



PROFESSIONAL ETHICS EXECUTIVE COMMITTEE

Open Meeting Agenda

**November 7, 2018
Durham, NC**



**AICPA Professional Ethics Executive Committee
Open Agenda
November 7, 2018
Durham, NC**

Open Meeting: Phone Access: +1 669 900 6833 (US Toll) or +1 646 876 9923 (US Toll)
Meeting ID: 281 188 088 **Web Access:** <https://aicpa.zoom.us/j/281188088>
International numbers available: <https://zoom.us/u/aexwi71EqO>

November 7 th	<i>Open Meeting Begins</i>	
9:00 a.m. – 9:10 a.m.	Welcome Mr. Burke will welcome the Committee members and discuss administrative matters.	
9:10 a.m. – 10:30 a.m.	Leases Ms. Snyder and Mr. Mercer will request the Committee's approval to adopt the revised proposal. ❖ External Link – Leases Exposure Draft ❖ External Link – Comment Letters	Agenda Item 1A Agenda Item 1B Agenda Item 1C Agenda Item 1D Agenda Item 1E
10:30 a.m. – 10:45 a.m.	<i>Break</i>	
10:45 a.m. – 11:30 a.m.	Disclosing Client Information In Connection With A Quality Review Mr. Mercer will request that the Committee consider commenters' suggested revisions and approve adoption of the revised proposal. ❖ External Link: Exposure Draft ❖ External Link: Comment Letters	Agenda Item 2A Agenda Item 2B Agenda Item 2C Agenda Item 2D
11:30 a.m. – 12:30 p.m.	Information Technology and Cloud Services Ms. Miller and Ms. Gorla will provide the Committee with a summary of the responses received on the Information System Services exposure draft and seek the Committee's direction on the Task Force's preliminary way forward. ❖ External Link – Information Systems Services Exposure Draft ❖ External Link – Comment Letters	Agenda Item 3A Agenda Item 3B Agenda Item 3C Agenda Item 3D Agenda Item 3E
12:30 p.m. – 1:30 p.m.	<i>Lunch</i>	
1:30 p.m. – 2:30 p.m.	Staff Augmentation Ms. Snyder and Mr. Mercer will request that the Committee approve exposure of the Task Force's revised proposal for comment.	Agenda Item 4A Agenda Item 4B Agenda Item 4C

2:30 p.m. – 3:30 p.m.	State and Local Government Ms. Miller and Ms. Gorla will seek the Committee's feedback on the Task Force's proposed revisions. <ul style="list-style-type: none"> ❖ External Link – SLG Exposure Draft ❖ External Link – Comment Letters 	Agenda Item 5A Agenda Item 5B.1 Agenda Item 5B.2 Agenda Item 5C Agenda Item 5D
3:30 p.m. – 3:45 p.m.	<i>Break</i>	
3:45 p.m. – 4:00 p.m.	IESBA Update Ms. Gorla will update the Committee on recent IESBA activity.	
4:00 p.m. – 4:15 p.m.	NOCLAR Mr. Denham will update the Committee on the Task Force's progress. <ul style="list-style-type: none"> ❖ External Link – NOCLAR Exposure Draft ❖ External Link – Comment Letters 	
4:15 p.m. – 4:55 p.m.	External Board of Directors of Firms Mr. McKeown will update the Committee on the Task Force's direction and request feedback.	Agenda Item 6A
4:55 p.m. – 5:00 p.m.	Minutes of the Professional Ethics Executive Committee Open Meeting The Committee is asked to approve the minutes from the August 2018 open meeting.	Agenda Item 7
	<i>Open Meeting Concludes</i>	
Informational Purposes Only	Other Outstanding Exposure Drafts and Other Items <ul style="list-style-type: none"> ❖ External Link – Technical Correction 	
Informational Purposes Only	Committee Project Agenda <ul style="list-style-type: none"> ❖ External Link - Project Agenda 	
	Future Meeting Dates <ul style="list-style-type: none"> • February 12-13th, 2019 – New Orleans • May 2019 – TBD • July/August 2019 – TBD 	

**Professional Ethics Executive Committee
Leases Task Force**

Task Force Members

Lisa Snyder (Chair), Bill Mann, Chris Cahill, Nancy Miller, David East, Brian Lynch
Staff: Brandon Mercer

Task Force Charge

Revise the independence guidance based upon the revised accounting standards on leases issued by the Financial Accounting Standards Board (FASB).

Reason for Agenda Item

The purpose of the agenda item is to obtain PEEC approval of suggested revisions to the exposed standard. The Task Force requests that PEEC approve the revised standards at **Agenda Item 1B** for adoption.

Background

The AICPA received seven (7) comment letters on the Leases Exposure Draft. The Task Force held two conference calls in March and April to discuss the comment letters. At the May 2018 PEEC meeting, the Task Force requested feedback on some possible revisions pursuant to the comments and Task Force discussions. The Task Force held two conference calls in June 2018 to address the feedback received from PEEC and to make revisions to the proposed standard. At the August PEEC meeting, additional revisions were made and the Task Force was instructed to address the remaining open issues and distribute a revised standard to the Committee for input. The Task Force held a conference call on October 2, 2018 and distributed a draft to PEEC for preliminary input via email on October 5, 2018. The Task Force's suggested revisions are presented in this agenda item and at **Agenda Item 1B**.

Summary of Issues**Applicability and Structure of Paragraphs .02 - .04**

At the August 2018 PEEC meeting, the Committee discussed the applicability of the provisions and safeguards in paragraphs .02 and .03, and made various revisions to the structure of the Task Force's revised proposal as a result of the discussions. Specifically:

- Paragraph .02 addresses leases of a specific subset of covered members that enter a lease during the period of professional engagement. The paragraph was restructured to clarify that the requirements of market terms, arm's length, and materiality are applicable at entry. In contrast, the requirement that payments be made in compliance with the lease terms was separated from the list and clarified to only be applicable once the lease has been entered into. This resolved the confusion surrounding the timing of the application of safeguards.

- Paragraph .03 was revised to address existing leases of the same specific subset of covered members as addressed in paragraph .02. Existing leases include those leases that were entered into prior to an event that made independence a requirement, which were previously addressed at paragraph .04 of the proposal (Grandfathering paragraph). As a result of the change, paragraph .04 was considered unnecessary and was removed from the proposal.
- Paragraph .03 was also revised to address leases that are immaterial at entry, but due to a change in circumstances, the leases becomes material after the lease was entered or renegotiated.
- All other leases that are not specifically addressed in paragraphs .02 and .03, including those outside the specific subset of covered members, would be subject to the Conceptual Framework. The Independence Rule requires that members use the Conceptual Framework to evaluate situations that are not specifically addressed in the rules and interpretations; PEEC agreed that this approach was appropriate for these other leases.

Action Needed:

The Task Force requests that PEEC review the revisions to the proposed standard presented at Agenda Item 1B, and approve the proposal for adoption.

Revision to the “Client Affiliates” Interpretation [1.224]

PEEC discussed the proposed revision to the “Affiliates” interpretation [1.224] which proposed granting relief to covered members who have a lease with certain affiliates of the attest client. The Task Force, based upon revisions made to the Leases proposal, has revised the provisions related to affiliates and proposes that PEEC adopt the revision to paragraph .02 of the “Affiliates” interpretation as presented below and at Agenda Item 1B. The revision stipulates that the specific subset of covered members addressed by the Leases interpretation may have leases with certain sister and parent affiliates that do not comply with the Leases interpretation. However, the member should use the Conceptual Framework to evaluate whether any threats created by the lease are at an acceptable level:

.02 When a client is a financial statement attest client, members should apply the “Independence Rule” [1.200.001] and related interpretations applicable to the financial statement attest client to their affiliates, except in the following situations:

e. A covered member who is an individual on the attest engagement team, an individual in a position to influence the attest engagement, or the firm may have a lease which does not meet the requirements of the “Leases” interpretation [1.260.040] of the “Independence Rule” [1.200.001] with an entity described under items c-l of the definition of affiliate during the

period of the professional engagement. The covered member should use the “Conceptual Framework for Independence” interpretation [ET sec. 1.210.010] to evaluate whether any threats created by the lease are at an acceptable level. If the covered member concludes that threats are not at an acceptable level, the covered member should apply safeguards to eliminate the threats or reduce them to an acceptable level.

Items c-l of the definition of “Affiliate” which are subject to the proposed revision above are as follows:

- c. An entity (for example, parent, partnership, or LLC) that controls a financial statement attest client when the financial statement attest client is material to such entity.
- d. An entity with a direct financial interest in the financial statement attest client when that entity has significant influence over the financial statement attest client, and the interest in the financial statement attest client is material to such entity.
- e. A sister entity of a financial statement attest client if the financial statement attest client and sister entity are each material to the entity that controls both.
- f. A trustee that is deemed to control a trust financial statement attest client that is not an investment company.
- g. The sponsor of a single employer employee benefit plan financial statement attest client.
- h. Any entity, such as a union, participating employer, or a group association of employers, that has significant influence over a multiemployer employee benefit plan financial statement attest client and the plan is material to such entity.
- i. The participating employer that is the plan administrator of a multiple employer employee benefit plan financial statement attest client.
- j. A single or multiple employer employee benefit plan sponsored by either a financial statement attest client or an entity controlled by the financial statement attest client. All participating employers of a multiple employer employee benefit plan are considered sponsors of the plan.
- k. A multiemployer employee benefit plan when a financial statement attest client or entity controlled by the financial statement attest client has significant influence over the plan and the plan is material to the financial statement attest client.
- l. An investment adviser, a general partner, or a trustee of an investment company financial statement attest client (fund) if the fund is material to the investment adviser, general partner, or trustee that is deemed to have either control or significant influence over the fund. When considering materiality, members should consider investments in, and fees received from, the fund.

Action Needed:

The Task Force requests that PEEC review the Task Force’s suggested revisions to the “Client Affiliates” interpretation [1.224] at Agenda Item 1B and approve the proposed revisions for adoption.

Effective Date

Some commenters requested a one-year delay in the effective date in order to allow firms to implement appropriate identification, evaluation, and monitoring procedures. The Task Force noted that the effective date of the proposal should be revised to “fiscal years beginning after” December 15, 2019 to allow members and clients the time to implement and further align with the FASB standard effective date. This revision is reflected at **Agenda Item 1B**.

Action Needed:

Does PEEC agree with the effective date of “fiscal years beginning after December 15, 2019?”

Action Needed

Staff requests that PEEC discuss the suggested revisions above and approve the proposed standard for adoption.

Materials Presented

Agenda Item 1B: Revisions to the Exposure Draft

Agenda Item 1C: Comment Letter Summary – General Comments

Agenda Item 1D: Comment Letter Summary – Response to Questions from Exposure Draft

Agenda Item 1E: Exposed Proposal

Revised Proposal – Revised “Leases” Interpretation and “Client Affiliates” Interpretation

[Changes to the exposed proposal are shown. Additions appear in **boldface underline** and deletions are struck through.]

1.260.040 Leases

- .01 When a *covered member* enters into **or has** a lease with an *attest client*, self-interest, familiarity, and undue influence *threats* to the *covered member's* compliance with the “Independence Rule” [1.200.001] may exist.

~~This paragraph excludes leases addressed by paragraph .04 of the “Loans and Leases With Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001].~~

New or Renegotiated Leases

- .02 If a *covered member* **who is an individual on the attest engagement team, an individual in a position to influence the attest engagement, or the firm** enters into a lease **or renegotiates terms of an existing lease** with an *attest client* during the *period of the professional engagement*, threats to compliance with the “Independence Rule” [1.200.001] 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*, unless all of the following *safeguards* are met **at the time of entering into or renegotiating the lease** during that period:

- a. The lease is ~~entered into~~ on market terms and established at arm's length.
- b. ~~All amounts are paid in accordance with the lease terms or provisions.~~
- c. The lease is not material to any of the following parties to the lease: **When evaluating materiality, all leases between the parties should be considered, both individually and in the aggregate.**
 - i. ~~The firm;~~
 - ii. ~~An individual participating on the attest engagement team;~~
 - iii. ~~An individual in a position to influence the attest engagement;~~
 - iv. ~~The attest client.~~

Once the covered member enters into or renegotiates the lease, threats to the covered member's compliance with the “Independence Rule” [1.200.001] 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 if the lease amounts are not paid in accordance with the lease terms or provisions by the due date or within any available grace periods, during the period of the professional engagement.

Existing Leases

.03 If the a covered member who is an individual on the attest engagement team, an individual in a position to influence the attest engagement, or the firm has a lease with an attest client that was: ~~meets the safeguards in paragraph .02, as applicable,~~

- a. Entered into or renegotiated prior to the:
 - i. period of the professional engagement,
 - ii. member becoming a covered member, or
 - iii. counterparty becoming an attest client or an affiliate of a financial statement attest client,

or

- b. Entered into or renegotiated during the period of the professional engagement, in compliance with paragraph .02, but, due to a change in circumstances after the lease is entered into or renegotiated, the lease becomes material to any party to the lease during the period of the professional engagement,

the *covered member* should evaluate the significance of any ~~other threats~~ to determine whether the *threats* are at an *acceptable level*. If the *covered member* determines that *threats* are not at an *acceptable level*, the *covered member* should apply ~~additional safeguards~~ to eliminate or reduce the *threats* to an *acceptable level*. If no *safeguards* are available to eliminate or reduce *threats* to an *acceptable level*, *independence* would be *impaired*.

The significance of the *threats* will depend on factors such as the following:

- a. The role of the *covered member* on the *attest engagement* or with the *firm*,
- b. The materiality of the lease to the *covered member* or the attest client during the period of the professional engagement, ~~other than those covered members identified in paragraph .02~~
- c. Whether multiple leases exist ~~are entered into~~ with the *attest client* and, if so, the aggregate materiality of those leases to the *covered member* or the *attest client*,
- d. The extent to which the lease will be subject to attest procedures or financial statement disclosures,
- e. The duration of the lease term, and
- f. Whether the lease is on market terms or established at arm's length.

However, threats to compliance with the "Independence Rule" [1.200.001] 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, if the lease amounts are not paid in accordance with the lease terms or provisions by the due date or within any available grace periods, during the period of the professional engagement.

Grandfathered Leases

~~.04 Irrespective of materiality, threats to compliance with the "Independence Rule" [1.200.001] would be at an acceptable level and independence would not be impaired provided that the lease is entered into on market terms and established at arm's length, and during the period of professional engagement all amounts are paid in accordance~~

~~with the lease terms and provisions, the terms do not change in any manner not provided for in the original lease, and any of the following conditions are met:~~

- ~~g. The *covered member* entered into the lease with the *attest client* prior to becoming a *covered member* with respect to the *attest client*.~~
- ~~h. The *covered member* entered into the lease with a counterparty for which *independence* was not required, and that counterparty to the lease later becomes, acquires, or is acquired by an *attest client*.~~
- ~~i. The *attest client* entered into the lease with a counterparty which was not required to be independent of the *attest client*, and that counterparty to the lease later acquires or is acquired by the *covered member*.~~
- ~~j. The lease existed prior to December 15, 2019 and the lease was permitted under the preexisting requirements of the “Independence Rule” [1.200.001] and its interpretations.~~

~~Automatic renewals provided for in the original lease are not considered changes in terms for purposes of this interpretation.~~

~~Covered Member Leases Primary Residence from Attest Client~~

~~.05 Irrespective of materiality, if a *covered member* leases his or her primary residence from a lessor *attest client*, *threats* to compliance with the “Independence Rule” [1.200.001] would be at an *acceptable level* and *independence* would not be *impaired*, provided the *covered member* complies with the provisions in paragraph .04.~~

.04 This interpretation excludes leases addressed by [paragraph .04](#) of the “Loans and Leases with Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001].

.05 **Refer to the “Client Affiliates” interpretation [1.224.010] of the “Independence Rule” [1.200.001] for additional guidance on leases held with certain affiliates of a financial statement attest client. [Prior reference: paragraph .17 of ET section 101]**

.06 This interpretation is effective **for fiscal years beginning after** December 15, 2019, with early implementation allowed.

1.224.010 Client Affiliates

.01 *Financial interests in, and other relationships with, affiliates of a financial statement attest client may create threats to a member's compliance with the "[Independence Rule](#)" [1.200.001].*

.02 *When a client is a financial statement attest client, members should apply the "[Independence Rule](#)" [1.200.001] and related interpretations applicable to the financial statement attest client to their affiliates, except in the following situations:*

a. A covered member may have a loan to or from an individual who is an officer, a director, or a 10 percent or more owner of an affiliate of a financial statement attest client during the period of the professional engagement unless the covered member knows or has reason to believe that the individual is in such a position with the affiliate. If the covered member knows or has reason to believe that the individual is an officer, a director, or a 10 percent or more owner of the affiliate, the covered member should evaluate the effect that the relationship would have on the covered member's independence by applying the "[Conceptual Framework for Independence](#)" [1.210.010].

b. A member or the member's firm may provide prohibited nonattest services to entities described under items c–l of the definition of affiliate during the period of the professional engagement or during the period covered by the financial statements, provided that it is reasonable to conclude that the services do not create a self-review threat with respect to the financial statement attest client because the results of the nonattest services will not be subject to financial statement attest procedures. For any other threats that are created by the provision of the nonattest services that are not at an acceptable level (in particular, those relating to management participation), the member should apply safeguards to eliminate or reduce the threats to an acceptable level.

c. A firm will only have to apply the "[Subsequent Employment or Association With an Attest Client](#)" interpretation [1.279.020] of the "Independence Rule" if the former employee, by virtue of his or her employment at an entity described under items c–l of the definition of affiliate, is in a key position with respect to the financial statement attest client. Individuals in a position to influence the attest engagement and on the attest engagement team who are considering employment with an affiliate of a financial statement attest client will still need to report consideration of employment to an appropriate person in the firm and remove themselves from the financial statement attest engagement, even if the position with the affiliate is not a key position.

d. A covered member's immediate family members and close relatives may be employed in a key position at an entity described under items c–l of the definition of affiliate during the period of the professional engagement or during the period covered

by the *financial statements*, provided they are not in a *key position* with respect to the *financial statement attest client*.

e. A covered member who is an individual on the attest engagement team, an individual in a position to influence the attest engagement, or the firm may have a lease which does not meet the requirements of the “Leases” interpretation [1.260.040] of the “Independence Rule” [1.200.001] with an entity described under items c-I of the definition of *affiliate* during the *period of the professional engagement*. The covered member should use the “Conceptual Framework for Independence” interpretation [ET sec. 1.210.010] to evaluate whether any *threats* created by the lease are at an *acceptable level*. If the covered member concludes that *threats* are not at an *acceptable level*, the covered member should apply *safeguards* to eliminate the *threats* or reduce them to an *acceptable level*.

.03 A member must expend best efforts to obtain the information necessary to identify the *affiliates* of a *financial statement attest client*. If, after expending best efforts, a member is unable to obtain the information to determine which entities are *affiliates* of a *financial statement attest client*, *threats* would be at an *acceptable level* and *independence* would not be *impaired* if the member (a) discusses the matter, including the potential impact on *independence*, with *those charged with governance*; (b) documents the results of that discussion and the efforts taken to obtain the information; and (c) obtains written assurance from the *financial statement attest client* that it is unable to provide the member with the information necessary to identify the *affiliates* of the *financial statement attest client*.

.04 This interpretation does not apply to a *financial statement attest client* that is covered by the “[Entities Included in State and Local Government Financial Statements](#)” interpretation [1.224.020] of the “Independence Rule” [1.200.001]. [Prior reference: paragraph .20 of ET section 101]

Acquisitions and Other Business Combinations That Involve a Financial Statement Attest Client

.05 The exception in [paragraph .06](#) would apply when (1) a *financial statement attest client* is acquired during the *period of the professional engagement* by either a non-client or a nonattest client (acquirer), (2) the *attest engagement* covers only periods prior to the acquisition, and (3) the member or member’s firm will not continue to provide *financial statement attest services* to the acquirer.

.06 *Independence* will not be considered *impaired* with respect to the *financial statement attest client* because a member or member’s firm has an interest in or relationship with the acquirer that may otherwise *impair independence* as a result of the requirements of this interpretation or the definition of “*attest client*” (as it relates to the entity or person that engages the member or member’s firm to perform the *attest engagement*).

.07 Notwithstanding [paragraph .06](#), a member should give consideration to the requirements of the “[Conflicts of Interest](#)” interpretation [1.110.010], under the “Integrity and

Objectivity Rule” [1.100.001], with regard to any relationships that the *member* knows or has reason to believe exist with the acquirer, the *financial statement attest client*, or the *firm*.

.08 A *member* should refer to [paragraph .03](#) of “Application of the AICPA Code” [0.200.020] for guidance on circumstances involving foreign network firms.

Effective Date

.09 [Paragraphs .01–.04](#) are effective for engagements covering periods beginning on or after January 1, 2014. Early implementation is allowed.

[See [Revision History Table](#).]

Nonauthoritative questions and answers regarding the application of the independence rules to affiliates of employee benefit plans are available at <http://www.aicpa.org/interestareas/professionalethics/resources/tools/downloadabledocuments/faqs-application-independence-rules-affiliates-of-employee-benefit-plans.pdf>.

Final Version – Revised “Leases” Interpretation and “Client Affiliates” Interpretation

1.260.040 Leases

- .01 When a *covered member* enters into or has a lease with an *attest client*, self-interest, familiarity, and undue influence *threats* to the *covered member's* compliance with the “Independence Rule” [1.200.001] may exist.

New or Renegotiated Leases

- .02 If a *covered member* who is an individual on the attest engagement team, an individual in a position to influence the attest engagement, or the firm enters into a lease or renegotiates terms of an existing lease with an *attest client* during the *period of the professional engagement*, threats to compliance with the “Independence Rule” [1.200.001] 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*, unless all of the following *safeguards* are met at the time of entering into or renegotiating the lease:
- a. The lease is on market terms and established at arm's length.
 - b. The lease is not material to any of the parties to the lease. When evaluating materiality, all leases between the parties should be considered, both individually and in the aggregate.

Once the covered member enters into or renegotiates the lease, threats to the covered member's compliance with the “Independence Rule” [1.200.001] 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 if the lease amounts are not paid in accordance with the lease terms or provisions by the due date or within any available grace periods, during the period of the professional engagement.

Existing Leases

- .03 If a *covered member* who is an individual on the attest engagement team, an individual in a position to influence the attest engagement, or the firm has a lease with an attest client that was:
- a. Entered into or renegotiated prior to the –
 - i. period of the professional engagement,
 - ii. member becoming a covered member, or
 - iii. counterparty becoming an attest client or an affiliate of a financial statement attest client,
 - or
 - b. Entered into or renegotiated during the period of the professional engagement, in compliance with paragraph .02, but, due to a change in circumstances after the lease is entered into or renegotiated, the lease becomes material to any party to the lease during the period of the professional engagement,

the *covered member* should evaluate the significance of any *threats* to determine whether the *threats* are at an *acceptable level*. If the *covered member* determines that *threats* are not at an *acceptable level*, the *covered member* should apply *safeguards* to eliminate or reduce the *threats* to an *acceptable level*. If no *safeguards* are available to eliminate or reduce *threats* to an *acceptable level*, *independence* would be *impaired*.

The significance of the *threats* will depend on factors such as the following:

- a. The role of the *covered member* on the *attest engagement* or with the *firm*,
- b. The materiality of the lease to the *covered member* or the attest client during the period of the professional engagement,
- c. Whether multiple leases exist with the *attest client* and, if so, the aggregate materiality of those leases to the *covered member* or the *attest client*,
- d. The extent to which the lease will be subject to attest procedures or financial statement disclosures,
- e. The duration of the lease term, and
- f. Whether the lease is on market terms or established at arm's length.

However, threats to compliance with the "Independence Rule" [1.200.001] 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, if the lease amounts are not paid in accordance with the lease terms or provisions by the due date or within any available grace periods, during the period of the professional engagement.

- .04 This interpretation excludes leases addressed by [paragraph .04](#) of the "Loans and Leases with Lending Institutions" interpretation [1.260.020] of the "Independence Rule" [1.200.001].
- .05 Refer to the "Client Affiliates" interpretation [1.224.010] of the "Independence Rule" [1.200.001] for additional guidance on leases held with certain affiliates of a financial statement attest client. [Prior reference: paragraph .17 of ET section 101]
- .06 This interpretation is effective for fiscal years beginning after December 15, 2019, with early implementation allowed.

