



Big Thinking. Personal Focus.

June 14, 2018

Samuel L. Burke, Chair  
AICPA Professional Ethics Executive Committee

Toni Lee-Andrews, Director, CPA, PFS, CGMA  
Professional Ethics Division

Dear Mr. Burke & Mrs. Lee-Andrews:

We appreciate the opportunity to provide comments on the AICPA's Exposure Draft Proposed Revised Interpretation "Information System Services (formerly Information Systems Design, Implementation, or Integration)" issued by the AICPA Professional Ethics Division dated March 15, 2018 (herein referred to as ED or Interpretation). We understand that one intent of the ED, among other things, is to provide clarifying guidance to assist members with interpreting the definition of a financial information system as well as to enhance guidance on the related effects on a member's independence.

We appreciate the consultation that occurred with current information technology experts to inform the Professional Ethics Executive Committee's (PEEC) thoughts and clarifying guidance as outlined in the ED. We believe that the consultation with IT experts has enhanced the specificity in which certain aspects of information system services are defined and explained.

Further, we agree with the underlying premise that when a member provides nonattest services related to an attest client's information systems, management participation and self-review threat exists.

The interpretation of financial information system concludes that when the information system aggregates source data underlying the financial statements, **or** generates information that is significant to the financial statements or financial processes as a whole, the system is considered a financial information system. A financial process is intended to include broad processes that affect financial reporting such as information technology general controls and information generated by the system is significant if it is probable that it will be material to the financial statements of the attest client.

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We believe that members should have latitude in mitigating threats to independence when providing information system services to attest clients. The ED, in our opinion, is too confusing and restrictive and doesn't take into consideration the vital role that members' play in providing value-added information system services and products to clients. Additionally, the AICPA's members need to stay relevant in today's fast-changing environment driven by technology, and this Interpretation's definition itself of what constitutes a financial information system is flawed and not in tune with the overall concerns of the AICPA in maintaining member relevance in the area of technology.

We believe that the Interpretation's criteria of "aggregating source data" to define a financial information system is too broad and should be removed. Aggregating source data is a basic formulaic functionality that is no different than what Excel can do and for which you already provide an exception. Why confuse the matter by having such a broad, routine functionality in the determination of "financial information system" when you provide an exception for templates?

We also believe that the criteria for defining a financial information system of generating information that is significant to the financial statements or financial processes as a whole should be eliminated for the various reasons as set forth below.

Perhaps, a simpler defining of a financial information system is in order such that information system services provided on an attest client's "primary financial information system (e.g., general ledger system)" would impair independence if independence and self-review threats cannot be mitigated. This would afford the member the opportunity to assist management with information system services and ancillary products that do not effectuate journal entries in the primary financial information system provided that there is documentation of mitigating factors. We believe members can mitigate threats to independence by having the competent attest client management take ownership of the consultative advice and products and mitigate the self-review threat by performing the same audit procedures as if the member did not provide the IT services or products to the attest client.

With the fast pace of technological change and the AICPA's belief that the profession needs to adapt quickly by embracing technology to remain relevant, we believe that PEEC should pause to consider that for AICPA members to remain relevant in today's and future operating environments, members need to have greater flexibility with respect to providing technological expertise to attest clients as value-added services.

### **The Concept of Significance or Materiality**

We request that PEEC reconsider the concept of using significance or materiality when determining a financial information system. We believe that using the word “significant” in the context of assessing a member’s independence places undue burden on the member due to variability of the impact to the financial statements that the financial information system can have on future periods.

- Notwithstanding the member’s judgements in determining significance/materiality, materiality is generally determined using metrics driven by financial statement results. Therefore, materiality can rise or fall over time. What may not rise to the level of significance in the year of design and/or system implementation could rise to a level of significance in a subsequent period in which the member performs attest services. This could jeopardize a member’s independence in the future period through no action of its own.
- The volume of transactions processed through the financial information system can increase over time, thereby having an impact on the significance of the financial information to the financial statements as a whole. Again, this could jeopardize a member’s independence in the future period through no action of its own.

Whereas, we do believe that a member’s independence must be assessed prior to the performance of nonattest services for an attest client, we generally disagree with the notion of using significance or materiality in making the assessment on the premise that the member would not have the ability to control or take action to prevent independence from being impaired. We believe this presents undue burden on the member in making its assessment.

### **Financial Processes and Information System General Controls**

We request that PEEC reconsider using financial processes in the broadest sense that may affect a financial process such as information technology general controls to define or determine whether the information system is deemed to be a financial information system.

Our belief is that a member’s expertise in financial processes and information technology general controls should be shared with the attest client when the attest client is implementing a financial information system. Permitting the member to assist management with the initial design of a financial information system provides inherent benefits that outweigh the risks of not having the member involved. Further, when the member evaluates the financial processes and controls such as information general controls in connection with an audit, the member would most likely share its knowledge and expertise by making recommendations to change or add controls where necessary.

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The attest client would be best served having such knowledge on the front end of a financial information system implementation than on the back end of an audit.

Additionally, an IT consultant may not be the best solution provider for financial information processes or underlying information system controls. Moreso, IT consultants are often more focused on the functionality of the system itself and the success of the implementation plan, rather than on the processes themselves or the related controls.

The AICPA has set a precedent of giving deference to a member's expertise and the relationship with the attest client. We believe this situation is no different, and the management participation and self-review threats can be effectively mitigated when the attest client is competent and accepts responsibility for the advice.

### **Exceptions for Fixed Asset Software and Deferred Tax Templates**

Under the proposed defining criteria for financial information system in the ED, we believe that the AICPA should expand the list of exceptions.

