



June 15, 2018

Ms. Toni Lee-Andrews
Ethics Team
AICPA
220 Leigh Farm Road
Durham, NC 27707

Re: March 15, 2018 PEEC Exposure Draft (ED), *Proposed Interpretation to the AICPA Code of Professional Conduct: Information Systems Services (ET sec 1.295.145)*

Dear Ms. Lee-Andrews:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to speak on behalf of local and regional firms and represent those firms' interests on professional issues in keeping with the public interest, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective.

TIC has reviewed the ED and is providing the following comments for your consideration.

GENERAL COMMENTS

It is TIC's understanding that this interpretation is being proposed to address questions received by the ethics team related to the performance of IT services and how those services could impact independence. While TIC is appreciative of PEEC's efforts to address these detailed questions, TIC is concerned that proposing such rules-based interpretive guidance could lead to more confusion and additional questions, especially in an area that is ever changing where new technologies are developed almost daily.

TIC would suggest that PEEC consider whether such rules-based guidance is necessary, or whether issuing some general, principles-based guidelines in an interpretation and then having related FAQs that address specific fact patterns might be more appropriate. This would be similar to how PEEC handled the Long Association issue that was originally proposed as an interpretation but ended up being issued as final in a Q&A format. TIC believes that Q&As would also be easier to add to and update as new technologies are developed and new issues need to be addressed. TIC has had some discussions with the ethics staff regarding this idea and would be happy to assist in the development of these FAQs if PEEC should decide to go in that direction. For example, TIC believes that open source coding and the transfer of code between different COTS which are not addressed in this interpretation might be good issues to address in FAQs.

TIC also shared our letter with the staff of the Assurance and Advisory Innovation team and they agreed with many of TICs concerns.

If the interpretation moves forward as proposed, TIC suggests adding specific language to the initial paragraph to communicate that the primary purpose of this interpretation is to clarify, and not completely revamp, the existing guidance. TIC believes some readers may come to the same conclusion as TIC, that this interpretation is more restrictive and imposes additional requirements on the Member that are not already in the existing ethics literature.

In addition, it is TIC's understanding, from discussing this ED in our May meeting with PEEC, that it would only apply to IT related services that are performed as a separate service, and not those IT services performed as part of a financial statement audit or other assurance services. TIC believes this is very important to explicitly indicate in the Interpretation, as many times an auditor will perform some of the procedures noted in this interpretation as part of their overall audit of the financial statements and, in those cases, these services would typically not result in an impairment to independence.

TIC believes this point will become even more critical as auditors move more towards a continuous audit, whereby they will be performing procedures throughout the year to gain audit evidence and will be using technology more and more to gather evidence related to whether the financial information is presented fairly in all material respects in an entity's financial statements. TIC is aware that this is a huge undertaking by the AICPA and even just this week at the Engage conference TIC has heard AICPA senior leadership expressing their support for these new and innovative approaches to performing an audit. TIC fears that some of the language in this ED could preclude an auditor from being able to perform certain procedures that would be deemed necessary when performing a continuous audit and TIC does not believe that was the intent of the ED.

In addition, TIC believes that providing information or a process to reorganize/summarize client information should be distinguished from actually making management decisions for purposes of this ED.

SPECIFIC COMMENTS

Question 1: Do you believe the terminology used in the proposal is consistent with industry practice and will be readily understood by Members who do and do not practice in this arena?

TIC believes that certain terminology used in this proposal does not appear to be in line with industry practice as it relates to information systems specialists in this line of practice, and does not appear in line with terminology used by Members who do not practice in this area. This represents a very technical area where terminology is specialized and continuously changing as technology advances, and more capabilities are created.

For example, in Section .02 a. iii of the ED, TIC foresees a potential issue with the definition of a financial information system which defines it as “a system that gathers data that assist management in making decisions that directly impact financial reporting.” TIC believes this implies that there is a possibility that any information system could have a material impact on financial decisions made by management. The definition also is so broad that it could include Big Data and non-financial data as well. TIC believes it is possible that a system, once installed, could provide new information to management that they were not previously aware of, or information that was not previously available, but it also provides significant insight into a company’s operations, results, or activities, in a non-financial way.

TIC believes that just providing information to management does not automatically mean management will use that information to make financial decisions that would have a material impact. Therefore, TIC believes that Section .02a. iii as written could imply that providing this information results in an automatic trigger to independence which TIC does not believe would always be the case.