1.224.010 Client Affiliates

.01 *Financial interests in, and other relationships with, affiliates of a financial statement attest client may create threats to a member's compliance with the ["Independence Rule"](#) [1.200.001].*

.02 *When a client is a financial statement attest client, members should apply the ["Independence Rule"](#) [1.200.001] and related interpretations applicable to the financial statement attest client to their affiliates, except in the following situations:*

a. A covered member may have a loan to or from an individual who is an officer, a director, or a 10 percent or more owner of an affiliate of a financial statement attest client during the period of the professional engagement unless the covered member knows or has reason to believe that the individual is in such a position with the affiliate. If the covered member knows or has reason to believe that the individual is an officer, a director, or a 10 percent or more owner of the affiliate, the covered member should evaluate the effect that the relationship would have on the covered member's independence by applying the ["Conceptual Framework for Independence"](#) [1.210.010].

b. A member or the member's firm may provide prohibited nonattest services to entities described under items c–l of the definition of affiliate during the period of the professional engagement or during the period covered by the financial statements, provided that it is reasonable to conclude that the services do not create a self-review threat with respect to the financial statement attest client because the results of the nonattest services will not be subject to financial statement attest procedures. For any other threats that are created by the provision of the nonattest services that are not at an acceptable level (in particular, those relating to management participation), the member should apply safeguards to eliminate or reduce the threats to an acceptable level.

c. A firm will only have to apply the ["Subsequent Employment or Association With an Attest Client"](#) interpretation [1.279.020] of the "Independence Rule" if the former employee, by virtue of his or her employment at an entity described under items c–l of the definition of affiliate, is in a key position with respect to the financial statement attest client. Individuals in a position to influence the attest engagement and on the attest engagement team who are considering employment with an affiliate of a financial statement attest client will still need to report consideration of employment to an appropriate person in the firm and remove themselves from the financial statement attest engagement, even if the position with the affiliate is not a key position.

d. A covered member's immediate family members and close relatives may be employed in a key position at an entity described under items c–l of the definition of affiliate during the period of the professional engagement or during the period covered

by the *financial statements*, provided they are not in a *key position* with respect to the *financial statement attest client*.

e. A *covered member* who is an individual on the attest engagement team, an *individual in a position to influence the attest engagement*, or the *firm* may have a lease which does not meet the requirements of the “Leases” interpretation [1.260.040] of the “Independence Rule” [1.200.001] with an entity described under items c-l of the definition of *affiliate* during the *period of the professional engagement*. The *covered member* should use the “Conceptual Framework for Independence” interpretation [ET sec. 1.210.010] to evaluate whether any *threats* created by the lease are at an *acceptable level*. If the *covered member* concludes that *threats* are not at an *acceptable level*, the *covered member* should apply *safeguards* to eliminate the *threats* or reduce them to an *acceptable level*.

.03 A *member* must expend best efforts to obtain the information necessary to identify the *affiliates* of a *financial statement attest client*. If, after expending best efforts, a *member* is unable to obtain the information to determine which entities are *affiliates* of a *financial statement attest client*, *threats* would be at an *acceptable level* and *independence* would not be *impaired* if the *member* (a) discusses the matter, including the potential impact on *independence*, with *those charged with governance*; (b) documents the results of that discussion and the efforts taken to obtain the information; and (c) obtains written assurance from the *financial statement attest client* that it is unable to provide the *member* with the information necessary to identify the *affiliates* of the *financial statement attest client*.

.04 This interpretation does not apply to a *financial statement attest client* that is covered by the “[Entities Included in State and Local Government Financial Statements](#)” interpretation [1.224.020] of the “Independence Rule” [1.200.001]. [Prior reference: paragraph .20 of ET section 101]

Acquisitions and Other Business Combinations That Involve a Financial Statement Attest Client

.05 The exception in [paragraph .06](#) would apply when (1) a *financial statement attest client* is acquired during the *period of the professional engagement* by either a non-client or a nonattest client (acquirer), (2) the *attest engagement* covers only periods prior to the acquisition, and (3) the *member* or *member’s firm* will not continue to provide *financial statement attest services* to the acquirer.

.06 *Independence* will not be considered *impaired* with respect to the *financial statement attest client* because a *member* or *member’s firm* has an interest in or relationship with the acquirer that may otherwise *impair independence* as a result of the requirements of this interpretation or the definition of “*attest client*” (as it relates to the entity or person that engages the *member* or *member’s firm* to perform the *attest engagement*).

.07 Notwithstanding [paragraph .06](#), a *member* should give consideration to the requirements of the “[Conflicts of Interest](#)” interpretation [1.110.010], under the “Integrity and

Objectivity Rule” [1.100.001], with regard to any relationships that the *member* knows or has reason to believe exist with the acquirer, the *financial statement attest client*, or the *firm*.

.08 A *member* should refer to [paragraph .03](#) of “Application of the AICPA Code” [0.200.020] for guidance on circumstances involving foreign network firms.

Effective Date

.09 [Paragraphs .01–.04](#) are effective for engagements covering periods beginning on or after January 1, 2014. Early implementation is allowed.

[See [Revision History Table](#).]

Nonauthoritative questions and answers regarding the application of the independence rules to affiliates of employee benefit plans are available at <http://www.aicpa.org/interestareas/professionalethics/resources/tools/downloadabledocuments/faqs-application-independence-rules-affiliates-of-employee-benefit-plans.pdf>.

COMMENT SUMMARY
PROPOSED Revised “Leases” interpretation of the “Independence Rule”

Comment Letter		Feedback Highlights	Task Force Response
CL 1	AICPA Technical Issues Committee (TIC) Support	General Comments <ul style="list-style-type: none"> TIC believes that the specific identification of familiarity and undue influence threats in paragraph 01 of the ED should be removed; TIC believes that these would not be significant threats. TIC also notes that ET sec 1.260.020, Loans and Leases with Lending Institutions, only identifies self-interest as a threat. TIC believes this is appropriate. The ED does a very good job of conforming ET sec 1.260.040 with 1.260.020 except for the references to familiarity and undue influence threats, which based on the definitions, would not be significant threats. 	The Task Force and PEEC previously discussed the identification of threats at length and determined that familiarity and undue influence threats would exist to the point which they should be addressed by safeguards. PEEC believed that entry of the lease could be influenced by both threats, hence the safeguard of market terms established at arm's length.
CL 2	NASBA Support	General Comments <ul style="list-style-type: none"> In comparing the proposed revisions to the existing loan interpretation (1.260.020), we noted that the loan interpretation includes a fundamental safeguard that is absent from this proposal, i.e., the Code only permits loans to a covered member from an attest client if the attest client makes loans as part of its normal business operations. We understand the PEEC considered this fact and concluded that because real estate investment trusts, which are not lending institutions, frequently issue real estate leases, the addition would not be appropriate. However, we also note that the current definition of “lending institution” does incorporate automobile lessors. Thus, for consistency purposes and 	PEEC and the Task Force determined that leases are in many cases with non-lending institutions or individuals, especially in smaller geographical areas and in real estate.

Comment Letter	Feedback Highlights	Task Force Response
	<p>to significantly strengthen the proposed leases interpretation, we suggest that PEEC consider whether a similar notion pertaining to lessors more broadly should be incorporated into this standard as a fundamental safeguard.</p> <ul style="list-style-type: none"> • <i>Lending institution. An entity that, as part of its normal business operations, makes loans.</i> This definition is not meant to include an organization that might schedule payment for services for a client over a period of time. Examples of such entities are banks, credit unions, certain retailers, and insurance and finance companies. For example, for automobile leases addressed by the “Loans and Leases with Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001], an entity is considered a lending institution if it leases automobiles as part of its normal business operations. [Prior reference: paragraph .09 of ET section 92] 	
<p>CL 3</p> <p>KPMG Support</p>	<p>General Comments</p> <ul style="list-style-type: none"> • We recommend that PEEC consider an exemption...for short-term leases such as short-term rental properties, car rentals, and technology rentals. Self-interest, familiarity, and undue influence threats related to such leases are low because of the brief duration of the lease. The burden on the firm and covered member to track such leases could be prohibitively high with respect to the low level of threats to independence resulting from short-term leases. We believe that a reasonable lease term to qualify for the exemption would be a term not to exceed thirty days. In order to qualify for the short-term lease exclusion, the lease should not have a renewal option that extends the rental period beyond the period defined as short-term. We 	<p>The Task Force had concerns around how to set a standard for what defines short term, but agreed that a conceptual framework approach may be more appropriate for such short term leases. The duration of the lease term was added to the proposal as a factor for members to consider when evaluating the threat to independence.</p>

Comment Letter	Feedback Highlights	Task Force Response
	<p>propose PEEC consider the following wording be added to paragraph .01 in order to address the comments reflected above:</p> <p><i>1.260.040.01.b</i> <i>This interpretation excludes short-term leases entered into by a covered member with an attest client, as threats to compliance with the “Independence Rule” [1.200.001] would be at an acceptable level and independence would not be impaired provided that the lease term is ## days or less, and there is no renewal or extension to the lease term beyond ## days.</i></p> <ul style="list-style-type: none"> • We believe that paragraph .06 is repetitive of the second paragraph of .01, as both discuss the exclusions around leases addressed by paragraph .04 of the “Loans and Leases with Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001]. We recommend that PEEC replace the second paragraph of paragraph .01 with paragraph .06, and remove paragraph .06. 	<p>The Task Force agrees but proposed removal of the sentence from paragraph .01.</p>
<p>CL 4</p> <p>Deloitte LLP Support</p>	<p>General Comments</p> <ul style="list-style-type: none"> • Paragraph .02 – <i>Materiality Considerations for multiple leases</i>. Paragraph .02 (c) describes materiality safeguards for the firm, individuals participating on the attest engagement team, individuals in a position to influence the attest engagement, and the attest client that must be met to be able to conclude that threats to compliance with the Independence Rule (1.200.001) are or can be reduced to an acceptable level to avoid an independence impairment. However, there is no specific guidance in paragraph .02 related to the materiality considerations for multiple leases. We request the 	<p>Language was added to paragraph .02 regarding aggregation of leases for materiality.</p>

Comment Letter	Feedback Highlights	Task Force Response
	<p>PEEC consider clarifying whether it is necessary to consider aggregate materiality for purposes of applying the paragraph .02(c) safeguards in cases where multiple leases exist between the covered member and the attest client.</p> <ul style="list-style-type: none"> Paragraph .04 – <i>Grandfathered Leases</i>. We request the PEEC consider clarification to Paragraph .04(c) which states, “The attest client entered into the lease with a counterparty which was not required to be independent of the attest client, and that counterparty to the lease later acquires or is acquired by the covered member.” The current wording is not clear. We believe the intent of this paragraph is to address situations whereby an existing attest client is party to a lease, and the counterparty to such lease, at inception, was not associated with the covered member. However, such counterparty is subsequently acquired by, or acquires the covered member (i.e., the counterparty becomes associated with the covered member, in which case the independence rules would then be applicable to that counterparty). Please clarify PEEC’s intent. In addition, the final sentence in paragraph .04 of the Proposed Interpretation states that “Automatic renewals provided for in the original lease are not considered changes in terms for purposes of this Interpretation.” We believe that addressing only this narrow aspect of a lease in the Interpretation could be read to imply that the application of other common lease terms (e.g., an election to extend a lease on a month-to-month basis at the end of its primary lease term) would be a change in terms for purposes of the Interpretation. We request that the PEEC consider broadening the scope of this sentence to indicate that the application of any provision of an original lease agreement is not considered a 	<p>Paragraph was deleted. Such leases are now subject to the Conceptual Framework approach at paragraph .03 (as revised).</p>

Comment Letter	Feedback Highlights	Task Force Response
	<p>change in terms for purposes of this Interpretation.</p> <ul style="list-style-type: none"> • <i>Paragraph .05 - Covered Member Leases Primary Residence from Attest Client.</i> In our view, paragraph .05 of the Proposed Interpretation does not provide any special exception for leases related to primary residences. Rather, it appears to serve as a reinforcement of the grandfathering provisions already included in paragraph .04 that are available for any leasing arrangement and therefore may be superfluous/unnecessary. If our understanding is correct, PEEC should consider omitting the paragraph if it does not intend to provide any specific exception for primary residence leases. As an alternative, PEEC could consider including an explicit reference to leases on primary residences as an example of leases that can be grandfathered under the provisions of paragraph .04. • <i>Decision Tree.</i> We request the PEEC consider creating a decision tree to assist practitioners in understanding the new requirements under the interpretation. Given the complexity and analysis that may be required for implementation, a decision tree would provide greater clarity and guidance to members in applying the interpretation. 	<p>Paragraph was deleted.</p> <p>Once adopted, staff will prepare a decision tree if PEEC and the Task Force agree that it would be helpful in implementation efforts.</p>
<p>CL 5 Grant Thornton Support</p>	<p>General Comments</p> <ul style="list-style-type: none"> • Grant Thornton suggests the PEEC consider providing examples or illustrations to assist in the application of the new interpretation. 	<p>Once adopted, staff will prepare examples or illustrations if PEEC and the Task Force agree that it would be helpful in implementation efforts.</p>

Comment Letter	Feedback Highlights	Task Force Response
<p>CL 6</p> <p>PwC Support</p>	<p>General Comments</p> <ul style="list-style-type: none"> • We agree with the PEEC's position that the financial statement presentation of a lease should not result in a de-facto conclusion that the lease is permissible or impermissible from an independence perspective. Regardless of whether a lease is classified as an operating or a capital lease, we believe that independence should be evaluated on the basis of the lease's effect on the auditor's objectivity and professional skepticism. However, while we support a model that doesn't default to US GAAP classification, we do have concerns regarding the approach being proposed by the PEEC. • In our view, goods and services obtained as a consumer in the ordinary course of business do not, generally, impair an auditor's objectivity or professional skepticism. The current "Leases" interpretation implicitly recognizes this by permitting covered members to enter into an operating lease with an attest client, provided that the terms and conditions set forth in the lease agreement are comparable with other leases of a similar nature, and all amounts are paid in accordance with the lease terms and provisions. • Accordingly, our overarching recommendation is for the PEEC to align more closely with the IESBA Code of Ethics for Professional Accountants by establishing a more principles-based approach that treats leases as permissible provided they are entered into in the normal course of business and on an arm's length basis. Under a principles-based approach such as this, the materiality of the lease to the covered member would be one of the factors to be considered when evaluating threats to 	<p>The Proposal requires market terms established at arm's length and payment compliance.</p> <p>PEEC did not agree that a wholesale Conceptual Framework approach was appropriate, and felt that materiality was a necessary safeguard in particular for members described in .02. As revised, PEEC has applied the Conceptual Framework approach</p>

Comment Letter	Feedback Highlights	Task Force Response
	<p>independence, rather than the automatic trigger for an independence impairment as is being proposed. Because of the pervasive use of leasing arrangements to acquire a wide range of consumer goods, this approach would also help to mitigate the potential for any undue burden or hardship that a bright-line test might otherwise create. It would also ensure consistency with the current treatment of automobile leases in the Code of Conduct, which takes the preferred approach of exempting such transactions from the prohibition on loans without regard to materiality. Appendix A expands on the principal suggestion described above, and also offers detailed comments and recommendations regarding other areas of the proposal.</p>	<p>to all leases not held by the covered members specified in .02. Leases not specifically addressed by the interpretation are subject to the Conceptual Framework.</p>
<p>CL 7</p> <p>EY Support</p>	<p>General Comments</p> <p>We are supportive of PEEC's Proposed Revision that prescribes a conceptual framework to evaluate threats and safeguards to independence arising from leases between attest clients and covered members. We believe that the approach of evaluating lease transactions similar to the evaluation required for other business relationships is the most appropriate approach and consistent with other regulatory schemes. Fundamentally, lease transactions are procurement transactions whereby the lessee is contracting for the right to use an asset for a period of time. While the Code generally permits procurement by the member from attest clients, we agree that the typical terms of a lease arrangement often results in additional independence threats, thus requiring an additional evaluation of threats and safeguards that are generally not needed for typical, one-off procurement transactions. While we are generally supportive, we do wish to provide the following comments.</p>	

Comment Letter	Feedback Highlights	Task Force Response
	<ul style="list-style-type: none"> <li data-bbox="661 233 1440 667">• <i>Applicability and application of paragraph .02 and .03.</i> Consideration should be given to clarifying the leases subject to 1.260.040.02. The phrase “a covered member enters into a lease” could be read to apply to only new leases entered into during the period of professional engagement by a professional that is a covered member when the lease is executed, and not include leases entered into by a professional prior to becoming a covered member. The business relationship and loan interpretations use terms such as “has” or “had”. Use of the term “has”, in this situation seems to be more appropriate when considering the application of the grandfathering provisions. <li data-bbox="661 704 1440 967">• If 1.260.040.02 was intended to only apply to new leases entered into during the period of professional engagement by a professional that is a covered member when the lease is executed, then we believe that paragraph 1.260.040.04 is not a grandfathering provision but rather addresses circumstances other than those described in 1.260.040.02, and should therefore be titled differently than “Grandfathered Leases”. <li data-bbox="661 1005 1440 1396">• In addition, we believe that the requirements of paragraph 1.260.040.03, and its interaction with paragraph 1.260.040.02 could be confusing to members and in some circumstances place an undue burden on a firm to document safeguards when there are minimal threats. Paragraph 1.260.040.03 provides that even if the minimum safeguards required in paragraph 1.260.040.02 are met, the member should consider other threats and potential safeguards. It is unclear why there is a need to consider other threats if the lease is immaterial to the attest client and the covered members, since we believe that threats in those facts and 	<p data-bbox="1470 233 1911 326">Paragraphs revised and includes the word “has” pursuant to the structural revisions.</p> <p data-bbox="1470 704 1911 764">Grandfathering paragraph was deleted.</p> <p data-bbox="1470 1005 1911 1198">Structural revisions have clarified the interaction of the paragraphs. Paragraph .03 no longer requires an additional evaluation of threats after compliance with paragraph .02.</p>

Comment Letter	Feedback Highlights	Task Force Response
	<p>circumstances are already at an acceptable level. We believe that it would be more appropriate to provide for a general evaluation of threats and safeguards consistent with paragraph .03 when the lease is immaterial to the attest client but material to a category of covered member not specified in paragraph .02c (i.e., a partner, partner equivalent or manager that provides more than 10 hours of nonattest services to the attest client within any fiscal year, or a partner or partner equivalent in the office in which the lead attest engagement partner or partner equivalent primarily practices in connection with the attest client). That approach would recognize that immaterial leases do not result in significant threats, and provide guidance to firms on how leases with certain categories of covered members, despite being material to that covered member, may have sufficient safeguards to objectivity and professional skepticism.</p>	

**COMMENT SUMMARY – RESPONSES TO SPECIFIC QUESTIONS
PROPOSED Revised “Leases” interpretation of the “Independence Rule”**

Question 1: Are there any exceptions that should be extended to affiliates of financial statement attest clients?

PEEC Response: See proposed revision to the Affiliates interpretation providing exceptions for certain affiliates as suggested by commenters.

CL 1	TIC	TIC agrees that the provisions of this section should apply to affiliates and exceptions should not be extended.
CL 2	NASBA	No, NASBA does not believe that the PEEC should add any exceptions to a covered member’s leasing arrangements with affiliates of financial statement attest clients as (i) exceptions would add unnecessary complexity to the interpretation, and (ii) such treatment would be inconsistent with the way that other financial relationships (e.g., banking or brokerage relationships) are treated under the Code.
CL 3	KPMG	We do not believe that exceptions should be provided for affiliates of attest clients.
CL 4	Deloitte	n/a
CL 5	Grant Thornton	Grant Thornton believes that as ownership interests can change frequently in our current business environment, it would be our recommendation to only require leases that exist between a covered member and the attest client to be evaluated. We do not believe that a lease that exists between an affiliate (e.g., parent or a brother-sister entities not audited by the firm) and a covered member would impair the ability of a firm to be compliant with the Independence rule.
CL 6	PwC	Yes, we believe that exceptions should be extended to certain affiliates. Under the principles-based approach that we’ve recommended in Section I, a lease entered into with an unaudited affiliate under common control with (i.e., a “sister entity”) or upstream of the financial statement attest client could be deemed to raise threats to independence that are less significant than those created by a leasing arrangement with a material subsidiary. This is because, among other considerations, the former would not be subject to financial statement attest procedures or financial statement disclosures. However, the proposal makes no such distinction. In this scenario, the impact on independence would be considered

		<p>to be the same, incorrectly in our view, and would represent a breach of the Code of Conduct reportable to those charged with governance. Establishing a more principles-based approach for evaluating the permissibility of leases, as we've suggested, would allow for flexibility in the independence evaluation and help to avoid disparate and overly prescriptive conclusions relating to certain affiliates, such as those described above.</p> <p>If the PEEC decides to retain the prohibition on material leases with respect to members of the attest engagement team and those individuals in a position to influence the attest engagement, the prohibition should only apply to arrangements with the financial statement attest client and with those affiliates subject to financial statement attest procedures (i.e., downstream affiliates). Limiting the proposed prohibition as such would establish a more meaningful framework that appropriately restricts transactions based on whether they may be subject to financial statement attest procedures or financial statement disclosures.</p>
CL 7	EY	<p>We believe PEEC should consider whether all of the minimum safeguards in paragraph 1.260.040.02 of the Proposed Revision should apply to leases with affiliates that are not subject to an audit by the member. When the lease is with a parent or a sister affiliate, one of the major threats to independence related to leases (having to audit your own transaction) is non-existent. This indicates that a lesser level of safeguards are generally necessary to reduce the relevant threats to an acceptable level. We believe that a general threats and safeguards evaluation consistent with paragraph 1.260.040.3 will be sufficient in these circumstances.</p>

Question 2: Are there any other situations or circumstances that should be grandfathered which are not grandfathered in the proposal?

PEEC Response: The leases that were “grandfathered” in the Proposal are now covered by a conceptual framework approach in the revised paragraph .03, rather than assigning specific safeguards to the leases specified in the Proposal. PEEC determined that the primary residence paragraph was not necessary as it did not provide any additional relief beyond what was contemplated in the Proposal, based on the comments. As revised, such leases would be addressed similarly to leases of other types of property.

CL 1	TIC	TIC cannot think of any other situations or circumstances that should be grandfathered.
CL 2	NASBA	No, NASBA does not believe there are other situations involving a covered member's lease with an

		attest client that should be grandfathered (in addition to those scenarios suggested).
CL 3	KPMG	<p>We believe that PEEC should consider modifying the interpretation to include the following items as circumstances that should be grandfathered:</p> <ul style="list-style-type: none"> a) When a covered member enters into a lease with a counterparty prior to independence being required, but the lease with the counterparty is later sold or transferred to a counterparty who is an attest client; and b) When a covered member enters into a lease with an attest client that is immaterial to the covered member or the attest client but subsequently becomes material to the covered member or the attest client.
CL 4	Deloitte	<p>Paragraph .04 of the Proposed Interpretation does not address the circumstances whereby a member enters into a lease with a counterparty for which independence is not required, and such lease is subsequently sold / transferred to a counterparty for which independence is required. In our view, the interpretation should allow for grandfathering of such leases similar to the grandfathering provisions applicable for mortgages and immaterial unsecured loans described in Interpretation 1.260.020.02(b)(ii), Loans and Leases With Lending Institutions.</p>
CL 5	Grant Thornton	<p>Grant Thornton agrees with the circumstances provided in the proposal for grandfathered leases. However, we suggest that PEEC consider providing further guidance on whether renewal of terms (or specific terms) of the original lease would be covered under grandfathered leases in the interpretation or in a frequently asked questions document. Specific examples should be provided. The proposal does state that automatic renewals provided for in the original lease are not considered changes in terms. However, specific guidance is not provided on whether other renewal of terms (not automatic renewals), but may be acceptable if the term revisions are not material to the original lease or are an extension of the original lease.</p>
CL 6	PwC	<p>As described in more detail in Section III.A, if the PEEC decides to retain the prohibition on material leases as proposed, we recommend that an exemption be provided for leases of primary residences entered into after the covered member is required to be independent of the lessor. An exemption for new leases of primary residences would help to eliminate a potentially significant hardship for covered members and their immediate family members who may otherwise see their range of options for housing in certain markets of the country considerably reduced by the independence restriction on material leases.</p>
CL 7	EY	<p>Since many leasing transactions, particularly in residential real estate, are for periods of one year or</p>

		less without automatic renewals, the grandfathering provisions in paragraph 1.260.040.04 will provide insufficient relief in many situations. We believe that PEEC should consider whether there are safeguards available that would allow for a on-time, arms-length, ordinary course renewal of a short term lease on market terms as part of its grandfathering provision, subject to the general evaluation of threats and safeguards in 1.260.040.03, even if such renewals are not “automatic” or provided for in the lease document, particularly with respect to primary residence leases.
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Question 3: Do you agree with the application of the materiality safeguard in paragraph .02? Specifically, do you agree that there are no safeguards available when a covered member specified in paragraph .02 has a lease with the attest client that is material to the covered member?

PEEC Response: PEEC agreed that material leases between certain covered members specified in paragraph .02 and the attest client would render threats at an unacceptable level, and that safeguards could not reduce the threat to an acceptable level. Thus, PEEC did not reduce the scope of covered members subject to paragraph .02; however, see revisions to paragraphs .02 and .03 to clarify the timing of safeguard application including materiality.

CL 1	TIC	TIC agrees that with the application of the materiality safeguard in paragraph .02 and TIC agrees that no safeguards would be available in the case of a material lease with a covered member.
CL 2	NASBA	Yes, NASBA agrees that the materiality safeguard is essential within the context described in paragraph .02 of the proposed interpretation, that is, entering into a lease that is material to certain covered members creates an insurmountable threat to the firm's independence.
CL 3	KPMG	We agree that when a lease with a covered member is material to the covered member, there are no safeguards available that would reduce the threat to an acceptable level.
CL 4	Deloitte	We agree with the application of the materiality safeguard in paragraph .02, and that there are no safeguards available when a covered member specified in such paragraph has a lease with the attest client that is material to that covered member.
CL 5	Grant Thornton	Grant Thornton agrees with the application of materiality in evaluating leases between a covered member and an attest client.
CL 6	PwC	We do not agree with the application of the materiality safeguard in paragraph .02 as it relates to members of the attest engagement team and individuals in a position to influence the attest

		engagement for the reasons outlined in our detailed comments and suggestions above. However, as described in more detail in Section III.A, if the revised interpretation is to establish some form of a bright-line test based on materiality, we recommend that the PEEC give consideration to limiting that prohibition to those leasing transactions entered into by the attest engagement partner (or partner equivalent) and by the firm. Please refer to our detailed comments and recommendations in Section III.A.
CL 7	EY	n/a

Question 4: Do you agree that there are no safeguards that would reduce the threat to an acceptable level when the lease with a covered member is material to the attest client?

