

Sept. 10, 2014

Ms. Lisa A. Snyder, CPA  
Director - Professional Ethics Division  
American Institute of Certified Public Accountants  
1211 Avenue of the Americas, 19th Floor  
New York, NY 10036  
[lsnyder@aicpa.org](mailto:lsnyder@aicpa.org)

Re: AICPA PEEC – Exposure Draft – Dated June 16, 2014

Dear Ms. Snyder,

The Professional Ethics Committee (the committee) of the Pennsylvania Institute of Certified Public Accountants (PICPA) appreciates the opportunity to provide its comments on the proposed revisions to the AICPA Code of Professional Conduct (the code). The PICPA is a professional association of more than 21,000 members working to improve the profession and better serve the public interest. Founded in 1897, the PICPA is the second-oldest CPA organization in the United States. Membership includes practitioners in public accounting, education, government, and industry. The committee is a cross-section of our membership, with practitioners from large, regional, and small public accounting firms, members serving in business and industry, and accounting educators.

The committee is concerned about the overall appearance of permitting a practitioner to continue on an attest engagement despite an independence breach. The committee notes that independence is the fundamental underpinning of most attest engagements. At the same time, the committee understands the complexities involved in complying with the independence guidance, and agrees that in certain cases the public interest may not be served by having the firm resign from the attest engagement. The committee suggests exploring a revised approach in which a process is created for curing certain independence breaches, and allowing the report to be reissued under the new circumstances (after independence is reestablished). That way the guidance never suggests that an attest report can be allowed to remain where independence is breached. The committee also supports reconsideration of the independence guidance for situations in which the integrity, and objectivity of the engagement team is not compromised.

The committee's comments and concerns regarding the proposed guidance are noted below.

### General Comments

Exposure document process – Due to the significance of the proposed guidance and potential changes that could arise in the exposure process, the committee recommends that the AICPA Professional Ethics Executive Committee (PEEC) re-expose any revised proposal for further input.

Regulatory input – The committee recommends that the PEEC reach out directly to key regulatory agencies to determine their perspective on the proposed revisions. The proposed standards would require the practitioner to consider the perspective of external financial statement users. The committee believes

that the PEEC is in the best position to gain the input from regulatory bodies, and that such input should be an integral part of any final guidance with respect to independence breaches.

**Legal perspective** – The committee recommends that the perspective of attorneys and malpractice carriers be consulted to ensure that their concerns are considered. The committee believes that the proposed approach may be difficult to defend in litigation. As the proposed guidance is cumbersome, the committee thought that it may be difficult for a jury to understand.

**Enforcement** – The exposure document notes that the guidance would not preclude an investigation or enforcement action. The committee recommends clarifying where the enforcement actions could come from (i.e., PEEC, regulatory bodies, state boards of accountancy, etc.).

**Appearance questions** – Considering the pressure for greater transparency in the audit report as proposed by the IAASB and PCAOB (and likely the AICPA at a future date), it seems that these independence breaches would be publicly disclosed, in addition to the disclosure to those charged with governance as is required in the proposed guidance. Therefore, the committee supports the addition of a requirement for the responsible party to consider the overall appearance of the independence breach, and the steps taken to address the breach, based on whether a reasonable and informed third party who is aware of the relevant information would conclude that the steps taken to address the breach are appropriate. It is unclear whether this revised approach to an independence breach would convey a conflicting message to the public (i.e., that it is acceptable to breach an independence requirement if you take corrective actions). It is not clear how this would be perceived by financial statement users, and their input would be important before finalizing any standard. The revised approach suggested at the outset of our response may provide greater clarity to financial statement users.

**Examples** – Specific examples as to how the proposed guidance would work in practice would help to assess whether or not the guidance being proposed is appropriate. While the intent of the guidance seems to permit the practitioner to take certain corrective actions in certain situations without having to resign from an engagement, it is not clear whether the message conveyed by the new approach is that a “cure” to an independence violation is possible.

**Policies and procedures** – The requirement for a firm to have “policies and procedures designed to provide it with reasonable assurance that the firm, its personnel, and, when applicable, others subject to independence requirements, maintain independence when required,” seems more suited to the AICPA’s Quality Control Standards, which would then be covered by peer review. While this aspect of the firm’s quality control system is important, the rationale for having it as a prerequisite for the application of the new proposed guidance is unclear. Ultimately, the facts and resulting circumstances would be the same, whether or not they had appropriate policies and procedures. This leads to the perception that the guidance within the code is exacting a punitive measure. Furthermore, requiring effective policies and procedures as a prerequisite creates a number of complexities. For example, how would a subsequent inspection, or peer review finding that the firm’s policies and procedures were not properly designed, impact previous decisions to implement this guidance and not resign from the engagement? Would the firm have to revise its previous conclusions? How would this work in practice? Further, the proposed prerequisite to the application of the guidance raises questions regarding the ability of third parties to accept any decision to take corrective actions to address a breach without also considering and testing the

appropriateness of the firm’s policies, procedures, and compliance therewith. Would third parties be in a position to perform this type of evaluation? The committee agrees that the policies and procedures should be communicated to those charged with governance. The committee supports practice guidance that emphasizes the need to have properly designed policies and procedures in place.