The unintended consequence of now having access to this new information is that it could lead to management making significant financial decisions based on that information. TIC would ask PEEC to consider whether clarity could be added as to what would be considered a financial information system or, at least, add that it would be limited to direct financial information systems.

In addition, Section .02 b of the ED indicates the following:

“Designing an information system means determining how a system or transaction will function, process data, and produce results (for example, reports, journal vouchers, and documents such as sales and purchase orders) to provide a blueprint or schematic for the development of software code (programs) and data structures.”

TIC is curious if the definition used here is intended to apply overall as it relates to any information system, or should the focus be on financial information systems? TIC believes clarity should be provided here.

In addition, as it relates to the design aspect, TIC would propose that clarity be given on this as it does not relate to design of a system for the client through determining the best commercial off-the-shelf solution for their set up. Some questions TIC believes need clarification include the following:

- Does design or development extend to compiling of open source information to build a software system for a customer?
- Would there be a threat to independence if the design and/or development was overseen by management, in such that the Member was acting as a subcontractor with specific oversight by management as to have management approve/evaluate/accept the results of their requested design?

Section .07 references the installation on a customer's server. TIC believes there are many instances, including the expansion of practice to install on a cloud system, where the client no longer maintains servers, but uses another third party to host and maintain the server, access, etc. TIC suggests expanding this definition to indicate customer's "designated hosting site" may fit more, and allow for more industry changes, including changes in terminology or technology that could happen in the future.

TIC also would note that this issue goes beyond just the cloud and could apply to decentralized networks where there is no singular installation place. TIC would suggest that instead of making this more of a standard that would apply to all networks, that PEEC consider instead developing a series of Q&As that address particular current fact patterns that are relevant to current technology but also could be updated in the future as additional technologies are introduced.

In Section .18, TIC believes an application program interface (API) may not be the right term to use here. For example, a Member could use a third-party tool that performs data translation services. In such cases, it's not usually an API connector performing these services, but rather a program for data translation purposes.

Question 2: *The definition of a financial information system proposes in part to include a system that generates information that is significant to the financial statements or financial processes taken as a whole.*

- a. *The proposal currently does not include specific guidance on what is "significant," leaving the determination to the professional judgment of the Member. Do you believe this is appropriate? If you believe specific guidance should be included, please explain how you believe "significant" should be defined.*

TIC believes that the term "significant" can be very broadly interpreted, to the point it may be more restricting in this environment. The world of financial systems is becoming more complicated between enterprise resource planning, financial planning and analysis, business intelligence and other tools. As addressed in our previous comment on section.02.a.iii., significant influence can be gained through information that management may not be able to understand or process, that is not directly financially related, but could cause management to make significant decisions that could have a material impact. For example, would the Member be responsible for ascertaining whether this was possible, or assume that it is always the case? TIC believes this could cause the interpretation to be more restrictive. TIC believes additional clarity or examples would help, if not in this interpretation but perhaps in a related Q&A document.

- b. *By including the concept of "significant" in the definition of a financial information system, it could be perceived that PEEC has proposed a less restrictive standard than the current interpretation, which would allow the Member to design or develop a component of the*

financial information system that is not significant to the financial statements or financial process as a whole. Do you believe this exception is appropriate? Why or why not?

TIC believes that the concept that “significant” is less restrictive than the current application may not be accurate. For example, there are instances where a component of the financial information system may not be significant at the time of design or develop stage, but may be in the future. There also could be cases where it may not be directly significant, but may be used to support substantive analytics or data analysis and may end up being indirectly significant. Therefore, with a broad definition of significant, this may cause issues.

- c. *Do you think the phrase “financial process” makes it clear that Members should be thinking broadly about processes that may affect a financial process such as information technology general controls?*

Yes, TIC believes that the term and definition in the background is clear, but it does not appear to fully carry into the interpretation itself.

Question 3: *One of the factors proposed that may assist Members in determining whether a nonattest service is related to a financial system is whether the system gathers data that assists management in making decisions that directly affect financial reporting. Do you believe this would include management-level dashboard reporting? Why or why not?*

TIC does not feel that management-level dashboard reporting should be a factor for determining whether the system gathers data that assists management in making decisions that directly affect financial reporting. This appears to counter the proposed consideration of what comprises significant. TIC believes this could be interpreted to note that any system that provides information in management-level dashboard reporting could be considered significant.