PEEC Response: No revisions needed as commenters and Task Force agree with the safeguard.

CL 1	TIC	TIC agrees that there are no safeguards that would reduce the threat to an acceptable level in this circumstance.
CL 2	NASBA	Yes, NASBA agrees that a lease agreement between a covered member (as described in paragraph .02 of a proposed interpretation) and an attest client that is material to the attest client impairs independence.
CL 3	KPMG	We agree that when a lease with a covered member is material to the attest client, there are no safeguards available that would reduce the threat to an acceptable level.
CL 4	Deloitte	n/a
CL 5	Grant Thornton	Grant Thornton agrees there are no safeguards that would reduce the threat to an acceptable level when the lease with a covered member is material to the attest client. We do believe firms could appropriately segregate an individual that is not in the chain of command (or does not meet the other criteria for being a covered member) with leases that were material to an attest client which would result in the individual not being classified as a covered member.
CL 6	PwC	As indicated in Section I, we believe that independence would be impaired by a lease that is material to the attest client and agree that such leases should be prohibited. However, although we agree with the

		direction of the PEEC's proposal in this respect, we note that, for financial statement attest clients, a lease that is material to any affiliate of the financial statement attest client would also be prohibited under the proposal. As described in more detail in our response to Question 1, we believe that a lease entered into with an unaudited entity that is under common control with (i.e., a "sister entity") or upstream of the financial statement attest client raises threats to independence that can be less significant than those created by a lease entered into with the financial statement attest client itself or with a material subsidiary. Therefore, for the reasons outlined in our response to Question 1, we do not agree that a lease that is material to a sister entity or an upstream affiliate represents an unequivocal impairment of independence in all circumstances. A more principles-based approach that looks at whether the material lease could be subject to financial statement attest procedures or financial statement disclosures may be more appropriate.
CL 7	EY	n/a

Question 5: Do you agree that the requirements of the proposal should extend to immediate family, as proposed?

PEEC Response: No revisions necessary, commenters agree that the provisions should extend to immediate family as proposed.

CL 1	TIC	TIC agrees that the requirements should extend to immediate family.
CL 2	NASBA	Yes, NASBA agrees that the requirements of the proposed interpretation should also apply to the covered member's immediate family, which is generally consistent with the application of other independence interpretations in the Code to those persons.
CL 3	KPMG	We agree with the proposed interpretation with respect to including the immediate family members of the covered members.
CL 4	Deloitte	In our view, it is reasonable to expect that rules on leases applicable to covered members should also apply to the immediate family of those individuals. We note, however, that while the Explanation of the Proposed Revision section of the Exposure Draft (see "Applicability") indicates that "the requirements of the proposed revision extend to the immediate family of the covered member and to affiliates of a financial statement attest client," the Proposed Interpretation does not explicitly include such language. This appears inconsistent with other areas of the AICPA Code where the rules and interpretations

		intended to apply to the immediate family member of covered members are explicitly stated in the rule/interpretation. PEEC should consider including such language in the body of the proposal to avoid any ambiguity or confusion in applying the standard.
CL 5	Grant Thornton	Grant Thornton agrees immediate family member should also be required to comply with the requirements of the proposal for leases similar to other financial relationship requirements under the AICPA's Independence Rules.
CL 6	PwC	We agree that the provisions of the proposed revised interpretation should also apply to leases entered into by the immediate family members of covered members.
CL 7	EY	n/a

Question 6: What do you foresee as major obstacles to implementation or hardships? Do you expect significant changes in quality controls, procedures, tools, or technology to monitor leases?

PEEC Response: PEEC has considered the hardships noted in the responses and has reduced the scope of leases explicitly addressed in the proposal, leaving more leases subject to the Conceptual Framework approach. PEEC also removed the required additional evaluation of threats, as suggested by commenters. PEEC believes that the revisions relieve to some extent the perceived hardships of additional monitoring of a large population of leases. In addition, the revision related to affiliates of the attest client reduced the scope of the original proposal.

Additional member enrichment activities such as decision trees, illustrations, or FAQ will be prepared by staff after adoption if PEEC believes it would be beneficial.

CL 1	TIC	TIC believes that the only threat to independence represented by leases is a self-interest threat. Based on the definitions of familiarity threat and undue influence threat, they are not significant in a lease between a covered member and an attest client that meets the safeguards in paragraph 02. The standard as written would create a hardship by adding the requirement to evaluate (and document) these threats and safeguards when TIC does not believe these threats would ever be significant. In addition, TIC does not believe any other threats, as contemplated in paragraph 03, would be relevant or significant to a lease that meets the safeguards in paragraph 02. Rather than requiring an evaluation of any other threats, TIC recommends this requirement be removed from the ED and the factors in paragraph 03 be retained solely for purposes of evaluating the self-interest threat. Since these other threats are not relevant or significant, this effort will not add anything to the independence
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		<p>determination.</p> <p>Other than the issues in the preceding paragraph, the interpretation should not require significant changes to monitor leases.</p>
CL 2	NASBA	<p>NASBA believes that two possible challenges to implementation may fall more heavily on practitioners in smaller firms:</p> <ul style="list-style-type: none"> (i) lack of awareness of the revised independence requirements, which would prevent firms from preparing for the changes, and (ii) inter-relationships between the smaller firms and their clients are likely to be more prevalent than in larger firm environments, thus the smaller firms (especially in more rural areas) may find it challenging to avoid or safeguard against situations that create significant threats to their independence. Thus, we believe these practitioners will need significant lead time to develop appropriate safeguards and effectively implement the proposed revisions.
CL 3	KPMG	<p>Other than the impact on short-term leases as previously discussed, we don't anticipate significant changes in processes as a result of implementing this interpretation.</p>
CL 4	Deloitte	<p>In our view, the Proposed Interpretation as written may require significant consideration of and potential revisions to a member's existing controls, processes, procedures, systems and human resources in order to appropriately identify and effectively monitor its professionals' leasing arrangements. This view is based in part on the notion that under the Proposed Interpretation, a significant population of operating leases, which are currently "scoped out" under the extant code, will need to be identified, monitored and evaluated. We ask PEEC to consider the following:</p> <ul style="list-style-type: none"> • We believe the Proposed Interpretation covers all leasing arrangements, regardless of the substance or length of the arrangements. Lease arrangements may include, for example, (a) short-term auto leasing arrangements (also known as "buy-back" or "purchase-repurchase" arrangements that are popular for extended vacations and which technically qualify as a lease rather than a rental), (b) short-term lodging arrangements on vacation and apartment rentals such as those offered by Airbnb or VRBO and (c) personal leases for appliances, home furnishings, and computers. We ask PEEC to evaluate the potential threats to independence arising from these type of lease arrangements and consider whether excluding such arrangements from the scope of the Proposed Interpretation would be appropriate based on the potential threats. We recognize the likelihood of such leases being material to the firm, its professionals or to the attest client may be very low, and thus, will likely not violate the Proposed Interpretation. However, absent specific

		<p>exclusion of such arrangements, members will be responsible for gathering necessary information (likely a very significant volume of information for many firms) to be able to evaluate such arrangements and make a determination on compliance with the Proposed Interpretation.</p> <ul style="list-style-type: none"> Paragraph .02 includes certain “bright-line” conditions and considerations for evaluating leasing arrangements. We agree that such bright-line conditions and related safeguards are responsive in addressing the most significant threats to independence arising from leasing arrangements. Additionally, paragraph .03 of the Proposed Interpretation establishes a requirement for further analysis to be performed on lease arrangements that have already met the safeguards in paragraph .02. While this additional analysis of threats to independence may have precedent in the rules and interpretations of the AICPA Code, we ask the PEEC to consider that the requirement for additional analysis be limited to circumstances whereby the covered member “knows or has reason to believe” that certain factors may be present. Such an approach has been adopted in other sections of the Code, including Interpretation 1.224.010 Client Affiliates related to certain lending relationships and acquisitions; and Interpretation 1.270.100 Close Relatives, with respect to financial interests of close relatives. We believe that the additional analysis that may be necessary under this approach, coupled with the bright line conditions and safeguards included in paragraph .02, should serve to adequately address the most significant threats to independence arising from leasing arrangements.
CL 5	Grant Thornton	Grant Thornton believes it would be appropriate to have a period of transition to allow firms to determine if changes need to be made to internal policies in identifying any leases that exist between the firm or covered members and attest clients. Firms will also need to determine whether their existing quality control procedures require revision due to the new interpretation. We do not believe that significant changes would be needed as long as attest clients are only considered to be the attest client and downward affiliates. We agree that existing leasing relationship between a covered member and an attest client could be grandfathered which should alleviate potential hardships.
CL 6	PwC	Given the pervasive use of leasing arrangements, our main concern relates to the potential hardship and disruption that a bright-line test based on materiality would create for covered members and their immediate family members. Although real estate property and automobiles are perhaps the most prominent examples of assets available for leasing, the PEEC must recognize that leases are also widely utilized for a broad spectrum of other routine consumer goods, ranging from technology products – for example, cellular phones, tablets, computers, cable and internet equipment – to household equipment such as appliances, furniture, and power tools. A blanket prohibition on the basis of materiality could restrict the opportunities currently available to covered members and their

		<p>immediate family members to acquire housing and personal consumer goods.</p> <p>As a practical matter, a prohibition based on the materiality of the lease would also disproportionately affect junior-level professional staff on the attest engagement team, in particular those persons with a high student loan debt burden. A junior-level staff person could easily find himself or herself running afoul of the materiality threshold, especially if leases have to be aggregated (such as may be the case, for example, if an associate on the attest engagement team and his or her spouse lease their personal cell phones, tablets, and cable and internet equipment from the same wireless service provider). Furthermore, this could also potentially have a detrimental effect on the ability of firms to attract and retain first-rate talent, such as interns, associates, and senior associates, increasing staff recruiting and retention costs for firms.</p> <p>The potential impact of a prohibition on these consumer relationships is exacerbated by the fact that the grandfathering provisions in paragraph .04 of the proposed revised interpretation do not provide the same level of relief as the grandfathering currently available for pre-existing loans, as discussed in more detail in Section III.A. While a firm could theoretically reassign a staff person holding an impermissible lease to a different attest engagement, this may not be a practical solution for certain firms, especially smaller firms (where the pool of available staff with the requisite expertise may be limited) as well as those firms with a large portfolio of attest clients from an industry involved in the business of leasing (such as real estate). This safeguard would likely also not be available to the firm if the staff person holding the impermissible lease is a covered member by virtue of being in a position to influence the attest engagement as it may not be feasible to “isolate” the individual.</p>
CL 7	EY	n/a

Question 7: Do you agree that it is appropriate to grandfather primary residence leases in a similar manner to home mortgages, as proposed?

PEEC Response: PEEC removed the primary residence paragraph as it provided no additional relief beyond the leases that were “grandfathered” under the Proposal, and pursuant to the removal of the grandfathering paragraph. Such leases would be subject to the same requirements as leases of other types of property as described in the revised Proposal.

PEEC did not believe that threats would be at an acceptable level if a covered member specified in paragraph .02 entered a material lease with an attest client, even if it was a primary residence lease. However, such existing leases of those specific covered members would be subject to the Conceptual Framework approach contained in paragraph .03 of the revised

proposal.

Renewals are addressed in the revised Proposal by using the concept of “renegotiation” of a lease as equivalent to entering into a lease.

CL 1	TIC	TIC believes it is appropriate to grandfather primary residence leases.
CL 2	NASBA	Yes, NASBA believes it is appropriate to grandfather primary residence leases in a similar manner to home mortgages, as proposed, since under the new lease accounting standard, leases generally will be treated as secured loans.
CL 3	KPMG	We believe it is appropriate to grandfather primary residence leases. However, since primary residence leases meet the grandfathering criteria in paragraph .04, we don't believe that paragraph .05 is necessary and could be confusing to practitioners.
CL 4	Deloitte	<p>We agree. Also see Item B in the Additional Comments and Feedback section (below)</p> <p>Paragraph .04 – Grandfathered Leases. We request the PEEC consider clarification to Paragraph .04(c) which states, “The attest client entered into the lease with a counterparty which was not required to be independent of the attest client, and that counterparty to the lease later acquires or is acquired by the covered member.” The current wording is not clear. We believe the intent of this paragraph is to address situations whereby an existing attest client is party to a lease, and the counterparty to such lease, at inception, was not associated with the covered member. However, such counterparty is subsequently acquired by, or acquires the covered member (i.e., the counterparty becomes associated with the covered member, in which case the independence rules would then be applicable to that counterparty). Please clarify PEEC's intent.</p> <p>In addition, the final sentence in paragraph .04 of the Proposed Interpretation states that “Automatic renewals provided for in the original lease are not considered changes in terms for purposes of this Interpretation.” We believe that addressing only this narrow aspect of a lease in the Interpretation could be read to imply that the application of other common lease terms (e.g., an election to extend a lease on a month-to-month basis at the end of its primary lease term) would be a change in terms for purposes of the Interpretation. We request that the PEEC consider broadening the scope of this sentence to indicate that the application of any provision of an original lease agreement is not considered a change in terms for purposes of this Interpretation.</p>

CL 5	Grant Thornton	Grant Thornton agrees it would be appropriate to grandfather primary residence leases and individuals could renew the lease if the leases meet the safeguards established. We suggest the PEEC consider providing examples to assist with the application of this change, including clarification regarding automatic renewals and if rent increases are considered a change in terms.
CL 6	PwC	Yes, if the PEEC decides to retain the prohibition on material leases as proposed, it would be appropriate to grandfather leases for primary residences as these transactions would likely be material to covered members, particularly junior-level professional staff. Please also refer to our detailed comments and recommendations in Section III.A.
CL 7	EY	Since many leasing transactions, particularly in residential real estate, are for periods of one year or less without automatic renewals, the grandfathering provisions in paragraph 1.260.040.04 will provide insufficient relief in many situations. We believe that PEEC should consider whether there are safeguards available that would allow for a on-time, arms-length, ordinary course renewal of a short term lease on market terms as part of its grandfathering provision, subject to the general evaluation of threats and safeguards in 1.260.040.03, even if such renewals are not “automatic” or provided for in the lease document, particularly with respect to primary residence leases.

Question 8: Are there any other factors affecting the significance of the threats to independence that you believe should be added to paragraph .03? Do you believe any of the factors in paragraph .03 should be removed?

PEEC Response: PEEC added duration of the lease term and other factors to the list in paragraph .03.

CL 1	TIC	TIC believes the factors affecting the significance of the threats in paragraph .03 are appropriate.
CL 2	NASBA	NASBA believes that the factors in paragraph .03 are sufficient as proposed, however, paragraph .03(d), the extent to which the lease will be subject to attest procedures or financial statement disclosures, seems to imply a possible self-review threat, which is not otherwise mentioned in the proposed interpretation. Also, from a practical standpoint, it is questionable whether the practitioner will be able to effectively assess this factor during pre-engagement.
CL 3	KPMG	We have no changes to propose to paragraph .03.
CL 4	Deloitte	n/a

CL 5	Grant Thornton	Additional considerations that could be given would be the length of time of the lease as well as the date the lease originated. These factors could potentially impact the significance of a leasing relationship as well as the determination of whether a leasing relationship between a covered member or firm and the attest client may impair the firm's independence in fact or appearance.
CL 6	PwC	<p>The possible factors to consider in evaluating the significance of the threats to independence created by a lease would vary based on the specific facts and circumstances of the leasing arrangement. Therefore, as it relates specifically to paragraph .03 of the proposed revised interpretation, a list of the most likely and relevant factors, that is not intended to be all-inclusive (as proposed by the PEEC in paragraph .03) should be sufficient.</p> <p>However, as it relates to the proposal as a whole (and as described in more detail in Section I), we recommend that the materiality of the lease to the attest engagement team member or to the individual in a position to influence the attest engagement be identified in the revised interpretation as one of the factors to be considered when evaluating the impact on independence. Under this approach, rather than cause an automatic impairment of independence in all circumstances, the materiality of the lease should trigger a "threats and safeguards" evaluation taking into consideration factors such as those we have suggested in Section I and others as relevant.</p>
CL 7	EY	n/a

Question 9: Do you agree that an effective date consistent with the FASB Update effective date for private companies is appropriate (December 15, 2019)? If not, what is a more appropriate effective date?

PEEC Response: The effective date should be effective for "fiscal years beginning" after December 15, 2019 to be fully consistent with the FASB standard. PEEC will discuss when adopting the standard at its November 2018 meeting.

CL 1	TIC	TIC believes the effective date is appropriate as proposed.
CL 2	NASBA	NASBA believes it is appropriate to sync the effective date of the proposed independence standard, which requires a new approach to addressing leasing relationships, to that of the FASB Update for leases.
CL 3	KPMG	We believe the proposed December 15, 2019 effective date, with early implementation allowed, is appropriate.

CL 4	Deloitte	Given the nature of the potential operational and procedural changes that may be necessary to comply with the Proposed Interpretation, members will need to perform a comprehensive review of their existing processes. While we believe that the proposed December 15, 2019 effective date should provide sufficient time to allow firms and practitioners to update their controls, procedures, tools or technology to effectively implement the provisions of the interpretation, such determination will be contingent upon its final scope and requirements.
CL 5	Grant Thornton	Grant Thornton does not believe the effective date of the proposal needs to be consistent with that of the FASB leasing standard. Based on the proposed revisions, we believe the proposed replacement of the extant GAAP categorization approach with a conceptual framework approach can be effective at any date. PEEC should consider allowing a one year effective date to provide adequate time for members to implement the proposed revisions.
CL 6	PwC	Yes, we agree that the PEEC's proposed effective date of December 15, 2019 is appropriate, provided that, upon adoption of the revised interpretation by the PEEC, this date still allows members sufficient time (for example, 1 year) to make the necessary changes to their policies, processes and procedures to implement the interpretation.
CL 7	EY	n/a

Text of Exposed Revisions to “Leases” Interpretation

[Additions appear in boldface italic and deletions are in strikethrough.]

1.260.040 Leases

.01 When ~~If a covered member enters into a lease ing agreement with an attest client during the period of the professional engagement, the self-interest, familiarity, and undue influence threats to the covered member’s compliance with the “Independence Rule” [1.200.001] may exist. would be at an acceptable level and independence would not be impaired if all the following safeguards are met:~~

- ~~a. The lease meets the criteria of an operating lease (as described in GAAP).~~
- ~~b. The terms and conditions set forth in the lease agreement are comparable with other leases of a similar nature.~~
- ~~c. All amounts are paid in accordance with the lease terms or provisions.~~

This paragraph excludes leases addressed by paragraph .04 of the “Loans and Leases With Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001].

.02 If a covered member enters into a lease with an attest client during the period of the professional engagement, ~~threats to compliance with the “Independence Rule” [1.200.001] 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, if a covered member has a lease that meets the criteria of a capital lease (as described in GAAP). Accordingly, independence would be impaired because the lease would be considered to be a loan with an attest client. unless all of the following safeguards are met during that period:~~

- a. The lease is entered into on market terms and established at arm’s length.***
- b. All amounts are paid in accordance with the lease terms or provisions.***
- c. The lease is not material to any of the following parties to the lease:***
 - i. The firm***
 - ii. An individual participating on the attest engagement team***
 - iii. An individual in a position to influence the attest engagement***
 - iv. The attest client***

.03 If the covered member meets the safeguards in paragraph .02, as applicable, the covered member should evaluate the significance of any other threats to determine whether the threats are at an acceptable level. If the covered member determines that threats are not at an acceptable level, the covered member should apply additional safeguards to eliminate or reduce the threats to an acceptable level. If no safeguards are available to eliminate or reduce threats to an acceptable

level, independence would be impaired. The significance of the threats will depend on factors such as the following:

- a. The role of the covered member on the attest engagement or with the firm***
- b. Materiality of the lease to the covered member, other than those covered members identified in paragraph .02***
- c. Whether multiple leases are entered into with the attest client and, if so, the aggregate materiality of those leases to the covered member or the attest client***
- d. The extent to which the lease will be subject to attest procedures or financial statement disclosures***

Grandfathered Leases

.04 Irrespective of materiality, threats to compliance with the “Independence Rule” [1.200.001] would be at an acceptable level and independence would not be impaired provided that the lease is entered into on market terms and established at arm’s length, and during the period of professional engagement all amounts are paid in accordance with the lease terms and provisions, the terms do not change in any manner not provided for in the original lease, and any of the following conditions are met:

- a. The covered member entered into the lease with the attest client prior to becoming a covered member with respect to the attest client.***
- b. The covered member entered into the lease with a counterparty for which independence was not required, and that counterparty to the lease later becomes, acquires, or is acquired by an attest client.***
- c. The attest client entered into the lease with a counterparty which was not required to be independent of the attest client, and that counterparty to the lease later acquires or is acquired by the covered member.***
- d. The lease existed prior to December 15, 2019 and the lease was permitted under the preexisting requirements of the “Independence Rule” [1.200.001] and its interpretations.***

Automatic renewals provided for in the original lease are not considered changes in terms for purposes of this interpretation.

Covered Member Leases Primary Residence from Attest Client

.05 Irrespective of materiality, if a covered member leases his or her primary residence from a lessor attest client, threats to compliance with the “Independence Rule” [1.200.001] would be at an acceptable level and independence would not be impaired, provided the covered member complies with the provisions in paragraph .04.

.06 This paragraph *interpretation* excludes leases addressed by [paragraph .04](#) of the “Loans and Leases with Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001].

.07 *This interpretation is effective December 15, 2019, with early implementation allowed.*

Final Text of Exposed Revisions to “Leases” Interpretation

1.260.040 Leases

.01 When a *covered member* enters into a lease with an *attest client*, self-interest, familiarity, and undue influence *threats* to the *covered member’s* compliance with the “Independence Rule” [1.200.001] may exist.

This paragraph excludes leases addressed by paragraph .04 of the “Loans and Leases With Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001].

.02 If a *covered member* enters into a lease with an *attest client* during the *period of the professional engagement*, threats to compliance with the “Independence Rule” [1.200.001] 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*, unless all of the following *safeguards* are met during that period:

- a. The lease is entered into on market terms and established at arm’s length.
- b. All amounts are paid in accordance with the lease terms or provisions.
- c. The lease is not material to any of the following parties to the lease:
 - i. The *firm*;
 - ii. An individual participating on the attest engagement team;
 - iii. An *individual in a position to influence the attest engagement*;
 - iv. The *attest client*.

.03 If the *covered member* meets the *safeguards* in paragraph .02, as applicable, the *covered member* should evaluate the significance of any other *threats* to determine whether the *threats* are at an *acceptable level*. If the *covered member* determines that *threats* are not at an *acceptable level*, the *covered member* should apply additional *safeguards* to eliminate or reduce the *threats* to an *acceptable level*. If no *safeguards* are available to eliminate or reduce *threats* to an *acceptable level*, *independence* would be *impaired*. The significance of the *threats* will depend on factors such as the following:

- a. The role of the *covered member* on the *attest engagement* or with the *firm*
- b. Materiality of the lease to the *covered member* other than those *covered members* identified in paragraph .02

- c. Whether multiple leases are entered into with the *attest client* and, if so, the aggregate materiality of those leases to the *covered member* or the *attest client*
- d. The extent to which the lease will be subject to attest procedures or financial statement disclosures

Grandfathered Leases

- .04 Irrespective of materiality, *threats* to compliance with the “Independence Rule” [1.200.001] would be at an *acceptable level* and *independence* would not be *impaired* provided that the lease is entered into on market terms and established at arm’s length, and during the *period of professional engagement* all amounts are paid in accordance with the lease terms and provisions, the terms do not change in any manner not provided for in the original lease, and any of the following conditions are met:
- a. The *covered member* entered into the lease with the *attest client* prior to becoming a *covered member* with respect to the *attest client*.
 - b. The *covered member* entered into the lease with a counterparty for which *independence* was not required, and that counterparty to the lease later becomes, acquires, or is acquired by an *attest client*.
 - c. The *attest client* entered into the lease with a counterparty which was not required to be independent of the *attest client*, and that counterparty to the lease later acquires or is acquired by the *covered member*.
 - d. The lease existed prior to December 15, 2019 and the lease was permitted under the preexisting requirements of the “Independence Rule” [1.200.001] and its interpretations.

Automatic renewals provided for in the original lease are not considered changes in terms for purposes of this interpretation.

Covered Member Leases Primary Residence from Attest Client

- .05 Irrespective of materiality, if a *covered member* leases his or her primary residence from a lessor *attest client*, *threats* to compliance with the “Independence Rule” [1.200.001] would be at an *acceptable level* and *independence* would not be *impaired*, provided the *covered member* complies with the provisions in paragraph .04.
- .06 This interpretation excludes leases addressed by [paragraph .04](#) of the “Loans and Leases with Lending Institutions” interpretation [1.260.020] of the “Independence Rule” [1.200.001].
- .07 This interpretation is effective December 15, 2019, with early implementation allowed.

**Professional Ethics Executive Committee (PEEC)
Disclosing Information in Connection with a Quality Review**

Staff

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Reason for Agenda Item

On June 20, 2018, the PEEC issued an exposure draft entitled “Disclosing Information in Connection with a Quality Review” (the Exposure Draft), which proposed a new interpretation (the Proposal) of the “Confidential Client Information” Rule (the Rule). The purpose of this agenda item is to present the comments received in response to the Exposure Draft and suggested revisions to the Proposal for PEEC consideration. Staff requests that PEEC revise the Proposal as appropriate and vote to adopt the Proposal, as revised (See **Agenda Item 2B**).

