member’s firm and would be deleted from the AICPA Code effective January 1, 2014.

Text of Proposed Reestablishment of Interpretation No. 101-8 Under Rule 101

(Additions appear in **boldface italic**, and deletions are ~~stricken~~.)

101-8 Effect on Independence of Financial Interests in Nonclients Having Investor or Investee Relationships With a Covered Member's Client

Introduction

Financial interests in nonclients that are related in various ways to a client may impair independence. Situations in which the nonclient investor is a partnership are covered in other rulings [ET section 191.138–.139 and .162–.163].

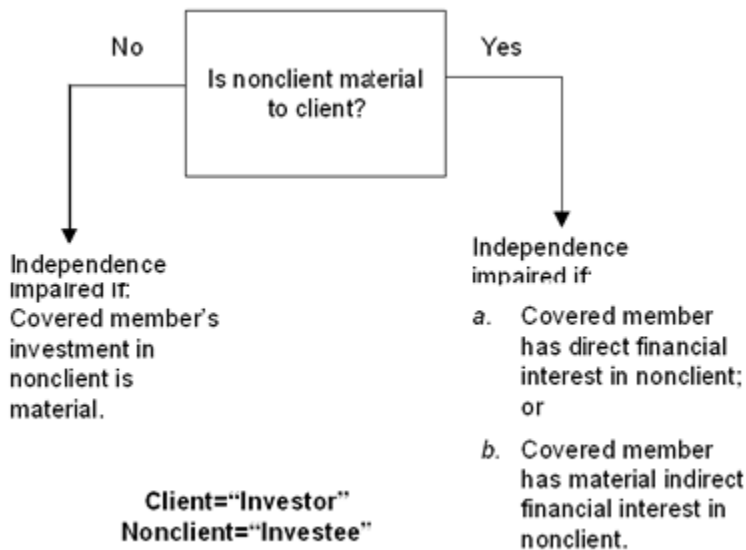
Terminology

The following specifically identified terms are used in this interpretation as indicated:

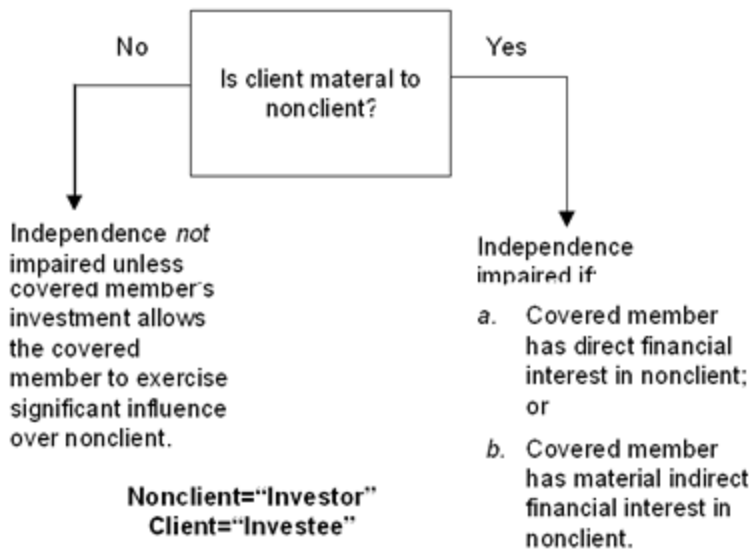
1. *Client*. The term *client* means the person or entity with whose financial statements a covered member is associated.
2. *Significant ~~influence~~*. The term *significant influence* is as defined in ~~FASB~~**Financial Accounting Standards Board ASC**Accounting Standards Codification 323-10-15.
3. *Investor*. The term *investor* means (a) a parent, (b) ~~a~~ general partner, or (c) ~~a~~ natural person or corporation that has the ability to exercise significant influence.
4. *Investee*. The term *investee* means (a) a subsidiary or (b) an entity over which an investor has the ability to exercise significant influence.

Interpretation

~~Where~~**When** a nonclient investee is material to a client investor, any direct or material indirect financial interest of a covered member in the nonclient investee would be considered to impair independence with respect to the client investor. If the nonclient investee is immaterial to the client investor, a covered member's material investment in the nonclient investee would cause an impairment of independence.



~~Where~~**When** a client investee is material to nonclient investor, any direct or material indirect financial interest of a covered member in the nonclient investor would be considered to impair independence with respect to the client investee. If the client investee is immaterial to the nonclient investor, and if a covered member's financial interest in the nonclient investor allows the covered member to exercise significant influence over the actions of the nonclient investor, independence would be considered to be impaired.



