

January 27, 2014

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We have reviewed the November 26, 2013 Exposure Draft – Proposed Conflict of Interest Interpretations and submits the following comments and proposed revisions to Proposed Rule 102-2, *Conflicts of Interest for Members in Public Practice*:

1. The proposed edits to the first paragraph of 101-2 have the effect of removing the definition of conflict of interests. In our opinion, the meaning of conflict of interests is neither simple nor self-explanatory and we believe an effective standard about the impacts of a conflict of interest must include a clear definition. Moreover, if a member were ever to be challenged about a conflict of interests and our professional ethics rules do not contain a definition applicable to its interpretation, a court would default to a broad legal definition, which may vary between jurisdictions. We believe the profession would be better served with a clear definition.

The existing definition, which is the first sentence in 101-2 as it is currently written, makes it clear that the existence of a potential conflict and the assessment of its potential impact are through the eyes of the client. As edited, the proposed interpretation says that "a member should use professional judgment, taking into account whether a reasonable and informed third party who is aware of the relevant information would conclude that a conflict of interest exists." It seems that the language as proposed would result in less matters being identified as actual conflicts because, in practice, a client cannot remove emotion from the equation. However, if you assume the client is the primary entity impacted by the conflict of interest¹ and that the client is the one that will evaluate the impact for purposes of a consent, in our opinion, the existence and impact of a potential conflict² of interest should continue to include assessment through the eyes of the client.

¹ A third party's evaluation of the impact of the relationship between a member and its client are addressed within the context of independence. Conflicts of interest, on the other hand, primarily address the impact on a client of the relationship between a member and third parties.

² The proposed interpretation makes no distinction between potential conflicts and actual conflicts. Clients would tend to assess potential conflicts more severely for both existence and impact. We believe making such a distinction would be appropriate.

2. We agree that applying the same conceptual framework currently applied to independence issues is appropriate and beneficial for conflicts of interest that could impair a member's objectivity. At the same time, we believe that the application of the conceptual framework should not have the impact of reducing the clarity of the issue. The existing interpretation clearly says that a conflict of interest is a relationship that may be viewed as impairing the member's objectivity. The proposed interpretation says that "a conflict of interest creates adverse interest and self-interest threats to the member's compliance with the integrity and objectivity rule." We believe the former is much clearer than the latter. The inclusion of a clear definition of a conflict of interest that can then be talked about within the context of the conceptual framework might resolve this issue.
3. We agree with the proposed revision in Paragraph 5 requiring the member (firm) to take "reasonable steps" to identify circumstances that might cause a conflict of interest prior to accepting a new client relationship, engagement, or business relationship. We believe this is, for the most part, already being done under the current standards. The revision merely documents the expectation and will not significantly change current practice.

Paragraph 7 discusses how "an effective conflict identification process" will assist the member in identifying actual or potential conflicts of interest. The proposed guidance includes the statement that the identification process "includes matters identified by external parties, such as clients or potential clients." It is unclear why such a statement is necessary and we are concerned that it implies a positive obligation to pursue such information rather than an obligation to respond to such information when received. Additional explanation as to the intent and objective of this provision would assist members in structuring their systems to include these matters.

4. While we agree with the proposed revision in paragraph 9 requiring the member to evaluate the significance of identified conflicts of interest to determine if the conflict of interest threat is significant and applying safeguards to reduce the threat to an acceptable level, we have specific concerns regarding the clarity of the guidance provided in this paragraph ("Evaluation of a Conflict of Interest").

The first sentence of this section says "when a conflict of interest has been identified, the member should evaluate the significance of the threat created by the conflict of interest to determine if the threat is at an acceptable level." Acceptable for what? How can a member evaluate whether the risk is acceptable or unacceptable without clarity about the purpose for which the evaluation is being made? We assume this evaluation is being performed for the purpose of determining whether the member might, despite the conflict, be able to perform the service with integrity and objectivity. We suggest that context be added to the first paragraph as follows (edits to the proposed text are indicated by red underlined text or red strikeout text):

Evaluation of a Conflict of Interest

To determine whether it would be appropriate for the member to provide a professional service ~~W~~When a conflict of interest has been identified, the member is required to ~~sho~~ld evaluate the significance of the threat created by the conflict of interest to determine if the threat is at an acceptable level³. The threat is considered to be "at an acceptable level" when the significance of the threat combined with the safeguards applied reduce the risk of the threat to a level where a reasonable and informed person would likely conclude that the service could be performed with integrity and objectivity. Members should consider both qualitative and quantitative factors when evaluating the significance of the threat, including the extent to which existing safeguards already reduce the threat to an acceptable level. In evaluating the significance of an identified threat, members should consider the following:

- The significance of relevant interests or relationships.
- The significance of the threats created by performing the professional service or services. In general, the more direct the connection between the professional service and the matter on which the parties' interests are in conflict, the more significant the threat to compliance with the rule will be.

If the member concludes that the threat is not at an acceptable level, the member should apply additional safeguards to eliminate the threat or reduce it

5. We believe the interpretation should require that disclosure to the client of the conflict of interest be made in writing.
6. We agree with the proposed concepts of "general disclosure" versus "specific disclosure" to the client as outlined in paragraphs 12-14. However, we believe that the guidance as currently worded is not as clear as it could be regarding disclosure responsibilities for potential and identified conflicts of interest⁴. We suggest that the interpretation permit general disclosures when there is only a potential for a conflict of interest to exist (i.e. when the member provides similar services to competing businesses). If an actual conflict of interest has been identified, regardless of its significance, the interpretation should require specific client disclosure and consent be obtained. While that disclosure "hierarchy" may be implied in the proposed interpretation, we suggest that it be made clearer to avoid any confusion.

³ The independence conceptual framework says the following about acceptable threats. "Threats are at an acceptable level when it is not reasonable to expect that the threat would compromise professional judgment". The definition inserted above is intended to reflect that definition using terms introduced in this interpretation.

⁴ See Footnote 2

If our recommendation about general and specific disclosure is not implemented, then we believe that paragraph 12 should be reworded to provide additional clarity. We suggest that context be added to paragraph 12 as follows (edits to the proposed text are indicated by red underlined text or red strikethrough text):

The member should consider ~~determine whether~~ the nature and significance of the conflict of interest to determine whether general disclosure is sufficient or is such ~~that~~ specific disclosure and specific consent is necessary. For this purpose, the member should exercise professional judgment in evaluating the circumstances that create a conflict of interest, including the parties that might be affected, the nature of the issues that might arise and the potential for the particular matter to develop in an unexpected manner.

7. Paragraph 16 states that “The member is encouraged to document the nature of the circumstances giving rise to the conflict of interest, the safeguards applied to eliminate or reduce the threats to an acceptable level, and the consent obtained”. We believe that the text “is encouraged to” should be replaced with “should”.

General Comment - We would suggest that future exposure drafts contain either paragraph numbers or sequentially numbered text lines. It is difficult to provide clear and concise comments without the ability to easily reference the exact text or paragraph that is the subject of our commentary.

Thank you for the opportunity to comment on the proposed Ethics Interpretation. If you have any questions, feel free to contact Brian Ross at Brian.Ross@plantemoran.com or me at Greg.Coursen@plantemoran.com.

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