For example, companies may use non-financial systems and related reports of information summarized using reports developed and designed by the Member, to the client’s specifications, to make financial management decisions. This information was used to facilitate the attest service and was not intended to be a part of management’s controls. TIC does not believe this should be a factor in determining whether a nonattest service is related to a financial system.

Question 4: *If adopted as proposed, do you believe the extended period of time would be needed to implement the guidance? Why or why not?*

TIC does not believe the proposal provides adequate time to adopt these changes, and an extended adoption period would be needed. Mainly, TIC believes additional time would be needed to evaluate existing IT consulting agreements in process and whether there now would

be any threats to independence. For example, some contracts may be for periods longer than one year, or may take more than one year for application, installation, testing, and go-live. TIC believes that contracts in place as of the proposed effective date may be affected and cause significant issues for companies, as well as consultants. TIC also would propose a grandfathering provision for contracts that are in place as of the effective date of this guidance to address this issue.

ADDITIONAL COMMENTS

Subscriptions and bundling of services

If a firm is performing services at the client's direction, but are opting to bill them according to a set monthly "subscription" fee for these services, is there a concern regarding the appearance of these services impairing independence per section .19? As with attest clients, firms do currently require a request, approval, and subsequent sign off to perform any work in these areas while they retain sole administrative oversight to their environment. TIC would suggest clarification here or perhaps Q&As that walk through particular fact patterns and whether they might impair independence.

External audit integration installations or access

For some firms, and in the future, there may be separate engagements set up, that would incorporate the installation of oversight software or programs, that would be used by auditors or auditor's API system to provide continuous monitoring and audit processing on a continuous basis. TIC believes there may be instances where the results of the auditor's continuous monitoring may be available to the client, or intentionally sent to the client (such as exception reports), and the client may use the results to perform financial analysis, or financial processing, or provide audit support for anomalies as identified. These situations are clearly intended to be a client interface solution, but they could ultimately be considered significant to the financial reporting process. TIC believes that specifically scoping out IT procedures that are directly related to obtaining audit evidence would help to clarify this issue.

Section .04 Discrete calculation

TIC believes this could be interpreted to not allow for reformatting of information, or calculating standard financial ratios or financial relationships from client provided data, and presenting back to the customer, or management, a report with such information that they may use for their financial decision-making process.

This could include design and development of a report format by the Member, (perhaps using Excel, related report tools, or a Member designed software), including addition of industry benchmarks, where the results are then presented to management. TIC believes this should fall under discrete, and there should there be an expansion of this definition to give consideration to situations such as these. For example, does this example previously noted constitute writing code as defined under "developing" in the definitions?

TIC also believes that paragraphs .04 and .16 of the ED seem to have some inconsistencies. In paragraph .04, the member is allowed to perform a discrete calculation but in paragraph .16, the Member cannot design and develop the rules or logic necessary to convert legacy system data to a format that is compatible with that of the new system. Some firms treat Excel, used to create financial information, as a separate financial information system. Taking information from legacy software and formatting it so that using Excel and adding calculations (rules and logic) may be interpreted as not creating a threat to independence and “discrete” under paragraph .04 but could be construed as disallowed under paragraph .16. TIC believes that this potential inconsistency should be addressed in the ED.

Interface Services

Paragraph .14 of the ED indicates the following:

“If a *member* provides interface services for a COTS financial information system software solution, *threats* to compliance with the “Independence Rule” would not be at an *acceptable level* and could not be reduced to an *acceptable level* by the application of *safeguards*; *independence* would be *impaired* except as provided for in paragraph .15.”

TIC believes that in many cases CPAs are not creating any data when performing these services, but, rather, are just moving data and, therefore, this should not create an immediate threat to independence that cannot be overcome with safeguards. For example, with advances in machine learning, you could have an interface that is bot-to-bot that has machine learning on each side of the application. This would not be considered an API, but TIC could foresee proper safeguards being in place to reduce any potential threats to independence to an acceptable level.

TIC believes that more than just APIs should be scoped out for purposes of paragraphs .13 through .15 of the ED.