Other relationships, such as those involving brother-sister common control or client-nonclient joint ventures, may affect the appearance of independence. The covered member should make a reasonable inquiry to determine whether such relationships exist, and if they do, careful consideration should be given to whether the financial interests in question would lead a reasonable observer to conclude that the specified relationships pose an unacceptable threat to independence.

In general, in brother-sister common control situations, an immaterial financial interest of a covered member in the nonclient investee would not impair independence with respect to the client investee, provided the covered member could not exercise significant influence over the nonclient investor. However, if a covered member's financial interest in a nonclient investee is material, the covered member could be influenced by the nonclient investor, thereby impairing independence with respect to the client investee. In like manner, in a joint venture situation, an immaterial financial interest of a covered member in the nonclient investor would not impair the independence of the covered member with respect to the client investor, provided that the covered member could not exercise significant influence over the nonclient investor.

If a covered member does not and could not reasonably be expected to have knowledge of the financial interests or relationship described in this interpretation, independence would not be considered to be impaired under this interpretation.

[Deleted effective November 30, 2011. ***Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.***]

Text of Proposed Reestablishment of Ethics Ruling No. 21 of ET Section 191

(Additions appear in boldface italic.)

21. Member as Director and Auditor of an Entity's Profit Sharing and Retirement Trust

.041 *Question*—A member serves in the dual capacity of director of an entity and auditor of the financial statements of that entity's profit sharing and retirement trust (the trust). Would independence be considered to be impaired with respect to the trust?

.042 *Answer*—Service as director of an entity constitutes participation in management functions that affect the entity's trust. Accordingly, independence would be considered to be impaired if any partner or professional of the firm served in such capacity.

[Deleted effective November 30, 2011. *Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.*]

Text of Proposed Reestablishment of Ethics Ruling No. 38 of ET Section 191

*(Additions appear in **boldface italic**, and deletions are ~~stricken~~.)*

38. Member as Co-Fiduciary With Client Bank

.075 Question—A member serves with a client bank in a co-fiduciary capacity with respect to an estate or **a** trust. Would independence be considered to be impaired with respect to the bank or the bank's trust department?

.076 Answer—Independence would not be considered to be impaired, provided the assets in the estate or trust were not material to the total assets of the bank ~~and~~ or the bank's trust department, **or both**.

[Deleted effective November 30, 2011. **Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.**]

Text of Proposed Reestablishment of Ethics Ruling No. 60 of ET Section 191

(Additions appear in boldface italic, and deletions are stricken.)

60. Employee Benefit Plans—Member’s Relationships With Participating Employer

.119 Question—A member has been asked to audit the financial statements of an employee benefit plan (“the plan²”) that may have one or more participating employer(s). Would independence be considered to be impaired with respect to the plan if the member had financial or other relationships with a participating employer(s)?

.120 Answer—Independence would be considered to be impaired with respect to the plan if any partner or professional employee of the firm had significant influence over such employer; was in a key position with the employer; or was associated with the employer as a promoter, *an* underwriter, or *a* voting trustee.

When auditing plans subject to the Employee Retirement Income Security Act of 1974 (ERISA), Department of Labor (DOL) regulations must be followed. *Currently, ~~DOL~~Department of Labor regulations are more restrictive than the position taken in this ruling⁺*

[Deleted Effective November 30, 2011. *Reestablished and effective October 31, 2012 until the earlier of January 1, 2014 or adoption of Interpretation 101-18.*]

¹ ~~Currently, DOL~~*Department of Labor* regulations are more restrictive than the position taken in this ruling.

Text of Proposed Reestablishment of Ethics Ruling No. 69 of ET Section 191

*(Additions appear in **boldface italic**, and deletions are ~~stricken~~.)*

69. Investment With a General Partner

.138 *Question*—A private, closely held entity is the general partner and controls (as defined in ~~G~~**generally A**~~accepted A~~**ccounting P**~~principles~~) limited partnership A. The member has a material financial interest in limited partnership A. The member's firm has been asked to perform an attest engagement for a new limited partnership (B), which has the same general partner as limited partnership A. Would independence be considered to be impaired with respect to limited partnership B?

.139 *Answer*—Because the general partner has control over limited partnership A, the covered member would be considered to have a joint closely held investment with the general partner, who has significant influence over limited partnership B, the proposed client. Accordingly, independence would be considered to be impaired with respect to limited partnership B if the covered member had a material investment in limited partnership A.