The AICPA has not considered other software products that mirror the functionality of the two exceptions (e.g., recalculating and accumulating financial data that can be significant to the financial statements). For example, a software that recomputes the present value of minimum lease payments for purposes of addressing the new lease accounting standard would seem to be very similar to a depreciation software.

Both exceptions are designed to accumulate data that can be significant to the financial statements of the attest client. Therefore, consideration should be given to either expanding the list to include other ancillary software or creating a broader definition to capture exceptions such as "all ancillary software or Excel templates that are not the client's primary financial information system (e.g., not the primary general ledger accounting software).

### **Assessing Management Participant and Self Review Threats to Independence**

The AICPA has often afforded the member the opportunity to assess threats to its independence as well as ways to mitigate those threats.

Members can effectively mitigate the self-review threat to its independence by not relying on the software when it audits areas such as fixed assets, taxes, or leases, essentially providing the same level of audit work and evidence that it would achieve through sampling and testing performed as if the calculations were generated by any other information system.

Members can effectively mitigate the management participation threat to independence by ensuring that the individual who oversees the work performed by the member is competent and able to understand and accept responsibility for it, and provides representation to that effect to the member.

The AICPA has always taken the position that members have critical knowledge and expertise to share with their attest client and should do so as long that the threats are mitigated.

### **Management Approvals within Software Products**

Some members have designed ancillary software that would greatly enhance the value provided to the attest client through structured decision tree guidance and calculation templates. Some have incorporated within the ancillary software or template certain definitive actions that are required to be taken by management such as signoffs and approvals of transactions, calculations, reports, and journal entries. Additionally, where guidance calls for management assumptions or input, ancillary software can require the input of management assumptions before they can move to the next stage for information processing and data accumulation. Whereas one can argue that the member may be assisting with the design of controls and processing of data within a software product, we believe that this view is myopic in that it doesn't take into consideration that software often has built-in approvals where management accepts responsibility for the controls, processes, calculations and reports at critical points in the processing of data. Affirmative actions taken by management afford members of management the opportunity to purposefully and formally document their understanding of the controls and processes as well as document their acceptance and approval of the assumptions, calculations, reports, journal entries, etc.

### **Recommendation to Focus on the Primary Financial Information System**

Rather than providing exceptions for specific applications, we encourage you to consider a modification to the definition of a financial information system. The definition should permit a member to design a financial information system that accumulates data but does not serve as the attest client's primary financial information system or effectuate journal entries in a client's primary accounting system without the approval of the client.

Ancillary or secondary software applications generally pertain to specific areas (e.g., fixed assets, taxes, leases, etc.) that can, and generally do, affect financial statements. However, a member can effectively mitigate threats to independence while providing expertise to the client in line with the AICPA's prerogative of encouraging the sharing of member's knowledge and intellect while allowing for management to oversee the work, documentation of competencies of the individual overseeing the work and management taking responsibility for it and representing as such to the member.

## **Non-financial Customizations to Commercial Off-the-Shelf (COTS) Financial Information Systems**

If it is determined that a modification to the definition of a financial information system is not in order, we would encourage the PEEC to revise the guidance to address the impact of non-financial modifications/customizations to COTS Financial Information Systems. If a member were to modify/customize an attest client's data within a COTS financial information system software solution, threats to compliance with the "Independence Rule" may be reduced to an acceptable level by the application of safeguards.

As examples:

- An attest client asks the member to modify information tracked in the inventory item file of the COTS Financial Information System by adding fields to track color and size of its shoe inventory. Does this modification impair the member's independence?
- If a member, at the attest client's request, added a field to track a vendor's alternate email address in the same COTS solution that aggregates data underlying the financial statements, would the member's independence be impaired?

In the examples above, assume that the COTS solution is used to process accounts payable and also generate the financial statements. Clearly, these modifications have no impact on the financial statements or financial reporting process as a whole. However, as the drafted, we are interpreting that these modifications to COTS financial information system would impair the member's independence.

### **Clarification Regarding the Aggregation of Source Data**

The interpretation concludes that when the information system aggregates source data underlying the financial statements, **or** generates information that is significant to the financial statements or financial processes as a whole, the system is considered a financial information system. If PEEC does not reconsider and eliminate the aggregation of source data portion of the defining criteria, PEEC should provide specific examples of financial information systems that do not aggregate source data to provide clarity to members on what would be acceptable.

### **Timeline and Impact of This ED on Prior Conclusions Reached**

If the ED is adopted as proposed, we believe an extended period of time would be needed to implement the guidance, as many firms will need to evaluate the impact of the interpretation on their existing attest clients.

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Additionally, there may be situations where determinations were made that independence was not impaired because threats were mitigated under previous guidance, but under the newly clarified Interpretation, a different conclusion that impairment exists could be reached. Members that acted in good faith by following the threat mitigation documentation in previous guidance could now likely conclude that their independence is impaired under this ED. This would cause undue burden on the member.

Overall, our firm understands the need for this exposure draft, but believes that it will create additional burdens for firms with a technology practice. The direction of the industry is changing rapidly, as documented in the June 2018 edition of the "Journal of Accountancy." This issue has several articles which speak to technology changing the accounting profession, and while we believe new rules and guidance are needed to adhere to independence with technology advancements, we feel this exposure draft is short sighted and conflicts with the direction of the industry.

We appreciate the opportunity to provide comments on "Information System Services" exposure draft of Mary 15, 2018. We would be happy to discuss in greater detail if you have any questions.

Very truly yours,

*Schneider Downs & Co., Inc.*

Certified Public Accountants

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