Data Translation

Paragraph .17 of the ED states the following:

“
If a *member* performs data translation services for a COTS financial information system software solution, *threats* to compliance with the “Independence Rule” would not be at an *acceptable level* and could not be reduced to an *acceptable level* by the application of *safeguards* and *independence* would be *impaired* except as provided for in paragraph .18.”

TIC believes that in certain cases, data transformation would be a normal threat that could be overcome with certain safeguards (such as completeness checks), and should not be considered a threat that cannot be overcome. For example, if a client had an accounting system that allowed for exports to comma-separated values (CSV) in a spreadsheet for all the transactions that they 100% coded and take full responsibility for and then gives this information to the CPA whereby the CPA imports the information into some other software after changing the columns around to fit their format for purposes of reperformance and retesting, TIC does not believe this situation

should result in an automatic threat to independence. In these situations, the spreadsheet is not an API, and the ability to export data is usually a reporting/exporting feature or maybe even just a query of the underlying data. TIC believes this situation should be clarified for purposes of this ED as it is very common when performing audits of private companies.

System and Network Maintenance, Support, and Monitoring and Hosting

TIC believes the substance of how the software is used and who performs the various functions should continue to be the relevant criteria, not who holds the license (especially if the license holder is only used for purposes of obtaining a discount). TIC would ask that PEEC review this current proposal and the hosting FAQs to ensure they are consistent with the previously issued guidance.

As it relates to paragraphs .19 and .20 of the ED, TIC was a bit confused as to why discrete functions could be overcome but ongoing functions, processes, and activities could not. TIC believes there could be instances where ongoing maintenance, support, and monitoring activities could be performed by the CPA on more of an ongoing basis (as part of the continuous audit process for example), where there could be appropriate safeguards in place that could overcome any potential threats to independence. TIC believes that leaving this in the ED as an automatic threat will result in issues down the line as auditors start focusing more on the continuous audit through use of new technologies.

If PEEC believes there are specific cases where performing of these ongoing activities would pose a clear threat to independence, perhaps they should include those specific examples rather than implying that performance of such services would be an automatic threat to independence that cannot be overcome.

Issues Related to Hosting

In addition to this ED, TIC discussed the recently drafted Q&As on hosting with PEEC and the ethics staff in our May 2018 meeting. While we sent some of those comments under separate email cover to the ethics team, TIC would like to reiterate some of the major points in this letter as we feel there could be some implications and carryover to this ED as well.

ET 1.125.120 discusses specific actions related to bookkeeping and payroll services and describes those actions that either do or do not impair independence. None of those procedures are dependent on who is the software licensee.

ET 1.295.143.04c (Hosting) indicates that using general ledger software to facilitate bookkeeping services does not impair independence as long as copies are provided as described in that section. While it does not specifically indicate whether the software is licensed to the Member or the client, the examples indicate that it could be either.

During discussions with PEEC staff concerning the need for specific FAQs related to the hosting ED, the example of cloud based accounting software was discussed. In particular, these cloud-based systems may allow the client to provide access to the Member, or may allow the Member to provide discounts to clients who then access the software through the Member's group. That

discussion indicated that if the Member was the license holder, impairment of independence might occur.

Considering the license holder as a factor for determining whether or not independence has been impaired seems to be inconsistent between sections ET 1.295.120 and .143.04c. Also, TIC believes if sections 1.295.120 and .143.04c were consistently followed, a Member could develop different independence answers based on whether the Member or the client was the licensee. TIC would suggest taking another look at these sections to ensure they are consistent with existing guidance as TIC does not believe this ED was intended to impose additional independence requirements on the Member.

TIC notes that there are instances that occur frequently in practice where the Member may be able to obtain a discount to a software license for financial information systems, such as Quickbooks, whereby the Member is billed for the software, and the attest client is the beneficiary, by receiving the software at a discount to the market price. These discounts are offered by Quickbooks online almost across the board to anyone that has a ProAdvisor License (could be CPAs, non-CPAs, etc.).

TIC believes there will be a significant amount of concern over this interpretation as it relates to many of these ongoing relationships. An FAQ guide discussing these concerns or approaches would be beneficial.

TIC appreciates the opportunity to present these comments on behalf of PCPS Member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,

A handwritten signature in black ink that reads "Michael A. Westervelt". The signature is written in a cursive, flowing style.

Michael A. Westervelt, Chair
PCPS Technical Issues Committee
cc: PCPS Executive and Technical Issues Committees