Background

The Proposal originated from inquiries from the AICPA Tax Practice Responsibilities Committee regarding whether voluntary tax practice reviews (VTPR) are considered authorized reviews of members’ professional practice under the Rule, and thus do not require specific consent from clients to disclose information to tax practice reviewers. PEEC issued the Exposure Draft on June 20, 2018 with a comment period of sixty days.

The extant Confidential Client Information Rule (1.700.001) requires that members obtain specific consent of the client prior to disclosing confidential client information to others. An exception to the requirement to obtain specific consent is provided in certain circumstances, including when a member has a “review of a member’s professional practice under AICPA or state CPA society or Board of Accountancy authorization.” Peer reviews of an attest practice and reviews for prospective purchases of a practice are considered a review of the member’s practice for purposes of the exception to 1.700, and are addressed at ET Sec. 1.700.050. However, the extant Rule does not contain an exception for firm-on-firm reviews of a tax practice, such as a voluntary tax practice review. The Proposal clarifies that members obtaining a quality review of a tax practice would be in compliance with the Rule if the member ensures compliance with Treas. Reg. 7216 requirements related to quality reviews of a tax practice, and takes additional steps as necessary to reduce any remaining threat to an acceptable level. In addition, the reviewer is prohibited from using to their advantage or disclosing the information obtained during the review.

PEEC included specific questions in the Exposure Draft for commenters. Five comment letters were received in response to the Exposure Draft. The comments, including specific responses to questions included in the Exposure Draft, are presented below and at **Agenda Item 2D**. Staff also consulted with staff liaisons of the AICPA Tax Practice Responsibilities Committee and Tax Executive Committee for suggestions that would facilitate PEEC’s addressing the comments received. Those comments are incorporated into the discussions of the comments received below.

Summary of Issues

Comments are highlighted and sorted by question below. The full comments sorted by question and commenter are presented at **Agenda Item 2D** for reference.

Question 1: Is it clear that the proposal is applicable to quality reviews as described by Treas. Reg. 7216, which includes voluntary tax practice reviews, and similar reviews that would be subject to Treas. Reg. 7216?

- Two (CL2, CL4) of the five commenters agreed that the proposal was adequately clear as to the applicability of the proposed standard.
- One commenter (CL1) recommends a title that is clearer in excluding peer-review or other attest-centric reviews.
- One commenter (CL3) suggested a broader reference to “the appropriate federal regulations.”
- One commenter (CL5) believed that PEEC should reference the principles under Treas. Reg. 7216 and then describe them in the interpretation itself (see discussion later in this agenda).
- Additionally, one commenter (CL2), in response to Question 5 regarding potential hardships, noted that state level definitions may not be consistent with the Proposal, and may lead to confusion with the defined term “quality reviews” in some state regulations (FL, NY for example).

Regarding clarity of the intended distinction between quality reviews and peer reviews, the Proposal includes terminology in paragraph .01 to indicate that the quality reviews addressed by the Proposal explicitly include quality reviews *of a member’s tax practice*, which is not an attest-centric review. Although peer reviews are not explicitly excluded in the Proposal, peer reviews are addressed in the body of the *Confidential Client Information Rule* [1.700.001] as a “*review of a member’s professional practice under AICPA or state CPA society or Board of Accountancy authorization.*” If additional clarity is needed specifically regarding peer reviews, staff suggests PEEC consider revising the Proposal in paragraph .01 to reference “quality review *of a member’s tax practice*” to explicitly include only tax practice reviews, as shown below.

In response to Question 5 regarding hardships, one commenter (CL4) noted that not all firms may have a tax practice quality control document, and the proposal should include those members that do not have such a formal document but have general controls and policies in their practice. To address this concern, staff suggests PEEC consider broadening the scope in paragraph .01 of the Proposal to include the “member’s tax practice quality control *policies and procedures*,” which would include members who do not have such a formal document (see below).

.01 For purposes of the “Confidential Client Information Rule” [1.700.001], a review of a member’s professional practice includes a quality review **of a member’s tax practice** (for example, a voluntary tax practice review) performed under the ~~monitoring requirements of the~~ member’s tax practice quality control **policies and procedures** document. When a member uses a third party to perform such reviews of the member’s

tax practice, threats to compliance with the “Confidential Client Information Rule” [1.700.001] may exist.

Questions for PEEC:

Does PEEC approve the suggested revision to paragraph .01 to address clarity of the distinction between quality reviews and attest-centric practice reviews? Does PEEC agree that a conforming revision should be made to the title of the Proposal (i.e. “Disclosing Information in Connection with a Quality Review of a Member’s Tax Practice”)?

Does PEEC agree with the suggested revision to paragraph .01 to broaden the scope to firms with quality control policies and procedures, rather than a formal tax practice quality control document?

Does PEEC agree with one commenter’s suggestion to reference “appropriate federal regulations” rather than Treas. Reg. 7216 throughout?

Question 2: Is it clear that confidential state and local tax information is included in the scope of confidential client information addressed by the proposed interpretation? Is it clear that the requirements of Treas. Reg. 7216 would apply to that information in the context of the proposed standard?

One (CL2) of the five commenters agreed that the proposal appropriately included state and local tax information as written.

Four commenters suggested additional clarification to avoid confusion in the application to state and local tax information. Specifically:

- Two commenters (CL1, CL5) suggest the proposal apply to quality reviews of all tax information regardless of the jurisdiction;
- One commenter (CL3) suggests the member should ensure that laws of state and local authorities are not more restrictive; and
- One commenter (CL4) suggests explicitly indicating that the proposal specifically applies to state and local tax returns as well.

Based on comments received and the intent of PEEC to include more than just federal tax return information, staff suggests consideration of expanding the terminology in the Proposal to explicitly include any tax information, regardless of jurisdiction, and address laws of state and local authorities as shown below:

.02 To reduce the threat to an acceptable level, the member should, at a minimum, be satisfied that the member complies with the requirements of Treasury Regulation 301.7216-2(p) and any applicable state or local regulations related to disclosures of any federal, state, or local tax return information during such reviews. If the member

determines that threats have not been reduced to an acceptable level, the member should apply additional safeguards to reduce the threat to an acceptable level (for example, enter into a written confidentiality agreement with the reviewer or de-identify tax return information provided to the reviewer).

Question for PEEC:

Does PEEC agree with the suggested revision to explicitly include any tax information, regardless of jurisdiction, as shown above?

Question 3: Do you agree that a confidentiality agreement should be recommended as an additional safeguard if the member determines it is necessary instead of being a required safeguard for all quality reviews?

Three (CL1, CL4, CL5) of the five commenters agreed that the confidentiality agreement should be recommended if the member deems it necessary to reduce threat to an acceptable level. One commenter (CL2) believed that the confidentiality agreement should be strongly recommended even when threats are at an acceptable level. One commenter (CL3) believed that the recommendation of such an agreement may complicate an already complex situation as it relates to application of federal and state regulations already applicable to tax preparers and quality reviewers. Based upon comments received, staff does not recommend further revision to the Proposal in this regard.

Question for PEEC: Does PEEC continue to agree that the confidentiality agreement should be recommended as a safeguard only if the member determines it necessary, as exposed?

Question 4: Do you recommend the consideration of any other safeguards in paragraph .02?

Three (CL2, CL3, CL5) of the five commenters agreed that the proposed safeguards are appropriate and had no further recommendations.

One commenter (CL4) recommended considering redaction of the personal identifiable information of all engagements reviewed as an additional safeguard. Staff notes that the IRC prohibits the third party reviewer from retaining any “documents containing any information that may identify the taxpayer by name or identification number.” PEEC previously stopped short of requiring redaction of identifying information; under the Proposal, if a member has reason to believe that the third-party reviewer is not aware of, or not in compliance with the redaction requirements of the IRC, the member can use professional judgment and apply this safeguard as necessary to reduce threats to an acceptable level.

In addition, one commenter (CL1) recommended considering identification of what specific information should be removed in order to adequately de-identify the tax return (e.g. name, address, SSN/EIN, etc.). Staff notes that the IRC stipulates that the reviewer should not retain any information that would “identify the taxpayer by name or identification number.” The Proposal uses the term “de-identify” which is intended to mean any information that would identify the client/taxpayer.

Question for PEEC:

Does PEEC continue to agree that redaction of identifying information should be recommended as the member deems necessary, rather than a required safeguard?

Does PEEC believe that the term “de-identify” clearly covers name and identification number and any other information that may identify the taxpayer?

In related comments received in response to Question 1, one commenter (CL5) believed that the proposal should reference and list the principles contained in IRC 7216 itself. Specifically, the proposal should:

- include the more expansive requirements of IRC 7216 that apply to prohibition to use the information for any purpose, not just purposes of the review.
- underscore the requirements within the proposed interpretation by adding, for example, that disclosure should only be to the extent necessary for a peer review and the member should maintain a record of the review sufficient to identify the disclosed information, the third party and the purpose of the review.

PEEC previously agreed that the direct reference to Treas. Reg. 7216 was appropriate; members obtaining or performing quality reviews should be aware of Treas. Reg. 7216 requirements, and PEEC did not note any unintended consequences of the direct reference. If the member complies with Treas. Reg. 7216, the member would already be prohibited from using the information gathered for any other purpose.

Question for PEEC:

Does PEEC continue to agree that the direct reference to Treas. Reg. 7216, in conjunction with a similar reference in paragraph .04, is appropriate?

Additional informal comments related to the requirements of Treas. Reg. 7216 were received from the Tax Executive Committee staff. Specifically, paragraph .02 requires that the member receiving the quality review be satisfied that the member complies with Treas. Reg. 7216, but does not explicitly require the member to ensure that the third party reviewer is aware of or in compliance with the requirements of Treas. Reg. 7216. It was suggested that the member receiving the quality review should be required to ensure that the third party reviewer is aware of the requirements of Treas. Reg. 7216. Staff suggests PEEC consider adding the following sentence to paragraph .02:

“In addition, the member should be satisfied that the third party reviewer is aware of the requirements of Treas. Reg. § 301.7216-2(p).”

Question for PEEC:

Does PEEC agree that the member should be required to ensure that the third party reviewer is aware of the requirements of Treas. Reg. 7216? If so, does PEEC approve the addition of the sentence above to paragraph .02?

Question 5: Do you foresee any hardships or obstacles to implementation of the proposed standard?

Two (CL1, CL5) of the five commenters did not identify any hardships or obstacles to implementation of the proposal.

One commenter (CL3) believed that there may be complications from ensuring compliance with applicable state and/or local laws that may be more restrictive. Staff notes that members are already required to adhere to the more restrictive rules / laws that the member is subject to.

Question for PEEC: Does PEEC agree with the concerns regarding potential state regulator definitions of “quality review” or being less restrictive than state or local laws?

Other Comments

One commenter (CL1) recommended a delayed effective date of 3 months to allow members time to familiarize themselves with the proposal and consider what actions are necessary to implement.

One commenter (CL5) suggested providing example scenarios and FAQ to assist in the application of the proposed standard.

Action Needed: Does PEEC agree that a three-month delay in the effective date is appropriate as suggested by one commenter?

Does PEEC believe it is necessary to issue a practice aid with examples or an FAQ to assist members in implementing the Proposal?

Effective Date

The Proposal effective date was the last day of the month of which the Proposal appears in the Journal of Accountancy, with early implementation allowed. As noted above, if PEEC so

approves, the effective date will be delayed by three months after the originally proposed effective date.

Action Needed

Staff requests that PEEC discuss the revised proposal at **Agenda Item 2B**, and approve adoption of the proposed standard.

Communications Plan

The adoption of the new interpretation will be communicated to the AICPA Tax Practice & Ethics group and the Tax Practice Responsibilities Committee, as well as to distribution lists of internal and external stakeholders. The adopted standard will be included in the Journal of Accountancy at the next available release. The AICPA Communications team will issue public alerts and post on social media regarding the issuance of the new standard.

Materials Presented

Agenda Item 2B: Proposed Interpretation – Suggested Revisions

Agenda Item 2C: Treasury Regulations and AICPA Provisions

Agenda Item 2D: Comment Letter Summary

**Professional Ethics Executive Committee
Disclosures in Connection with Quality Reviews**

1.700.110 Disclosing Client Information in Connection With a Quality Review

.01 For purposes of the “Confidential Client Information Rule” [1.700.001], a review of a member’s professional practice includes a quality review of a member’s tax practice (for example, a voluntary tax practice review) performed under the ~~monitoring requirements of the~~ member’s tax practice quality control policies and procedures document. When a member uses a third party to perform such reviews of the member’s tax practice, threats to compliance with the “Confidential Client Information Rule” [1.700.001] may exist.

.02 To reduce the threat to an acceptable level, the member should, at a minimum, be satisfied that the member complies with the requirements of Treasury Regulation 301.7216-2(p) and any applicable state or local regulations related to disclosures of any federal, state, or local tax return information during such reviews. If the member determines that threats have not been reduced to an acceptable level, the member should apply additional safeguards to reduce the threat to an acceptable level (for example, enter into a written confidentiality agreement with the reviewer or de-identify tax return information provided to the reviewer).

In addition, the member should be satisfied that the third party reviewer is aware of the requirements of Treas. Reg. § 301.7216-2(p).

.03 Members who perform such reviews should not use to their advantage or disclose any confidential client information that comes to their attention during the review. Members should refer to Treasury Regulation 301.7216-2(p) for further guidance related to tax return information obtained during such a quality reviews.

**Professional Ethics Executive Committee
Disclosures in Connection with Quality Reviews**

Treas. Reg. Sec. 301.7216-2(p)

(p) Disclosure or use of information for quality, peer, or conflict reviews.

(1) The provisions of section 7216(a) and [§ 301.7216-1](#) shall not apply to any disclosure for the [purpose](#) of a quality or peer review to the extent necessary to accomplish the review. A quality or peer review is a review that is undertaken to evaluate, monitor, and improve the quality and accuracy of a [tax return preparer's](#) [tax](#) preparation, accounting, or auditing services.

A quality or peer review may be conducted only by attorneys, certified public accountants, enrolled agents, and enrolled actuaries who are eligible to practice before the Internal Revenue Service. See Department of the Treasury Circular 230, [31 CFR part 10](#).

[Tax](#) return information may also be disclosed to [persons](#) who provide administrative or support services to an individual who is conducting a quality or peer review under this paragraph (p), but only to the extent necessary for the reviewer to conduct the review.

[Tax](#) return information gathered in conducting a review may be used only for [purposes](#) of a review.

No [tax](#) return information identifying a [taxpayer](#) may be disclosed in any evaluative reports or recommendations that may be accessible to any [person](#) other than the reviewer or the [tax return preparer](#) being reviewed.

The [tax return preparer](#) being reviewed will maintain a record of the review, including the information reviewed and the identity of the [persons](#) conducting the review.

After completion of the review, no documents containing information that may identify any [taxpayer](#) by name or identification number may be retained by a reviewer or by the reviewer's administrative or support personnel.

[(2) NOT INCLUDED – addresses conflict reviews]

(3) Any [person](#) (including administrative and support personnel) receiving [tax](#) return information in connection with a quality, peer, or conflict review is a [tax return preparer](#) for [purposes](#) of sections 7216(a) and 6713(a).

[Tax](#) return information disclosed and used for [purposes](#) of a quality, peer, or conflict review shall not be disclosed or used for any other [purpose](#).

AICPA Confidential Client Information Rule

1.700.001 Confidential Client Information Rule

.01 A member in public practice shall not disclose any confidential client information without the specific consent of the client.

.02 This rule shall not be construed (1) to relieve a member of his or her professional obligations of the “[Compliance With Standards Rule](#)” [1.310.001] or the “[Accounting Principles Rule](#)” [1.320.001], (2) to affect in any way the member’s obligation to comply with a validly issued and enforceable subpoena or summons, or to prohibit a member’s compliance with applicable laws and government regulations, (3) to prohibit review of a member’s professional practice under AICPA or state CPA society or Board of Accountancy authorization, or (4) to preclude a member from initiating a complaint with, or responding to any inquiry made by, the professional ethics division or trial board of the Institute or a duly constituted investigative or disciplinary body of a state CPA society or Board of Accountancy. Members of any of the bodies identified in (4) above and members involved with professional practice reviews identified in (3) above shall not use to their own advantage or disclose any member’s confidential client information that comes to their attention in carrying out those activities. This prohibition shall not restrict members’ exchange of information in connection with the investigative or disciplinary proceedings described in (4) above or the professional practice reviews described in (3) above. [Prior reference: paragraph .01 of ET section 301]

1.700.050 Disclosing Client Information in Connection With a Review or Acquisition of the Member’s Practice

.01 For purposes of the “[Confidential Client Information Rule](#)” [1.700.001], a review of a member’s professional practice includes a review performed in conjunction with a prospective purchase, sale, or merger of all or part of a member’s practice. Such reviews may threaten a member’s compliance with the “[Confidential Client Information Rule](#).” To reduce the threat to an acceptable level, a member must take appropriate precautions (for example, through a written confidentiality agreement with the prospective purchaser) to help ensure that the prospective purchaser does not disclose any confidential client information obtained in the course of the review.

.02 *Members who perform such reviews should not use to their advantage or disclose any confidential client information that comes to their attention during the review. [Prior reference: paragraph .04 of ET section 301]*

.03 *Members who obtain client files as the result of acquiring all or part of another member's professional practice should not disclose any confidential client information contained in such files. Members should refer to the "[Transfer of Files and Return of Client Records in Sale, Transfer Discontinuance or Acquisition of a Practice](#)" interpretation under the "Acts Discreditable Rule" [1.400.205] for guidance related to client files obtained through acquiring a practice.*

**COMMENT SUMMARY – RESPONSES TO SPECIFIC QUESTIONS
PROPOSED "Disclosing Client Information in
Connection with a Quality Review" Interpretation of the
“Confidential Client Information Rule”**

Question 1: Is it clear that the proposal is applicable to quality reviews as described by Treas. Reg. 7216, which includes voluntary tax practice reviews, and similar reviews that would be subject to Treas. Reg. 7216?		
CL 1	New York State Society of CPAs (NYSSCPA)	We believe that while the body of the text makes clear that the proposed interpretation applies to quality reviews as described in Treas. Reg. 7216, the title of the proposed interpretation is less clear. We believe that Disclosing Client Information in Connection with a Quality Review would lead most practitioners to believe that the contents of the proposed interpretation address confidentiality issues associated with a peer review or other such attest-centric review. We therefore suggest that the title of the proposed interpretation address the content of the proposed interpretation. For example, Disclosure of Client Information in Connection with a Quality Review, Including Voluntary Tax Practice Reviews might be a more helpful title.
CL 2	Florida Institute of CPAs (FICPA)	The Committee believes the proposal is applicable. The example provided within paragraph .02 of the proposed interpretation is clear. In addition, there is explicit guidance within the proposed interpretation, “Performed under monitoring requirements of the member’s tax practice quality control document,” that confirms the intention of the interpretation to differentiate a quality review from other type of reviews that could be misconstrued by the reader and to be consistent with the interpretations of Treas. Reg. 7216.
CL 3	National Association of State Boards of Accountancy (NASBA)	NASBA believes the proposed interpretation is not clear enough and recommends the PEEC clarify the language and add a broader reference to “the appropriate federal regulations.”
CL 4	AICPA Technical Issues Committee (TIC)	Yes. TIC believes it is clear that the proposal is applicable to quality reviews as described by Treas. Reg. 7216 and similar reviews that would be subject to Treas. Reg. 7216.

CL 5	Grant Thornton	<p>Grant Thornton believes that it is clear that the proposed interpretation is applicable to quality reviews as described by Treasury Regulation 301.7216-2(p) (the “Regulation”). However, Grant Thornton believes PEEC should further consider whether it is appropriate to use of a specific reference to the Regulation in the proposed interpretation rather than focusing in the interpretation text on the principles themselves. Focusing on the principles themselves is preferable than reference to a specific IRS regulation. When using a specific reference, such as Treasury Regulation 301.7216-2(p), there is risk that the reference may become outdated or obsolete should the regulation be renumbered or amended in the future. To correct the reference, Grant Thornton suggests that the proposed interpretation instead reference “the principles under Treasury Regulation 301.7216” and then describe them in the interpretation itself.</p> <p>As a result, we believe the guidance included in the proposed interpretation should include the more expansive prohibitions described in the Regulation. For example, subsection .03 of the proposed interpretation references the Regulation as it relates to the explicit prohibition of reviewers using the review to their advantage or disclosing any confidential client information. While such prohibition is similar to the Regulation, the Regulation prohibits disclosure or use for any purpose, not just for the purpose stated in the proposed interpretation. Grant Thornton believes the prohibitions in the proposed interpretation should be more expansive, similar to the Regulation.</p> <p>Lastly, while the Regulation sets forth the requirements for a quality review, peer review or other similar review, we believe such requirements should be underscored within the proposed interpretation by adding, for example, that disclosure should only be to the extent necessary for a peer review and the member should maintain a record of the review sufficient to identify the disclosed information, the third party and the purpose of the review.</p>
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Question 2: Is it clear that confidential state and local tax information is included in the scope of confidential client information addressed by the proposed interpretation? Is it clear that the requirements of Treas. Reg. 7216 would apply to that information in the context of the proposed standard?

CL 1	NYSSCPA	<p>Because the proposed interpretation only discusses the Treasury Regulations, we believe that a member might conclude that the proposed interpretation only applies to quality reviews as applied to Federal income tax information. Therefore, we suggest that PEEC add clarifying language to the proposed interpretation specifying that the interpretation applies to quality reviews of all tax information regardless of the jurisdiction.</p>
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CL 2	FICPA	The Committee believes confidential state and local tax information is clearly in the scope of the proposed interpretation. Within Treas. Reg. 301.7216-2(p), as referenced in paragraph .03 of the proposed interpretation, it explicitly describes tax information in conjunction with tax return preparation that would be applicable for disclosure in connection with a quality review. In addition, Treas. Reg. 301.7216-2(P) provides which parties can be disclosed tax information in connection with a quality review. The regulation also provides protections for client confidential information to not allow disclosure of tax information used for a quality, peer, or conflict review for any other purpose.
CL 3	NASBA	NASBA believes some clarification of the scope of the proposed interpretation would be helpful. We also believe the member should ensure that the laws of state and/or local taxing authorities are not more restrictive than Treasury Reg. 7216 and suggest the PEEC add language to that effect.
CL 4	TIC	TIC believes this may not be totally clear with regard to SALT returns. The provisions mainly appear to be focused on IRS regulated returns, while the SALT returns would be under the jurisdiction of each State. TIC would suggest that something should be added to paragraph .02 to specifically state that this guidance applies to SALT returns as well.
CL 5	Grant Thornton	Grant Thornton suggests clarifying language be added to the interpretation to clearly indicate that the principles of the Regulation are intended to also be applied to confidential tax information of all types (federal, state, local as well as all types of returns) regardless of jurisdiction.

Question 3: Do you agree that a confidentiality agreement should be recommended as an additional safeguard if the member determines it is necessary instead of being a required safeguard for all quality reviews?

CL 1	NYSSCPA	We agree with PEEC that a written confidentiality agreement should be recommended as a safeguard to reduce the threat to an acceptable level. We believe PEEC's approach of suggesting possible safeguards is consistent with other interpretations within the Code of Professional Conduct.
CL 2	FICPA	The Committee believes a confidentiality agreement should be strongly recommended even when the threat is at an acceptable level. Confidentiality agreements provide additional protections to all parties involved, and are in the best interest of the client to reinforce the importance of maintaining confidentiality of client information in conjunction with Treas. Reg. 7216.
CL 3	NASBA	NASBA believes that a recommendation for a nondisclosure agreement between the quality reviewer

		and the ostensible reviewed client might complicate an already complex situation. There are extant applicable federal and state statutes that prohibit disclosure of tax information. Those federal and state statutes apply to quality reviewers as well as tax preparers.
CL 4	TIC	Yes, TIC believes that if they meet Treas. Reg. 7216, it should be up to the member to determine if a confidentiality agreement is necessary instead of being a required safeguard for all quality reviews. TIC believes that items related to firm practice and risk management should be left out of the standards and up to a member to make those determinations based on the circumstances.
CL 5	Grant Thornton	Grant Thornton agrees that a confidentiality agreement should be recommended as an additional safeguard if the member determines it is necessary instead of being a required safeguard for all quality reviews.

Question 4: Do you recommend the consideration of any other safeguards in paragraph .02?

CL 1	NYSSCPA	The best safeguards available would be the two identified in the proposed interpretation – a written confidentiality agreement or de-identifying the tax return information provided to the reviewer. We do not envision any additional safeguards that would adequately address the threat, however, the PEEC might consider identifying what specific information – name, address, SSN/EIN, etc. – should be removed in order to adequately de-identify the tax return.
CL 2	FICPA	No additional safeguards would be necessary if a confidentiality agreement is executed.
CL 3	NASBA	NASBA has no further recommendations.
CL 4	TIC	The only potential item TIC might ask PEEC to consider is redacting the personal identifiable information of all engagements reviewed as an additional safeguard.
CL 5	Grant Thornton	Grant Thornton believes the safeguards identified in paragraph .02 are the most appropriate safeguards available and has no additional recommendations.

Question 5: Do you foresee any hardships or obstacles to implementation of the proposed standard?