Also, the proposed guidance indicates that a firm should have policies and procedures, but it does not clearly specify that those policies and procedures need to be in operation during the period of the breach. The committee recommends that a requirement be added that these policies and procedures be communicated to firm personnel in writing annually.

Overall, it appeared that certain proposed requirements were added in a negotiation process, such that the underlying message seems to be that the PEEC was only comfortable in including the breach of independence guidance if it included certain punitive elements for firms lacking adequate systems for ensuring that independence is maintained. The committee believes that such punitive considerations should come into play in the enforcement process and that the guidance be revised until it is more broadly acceptable.

External communication – The proposed guidance requires communication to those charged with governance. However, the committee questions whether there are additional external parties that would need to receive the same communication as those charged with governance. For example, on an A-133 engagement would the practitioner need the concurrence of the cognizant agency? The committee recommends that the PEEC consider who, in addition to those charged with governance, would be in a position to overturn any decision made by the practitioner, and include these additional third parties as suggested parties to consult prior to continuing to apply the proposed guidance.

Use of terminology – Throughout, the proposed guidance refers to “addressing the consequences of a breach.” Practitioners are required to “address the consequences of a breach.” One manner of “addressing the consequences of a breach” may be to resign from the engagement. The committee proposes clarifying this phrase to say “address the consequences of a breach without resigning from the engagement.”

Failure to document – Due to the significance of the proposed actions, the committee supports requiring robust document. However, the committee is concerned that lack of sufficient documentation could result in an independence breach. It is not clear whether this breach could also be cured. The committee suggests that PEEC consider a clarification that the lack of sufficient documentation would not lead to an independence breach.

Link to practice aids – The committee recommends including a link at the end of this section on guidance to the AICPA practice aid that addresses independence breaches (once the practice aid is updated for the final proposed guidance on independence breaches).

## Specific Comments

### **Section – Introduction**

First paragraph –

- The first sentence could be clarified by adding that members are required to comply with the independence guidance where applicable.
- The second sentence could be clarified by adding “without resigning from the engagement” at the end of the sentence.

Second paragraph – The use of the word “resolve” in the final sentence makes it seem that a firm could resolve, or cure, an independence breach. Substituting “resolve” with “address” is one solution.

### **Section – Breaches Resulting in Significant Threats**

First paragraph – The first sentence refers to situations in which intent or incompetence cause a significant breach such that “the attest engagement team’s integrity, objectivity, and professional skepticism are compromised.” It is unclear why there is a need for the reference to intent and incompetence as the guidance could be stated more generally that in any case in which the attest engagement team’s integrity, objectivity, and professional skepticism are compromised, no actions can be taken to address the consequences of the breach other than resignation. The committee proposes restructuring the section to eliminate the first paragraph, generalizing the second paragraph (take out “In other situations”), and including, as “Item a.” under the second paragraph, the general guidance that no remedy is possible if the attest engagement team’s integrity, objectivity, and professional skepticism are compromised.

The committee does agree that in the event that a member of the engagement team caused the breach for reasons of self-interest, no remedy should be possible and the only response to address this breach is withdrawal from the engagement. It is not clear from the proposed guidance whether this is what was intended.

Item b. – “The breach is known to any other partner or partner equivalent who fails to ensure the breach is promptly communicated to an appropriate individual within the firm as described in this interpretation.” – This situation may not come to light, as it relies on any other partner or partner equivalent disclosing that the breach was known. The responsible party may not be able to ascertain this information. Further, it appears that this provision is somewhat punitive, seeking to preclude application of this guidance based on noncompliance with their quality control system. Ultimately, if the engagement team’s integrity, objectivity, and professional skepticism are not compromised, it is unclear why the firm would not be able to apply the guidance.

### **Section – Evaluating the Significance of a Breach**

Item d. – “The role of the individual if the breach relates to a member of the attest engagement team.” – It is not clear how an independence breach by someone on the attest engagement could be addressed without resigning from the engagement. This appears to conflict with the general guidance that if an attest engagement team’s integrity, objectivity, and professional skepticism are compromised, no actions can be taken to address the consequences of the breach other than resignation. A specific scenario in this case would help illustrate the proposed guidance.

## Section – Breaches Relating to Previously Issued Reports

The guidance for these engagements seem to follow all the guidance in the previous sections, so it is unclear why a separate section is needed. The committee recommends incorporating this guidance into the preceding general guidance.

Thank you for the opportunity to provide our comments related to the proposed revisions to the Code of Professional Conduct. Feel free to contact me at (717) 228-1711 or the PICPA staff liaison, Allison Henry, at (215) 972-6187 with any questions regarding our comments.

Sincerely,



Francis X. Ryan, CPA  
Chair, PICPA Professional Ethics Committee

cc: Allison Henry, CPA, PICPA Staff Liaison