[Deleted effective November 30, 2011. ***Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.***]

Text of Proposed Reestablishment of Ethics Ruling No. 81 of ET Section 191

(Additions appear in **boldface italic**, and deletions are ~~stricken~~.)

81. Member's Investment in a Limited Partnership

.162 Question—A member is a limited partner in a limited partnership (LP), including a master ~~limited partnership~~**LP**. A client is a general partner in the same LP. Is independence considered to be impaired with respect to ~~(1a)~~ the LP, ~~(2b)~~ the client, and ~~(3c)~~ any subsidiaries of the LP?

.163 Answer—

- a.** A covered member's ~~limited partnership~~**LP** interest in the LP is a direct financial interest in the LP that would impair independence under ~~i~~**Interpretation** 101-1.A.1 [ET section 101.02].
- b.** The LP is an investee of the client because the client is a general partner in the LP. Therefore, under ~~i~~**Interpretation No.** 101-8 [ET section 101.10], if the investment in the LP were material to the client, a covered member's financial interest in the LP would impair independence. However, if the client's financial interest in the LP were not material to the client, a covered member's immaterial financial interest in the LP would not impair independence.
- c.** If the covered member is a limited partner in the LP, the covered member is considered to have an indirect financial interest in all subsidiaries of the LP. If the indirect financial interest in the subsidiaries were material to the covered member, independence would be considered to be impaired with respect to those subsidiaries under ~~i~~**Interpretation No.** 101-1.A.1 [ET section 101.02].

If the covered member or client general partner, individually or together can control the LP, the LP would be considered a joint closely held investment under ET section 92.16.

[Deleted effective November 30, 2011. **Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.**]

Text of Proposed Reestablishment of Ethics Ruling No. 98 of ET Section 191

(Additions appear in boldface italic, and deletions are ~~stricken~~.)

98. Member’s Loan From a Nonclient Subsidiary or Parent of an Attest Client

.196 Question—A member has obtained a loan from a nonclient. The member’s firm performs an attest engagement for the parent or a subsidiary of the nonclient. Does the loan from the nonclient subsidiary or parent impair independence?

.197 Answer—A covered member’s loan that is not a “grandfathered” or “permitted” loan under ~~i~~**Interpretation No. 101-5** [ET section 101.07] from a nonclient subsidiary would impair independence with respect to the client parent. However, a loan from a nonclient parent would not impair independence with respect to the client subsidiary, as long as the subsidiary is not material to its parent.

[Deleted effective November 30, 2011. ***Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.***]

Text of Proposed Reestablishment of Ethics Ruling No. 106 of ET Section 191

*(Additions appear in **boldface italic**, and deletions are ~~stricken~~.)*

106. Member Has Significant Influence Over an Entity That Has Significant Influence Over a Client

.212 *Question*—Would independence be considered to be impaired if a member or his or her firm had significant influence, as defined in ET section 92.27, over an entity that has significant influence over a client?

.213 *Answer*—Independence would be considered to be impaired if any partner or professional of the firm had significant influence over an entity that has significant influence over a client. By having such influence over the nonclient entity, the partner or professional employee would also be considered to have significant influence over the client.

See ~~Interpretation No.~~ **Interpretation No.** 101-8 [**ET section 101.10**] for further guidance.

[Revised July 2002 to reflect conforming changes necessary due to the revision of Interpretation No. 101-1. Deleted effective November 30, 2011. **Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.**]

Text of Proposed Reestablishment of Ethics Ruling No. 111 of ET Section 191

(Additions appear in boldface italic.)

111. Employee Benefit Plan Sponsored by Client

.222 Question—A member or his or her firm provides asset management or investment services that may include having custody of assets, performing management functions, or making management decisions for an employee benefit plan (the plan) sponsored by a client. Would independence be considered to be impaired with respect to the plan and the client sponsor?

.223 Answer—The performance of investment management or custodial services for a plan would be considered to impair independence with respect to the plan. Independence would also be considered to be impaired with respect to the client sponsor of a defined benefit plan if the assets under management or in the custody of the member are material to the plan or the client sponsor.

Independence would not be considered to be impaired with respect to the client sponsor of a defined contribution plan, provided the member does not make any management decisions or perform management functions on behalf of the client sponsor or have custody of the sponsor's assets.

[Deleted effective November 30, 2011. ***Reestablished and effective October 31, 2012, until the earlier of January 1, 2014, or adoption of Interpretation No. 101-18.***]