CL 1	NYSSCPA	We have not identified any hardships or obstacles to implementation of the proposed interpretation.
CL 2	FICPA	<p>Yes. The diversity of definitions by state can lead to confusion if the state definition contradicts the definition per Treas. Reg. 7216 and the proposed interpretation.</p> <p>One example, from Florida defines a quality review under Florida Statue 473.316 as “A study, appraisal, or review of one or more aspects of the professional work of an accountant in the practice of public accountancy which is conducted by a professional organization for the purpose of evaluating quality assurance required by professional standards, including a quality assurance review. The term includes a peer review as defined in s. 473.3125.”</p> <p>Another example from New York defines quality reviews under Article 149 as “A review of the firm’s attest services.”</p>
CL 3	NASBA	NASBA does not foresee any other complications from application of the proposed interpretation other than ensuring compliance with applicable state and/or local laws that may be more restrictive.
CL 4	TIC	TIC believes this could present an obstacle for firms that do not currently have a formal system of quality control review document (for example, if they are strictly a tax practice). Therefore, TIC would suggest changing the terminology in the interpretation to firm’s policies and procedures to be reflective of these situations.
CL 5	Grant Thornton	Grant Thornton does not foresee any hardships or obstacles to implementation of the proposed standard.

General Comments

CL 1	NYSSCPA	PEEC has suggested an effective date for the final interpretation of the last day of the month in which the final interpretation appears in the Journal of Accountancy. We recommend delaying the effective date by three months to allow members adequate time to familiarize themselves with the interpretation and consider what actions, if any, need to be taken to implement the interpretation.
CL 2	FICPA	None

CL 3	NASBA	None
CL 4	TIC	TIC appreciates the work of PEEC to clarify whether quality reviews as described by Treas. Reg. 7216 were included in those exceptions to obtaining specific client consent. We believe this is a welcome clarification and should result in less diversity in practice.
CL 5	Grant Thornton	Grant Thornton suggests that PEEC consider providing illustrative example scenarios and frequently asked questions to assist in the application of the new interpretation.

Information Technology and Cloud Services Task Force

Task Force Members: Shelly VanDyne (Chair), Cathy Allen, Katie Jaeb, Anna Dourdourekas, Dan O'Daly, John Ford, Nancy Miller. **Staff:** Ellen Gorla, Michele Craig

Task Force Objective

Recommend to the Committee any changes necessary to the nonattest services subtopic considering current information technology (including cloud) service offerings by members.

Reason for Agenda*Hosting Services*

At the August meeting the Committee agreed to extend the effective date of the Hosting Services interpretation to July 1, 2019, primarily to give software vendors additional time to implement any necessary changes to their business practices. The Committee also requested the Task Force (1) consider whether the FAQs are consistent with the hosting services interpretation; (2) whether the interpretation is consistent in terms of how it addresses working on the client's general ledger vs. depreciation schedules; and (3) what cutting off access to a portal means.

The Task Force believes that the FAQs¹ are consistent with the Hosting Services interpretation. The Task Force believes that when the member provides an attest client with bookkeeping services using general ledger software that resides on the firm's server (or server leased by the firm) the member has assumed responsibility for maintaining the client's financial information, in total and become a part of the client's internal control over financial reporting, which is a management responsibility that impairs independence. The Task Force believes a general ledger is different than a depreciation schedule and that the interpretation addresses this difference.

The Task Force does not believe that the interpretation requires that the client's access to the portal be terminated, rather that access to the data or records that are *in the portal* be terminated within a reasonable period of time. When discussing this request, the Task Force decided to revise FAQ 3 to provide further clarification into what a reasonable period of time would be to terminate the client's access to the data or records that are in the portal. To do this the Task Force revised the answer to FAQ 3 to explain that a reasonable period would be as soon as practicable but, absent extenuating circumstances, no later than 60 days after the completion of the engagement or provision of the information to the attest client through the portal, whichever is longer. The Task Force believes 60 days is appropriate since this is consistent with the documentation standard on finalizing workpaper assembly.

Question for the Committee

1. Does the Committee have any comments related to the first 8 FAQs developed by the Task Force? The Task Force is still working on at least one additional FAQ.

Information Systems Services

The Committee received 27 [comment letters](#) on its [Information System Services exposure draft](#) Information System Services exposure draft. **Agenda Item 3B** is a summary of the comments by comment letter. **Agenda Item 3C** then sorts these comments by the interpretation's paragraph

¹ The Task Force is still discussing FAQ 9.

number and exposure draft question. Overall commenters were supportive of the proposal and offered up recommendations or insights for the Committee's consideration. The Task Force has just begun discussing the comments and would be interested in the Committee's thoughts on some of the matters discussed so far.

Questions for the Committee

1. Would adding "nonattest" to paragraph .01 of **Agenda Item 3D** make it clearer that the proposal is not intended to prohibit innovation in the assurance space and derail audit of the future (i.e., prohibit the use of certain technology to perform the attest engagement)?
2. Does incorporating the FIS acronym for the phrase "financial information system" throughout **Agenda Item 3D** help clarify that the information system is a financial one?
3. The proposed interpretation takes a very financial audit centric perspective. While a knowledgeable member should know to adapt the guidance to the subject matter of the attest engagement, does the Committee believe clarification would be helpful? For discussion purposes only, Staff has included strawman language in paragraph .03 of **Agenda Item 3D**.

Action Needed

The Committee is asked to familiarize itself with the feedback provided by commenters.

Materials Presented

Agenda Item 3B Summary of Comments by Comment Letter

Agenda Item 3C Summary of Comments by Paragraph Number and Other Relevant Categories

Agenda Item 3D Proposed Revised Interpretation (Marked Changes from Exposure Draft)

COMMENT SUMMARY**Proposed Revised Interpretation “Information System Services” (formerly Information Systems Design, Implementation, or Integration)**

Member comments on specific questions in the Exposure Draft are indicated by a parenthesized number which correlates to one of the two questions presented in the Exposure Draft (see below).

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

Comment Letter	Feedback Highlights
<p>CL 1</p> <p>New York State Society of Certified Public Accountants (NYSSCPA) Professional Ethics Committee</p> <p><i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> • (1) The terminology used in the proposed revised interpretation is sufficiently explained to allow non-technically minded members to understand the requirements of the interpretation. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a)We believe that the term “significant” should not be defined by the interpretation. Throughout the professional literature, the determination of what is or is not “significant” is left to the judgment of the professional. (b)We believe that this is appropriate in the context of this Proposal. Any guidance provided by PEEC as to what is “significant” would, in all probability, itself be subject to professional judgment in interpreting such guidance. We do not believe that the inclusion of the concept of “significant” in the definition of a financial information system means that PEEC has proposed a less restrictive standard. Rather, we believe that the PEEC has recognized that not all interactions with a client’s financial information system has either a direct or meaningful effect upon the client’s financial statements or financial processes. ○ (b)Accordingly, we approve of the exception and consider it appropriate. We also believe that the member’s judgment as to the component(s) being not significant should be appropriately documented. ○ (c)The definition of financial information system in paragraph .02 a. provides sufficient guidance to the member as to the fact that members should be thinking broadly about processes that may affect a financial process such as information technology general controls. However, we believe that the member should consider the factors listed when determining whether a non-attest service is related to a financial information system. As proposed, the definition indicates that these are factors the member may consider. We believe that the stronger language will emphasize processes that may affect a financial process by making their consideration presumptively mandatory. Accordingly, we request that the PEEC reconsider the wording in this section of the terminology. • (3) Dashboard reporting allows management to review key performance indicators on a near real time basis. We believe that the answer to this question is dependent on the

Comment Letter	Feedback Highlights
	<p>type of management-level dashboard reporting in question. There are many types of dashboards, including, but not limited to, human resources, sales, customer relationship management, operations, project management, etc. Some, but not all, of the types of dashboards available on the market may be considered to be part of the financial system. Accordingly, we believe that the interpretation should clearly indicate that those dashboard reports that assist management with making decisions that impact financial reporting should be included.</p> <ul style="list-style-type: none"> • (4) The proposed implementation date of one year after the publication of the revised interpretation in the Journal of Accountancy is sufficient time for practitioners to familiarize themselves with the revisions to ET 1.295.145; assess which, if any, engagements or services the revisions might affect; and determine how to efficiently and effectively adopt the revisions of the interpretation to those engagements or services.
<p>CL 2</p> <p>Piercy Bowler Taylor & Kern <i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> • (1) We believe the terms, as defined in para. 02 of the proposed interpretation are consistent with their usage in today's industry and would be understood well enough by those who are not practicing within the area. However, we recommend clarification as to whether the term, designing an information system, is intended to relate to both the development of a network and to a computer/server or to only one of those (since they are fairly independent of each other). <p>In addition, we believe definitions of the terms, interface, application program interface (API) and data translation, not commonly known to CP As, should be added to para . . 02 in the final version, perhaps by relocating them from paras .. 13, .15 and .16, respectively. See also our comment about the term, dashboard, in our response below to request no. 3.</p> <ul style="list-style-type: none"> • 2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) As discussed in the main body of this letter, we believe the proposed definition of financial information system should be narrowed considerably so as to make clear that the practice of importing a client's often unadjusted general ledger data from its trial balance into a member's electronic practice aids software is not intended to be covered by such definition and that adequate

Comment Letter	Feedback Highlights
	<p>useful (but nonprescriptive) guidance be provide to help members apply the necessary judgment to determine what is intended to be covered.</p> <ul style="list-style-type: none"> ○ (b) We do not agree that the proposal, as written, would readily support such a conclusion, but we firmly believe it should because we believe no design or development function of a component of the financial information system that is not significant to the financial statements or financial process as a whole should preclude a judgment that any related threat to independence is acceptable. ○ (c) Although the term financial process is not defined in the proposed interpretation, we believe it is generally understood by members as is the inclusion within its meaning of information technology general controls. However, as set forth elsewhere in this letter, we do not believe the language in the proposed interpretation allows for, or provides sufficient guidance as to, the application of professional judgment as to how to use it to assess the significance of any effect on a financial process of any feature specific functional thereof. • (3) We believe the term dashboard reporting has many meanings in different contexts and is likewise not commonly understood by members. Although used in the ED in a context that in our opinion should be expressly excluded from the definition of financial information system, because it would not be directly involved in the preparation of financial statements to be reported upon by the member, the term dashboard reporting does not appear anywhere in the proposed interpretation. We believe this definitional exclusion should be stated in the final version of the interpretation and that the term should be defined in para . . 02 thereof. • (4) We believe an extended period of time for implementation would be necessary if a final interpretation were to be adopted that required significant new documentation and internal approvals to support independence conclusions in covered circumstances or to deal with any conclusions as to independence impairments that unfortunately become necessary as a consequence of the final interpretation. <p>Other Comments</p>

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	<ul style="list-style-type: none"> <li data-bbox="667 266 1860 597"> <p>We understand that whenever a member judges an independence threat identified to be at an acceptable level, the member takes on a burden under the conceptual framework to create unnecessary, self-serving, "hoop-jumping" documentation of that judgment and the safeguards in place that are claimed to constitute an adequate basis therefor. Accordingly, we believe, on the other hand, that when the acceptability of such a threat is effectively prejudged in a published ethics interpretation or a standard, the member should be relieved of that documentation burden. To accomplish this, we believe that rather than characterizing such circumstances as threats that are acceptable, para. 03 of the final version of the proposed interpretation should state clearly that they should not be deemed threats at all.</p> <li data-bbox="667 639 1860 1003"> <p>Customizing a commercial off-the-shelf (COTS) financial information system, as described in para. 11 of the proposed interpretation, can entail matters of widely varying significance in relation to the overall functionality of the system relative to a client's financial processes or to preparing its financial statements as a whole. Accordingly, we believe that para. 12 of the proposed interpretation should provide for a significance evaluation by the member of the nature and extent of a COTS customization service, the results of which could enable a conclusion that any related threat to independence may be judged acceptable given relatively low significance and the applicability of adequate safeguards. In any event, the interpretation should not preclude such a judgment outright, as it now proposes. (See our response to the Committee's requests for specific comments no. 2b.)</p> <li data-bbox="667 1045 1860 1403"> <p>We believe that providing for early adoption would unduly expose members who choose not to early adopt to a significant litigation risk for failure to do so. Accordingly, we believe the final version should neither suggest nor prohibit but be silent on the option for early adoption. Although we have no difficulty with the assertion contained in the first sentence of the fourth paragraph of Part II of the Explanation of the Proposed Revisions that the "critical to the interpretation is whether the information system is a financial information system," our most forceful objection is the other conclusion in the ED that invokes the definition contained in para. 02a of the proposed interpretation of the term, financial information system, i.e., 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</p>

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	<p>financial information system." We see that definition as overly broad and vague especially when unsupported by useful guidance as to the meaning of "significant."</p> <ul style="list-style-type: none"> • As suggested in question 2a of the Request for Specific Comments and discussed further in our response thereto presented in the accompanying attachment, we agree that the determination of what is "significant," should necessarily be left to the professional judgment of the member. However, such a suggestion as to the need to apply professional judgment is not articulated, as we believe it should be, in the language of the proposed interpretation, itself, nor is any useful application guidance provided. • We believe the example of the application of judgment presented in the last paragraph of part II of the Explanation of the Proposed Revisions (which is likewise is not part of the interpretation, per se) is virtually unintelligible and must be rewritten more clearly to serve as useful guidance. • Additionally, without sufficient useful guidance, we find the proposed definition of the term, financial information system, to be too broad, far-reaching and imprecise to prevent it from being effectively interpreted as to preclude (inappropriately, in our opinion) independent auditors or accountants from performing procedures that are common to most audit firms (possibly except for the very largest) to assist small clients in the preparation of their financial statements with no opportunity to find any related threat to independence acceptable by complying with the independence-preserving constraints originally set forth in Ethics Interpretation 101-3 (ET sec. 1.295, most specifically 1.295. I 20.02c-e). We are referring specifically to the common practice of importing a client's often unadjusted general ledger data from its trial balance (which is typically created by a COTS financial information system maintained by the client) into the member's electronic practice aids software. Such software generally allows for adjustments and transfer of the adjusted data to a suitable template for creating professional-looking financial statements for the review and acceptance of responsibility by client management pursuant to ET sec. 1.295. Accordingly, we believe the final interpretation should expressly state that such use of a member's electronic practice aids software to aid in the preparation of a client's financial statements is permitted, as it

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	<p>has been heretofore pursuant to ET sec. 1.295, and does not constitute a threat to independence.</p> <ul style="list-style-type: none"> • If the foregoing is not expressly stated in the final interpretation, we believe the potential for interpreting its proposed definition of financial information system as precluding a member's independence when using an electronic information systems platform to provide such assistance services consistent with the extant language in ET sec. 1.295 would disrupt historical engagement arrangements, have an immeasurable adverse consequential effect on the ability of firms to provide audit and other attest services to small clients and constitute a formidable hardship and disservice to those clients. We sincerely hope this effect is not consistent with the Division's intent.
<p>CL 3</p> <p>Florida Institute of CPAs <i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> • (1) The Committee is concerned the proposed terminology is not consistent with the definition of Information Technology Services in Government Auditing Standards¹ (GAS). Because the proposed terminology is not consistent with GAS, the Committee believes this may create confusion for auditors when evaluating threats to independence. <p>With respect to “Configuring a COTS Financial System Software Solution”, the Committee believes paragraphs .09 and .10 should be expanded and at least one example provided. For example, the Committee is not sure “...selecting the predefined format of certain data attributes and the inclusion or exclusion of such attributes.” would be easily understood. Some auditors might not recognize “configuring” in this context would include actions such as defining the account number structure or financial information format.</p> <ul style="list-style-type: none"> • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) The Committee does not believe it is appropriate to define “significant” as it is a matter of auditor judgment. ○ (b) The Committee believes the exception is appropriate and the proposed standard is not, in the opinion of the Committee, less restrictive than current standards.

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	<ul style="list-style-type: none"> ○ (c) The Committee believes the phrase “financial process” clarifies member responsibilities relating to processes potentially affecting a financial process. • (3) The Committee believes management-level dashboard reporting assists management in making decisions directly affecting financial reporting. Additionally, the Committee believes dashboard reporting is a common method by which management accesses information, including financial information for decision making. • (4) The Committee believes the proposed interpretation should require the auditor to assess the ongoing effect of Information System Services retrospectively and prospectively when evaluating the effect of such services on independence. For example, an auditor should evaluate the effect of providing Information System Services provided in prior years the first year the entity becomes an assurance client and all years thereafter.
<p>CL 4 National Association of State Boards of Accountancy (NASBA) <i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> • (1) NASBA believes the terminology will be readily understood. We do caution PEEC to avoid the use of technology-related terms (for example, “dashboard”) that, given the rapid evolution of technology, may fall out of use in a short period of time. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) The term “significant” is linked to “materiality” in the explanation section of the Exposure Draft (bottom of page 6 as follows): <p style="margin-left: 40px;">“Information generated by the system is ‘significant’ if it is probable that it will be material to the financial statements of the attest client.”</p> <p>To strengthen the guidance, NASBA suggests that PEEC incorporate a similar linkage in the interpretation. Given the prevalence of the term “materiality” in the accounting and auditing literature, this change should enable the practitioner to more confidently apply professional judgment to the independence assessment.</p> <p>If PEEC is amenable to making such linkage, we further suggest that PEEC carefully consider whether the phrase, “probable that it will be material to the financial statements of the attest client” is the appropriate wording to guide practitioners.</p>

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	<ul style="list-style-type: none"> ○ (b) NASBA believes the exception is appropriate. However, we suggest that PEEC consider incorporating an additional requirement that practitioners also consider the aggregate impact of multiple design or development projects or engagements in determining significance to the financial statements or financial processes as a whole. NASBA believes the concept of “significance” should be tied to the concept of “materiality.” A practitioner may design or develop various components of an attest client’s financial information system that individually are not significant or material to the financial statements or financial processes as a whole. However, when aggregated, such work may in fact meet such threshold and should not be permitted under the exception. ○ (c) NASBA believes the phrase “financial process” encourages practitioners to think broadly about processes in determining whether their work relates to a financial information system. <ul style="list-style-type: none"> • (3) NASBA believes that, depending on its design and functionality, management-level dashboard reporting may be relevant in determining whether an information system service is related to a financial information system. The PEEC is encouraged to be careful in how such terms are presented in the interpretation, as today’s technological terms have the tendency to fall quickly out of use. PEEC may want to consider replacing “dashboard” with the phrase “business visual analytic and reporting application tools.” <p>NASBA suggests that PEEC consider issuing guidance on this point (perhaps in the form of a Frequently Asked Question (FAQ)) using the paragraph on page 7 before III. Request for Specific Comments.</p> <ul style="list-style-type: none"> • (4) NASBA agrees that practitioners may require an extended implementation period and that one year from publication of the final standard is the appropriate period. There may be some projects currently being performed by professionals that may need to be completed, transferred or terminated as a result of the proposal. This one-year time period would allow for an orderly transition. • Additional Comments <ul style="list-style-type: none"> ○ <i>Scope of the interpretation</i>

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	<p>The proposal focuses on the impact of information system services on financial reporting attestation engagements, but does not address the impact these services have on other types of attestation engagements. NASBA suggests that PEEC broaden the scope of the interpretation to go beyond financial reporting considerations and address the potential threats to independence that may exist in the context of other attest services. For example, a firm may install a non-financial system for an attest client and then issue a System and Organization Controls (SOC) 2 or 3 report on the same system, which would appear to raise self-review and management participation threats to the firm's independence.</p> <ul style="list-style-type: none"> ○ <i>Terminology</i> <p>We note that in par. 2(a) of the proposal, practitioners “may consider” four (4) factors in determining whether a nonattest service is related to a financial information system. We believe the practitioner should consider these factors given the critical distinction between financial and other information systems in the proposal.</p> <p>Also, for completeness purposes, i.e., since the interpretation defines “design” and “development” of an information system, we suggest that PEEC incorporate as an additional defined term “implementing an information system” in par. 2(d) of the interpretation.</p> ○ <i>System and Network Maintenance, Support and Monitoring</i> <p>We believe that PEEC may want to clarify the examples of permissible services described in paragraph .20b and .20c that appear to be part of the precluded services in paragraphs .19f and .19c, respectively.</p> <p>Additionally, we believe there could be misunderstanding as to what is a discrete, nonrecurring project. Some professionals may consider a discrete, nonrecurring project could be performed every other year, or two or three times within a five-year period. We suggest that PEEC consider whether further guidance could better distinguish the examples in pars. .19 and .20.</p>

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CL 5	Pre-certification Education Executive Committee <i>Supports as Drafted</i>	No Comments
CL6	Yeo and Yeo CPAs and Business Consultants <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> • While we fully support the need to better define and identify activities that would result in a member acting as Management and thereby impairing independence, we also recognize that, given the breadth of potential Information System Services, it is impractical to define every scenario where such an impairment may occur. We would ask that the parties take a closer look and reconsider the language contained within section 19 contained under “System and Network Maintenance, Support and Monitoring” • We believe the committee has done a very good job in clarifying most Information System Services relative to system design, implementation, installation, configuration, customization, and services related to interface modification and data translation. We would ask that the parties take a closer look and reconsider the language contained within section 19 contained under “System and Network Maintenance, Support and Monitoring”. • We believe that the language as written is overly narrow and fails to recognize that the listed services are delivered in a myriad of ways. In fact, these value added services are increasing provided by members to the market and are often not provided in place of management, but at the request of management. While seemingly innocuous, this distinction is extremely important. It is very commonplace, especially within small and mid-sizes organizations for management to retain all decision making responsibilities and simply assign a member a task or series of tasks. In these cases, it is our belief that members are not acting as management. • While it is logical that a firm should not audit the work it has performed, a blanket independence impairment does not seem appropriate. For the purposes of identifying what impairs independence, we believe the key distinction in the examples listed in section 19 should be management’s decision making status and involvement in the delivery process.

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	<ul style="list-style-type: none"> <p>We believe that the second sentence of section 19 should be amended to read as follows:</p> <p>“If post-implementation services involve the attest client <i>delegating any type of decision making authority and</i> outsourcing an ongoing function, process, or activity to the member that in effect would result in the member assuming a management responsibility, 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.”</p> <p>We believe that 19(a) should be clarified to read:</p> <p>“Operates the attest client's network, such as managing the attest client’s systems or software applications <i>without specific and continuous direction from management</i>”</p> <p>We believe that 19(b) should remain as drafted as this is a service where the member would clearly be acting as management.</p> <p>We believe that 19(c) should be clarified to read:</p> <p>“Has responsibility for monitoring or maintaining the attest client's network performance <i>without specific and continuous direction from management</i>”</p> <p>We believe that 19(d) should be clarified to read:</p> <p>“Operates or manages the attest client’s information technology help desk <i>where management has not dictated an industry standard framework to be used (ITIL, ITSM, etc.) and a set of standard operating procedures</i>”</p> <p>We believe that 19(e) should be clarified to read:</p> <p>“Has responsibility to perform ongoing network maintenance, such as updating virus protection solutions, applying routine updates and patches, or configuring user settings <i>without specific and continuous direction from management</i>”</p>

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	<ul style="list-style-type: none"> We believe that 19(f) should be clarified to read: “Has responsibility for maintaining the security of the attest client’s networks and systems <i>without specific and continuous direction from management</i>” We believe a statement similar to paragraph 08 should be added to this section to read: <i>“When a member provides system and network maintenance, support and monitoring under the specific direction of management, with management retaining responsibility for such functions, threats to compliance with the “Independence Rule” would be at an acceptable level, provided all the requirements of the “Nonattest Services” subtopic of the “Independence Rule” are met.”</i> It does appear that the committee has also drawn a major distinction between discrete nonrecurring and on-going services and it appears that it considers recurring or ongoing services as much more likely to impair independence. We do not believe this is the case. Technology has made nearly all of these service portable and easily replaceable. Management can at any time decide to replace a member with any number of alternatives. The fact that services are easily moved only further empowers the independence of management to operate their businesses as they see fit and reinforces the member’s responsibility to act in an ethical and professional manner.
CL 7 Crowe LLP <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> (1) We believe the terminology is consistent with industry practice unless otherwise noted in our observations we have provided on the interpretation. (2)(a)(b)(c) <ul style="list-style-type: none"> (a) We believe the determination of “significant” should be left to professional judgment. The auditing standards provide guidance on determining significance to the financial statements; therefore, we do not believe this should be defined within the professional code. (b) While providing an exception for non-significant components makes sense in theory, it would be difficult to apply in practice since the evaluation of significance would require on-going consideration. If the component becomes significant in the future, the member’s independence would become impaired at that time. We

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	<p>believe it is possible for a component to be unrelated to the financial statements even though the component is part of a financial information system and providing services related to the component should not impair independence. See our observations provided above related to this point.</p> <ul style="list-style-type: none"> ○ (c) We do not believe the term “financial processes” utilized in paragraph .02a is a term widely understood in the industry. We suggest adding an explanation similar to how the term is defined on page 6 of the proposal. We believe it would be helpful to include this explanation in the interpretation or in non-authoritative guidance. • (3) Dashboard reporting can vary widely in its usage, which makes it difficult to broadly assess independence implications. We agree that if the dashboard reporting is used by management in setting or evaluating reserves or other financial related amounts or disclosures, then that system would be related to financial statements and would impair independence. However, if the dashboard reporting assists management with improving efficiency or effectiveness of operations, the system would be unrelated to the financial statements and would not impair independence. • (4) We believe an extended period of time would be necessary to allow discontinuation of services that would be deemed to impair independence under the clarified interpretation. • Other Observations <ul style="list-style-type: none"> ○ The definition of a commercial-off-the-shelf (COTS) system refers to a third-party vendor, but we believe it would be helpful to specifically state in the interpretation that a member cannot provide implementation, installation, configuration or customization services for a system the member designed or developed. We believe it is important to clarify this point because members could be designing systems that are COTS. A member could incorrectly apply paragraphs .05-.18 by assuming they can install or implement a system they designed as long as it is a COTS system. ○ Paragraph .03 permits a member to design, develop and implement a non-financial information system, but this section does not address configuration or

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	<p>customization. We suggest clarifying paragraph .03 to permit a member to configure and customize a COTS non-financial information system as threats to independence would appear to be at an acceptable level, provided all of the requirements of a non-attest service are met.</p> <ul style="list-style-type: none"> ○ A member may design and develop custom solutions and products; design or develop modules/components for COTS systems; or design or develop components for a commercially available platform or development framework solution such as SharePoint. We believe the interpretation should address that design or development may include various methods. ○ We believe the term “template” used in paragraph .04 should be clarified. It is unclear if a template is a spreadsheet or web-based application. We believe the term “template” should refer to an Excel spreadsheet. ○ Paragraph .07 addresses situations where software is loaded on a computer. We believe this section should also address systems installed in cloud environments. ○ It is unclear to us whether paragraphs .11 and .12 apply to customization that is unrelated to financial reporting. For example, some customization may improve ease of use and may not impact how transactions or data are processed. We noted that paragraph .09 defines configuration as selecting the features, functions, and settings that determine how the software will perform certain transactions and process data. We believe the definition of “customize” in paragraph .11 should include similar language as we do not believe independence would be impaired if the member customized features that do not impact how transactions or data are processed. ○ For paragraphs .15 and .18, we assume that an “API developed by a third party” means that the API must be unaltered and auditable in how it is used and how it processes data that is moved through that API protocol. We suggest clarifying that point through the interpretation or in non-authoritative guidance.

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	<ul style="list-style-type: none"> ○ Paragraph .19e indicates that independence would be impaired if the member accepts responsibility for performing ongoing network maintenance. However, paragraph .20c states that independence would not be impaired if the member applies certain updates and patches on a discrete basis. We believe more guidance is necessary to assist members in differentiating between ongoing and discrete activities. For example, if the member applies updates and patches only at the direction of the client and under their supervision, would that be considered a discrete activity since the member is executing each update as a separate occurrence and is not taking responsibility for performing ongoing maintenance? ○ Paragraph .20 provides several examples of services that do not impair independence. Item (d) indicates that providing training or instruction on a new software solution does not impair independence. Is the reference to “new software” critical to the determination about whether this is an acceptable service? For example, would it be acceptable to provide training to new users of an existing software solution?
CL 8 Deloitte & Touche LLP <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> • (1) In our view, the terminology used in the proposal is consistent with industry practice. However, in an effort to provide additional guidance to members, the PEEC should consider clarifying whether there is an instance where a software package or solution designed or developed by a third party (i.e. not the member) would not be considered a commercial off-the-shelf software solution. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) In our view, use of the term “significant” in the context of determining whether the nonattest services to be performed relate to a financial information system is appropriate. We believe it would be difficult for the PEEC to be prescriptive in defining significance given the variation of factors to be considered when evaluating potential threats to independence (size and scale of clients involved, nature of the nonattest services, scope of audit procedures to be performed with respect to the clients, etc.). The factors included in .02 (a) of the Proposed Interpretation serve as useful considerations in determining significance and provide the member with the ability to use professional judgment when assessing such threats. To provide additional guidance, the PEEC may want to consider

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	<p>including in the Text to the Proposed Interpretation an additional consideration in .02 (a) related to materiality. Such concept was included within the Explanation of the Proposed Revision and states, "...Information generated by the system is "significant" if it is probable that it will be material to the financial statements of the attest client..."</p> <ul style="list-style-type: none"> ○ (b) In our view, including the concept of "significant" in the definition is appropriate. Consistent with our comments in 2.a. above, .02(a) of the Proposed Interpretation provides useful guidance to members identifying a financial information system and factors to consider when determining whether a nonattest service relates to such systems. We believe including "significant" in the definition provides the member with an ability to apply professional judgment when evaluating potential threats to independence. ○ (c) In our view, the PEEC should consider including clearer guidance of the PEEC's intent and expectation of members for evaluating independence threats when providing information system services that may affect a financial process; specifically, information technology general controls. We believe the PEEC's guidance should consider the scope of the member's audit when assessing the threats created by such services. A member may not be engaged to issue an opinion on an attest client's internal controls, which may result in the member not considering information technology general controls when evaluating threats to independence because the self -review threat may not be apparent or significant. • (3) In our view, we believe there may be situations where the design and implementation of a management-level dashboard reporting system may not be viewed as (1) related to a financial system and/or (2) assisting management in making decisions that directly affect financial reporting. In these circumstances, we believe these services would not pose significant threats to independence. Examples may include dashboard reports that serve only to display certain historical information and provide alternative views or trends of existing data from an attest client's financial systems or are operational in nature. In this case, the management-level dashboard reporting system designed by a member would use the client's existing financial systems as an input and would not be

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	<p>management's primary source for internal controls over financial reporting decision making.</p> <p>However, consistent with the Proposed Interpretation, the design and implementation of a system that provides management-level dashboard reporting may be indicative of providing nonattest service related to a financial system when that system (a) gathers data and provides such data in a dashboard report format that management uses to make decisions that directly affect financial reporting or (b) allows management to perform ongoing evaluations of the attest client's internal control as part of its monitoring activities.</p> <ul style="list-style-type: none"> • (4) Our view is the extended period of time is reasonable in order to provide members adequate time to evaluate and operationalize any changes that may be necessary to comply with the Proposed Interpretation. • Additional Comments and Feedback <ul style="list-style-type: none"> ○ A. Clarification of "Maintenance, Support, and Monitoring" <p>We note paragraphs .19, specifically item e., and .20 from the "<i>System and Network Maintenance, Support, and Monitoring</i>" section of the Proposed Interpretation and paragraph .04, specifically item f., from the Hosting Services Interpretation (ET Section 1.295.143-Effective September 1, 2018) (the "Hosting Interpretation") (refer to Appendix for excerpts). We are seeking confirmation from PEEC with regard to situations whereby a member licenses permissible software, as provided for under the Hosting Interpretation and permitted under the Proposed Interpretation (if not related to a financial system), and the permissible software requires certain bug fixes or other routine patches. In this case, all licensees of such software receive the bug fixes or other patches in accordance with the terms of the existing license. In our view, this would not constitute the outsourcing of an ongoing function, process, or activity to the member that in effect results in the member assuming a management responsibility and would not be indicative of a member's independence being impaired.</p> ○ B. Clarification with respect to "Monitoring" activities

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	<p>We note Section 1.295.030 Management Responsibilities of the extant AICPA Code of Professional Conduct (“Code”) paragraphs .01 and .02(l) and paragraph .20 of the Proposed Interpretation (refer to Appendix for excerpts).</p> <p>In our view, there appears to be a potential inconsistency between the extant Code and the Proposed Interpretation with respect to “monitoring activities.” Specifically, Section 1.295.030 of the extant Code considers monitoring activities a management responsibility, and the performance of such would impair independence. However, paragraph .20 of the Proposed Interpretation includes reference to the permissibility of “monitoring services that are discrete nonrecurring engagements.”</p> <p>We request the PEEC to clarify and perhaps include specific examples within the Proposed Interpretation of those circumstances whereby performance of monitoring services in a discrete nonrecurring manner, as provided for in the Proposed Interpretation, would not be considered a management responsibility and therefore not impair the member’s independence.</p>
<p>CL 9 Schneider Downs <i>Does not Support as Drafted</i></p>	<ul style="list-style-type: none"> • 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?

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	<ul style="list-style-type: none"> • 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. • 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 <p>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.</p> <ul style="list-style-type: none"> ○ 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

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	<p>attest services. This could jeopardize a member's independence in the future period through no action of its own.</p> <ul style="list-style-type: none"> ○ 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. <p>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.</p> <ul style="list-style-type: none"> ● Financial Processes and Information System General Controls <p>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.</p> <p>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.</p> <p>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.</p>

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	<p>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.</p> <p>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.</p> <ul style="list-style-type: none"> Exceptions for Fixed Asset Software and Deferred Tax Templates <p>Under the proposed defining criteria for financial information system in the ED, we believe that the AICPA should expand the list of exceptions.</p> <p>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.</p> <p>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).</p> Assessing Management Participant and Self Review Threats to Independence <p>The AICPA has often afforded the member the opportunity to assess threats to its independence as well as ways to mitigate those threats.</p> <p>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</p>

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	<p>through sampling and testing performed as if the calculations were generated by any other information system.</p> <p>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.</p> <p>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.</p> <ul style="list-style-type: none"> <p>Management Approvals within Software Products</p> <p>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.</p> <p>Recommendation to Focus on the Primary Financial Information System</p> <p>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</p>

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	<p>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.</p> <p>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.</p> <ul style="list-style-type: none"> Non-financial Customizations to Commercial Off-the-Shelf (COTS) Financial Information Systems <p>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.</p> <p>As examples:</p> <ul style="list-style-type: none"> ○ 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? <p>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.</p>

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	<ul style="list-style-type: none"> Clarification Regarding the Aggregation of Source Data <p>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.</p> Timeline and Impact of This ED on Prior Conclusions Reached <p>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.</p> <p>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.</p> <p>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.</p>
CL 10 Society of Louisiana CPAs Ethics Committee <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> (1) We believe that the terminology used is probably consistent with industry practice but we are not sure that members will understand and draw the required distinctions between aspects of a financial and nonfinancial information system. (2)(a)(b)(c)

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	<ul style="list-style-type: none"> ○ (a) We believe that specific guidance would be extremely helpful since the term “significant” can be assessed differently by various members. We also believe that examples are very beneficial and should be used. The one example in the ED, tends to raise questions than provide guidance. ○ (b) We feel that the exception only creates additional problems to be addressed at a later date. The concept of “significant” in this situation, only adds to a lack of clarity for this ED ○ (c) Yes, we see no problem with the term “financial processes” as used in this ED. • (3) Yes, because the intent of a dashboard is to provide a summary of concise, current information to management at a glance to allow them to make decisions. We feel that a number of these decisions could affect financial reporting. • (4) No, since firms are currently addressing nonattest services when performing attest service engagements, this does not appear to create issues that would require additional time to implement. A one year implementation date should be sufficient to allow firms to address the requirements in this ED. There may need to be a period of time for projects in process by these firms that would require “grandfathered status.”
CL 11 Sikich LLP <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> • (1) Section 1.295.145.02 of the proposed interpretation includes several definitions that we believe could be modified to improve understanding and to ensure consistent application by members: <ul style="list-style-type: none"> ○ a.iii states “A system that gathers data that assist management in making decisions that directly impact financial reporting” may be considered when evaluating whether the nonattest service is related to a financial information. We believe this nonattest service should not be considered part of a financial information system, as noted in our response to Question 3 below. This definition is overly broad as most, if not all, decisions made by management ultimately have an impact on financial reporting but few would result in a straight-line “direct” impact on financial reporting. Furthermore, without more specific guidance this lack of clarity could lead to inconsistent evaluation of the nonattest service among

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	<p>practitioners and an unnecessary limitation on the types of services clients value from members.</p> <ul style="list-style-type: none"> ○ b. utilizes the terms “blueprint” and “schematic” in the definition of the design of an information system. These terms are not common in attest services and, as a result, we believe this definition creates uncertainty to attest practitioners. We understand the objective is to differentiate that the design (establishing the framework for the process flow) of an information system is a necessary step to be performed prior to the development (primarily creating code) of an information system, but the terminology noted above is more prevalent to other professions and could create unintended diversity in application of the guidance. <p>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.</p> <ul style="list-style-type: none"> • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) We believe it is appropriate to have the determination of “significant” subject to the professional judgment of the member as this is consistent with the Conceptual Framework Approach. Page 6 of the Explanation of the Proposed Revision includes a definition of “significant” that still incorporates the professional judgment of the member as it relates “significance” to financial statement materiality, which is clearly subjective. Also, as noted in ET Section 1.210.010.07, “Threats are at an acceptable level either because of the types of threats and their potential effect or because safeguards have eliminated or reduced the threat, so that a reasonable and informed third party who is aware of the relevant information work perceive that the member’s professional judgment in not compromised.” Inherent in the Framework is the determination, based on the member’s judgment, that certain threats are more significant than others or that application of one or more safeguards can mitigate a threat. Incorporating the definition set forth in the Explanation would improve the guidance. In addition, we also believe it would be appropriate to require the member to document the rationale and reasoning justifying the determination that the system in not “significant”.

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	<ul style="list-style-type: none"> ○ (b) We believe the exception to allow a member to design or develop a component of the financial information system that is not significant to the financial statements or the financial process as a whole is appropriate. While some may argue this concept results in a less restrictive standard than the current interpretation, we believe, for the reasons articulated in our response to question 2.a, that the concept is appropriate. ○ (c) We do not believe the phrase “financial process” makes it clear that members should be thinking about information technology general controls or similar matters. The question itself demonstrates the lack of clarity when it asks if members should be thinking broadly about processes that may affect a financial process. We recommend the definition be changed to read “Financial information system is a system that aggregates source data underlying the financial statements or generates information that is significant to the financial statements or financial processes and/or controls, including but not limited to information technology general application controls, taken as a whole.” This incorporates the discussion on page 6 in the Explanation of the Proposed Revision. • (3) We believe that, as this interpretation is written, management level dashboard reporting would be included as a nonattest service related to a financial information system but we do not believe such inclusion is warranted. Decisions that directly impact financial reporting could be interpreted to cover virtually all management decisions that ultimately impact financial transactions – deciding to increase the number of workers assigned to the assembly line directly impacts the reporting of components of cost of goods sold, etc. As such, we believe the language “a system that gathers information” in the proposed factor above is overly broad and should be removed from the interpretation. Dashboard level reporting that does not alter the underlying recording or aggregation of data specifically utilized in financial reporting is essentially an enhanced tool or add-on that does not impact the functionality of the financial information system and therefore should be permissible with the application of the appropriate safeguards. Dashboard reporting facilitates management assumption of management responsibilities and does not involve the delegation of such to the member either in the creation of the dashboard to facilitate accumulation of information management deems important to the operation of the business or in the ultimate decisions made by management.

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	<ul style="list-style-type: none"> • (4) If this interpretation is adopted as proposed, or without major substantive changes to the guidance set forth, we believe the extended period of time for implementation, combined with an early implementation option is appropriate. Some members likely will need to make more fundamental changes to the way services are provided to clients and the additional time should allow for less disruption to the members' practices and allow clients to seek other alternatives should independence issues exist based on the revised interpretation. • Additional Comments/Questions Submitted <ul style="list-style-type: none"> ○ Section 1.295.145.04 of the proposed interpretation stipulates the design of an attest client's financial information system creates a threat to independence that could not be reduced to an acceptable level by the application of safeguards. There are many consulting and other nonattest services that result in specific recommendations for process improvements or modifications to the control environment that do not result in an impairment of independence provided all the requirements of the "Nonattest Services" subtopic of the "Independence Rule" are met. These other services could appear similar in nature to the concept of the design of a financial information system. The interpretation, as written, presumes the member will perform both design and development/implementation services which collectively pose a threat considerably greater than design services alone. We believe members should be able to design (create the blueprint) for a financial information system without impairing independence as long as management reviews and approves the design and performs all management responsibilities with respect to development and installation. These elements of the overall system implementation may well be performed by other members or vendors. ○ Sections 1.295.145.19 and .20 of the proposed interpretation address maintenance, support and monitoring services. Specifically, paragraph 19 d provides that independence would be impaired if the member "Has responsibility to perform ongoing network maintenance, such as updating virus protection solutions, applying routine updates and patches, or configuring user settings" while paragraph 20 establishes an exception if such services are "discrete nonrecurring engagements". As a practical matter, many members may enter into engagements covering an extended period of time for which they could be

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	<p>compensated on a retainer basis to provide such services on an as-needed basis. Such agreements reduce the need to create multiple engagement letters covering general services and, in effect, provide an understanding for the performance of multiple “discrete” services throughout the year. We believe forcing members to establish each instance of providing these services as “discrete” engagements places an unnecessary burden on the practitioner. We further believe all the requirements of the “Nonattest Services” subtopic of the “Independence Rule” can be met by having management provide specific and continuous direction to the member throughout the term of the services and, as such it should be acceptable for members to structure the arrangements with clients in a manner that facilitates effective utilization of members’ services.</p>
<p>CL 12 PCPS Technical Issues Committee <i>Does not Support as Drafted</i></p>	<ul style="list-style-type: none"> (1) 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. <p>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.</p> <p>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.</p>

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	<p>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.</p> <p>In addition, Section .02 b of the ED indicates the following:</p> <p style="padding-left: 40px;">“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.”</p> <p>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.</p> <p>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:</p> <ul style="list-style-type: none"> ○ 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? <p>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.</p>

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	<p>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.</p> <p>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.</p> <ul style="list-style-type: none"> • (2) (a)(b)(c) <ul style="list-style-type: none"> ○ (a) 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) 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

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	<p>significant. Therefore, with a broad definition of significant, this may cause issues.</p> <ul style="list-style-type: none"> ○ (c) 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. • (3) 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. <p>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.</p> <ul style="list-style-type: none"> • (4) 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 <ul style="list-style-type: none"> ○ <i>Subscriptions and bundling of services</i> <p>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</p>

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	<p>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.</p> <ul style="list-style-type: none"> ○ <i>External audit integration installations or access</i> <p>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.</p> <ul style="list-style-type: none"> ○ <i>Section .04 Discrete calculation</i> <p>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.</p> <p>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 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?</p>

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	<p>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.</p> <ul style="list-style-type: none"> ○ <i>Interface Services</i> <p>Paragraph .14 of the ED indicates the following:</p> <p>“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.”</p> <p>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.</p> <p>TIC believes that more than just APIs should be scoped out for purposes of paragraphs .13 through .15 of the ED.</p> <ul style="list-style-type: none"> ○ <i>Data Translation</i>

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	<p data-bbox="766 235 1346 261">Paragraph .17 of the ED states the following:</p> <p data-bbox="861 300 1860 464">“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.”</p> <p data-bbox="766 500 1860 932">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.</p> <ul data-bbox="720 971 1703 1003" style="list-style-type: none"> ○ System and Network Maintenance, Support, and Monitoring and Hosting <p data-bbox="720 1031 1860 1195">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.</p> <p data-bbox="720 1230 1860 1427">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</p>

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	<p>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.</p> <p>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.</p> <ul style="list-style-type: none"> ○ <i>Issues Related to Hosting</i> <p>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.</p> <p>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.</p> <p>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.</p> <p>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.</p> <p>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</p>

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	<p>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.</p> <p>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.).</p> <p>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.</p>
<p>CL 13 BeachFleischman <i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> • We humbly request that the Committee and all other related parties reconsider the language contained within section 19 under "System and Network Maintenance, Support and Monitoring" prior to issuing a final pronouncement. • We feel that the draft language should be modified to recognize that the listed services can be delivered in ways that would not result in the impairment of independence. As CPA firms continue to evolve, many are offering these services to increase the value added to their clients without making management decisions. It is very common for firms working with small and mid-sizes organizations to identify areas for improvement and offer best practices for the management of a network, the achievement of optimal performance, or the security of a system. These recommendations are provided to management who ultimately decides how and if they will be implemented. When an organization possesses individuals with the appropriate skillset to oversee and accept these services, we believe that the threat to independence can be reduced to an acceptable level such that these services can be provided without impairing independence. • We request that the Committee consider the following modifications to the examples listed in section 19 to clarify that independence is not impaired when management

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	<p>decisions are not made by member firms. We believe this distinction is consistent with standards in place over other services firms provide.</p> <ul style="list-style-type: none"> • We recommend modifying the second sentence of section 19 as follows: "If post-implementation services involve the attest client delegating any type of decision making authority and outsourcing an ongoing function, process, or activity to the member that in effect would result in the member assuming a management responsibility, 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." • We believe that 19(a) should be clarified to read: "Operates the attest client's network, such as managing the attest client's systems or software applications <u>without specific and continuous direction from management</u>" • We believe that 19(b) should remain as drafted as this is a service where the member would clearly be acting as management. • We believe that 19(c) should be clarified to read: "Has responsibility for monitoring or maintaining the attest client's network performance <i>without specific and continuous direction from management</i>" • We believe that 19(d) should be clarified to read: "Operates or manages the attest client's information technology help desk <i>where management has not dictated an industry standard framework to be used (ITIL, ITSM, etc.) and a set of standard operating procedures</i>" • We believe that 19(e) should be clarified to read: "Has responsibility to perform ongoing network maintenance, such as updating virus protection solutions, applying routine updates and patches, or configuring user settings <i>without specific and continuous direction from management</i>"

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	<ul style="list-style-type: none"> • <i>We believe that 19(f) should be clarified to read:</i> "Has responsibility for maintaining the security of the attest client's networks and systems <u>without specific and continuous direction from management</u>" • It appears that the Committee has drawn a distinction between discrete nonrecurring and on-going services and preliminarily concluded that recurring or ongoing services are more likely to impair independence. We believe that as long as management is ultimately making all key decisions and overseeing and taking responsibility for the work performed that recurring services would not be more likely to impair independence.
CL 14 Grant Thornton LLP <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> • (1) Grant Thornton believes the terminology used in the proposal is, in general, consistent with industry practice. While many in public practice refer to systems as "packaged" or "off-the-shelf," "COTS" is likely understandable by members who do and do not practice in this arena. Therefore, we recommend that PEEC consider further clarifying the term "COTS" in the interpretation or in a frequently asked question. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) Grant Thornton believes it is appropriate for the guidance to leave the determination of what is "significant" to the professional judgment of the member. Grant Thornton noted that explanation of the proposed interpretation states that information generated by a financial information system is considered "significant" if it is probable that the financial information system will be material to the financial statements of the attest client. However, specific details on how to apply the guidance were not provided within the proposed interpretation. While Grant Thornton does not believe specific guidance within the interpretation is needed, it may be helpful for PEEC to consider providing specific general application guidance or provide such details in an illustrative example scenario to assist with consistent application across the profession in nonauthoritative guidance. For example, Grant Thornton believes specific general application guidance such as how integral is the financial related system being considered for implementation to the audit client's operations, management's expected involvement in the

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	<p>implementation, including their expertise and knowledge, evaluation of the expected nonaudit fees to the audit fees and past experience (or involvement) with the audit client's financial information systems should be considered by PEEC. This additional guidance will assist members in determining what is "significant", and will also guide the member's in further evaluating their independence in appearance, including their integrity and objectivity when considering such implementation services. In addition, PEEC should consider incorporating the following scenarios in the nonauthoritative guidance addressing "significant":</p> <ul style="list-style-type: none"> ▪ "If proposing on a full COTS general ledger package implementation for an audit client, would this be considered material to the financial statements of the audit client or financial processes taken as a whole?" ▪ "If the general ledger COTS package implementation is for a division or branch of the audit client would the conclusion be different and why?" ▪ "If proposing on COTS tax provision software or fixed assets software package implementation for an audit client, would this be considered material to the financial statements of the audit client or financial processes taken as a whole?" <p>Grant Thornton believes the proposed interpretation should include documentation requirements with respect to evaluating the facts and circumstances of the proposed services, including the member's evaluation on whether the system generates information that is "significant" to the financial statements or financial processes taken as a whole, and any potential threats to the member's independence and the safeguards applied to eliminate or reduce the threats to an acceptable level, including documentation of discussions with, and agreement by, the lead audit or attest partner.</p> <ul style="list-style-type: none"> ○ (b) Grant Thornton agrees with the exception allowing 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 as such exception is consistent with the concept of applying a threats and safeguard approach to evaluating the self-review and management participation threats to the member's

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	<p>independence. Further, Grant Thornton believes it would be reasonable to determine that the provision of services relating to a financial information system that is not significant to the financial statements or financial process as a whole would not create a significant self-review and/or management participation threat to the auditor's independence such that the threat(s) would not be at an acceptable level. Furthermore, PEEC should consider providing examples in nonauthoritative guidance (e.g., frequently asked questions) of examples of what may constitute nonsignificant, including significant, design or development of a component of a financial information system.</p> <ul style="list-style-type: none"> ○ (c) Grant Thornton agrees that use of the phrase "financial process" in the proposed interpretation makes it clear that members should be thinking broadly about processes that may affect a financial process such as information technology general controls or other operational processes or functions that may have a financial statement impact. While we believe such objective is clear in the context of the proposed interpretation, it may be appropriate if such objective was explicitly stated within the interpretation. Providing such clarification and examples will assist members with a consistent application of the interpretation. Additionally it may be helpful to use the phrase "financial consolidation and reporting process" to provide further clarification. • (3) Grant Thornton believes that the factor "a system that gathers data that assist management in making decisions that directly impact financial reporting" is broad and should be clarified. We believe practitioners are generally focused on systems that generate reports and trial balances used to support management's financial statement assertions. While we understand that specifying that the system "directly impacts financial reporting" may be intended to limit the scope of the systems considered; however, providing clarified guidance and illustrative examples that differentiates systems which "directly" vs. "indirectly" impact financial reporting will assist with evaluating the criteria and applying the proposed interpretation. Further, Grant Thornton believes that inclusion of management-level dashboard reporting when considering a system that gathers data to assist management in making decisions that directly affect financial reporting as a financial system is subject to interpretation and evaluation of various factors such as the type of organization, how the dashboard reporting is used, etc. In general, Grant Thornton believes that management level dashboard reporting which directly relates to financial

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	<p>reporting should be considered in the evaluation of whether the system gathers data that assists management in making decisions that directly affect financial reporting. Therefore, the system would meet the definition of a financial information system and require evaluation under a threats and safeguard approach. Conversely, management-level dashboard reporting used for operational purposes that is not directly related to financial reporting would generally be excluded from such evaluation. In public practice, many reports are, in fact, custom built on an “off-the-shelf” system showing different points of view, periods, etc. for management and analytical purposes, all of which may not directly support financial reporting. Providing illustrative examples that analyze different scenarios involving management-level dashboard reporting as part of frequently asked questions would assist in applying the proposed interpretation.</p> <ul style="list-style-type: none"> • (4) Grant Thornton agrees with the proposed effective date one year after adoption is appropriate and it provides adequate time for members to evaluate and comply with the proposed revisions, including development of their policies. While we believe many of the concepts and guidance provided in the proposed revisions are commonly used in current public practice, we believe the additional time along with any transitional guidance provided for engagements in process will be used to evaluate what constitutes a financial information system and whether such systems are significant to financial reporting or a financial process. • Other Specific Comments (paragraphs .05 through .20) <ul style="list-style-type: none"> ○ “Implementation of a COTS Financial Information System Software Solution” – Consider using the term “data conversion” instead of “data translation”, defining or clarifying “maintenance” and “support”, and providing example scenarios which include discussion of maintenance and support-type services. ○ “Customize a COTS Financial Information System Software Solution” – Under the extant interpretation, customization services involving insignificant modifications to source code underlying an attest client’s existing financial information system would be permitted. Consider updating paragraph .12 of the proposed interpretation to be consistent with the extant interpretation which

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	<p>specifies the services as prohibited if they involve “other than insignificant modifications or enhancements”.</p> <ul style="list-style-type: none"> ○ “Interface a COTS Financial Information System Software Solution” – Consider also referring to “interface” services as “integrations”. ○ “Data Translation Services Related to a COTS Financial Information System Software Solution” – Consider also referring to “data translation” services as “data conversion” services. ○ “System and Network Maintenance, Support, and Monitoring” – Consider defining “maintenance”, “support” and “monitoring”. We recognize examples were provided in paragraph .19 of maintenance, supporting and monitoring services which are not permissible and those which may be permitted if performed as discrete, nonrecurring project where all the requirements of the “Nonattest Services” subtopic of the “Independence Rule” are met were provided in paragraph .20. However, we believe it would be helpful to provide additional clarification and example scenarios in which permissible services are being provided over multiple periods as separate and distinct projects that would not be considered outsourcing an ongoing management responsibility.
<p>CL 15 Joint Response - Multiple Firms <i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> • We would ask that the parties take a closer look and reconsider the language contained within section 19 contained under “System and Network Maintenance, Support and Monitoring”. • We believe that the language as written is overly narrow and fails to recognize that the listed services are delivered in a myriad of ways. In fact, these value added services are increasingly provided by members to the market and are often not provided in place of management, but at the request of management. While seemingly innocuous, this distinction is extremely important. It is very commonplace, especially within small and mid-sizes organizations for management to retain all decision making responsibilities and simply assign a member a task or series of tasks. In these cases, it is our belief that members are not acting as management.

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	<ul style="list-style-type: none"> While it is logical that a firm should not audit the work it has performed, a blanket independence impairment does not seem appropriate. For the purposes of identifying what impairs independence, we believe the key distinction in the examples listed in section 19 should be management's decision making status and involvement in the delivery process. We believe that the second sentence of section 19 should be amended to read as follows: <p>"If post-implementation services involve the attest client delegating any type of decision making authority and outsourcing an ongoing function, process, or activity to the member that in effect would result in the member assuming a management responsibility, 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."</p> We believe that 19(a) should be clarified to read: <p>"Operates the attest client's network, such as managing the attest client's systems or software applications <u>without specific and continuous direction from management</u>"</p> We believe that 19(b) should remain as drafted as this is a service where the member would clearly be acting as management. We believe that 19(c) should be clarified to read: <p>"Has responsibility for monitoring or maintaining the attest client's network performance <u>without specific and continuous direction from management</u>"</p> We believe that 19(d) should be clarified to read: <p>"Operates or manages the attest client's information technology help desk where <u>management has not dictated an industry standard framework to be used (ITIL, ITSM, etc.) and a set of standard operating procedures</u>"</p>

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	<ul style="list-style-type: none"> • We believe that 19(e) should be clarified to read: “Has responsibility to perform ongoing network maintenance, such as updating virus protection solutions, applying routine updates and patches, or configuring user settings <u>without specific and continuous direction from management</u>” • We believe that 19(f) should be clarified to read: “Has responsibility for maintaining the security of the attest client’s networks and systems <u>without specific and continuous direction from management</u>” • It does appear that the committee has also drawn a major distinction between discrete nonrecurring and on-going services and it appears that it considers recurring or ongoing services as much more likely to impair independence. We do not believe this is the case. Technology has made nearly all of these services portable and easily replaceable. Management can at any time decide to replace a member with any number of alternatives. The fact that services are easily moved only further empowers the independence of management to operate their businesses as they see fit and reinforces the member’s responsibility to act in an ethical and professional manner.
CL 16 UHY LLP <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> • (1) Yes, this proposal is straightforward and should be understandable by all members. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) UHY LLP believes that leaving this determination to the professional judgment of the member is the best approach. ○ (b) UHY LLP believes this exception is appropriate. CPAs should be permitted and encouraged to help their clients solve problems in all areas except where it negatively affects their independence. ○ (c) Yes, we believe the phrase, “financial process,” encourages members to think broadly. However, it would be useful if the final Interpretation provided more examples that go beyond simply IT general controls. For example, it could be interpreted that any system along a platform could be considered a financial system, even a Customer Relationship Manager (CRM) system depending on how

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	<p>it is configured and what functions it performs (e.g., sometimes CRM systems are used for customer billing and aggregation of revenue for the financials). An example covering this type of information system would be helpful.</p> <ul style="list-style-type: none"> (3) Yes, UHY LLP believes this would include management-level dashboard reporting. A client will use these dashboards to make significant business decisions. If there is an error in the dashboards the client relies on, this could create a situation in which the member has negatively affected the client's business results by "generating information that affects a financial process." In addition, if the member applies judgment in configuring the dashboards and that judgment skews the reporting in favor of certain areas while ignoring other areas, this could create a conflict in the event that those business decisions turn out to be incorrect. <p>UHY LLP believes that, as members continue to expand relationships to perform implementation services for financial-related tools containing planning, consolidation, modeling, reporting and analytics functionality, such as BlackLine or Host Analytics), independence standards will need to clearly define what work members cannot perform for attest clients. It is our opinion that, as long as members limit their work to configuration and setup and stay away from implementation decisions that would have an effect on internal controls over financial reporting, assisting attest clients to implement finance-related tools should be an acceptable nonattest service.</p> <ul style="list-style-type: none"> (4) We believe the implementation period proposed is acceptable. <p>Other Comments</p> <ul style="list-style-type: none"> Text of Proposed Interpretation, "Information Systems Services" <p>Our comments in this section of the ED are limited to proposed paragraph 19, which deals with "System and Network Maintenance, Support and Monitoring." UHY LLP believes the restrictions outlined would NOT allow members to perform cybersecurity monitoring for attest clients, which is a service we have discussed providing. Our cyber-related services for attest clients would be limited to assessment that do not entail directly implementing changes to infrastructure (such as firewalls or security hardware/software).</p>
CL 17 Armanino LLP	<ul style="list-style-type: none"> Armanino agrees with the need to update the independence standards to reflect current realities of information technology service offerings and generally agrees with the

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<p><i>Supports with Recommendations</i></p>	<p>proposal. However, we believe the guidance contained in the Proposal can be improved with certain clarifications described below.</p> <ul style="list-style-type: none"> Armanino is concerned that specifically referencing application programming interfaces (APIs) may be inappropriately narrow and should be revised in the Proposal. Specifically, paragraphs .15 and .18 should be revised to clarify that members may use any generally available technique or technology, including application programming interfaces (APIs), to interface or provide data translation services for a commercial off-the-shelf (COTS) provided that the member's work does not alter how the COTS financial information system functions, processes data or produce results. Mentioning APIs alone is too limiting because there are many different techniques and technologies that members may utilize when interfacing or providing data translation services for COTS financial information system. And utilizing other available techniques should not create an unacceptable self-review threat to independence as long as the member's work does not alter how the COTS financial information system functions, processes data or produce results. Feedback on one of the specific questions raised in the Proposal: <p>(3) Armanino believes there would be situations where the design, development and implementation of management-level dashboard reporting would not directly affect financial reporting. For example, many management-level dashboard reporting systems may be primarily operational in nature (e.g., a system that reports on certain operational key performance indicators (KPIs) selected and designed by management), and may utilize information from the financial system solely as an input to the dashboard reporting system. In such an example, we believe the management-level dashboard reporting system would not directly affect financial reporting and that any potential threat to independence would likely remain at an acceptable level.</p>
<p>CL 18 Pannell Kerr Forster of Texas, P.C. (PKF Texas) <i>Does not Support as Drafted</i></p>	<ul style="list-style-type: none"> (1) No, due to the following reasons: <p>No scope limitation for assurance services: PKF Texas is first and foremost concerned that this interpretation will prevent technological innovation of the audit and other assurance services. The interpretation does not specifically scope-out services performed in conjunction or otherwise for the benefit of the audit or other assurance services. Currently, the preparation of financial statements is considered a non-attest service for which threats to independence must be considered. Without a specific scope limitation, we are concerned that this interpretation will specifically prohibit our Firm from innovating in the assurance space and derail the audit of the future. Based on our interactions with</p>

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	<p>the AICPA and other alliances of which we are members, the future of our profession will be based on technological innovation. We are actively growing our service offerings and working on various ways to improve audit efficiency and effectiveness through innovation and technology. This standard will most certainly limit our and the profession's ability to innovate.</p> <p>Technological obsolescence: We are further concerned that this standard cites various technologies and terms that are only current (or even past) technology. It fails to consider future technology that may not yet be identified. For example, APIs are specifically scoped out in areas such as paragraph .15, but there is newer technology that could meet the same intent of the standard such as bot-to-bot or other technology yet to be identified.</p> <p>Further, paragraphs .07 and .08 reference installations on a client's "computer" or "server." The theory of installation on a server is a bit dated as there are virtual environments, various configurations on cloud systems, and decentralized networks (blockchain).</p> <p>We recommend that this interpretation be moved to a FAQ or put all technology examples in an FAQ leaving only a principles-based interpretation. The integration could provide a framework to assess how to consider if there are threats to independence and if there are proper safeguards in place.</p> <p>Role of the CPA and what is code: We are of the understanding that a theoretical underpinning of this standard is that the Committee is trying to consider CPA's code a threat to independence that cannot be overcome. However, we are concerned that this theory is conceptually flawed, especially if IT services in conjunction with assurance services are not specifically scoped out.</p> <p>We are concerned that the interpretation does not take into consideration other sources and uses of code that could be then attributed to the CPA as they are not specifically addressed in the current rules-based interpretation. If the interpretation were more tailored to a decision framework, there would be more clarity on how to handle code that is outsourced, from open source, or code within a COTS that is copied and pasted from one COTS to another COTS (such as the Visual Basic of a macro).</p>

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	<p>In addition, paragraph .02 a.iii. appears to confuse the CPA's role in providing information (in the most general sense of the term, information, such as assurance is a type of information) with management decisions made from various sources of information. We believe the definition would meet the intent of the interpretation while retaining only i., ii, and iv.</p> <p>Penalty for the use of technology: Similar to the hosting interpretation issued, we believe this interpretation penalizes the use of technology. We can think of several examples which if the CPA were to perform a service on paper it would not be a threat to independence for which there are no safeguards. Yet when we leverage technology for the same outcome, we have a threat to independence for which there are no safeguards.</p> <p>For example, data translation services are cited as a threat that cannot be overcome. It is very common for a client to have an accounting system that allows for exports to comma-separated values (CSV). In this case the client could have taken full responsibility for all financial data, yet the CPA needs to re-order columns to fit a prescribed import format for purposes of reperformance and retesting. We do not believe this situation should result in an automatic threat to independence that cannot be overcome. 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.</p> <p>In this example, we believe we could put in various safeguards such as completeness checks, hash totals, etc. to overcome the threat to independence. Further, we may be required to perform such procedures if we are not allowed to install audit software of the future on a clients' network. We may need to leverage proprietary technology as part of the audit of the future and inputting client's raw data in a certain format would be a required procedure in the audit.</p> <p>This concern extends to interface services (paragraph .14) as we believe there could be proper safeguards that could be put into place for some interface services, as the CPA is not creating any data in these services and there may be proper safeguards other than the APIs (as referenced in paragraph .15). See comment above regarding technology obsolescence and the example of bot-to-bot.</p>

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	<ul style="list-style-type: none"> • (3) Similar to our response to Question 1, we believe paragraph .02 a.iii may be conceptually flawed. As such, we are concerned that this interpretation would overly limit dashboards. Even more concerning, should we develop audit software that has an audit dashboard, we would likely violate independence by having such a dashboard for the use during the audit if such assurance services are not specifically scoped out. Please note that the today and the future of engagement technology is having the client within the same platform in order to increase engagement efficiency and data security. For example, the AICPA's own PCR (preparation, compilation, review) software already allows the client to have access to certain areas in order to receive documents for signature, respond to requests for responses to analytical procedures, and upload supporting documents for the CPA's review. • (4) We do not believe the proposal provides adequate time to adopt these changes, and an extended adoption period would be needed. In addition, there is no mention of contracts in progress as many software matters take more than one year to fully adopt. Further, the interpretation does not have any grandfathering provisions for contracts or systems already in place as the effective date of this guidance.
CL 19 SingerLewak LLP <i>Does not Support as Drafted</i>	<ul style="list-style-type: none"> • (1) Generally, the exposure draft uses terminology that is consistent with industry practice. However, we would recommend that certain areas be clarified. For example, Section .02.c refers to developing an "information system" and there is an important distinction between an information system and financial information system (and, in this instance, we believe that a financial information system is more appropriate). • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) We believe that leaving "significant" vague is probably necessary, as the world of financial information systems is becoming more complicated between ERP, FPA, BI and other tools. The spirit of what is considered in the exposure draft may be better conveyed using "heavy influence" to indicate what's most important (that is, independence should be considered for impairment if the member has heavy influence on the manner in which financial transactions are processed and recorded in the books and records of the entity).

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	<ul style="list-style-type: none"> (3) We do not believe this should impair independence because this represents assisting the entity with a third-party tool to aggregate and present data that the entity's systems are already processing in the routine course of transaction management. We expect this support of FP&A or BI tools is where the profession will be going and it should not impair independence because it's simply helping technically aggregate information for management to make decisions. Furthermore, we are not sure this should impair independence if the "designing" is objectively similar to functionality that already exists in software applications in the broad marketplace. However, if the design is new or unique, then maybe that could be seen as impairing independence (but this may be overcome as long as management has instructed, and is in a position to approve/evaluate/accept the results of their requested design). <p>Other Comments</p> <ul style="list-style-type: none"> We support the general improvement of clarity on potential independence issues, but we feel that proposing such rules-based interpretive guidance could lead to more confusion and additional questions, especially in an area of professional services that is continually changing as new technologies and business practices are developed. <p>Additional Considerations</p> <ul style="list-style-type: none"> Commercial Off-The-Shelf (COTS) financial information systems <p>This concept is used throughout the exposure draft and it seems to ignore what is happening more and more in practice. COTS ignores the member will be in a position to advise clients on the kinds of metrics, key performance indicators, and dashboard views that might be of value to the entity and its management (based on the member's familiarity with the entity).</p> Designs or Develops a Financial Information System <p>The exposure draft states the following in paragraph .04, "When a member designs or develops an attest client's financial information system, 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."</p>

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	<p>We disagree with this statement because only some types design work would impair independence (that is, not all types of design work would impair independence).</p> <ul style="list-style-type: none"> <p>Install a COTS Financial Information System Software Solution</p> <p>The exposure draft states the following in paragraph .07, “To install a COTS financial information system software solution means the initial loading of software on a computer, normally onto a customer’s server.”</p> <p>We have significant concerns that this sentence does not contemplate current business practices. Almost all software (ERP and Accounting) is cloud-based and not installed on a customer’s server. This statement should be revised to incorporate modern technology systems.</p> <p>Configure a COTS Financial Information System Software Solution</p> <p>The exposure draft states the following in paragraph .09, “To configure a COTS financial information system software solution means selecting the software features, functionality options, and settings provided by the vendor that will determine how the software will perform certain transactions and process data. Configuration options may also include selecting the predefined format of certain data attributes and the inclusion or exclusion of such attributes” This statement may be too broad because, for example, it seems to allow the member to configure revenue recognition rules and/or options in a revenue/receivable module of a system for a client. Assuming the client management has final approval, per some of the guidance in this exposure draft, this may be permissible. But this gives the member control over the method of revenue recognition that is incorporated into the financial statements. We use this example because it’s an example of normal configuration work in an implementation project, but PEEC may not have considered the impact of this as opposed to choosing less impactful configuration settings in standard modules.</p> <p>Data Translation Services Related to a COTS Financial Information System Software Solution</p> <p>The exposure draft states the following in paragraph .18, “If a member uses an API developed by a third party to perform data translation services for a COTS financial information system software solution, threats to independence would be at an acceptable</p>

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	<p>level, provided the member will not be designing or developing code for the API to work and all the requirements of the 'Nonattest Services' subtopic of the 'Independence Rule' are met." We believe that API may not be used correctly in this paragraph. A member could use a third party tool that performs data translation services (that is, it's not usually an API connector but rather a program for data translation purposes).</p>
<p>CL 20 Oregon Society of CPAs Support with Recommendations</p>	<ul style="list-style-type: none"> • (1) The terminology used in the proposal was not readily understood by the subcommittee. The subcommittee includes members who do not generally provide information systems design, implementation or integration services. All of us found the terminology somewhat unclear. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) The definition of "significant" is reasonable. The decisions for what is and what isn't significant should be left up to the member. The member should be able to assess the independence issues related to designing or developing a component of the financial information system by applying requirements related to the "Independence Rule" and "Nonattest Services". ○ (b) Allowing members 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 is appropriate as long as the other requirements related to independence, etc. are met. A financial information system has many components and small businesses often do not have all parts of a financial information system due to the cost/benefit of implementation. ○ (c) The phrase "financial process" is vague and general phrase that could easily be applied to multiple interpretations and definitions. The entire process of accounting could be defined as a "financial process". Are we to interpret that the phrase applies all accounting or just a part of the accounting process to be covered in for 1.295.145 Information Systems Services? It should be carefully defined in such a way as to illustrate the broadness of the application. • (3) We believe that preparing a dashboard is a non-attest service because it should not be included as a part of a "financial information system" as defined in the section labeled "Terminology" in the proposed interpretation.

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	<ul style="list-style-type: none"> ○ a. Dashboard do not “aggregate source data underlying the financial statements or generate information that is significant to the financial statements or financial process as a whole”. ○ b. Dashboard aren’t generally part of “a system controls or system output subject to attest procedures”. ○ c. Dashboards are not “a system that generate data that is used as an input to the financial statements”. ○ d. Dashboards are not used to “gather data that assist management in making decisions that directly impact financial reporting”. ○ e. Dashboards are not “a system that is part of the attest client’s internal controls over financial reporting”. <p>As we understand them, dashboards gather financial information that already exists and presents it differently than a typical financial statement. We believe a member could perform this nonattest service for an attest client if the client assigns a competent member of client management to oversee the services and take responsibility for the quality, outcome, and ongoing maintenance for the dashboard.</p> <ul style="list-style-type: none"> • (4) An extended period of time would be needed to implement the guidance in order to allow time for members to understand the changes and to make changes in their current practices to appropriately serve their clients. <p>General Comments</p> <ul style="list-style-type: none"> • Increased clarity could be achieved for members who do and do not practice in this arena if examples were provided delineating between common activity causing and not causing concern.
CL 21 Anders Minkler Huber and Helm, LLP (Anders) <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> • (1) The terminology appears to be sufficiently clear. However, we feel the proposal lacks the appropriate definition and consideration of management’s decision making status and management’s involvement and specific and continuous direction. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) yes. We believe it is appropriate for the member to use professional judgement in making this determination.

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	<ul style="list-style-type: none"> ○ (b) yes. There are numerous ways a member can provide valuable insights and services to attest clients, and these opportunities should be made available to both parties. ○ (c) yes. We feel the phrase “financial process” is sufficiently clear. • (3) No, we do not believe it should include management dashboard reporting. Typically, dashboard reporting consists of obtaining data that is readily available in a company’s system and accumulating and presenting it in a summarized and simplified way so management is able to quickly review it and make decisions based upon it. It is not considered the accounting system nor is it a source document. • (4) Yes. If adopted as proposed, many clients may be disenfranchised and may need to seek new professional service providers, adopt new vendor contracts, and plan for unexpected costs. An extended period of time would be warranted to minimize the disruption to these clients. We feel two years would be necessary to implement this change. <p>Other Comments</p> <ul style="list-style-type: none"> • We understand the Committee’s efforts to better define and identify activities that would result in a member acting as management, thereby impairing independence. We are supportive of these efforts, and we agree with many aspects of the proposal clarifying most Information System Services relative to system design, implementation, installation, configuration, customization, and services related to interface modification and data translation. However, we have specific concerns regarding the language within section 19 contained under “System and Network Maintenance, Support and Monitoring”. • We believe that the language as written is overly narrow and fails to recognize that the listed services represent value added services that are provided at the request of and use by management, not as a replacement of management. We oppose these narrow definitions, and we feel they will cause harm to firms and their clients. It is very commonplace, especially within small and mid-sized organizations for management to retain all decision making responsibilities and simply assign a member a task or series of tasks. In these cases, it is our belief that members are not acting as management. It is

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	<p>entirely possible that a client be provided with varying sets of best practices for the management of a network, the achievement of optimal performance, or the security of a system. This would not be an uncommon outcome of an assessment that is defined in section 20 as not impairing independence. If that client directed a member whose staff contained the requisite skillset to follow a specific course and only that course, then the member will not have acted as management, but at their direction. While it is logical that a firm should not audit the work it has performed, a blanket independence impairment does not seem appropriate.</p> <ul style="list-style-type: none"> For the purposes of identifying what impairs independence, we believe the examples listed in section 19 should include acknowledgement and consideration of management's decision making status and involvement and specific and continuous direction in the delivery process.
<p>CL 22 KPMG LLP <i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> (1) We believe that the terminology used in the proposal is helpful. We also are providing specific comments elsewhere within this comment letter that might enhance or further clarify the terminology. <p>The proposed interpretation defines "API" as "application program interface," but we understand the "P" is generally understood by practitioners to mean "programming" rather than "program."</p> <p>The proposed interpretation provides an exception to designing an information system that would not include creation of a "template" that performs a discrete calculation. We believe a "template" is intended to mean an electronic document, for example an Excel spreadsheet, which can perform simple and routine calculations. We suggest adding language that indicates that a spreadsheet is an example of a template to assist members in consistent application.</p> <ul style="list-style-type: none"> (2)(a)(b)(c) <ul style="list-style-type: none"> (a) The explanation material to the proposed revision indicates that significant means material. However, that is not defined within the interpretation. We believe the PEEC should replace "significant" with "material," as material is a known and understood concept by members, and is a consistent term used throughout the rest of the Code.

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	<ul style="list-style-type: none"> ○ (b) We believe the concept of prohibiting the design of a material system is consistent with extant guidance. We also believe the exception to allowing design or development of a component of a financial information system that is not material to the financial statements or financial processes as a whole is appropriate. ○ (c) We support the proposed interpretation's use of the phrase "financial process" and believe it is clear that members should think broadly about processes that may affect a financial process. • (3) Yes, we believe it is clear that if information gathered from management-level dashboard reporting is used to impact the financial statements, then it is considered a financial system. • (4) We believe the proposed one-year implementation, with early implementation allowed, is appropriate. <p>Other Comments</p> <ul style="list-style-type: none"> • Designs or Develops a Financial Information System (ET 1.295.145.04) <p>We believe it is a matter of professional judgment as to whether the creation of a template is akin to designing a financial information system. It is possible that the concept of a "template" is subject to interpretation that could go beyond the AICPA's intent, but ultimately a member should evaluate whether they believe their template is more analogous, due to its complexity and sophistication, to designing a financial information system, in which case the design prohibition around such a template would apply.</p> <p>The proposed interpretation provides the example of a tax provision or depreciation calculation as a template that performs a discrete calculation that would not constitute design or development of a financial information system and will not impair independence. However, we believe these two examples may result in inherently different applications in terms of the inputs, number of calculations, subjectivity, and complexity and judgment involved, so to include these two examples together potentially</p>

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	<p data-bbox="716 228 1816 293">misleads practitioners as to what constitutes a “discrete calculation” and the intention behind the template exception.</p> <ul data-bbox="669 334 1749 399" style="list-style-type: none"> <li data-bbox="669 334 1749 399">• We ask that PEEC consider the following edits to clarify the exception regarding templates: <p data-bbox="716 423 1858 862">1.295.145.04 When a member designs or develops an attest client's financial information system, 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. Designing and developing a A template, such as a spreadsheet, that performs a simple, discrete calculations such as a tax provision or depreciation calculation does not constitute designing or developing does not constitute a financial information system. Designing and developing a template and will not impair independence, provided the template does not perform an activity that, if performed directly by the member, would impair independence and the member complies with all the requirements of the "Nonattest Services" subtopic [1.295] of the “Independence Rule”. The determination of whether the template is a financial information system is a matter of professional judgment.</p> <ul data-bbox="669 894 1428 927" style="list-style-type: none"> <li data-bbox="669 894 1428 927">• Installation and Configuration (ET 1.295.145.05-.10) <p data-bbox="716 959 1841 1154">The proposal uses the word “selecting” when describing configuration of a COTS financial information system software solution. We do not believe it is clear that management must determine the features and options for the system, and the member may only input management’s selection by physically selecting those client-determined settings. As noted above, we believe it should be permissible to configure a COTS information system, but only under the direction of management.</p> <p data-bbox="716 1195 1829 1260">We recommend the PEEC consider the following edit to clarify the member’s limitation around configuration of a COTS financial information system software:</p> <p data-bbox="766 1292 1862 1424"><i>1.295.145.09 To configure a COTS financial information system software solution means selecting the member selects the software features, functionality options, and settings provided by the vendor, as determined by the client, which will determine how the software will perform certain transactions and process data...</i></p>

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	<ul style="list-style-type: none"> Interface a COTS Financial Information System Software Solution (ET 1.295.145.13-.15) <p>We believe that the subtitle “interface a COTS financial information system software solution” could imply an ongoing relationship whereby the member runs or maintains a piece of the client’s system, and would generally not be permissible.</p> <p>As we believe the intent of the interpretation is to prohibit design of a financial information system, including any applications that allows financial systems to connect to one-another (i.e. an application programming interface), we suggest that PEEC remove the subsection on “Interface a COTS Financial Information System Software Solution” in paragraphs .13-.15, and incorporate paragraph .15 behind paragraph .04, as part of “Designs or Develops a Financial Information System” section, so that it would read as follows:</p> <p><i>1.295.145.04 When a member designs or develops an attest client’s financial information system, 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. Designing and developing a template that performs a discrete calculation such as a tax provision or depreciation calculation does not constitute designing or developing a financial information system and will not impair independence, provided the template does not perform an activity that, if performed directly by the member, would impair independence and the member complies with all the requirements of the “Nonattest Services” subtopic [1.295] of the “Independence Rule.”</i></p> <p><i>1.295.145. 15 05 If a member uses an application programming interface (API) that is developed by a third party to interface transfer information between legacy or third-party COTS financial information system software solutions, threats to independence would be at an acceptable level, provided the member will not be designing or developing code for the API to work and all the requirements of the “Nonattest Services” subtopic [1.295] of the “Independence Rule” are met.</i></p>
CL 23 EKS&H LLP	<ul style="list-style-type: none"> (2)(a) We believe the language in the proposal is overly narrow and fails to recognize that the consulting services are currently delivered in a myriad of ways. These services are

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<p><i>Does not support as drafted</i></p>	<p>increasingly provided by members not in place of management, but at the request of management. While seemingly innocuous, this distinction is extremely important. It is very commonplace, especially within small and mid-sizes organizations for management to retain major decision-making responsibilities and simply assign outside consultants routine tasks or series of tasks. In these cases, it is our belief that members are not necessarily assuming management responsibilities.</p> <p>It is entirely possible that a client be provided with varying sets of best practices for the management of a network, the achievement of optimal performance, or the security of a system. This would not be an uncommon outcome assessment described in paragraph .20. If a client directed a member to follow a specific course and only that course, then the member should not be viewed as acting as management, but rather acting at the direction of management. We do not believe such circumstances result in a self-review threat. Accordingly, we believe a key consideration in the examples in paragraph .19 should be management's participation in making decisions and management's active involvement in the consulting service delivery process.</p> <p>We believe the second sentence of paragraph .19 should be amended to read as follows: <i>"If post-implementation services involve the attest client <u>delegating any type of decision making authority and</u> outsourcing an ongoing function, process, or activity to the member that in effect would result in the member assuming a management responsibility, 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."</i></p> <p>We believe .19a. should be clarified to read:</p> <p><i>"Operates the attest client's network, such as managing the attest client's systems or software applications <u>without specific and continuous direction from management</u>"</i></p> <p>We believe .19c. should be clarified to read: <i>"Has responsibility for monitoring or maintaining the attest client's network performance <u>without specific and continuous direction from management</u>"</i></p>

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	<p>We believe .19d. should be clarified to read: “Operates or manages the attest client’s information technology help desk <u>where management has not dictated an industry standard framework to be used (e.g., ITIL, ITSM, etc.) and a set of standard operating procedures</u>”</p> <p>We believe .19e. should be clarified to read: “Has responsibility to perform ongoing network maintenance, such as updating virus protection solutions, applying routine updates and patches, or configuring user settings <u>without specific and continuous direction from management</u>”</p> <p>We believe .19f. should be clarified to read: “Has responsibility for maintaining the security of the attest client’s networks and systems <u>without specific and continuous direction from management</u>”</p> <ul style="list-style-type: none"> • (3) With regard to the committees’ solicitation of feedback on how management dashboards should be viewed in regard to whether or not they are part of the accounting and financial information system(s): <ul style="list-style-type: none"> ○ “Dashboard” is used much too broadly as a term to really have any meaningful reliability in terms of achieving the stated outcome for independence purposes. ○ Useful dashboards by design often are a combination of financial and non-financial information, so it seems that at a minimum, auditor judgement would be necessary to determine significance of reporting from financial perspective. ○ Analytics and dash boarding is rarely or never given the same weight as financial statements in terms of the picture of record of the financial health of the company. Analytics from the database up are meant more for data discovery, recognition of trends, quick ad-hoc analysis and “fast over accurate” decision making, which doesn’t seem to be consistent with the objectives of attest engagements. ○ Including management dash boarding at this stage I believe is premature given the inconsistent application of this practice in the middle market today and I believe would preclude many clients from receiving much needed services that could be provided by CPA firms like ourselves who are familiar with much of their data and

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	<p>relevant metrics and could assist them in harnessing available data integration and business intelligence technologies.</p> <p>Other Comments</p> <ul style="list-style-type: none"> • While we fully support the ongoing need to define and identify management activities that might impair independence of a member in public practice, we believe there are some practical aspects of providing such services that deserve additional consideration.
<p>CL 24 BDO USA, LLP <i>Supports with Recommendations</i></p>	<ul style="list-style-type: none"> • (1) We do 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 area. • (2)(a)(b)(c) <ul style="list-style-type: none"> ○ (a) We believe it would be appropriate to provide some guidance as to what would constitute information that is significant to the financial statements or financial processes taken as a whole, as, the term “significant” is very broad and could create varied and inconsistent application across the profession. The exposure draft notes on page six that “Information generated by the system is ‘significant’ if it is probable that it will be material to the financial statements of the attest client.” Thus, PEEC has concluded on the criteria that would designate “significant” information and, as such, it should be included in the interpretation to prevent misapplication. We also note that in this context, the Securities and Exchange Commission (SEC) believes that information would be “significant” if it is reasonably likely to be material to the financial statements of the audit client.¹ We suggest the following wording be included in the interpretation, consistent with the SEC language: “Information is significant to the financial statements if it is reasonably likely that it will be material to the financial statements of the attest client.” <p>Further, it would be beneficial to users of the Code to include guidance within the interpretation noting that the member may not know if the information generated by a system will be material to the financial statements until the financial statements are finalized, and thus, before deciding to perform certain services, the member should consider the nature of the information and the likelihood that it could be material or become material in the future to the financial statements. Such guidance might influence members to be proactive in preventing non-compliance with the Independence Rule, thus, benefitting the public interest.</p>

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	<p>Finally, Staff should consider publishing non-authoritative guidance concerning the topic in the form of a “frequently asked question,” (FAQ) as, we believe examples of systems that may generate significant financial information would be beneficial in order to mitigate confusion. Considering the pace of change within the information technology industry, such examples may be more properly located outside of the confines of the Code.</p> <ul style="list-style-type: none"> ○ (b) We believe the inclusion of the concept of “significance” is appropriate, as, a reasonable and informed third party would most likely conclude that the threats to independence would be at an acceptable level if a member were to design or develop a component of a financial information system that generates financial information that is insignificant to the financial statements or financial process as a whole. <p>Also, the proposal is consistent with the rules established by the SEC, as Rule 2-01(c)(4)(ii)(B) prohibits (unless the results of the services will not be subject to audit procedures): <i>“Designing or implementing a hardware or software system that aggregates source data underlying the financial statements or generates information that is significant (emphasis added) to the audit client’s financial statements or other financial systems taken as a whole.”</i></p> <p>Finally, the proposal appears to be consistent with the Code of Ethics of the International Ethics Standards Board for Accountants (IESBA) which also considers the significance of the information, as, paragraph 290.198 states that, <i>“Providing services to an audit client that is not a public interest entity involving design or implementation of IT systems that...generate information that is significant to the client’s accounting records or financial statements...creates a self-review threat.”</i></p> <ul style="list-style-type: none"> ○ (c) We believe the phrase “financial process” is broad, in that, it connotes any system, series of steps or operations that affect the financial statements or financial related management decisions affecting the financial statements. However, we believe it would be beneficial to include an example, such as information technology controls, within the interpretation itself so that the PEEC’s intent is clear. If the Committee does not believe such an example

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	<p data-bbox="863 228 1864 293">should be added, we would recommend that a FAQ be issued by Staff to clarify the intent</p> <ul data-bbox="667 358 1864 1162" style="list-style-type: none"> <li data-bbox="667 358 1864 1024">• (3) We assume “management-level dashboard reporting” to mean data aggregated to present key performance indicators in order to assist the client’s management to make decisions. We agree that dashboard reporting would be considered information that assists management in making decisions. Accordingly, if the information presented on the dashboard is used for financial reporting related decision-making, the member would need to determine whether the dashboard reports would have a significant impact on management’s decision making. While it might be challenging to determine how significant the dashboard reports are to management’s decision process, we would agree that if significant, this service should be considered customizing a COTS “financial information system” and thus, impair independence. We believe the PEEC should provide additional guidance concerning this issue in order to promote consistency in application of the Code, as, threats to independence created by customizing a client’s COTS system for dashboard reporting purposes could be viewed differently within the profession and among various stakeholders. For example, we do not believe it is intuitive that dashboard reporting services would be linked to a system that “generates information that impacts a financial process as a whole” (because the system gathers data that assists management in making decisions). Providing an example of this linkage in the final standard or through a FAQ would be beneficial. In addition, including dashboard reporting as an example in par. 11 under “Customize a COTS Financial Information System Software Solution” would be helpful. <li data-bbox="667 1065 1864 1162">• (4) We believe the extended period of one year after publication would be needed to implement the guidance, as, updates to policies and tracking systems for some firms may be a time consuming process. <p data-bbox="667 1260 894 1292">Other Comments</p> <ul data-bbox="667 1292 1864 1425" style="list-style-type: none"> <li data-bbox="667 1292 1864 1425">• While we appreciate the opportunity to comment on the proposed revised interpretation, the PEEC should note that it would be beneficial to all respondents if a “marked” version of the proposed revisions were included in the exposure draft document, or, at the very least, the extant guidance “unmarked” for comparison purposes. This would allow a

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	<p>respondent to clearly view the revisions to the extant interpretation and better understand how the proposal will impact current practice. A “marked” version has been included in previous exposure drafts and we would appreciate if this practice were continued in the future.</p> <ul style="list-style-type: none"> Paragraph .03 of the proposed interpretation addresses design, development or implementation services not related to a financial information system. While we appreciate non-authoritative guidance, we believe the PEEC should consider whether AICPA Staff FAQ no. 7 should be incorporated into the interpretation for clarification as to what would be considered unrelated to a financial information system or deleted from the Staff FAQs. FAQ no. 7 can be noted below: <i>What criteria should a member use to determine whether an attest client’s information system is unrelated to its financial statements or accounting records?</i> <p><i>Information systems that produce information that is reflected in the amounts and disclosures in the attest client’s financial statements, used in determining such amounts and disclosures, or used in effecting internal control over financial reporting are considered to be related to the financial statements and accounting records. However, information systems that are used only in connection with controlling the efficiency and effectiveness of operations are considered to be unrelated to the financial statements and accounting records. [Added Prior To June 2005]</i></p> <ul style="list-style-type: none"> We request that the PEEC consider including some examples of systems that would not be considered “financial information systems.” This would be valuable, as, many systems within an attest client may be integrated.
<p>CL 25 Baker Tilly Virchow Krause, LLP Supports with Recommendations</p>	<ul style="list-style-type: none"> (1) We believe the term “commercial off-the-shelf” (COTS) is overused, frequently misused and becoming less relevant; thus the concept should be retired and more precise terms should be utilized. For example, many traditional COTS systems are now moving to cloud deployments, which introduces different risks and configuration mechanisms that need to be considered and require more precise terminology in order to be differentiated from more traditional COTS systems. (2)(a)(b)(c) <ul style="list-style-type: none"> (a) We believe that for the interpretation to be consistently applied the term “significant” should be defined. We recommend that the following definition from

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	<p>the last paragraph on page six of the exposure draft be utilized to define “significant” in the interpretation, “Information generated by the system is “significant” if it is probable that it will be material to the financial statements of the attest client.”</p> <ul style="list-style-type: none"> ○ (b) Yes, this exception is appropriate. Under the current interpretation, in some circumstances, members are not able to undertake projects for clients that would be extremely unlikely to pose any threat to independence; thus we believe that allowing for more judgement is appropriate. ○ (c) No, especially considering that the auditing literature makes a clear distinction between processes and controls. We believe that if the exposure draft’s definition of a financial information system were modified to state that the items included in i. through iv. of paragraph .02a would typically meet the definition of, or be a part of, a financial information system (i.e., as opposed to how the lead in to i. through iv. is currently worded), the connection between internal controls over financial reporting, including information technology general controls, and their inclusion in the definition of financial information systems would be much clearer. • (3) Yes, based on bullet point iii. of paragraph .02a included in the definition of a financial information system (i.e., a system that gathers data that assists management in making decisions that directly affect financial reporting), we believe that management-level dashboard reporting would be included within the definition of a financial information system. As indicated in Specific Request for Comment 2c. above, we believe that the definition of a financial information system could be further clarified by stating that the items included in i. through iv. Of paragraph .02a would typically meet the definition of, or be a part of, a financial information system (i.e., as opposed to how the lead in to i. through iv. is currently worded). • (4) If adopted as proposed, we do not believe that an extended period of time would be needed to implement the guidance, as this guidance is generally less restrictive than current guidance, therefore, it would be unlikely that a previously permitted service would now be considered prohibited. <p>Other Comments</p>

Comment Letter	Feedback Highlights
	<ul style="list-style-type: none"> In paragraph .20 of the exposure draft, there appears to be a concept introduced that nonrecurring “maintenance, support and monitoring services” would not impair independence. We believe that whether a service impairs independence should be based upon the nature of the service and not whether it is recurring or nonrecurring. For example, if a member were to assume a management responsibility, even on a nonrecurring basis, we believe that independence would be impaired. We believe that the examples provided in paragraphs .19 and .20 of the exposure draft illustrate our point. The difference in the examples is not whether the services are recurring or nonrecurring, it is whether or not management responsibilities are being assumed. In the examples in paragraph .19, management responsibilities are assumed (this is emphasized by the use of the terms “operates,” “supervises,” “has responsibility for,” and “manages”), while in the examples in paragraph .20, management responsibilities are not being assumed (this is emphasized by the use of the terms “analyze,” “provide,” “apply,” and “assess”).
CL 26 The Auditor of State of Ohio <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> We do believe the terminology used will be readily understood by members, even if they do not work in this arena. We also feel “significant” should be a matter of professional judgment and not defined in the standard. We request an exception for systems like UAN that are required by law, cannot be customized by the client, has broad use, and has substantial safeguards in place be immune from the ‘design and development’ criteria.
CL 26 Kentucky Society of CPAs <i>Supports with Recommendations</i>	<ul style="list-style-type: none"> (1) See our comments above (and in question 3 below) relating to terms needing additional clarification. (2)(a)(b)(c) <ul style="list-style-type: none"> We agree with the approach used by PEEC. There is no need for specific guidance on “significant” due to the myriad circumstances and applications. (3) It could. Accordingly, we also suggest additional guidance be provided in this area. This guidance should also elaborate on the term “directly affect (or impact) financial reporting”. Dashboard reporting may both directly or indirectly impact financial reporting so additional guidance would be helpful.

Comment Letter	Feedback Highlights
	<ul style="list-style-type: none"> <li data-bbox="667 266 1858 399">• (4) We suggest at least one year after the appearance in the Journal of Accountancy. This would provide time for members and their firms to fully understand this guidance and implement into their practices. This would include the traditional CPE timeframes and offerings as well. <p data-bbox="667 435 892 464">Other Comments</p> <ul style="list-style-type: none"> <li data-bbox="667 505 1858 938">• Paragraph .04 in the Text of Proposed Interpretation – This paragraph notes that “...Designing and developing a template that performs a discrete calculation such as a tax provision or depreciation calculation does not constitute designing or developing a financial information system and will not impair independence, provided the template does not perform an activity that, if performed directly by the member, would impair independence and the member complies with all the requirements of the Nonattest Services subtopic 1.295 of the Independence Rule.” We suggest providing additional clarification on the application of the term “discrete”, which generally means “individually separate and distinct”. It is not uncommon for members to be providing accounting related services such as these, among others, on a recurring basis that may be monthly, quarterly, or when applicable. Further, in this same paragraph we suggest additional clarification on “the activity” the template would perform that would impair independence if performed directly by the member.

Comments on Exposure Draft-Sorted

Topic	Comments	Commenters
<i>Comments on Specific Interpretation Paragraphs</i>		
Introduction (.01)	<ul style="list-style-type: none"> Clarify that the interpretation only applies when a member is performing a separate IT engagement and does not apply when procedures described in the interpretation are performed as part of an attest engagement (i.e., when engagements 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. Without a specific scope limitation, concerned the proposal will prohibit innovation in the assurance space and derail audit of the future. They are actively growing our service offerings and working on various ways to improve audit efficiency and effectiveness through innovation and technology and believes the standard would limit this ability. 	<ul style="list-style-type: none"> CL12 CL18
Terminology (.02)- <i>Financial Information</i> <u>System definition is too broad (4 comments)</u>	<ul style="list-style-type: none"> clarification of designing an information system (2 comments- CL2, CL12) <ul style="list-style-type: none"> CL2 does designing and information system relate to both the development of a network and to a computer/server or to only one of those. definitions of the terms, interface, application program interface (API) and data translation, not commonly known to CP As, should be added (i.e., relocated from .13, .15 and .16) Recommends adding definition of financial process similar to the one found on page 6. Term dashboard reporting should be defined 	<ul style="list-style-type: none"> CL2, CL12 CL2 CL7 CL2

	<ul style="list-style-type: none"> • If the term dashboard is included in the standard, it should be replaced by a description that is less likely to fall out of use quickly. Such as “business visual analytic and reporting application tools” • Financial Information System- <ul style="list-style-type: none"> ○ Definition is too broad (4 comments -CL2, CL9, CL11, CL12) ○ financial information system definition is too broad, far reaching and imprecise to it would be interpreted to preclude members from assisting clients with the preparation of financial statements. Revise so that it is narrowed considerably to make clear that the practice of importing a client’s unadjusted GL data into a member’s practice aid software is not intended to be covered. ○ Definition 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 ○ Criteria of “aggregating source data” to define a financial information system is too broad and should be removed ○ 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. Consider limiting it to a “primary” financial information system so that members may assist clients with information system services and ancillary products that do not effectuate journal entries in the primary financial information systems provided that there is documentation of mitigating factors. ○ PEEC reconsider the concept of using significance or materiality when determining a financial information system because it places an undue burden on the member due to variability of the impact to the f/s that the system can have in future periods (i.e., may not be 	<ul style="list-style-type: none"> • CL4 • CL2, CL9, CL11, CL12 • CL2 • CL9 • CL9 • CL9 • CL9
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	<p>significant in the year of design but rise to significance later or the volume of transaction processed through system could grow over time)</p> <ul style="list-style-type: none"> ○ Clarify whether the significance test applies to the “discrete” exception as the 2 examples given could have a significant impact on the financial statements. ○ Definition is overly broad-“systems that gathers information” should be removed ○ Definition is so broad could include Big Data non-financial data as well ○ Providing information to management does not automatically mean this will be used to make financial decisions that would have a material impact ○ 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 provides significant insight into a company’s operations, results, or activities in a nonfinancial way. ○ appears to confuse the CPA’s role in providing information (in the most general sense of the term, information, such as assurance is a type of information) with management decisions made from various sources of information ○ consider including some examples of systems that would not be considered “financial information systems.” This would be valuable, as, many systems within an attest client may be integrated ○ elaborate on the term “directly affect (or impact) financial reporting”. ○ Provide specific examples of financial information systems that do not aggregate source data and if none can be developed, then eliminate this component from the definition. 	<ul style="list-style-type: none"> • CL9 • CL11 • CL12 • CL12 • CL12 • CL18 • CL24 • CL27 • CL27
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	<ul style="list-style-type: none"> • Practitioner “should consider” the four factors when determining non attest services vs. “may consider” given the critical distinction between financial and other information systems in the proposal • Suggest that PEEC incorporate as an additional defined term “implementing an information system” • Is the definition of “designing” intended to apply to all information systems as drafted or should the focus be on financial information systems? • Clarify if “designing” is intended to include determining the best COTS solution for a client that the client will set up. For example, does it extend to complying of open source information to build a software system for a client or if the client used the member as a subcontractor and oversaw the member’s work related to the design and development of the system. • Clarify the term COTS in the interpretation or in a FAQ as many in public practice refer to systems as “packaged” or “off the shelf”. • The term COTS is overused, frequently misused and becoming less relevant, thus the concept should be retired, and more precise terms should be used. 	<ul style="list-style-type: none"> • CL4 • CL4 • CL12 • CL12 • CL14 • CL25
Design, Development, or Implementation Services Not Related to a Financial Information System (. 03)- <u>Need to make clear that non financial systems are permissible vs. state that there are threats at an acceptable level (2 comments)</u>	<ul style="list-style-type: none"> • Rather than characterizing such circumstances as threats that are acceptable, final version of the proposed interpretation should state clearly that they should not be deemed threats at all so that members do not need to perform the documentation required by the conceptual framework. • Clarify paragraph .03 to permit a member to configure and customize a COTS non-financial information system as threats to independence would appear to be at an acceptable level, provided all of the requirements of a non-attest service are met • Should consider whether AICPA Staff FAQ no. 7 should be incorporated into the interpretation for clarification as to what would be considered unrelated to a financial information system or deleted from the Staff FAQs; 	<ul style="list-style-type: none"> • CL2 • CL7 • CL24

<p>Designs or Develops a Financial Information System (. 04)- <u>Template should refer to spreadsheet</u> (2 comments)</p>	<ul style="list-style-type: none"> • Term “template” used in paragraph .04 should be clarified...should refer to an Excel spreadsheet • Members should be able to design (create the blueprint) for a financial information system without impairing independence as long as management reviews and approves the design and performs all management responsibilities with respect to development and installation • Discrete calculation- should include reformatting of information, or calculating standard financial ratios or financial relationships from client provided data, and delivering to client a report that may be used for their financial decision-making process • Inconsistency between paragraphs .04 and .16- allowing performance of discrete calculation vs. not allowing designing and development to convert system data that is compatible (i.e. excel) • Disagree that a member designs or develops an attest client’s financial information would impair independence, because only some types design work would impair independence (that is, not all types of design work would impair independence) • Suggest adding language that indicates that a spreadsheet is an example of a template to assist members in consistent application and offered up suggested edits. • The two examples provided as exceptions in inherently different applications and including these two examples together may potentially mislead practitioners as to what constitutes a “discrete calculation” and the intention behind the template exception • Suggest providing additional clarification on the application of the term “discrete”, which generally means “individually separate and distinct”. • suggest additional clarification on “the activity” the template would perform that would impair independence if performed directly by the member • Suggest that members may be able to implement safeguards to 	<ul style="list-style-type: none"> • CL7 • CL11 • CL12 • CL12 • CL19 • CL22 • CL22 • CL27 • CL27
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	<p>address the threats created when designing. The self-review threat could be mitigated by not relying on the software and performing their own review or testing to see if the information generated by the system is accurate. The management participation threat can be mitigated by ensuring that the individual who oversees the work performed by the member is competent and able to understand and accept responsibility for the it. Also, sometimes the product developed will include certain definitive actions that are required to be taken by management such as signoffs and approvals of transactions, calculations, reports or journal entities.</p>	<ul style="list-style-type: none"> CL27
Implementation of a COTS Financial Information System Software Solution (.05-.06)	None	None
Install a COTS Financial Information System Software Solution (.07-.08)- <u>Need to reflect/incorporate current technology (4 comments)</u>	<ul style="list-style-type: none"> Paragraph .07 should also address systems installed in cloud environments Suggests expanding this definition to indicate customer's "designated hosting site" (i.e. install to cloud vs. server) to allow for more industry changes, including changes in terminology or technology that could happen in the future Develop Q&A that address current technology vs. a standard that would apply to all networks This paragraph should be revised to incorporate modern technology systems, as there are significant concerns that this paragraph does not consider current business practices 	<ul style="list-style-type: none"> CL 7 CL12 CL12 CL19
Configure a COTS Financial Information System Software Solution (.09-.10)- <u>Not easily understood or clear that management makes the selection (2 comments)</u>	<ul style="list-style-type: none"> "...selecting the predefined format of certain data attributes and the inclusion or exclusion of such attributes." may not be easily understood, paragraphs .09 and .10 should be expanded and at least one example provided do not believe it is clear that management must determine the features and options for the system, and the member may only input management's selection by physically selecting those client-determined settings (rewording provided) 	<ul style="list-style-type: none"> CL3 CL22

<p>Customize a COTS Financial Information System Software Solution (.11-.12)- <u>Should add guidance related to non-financial reporting (2 comments)</u></p>	<ul style="list-style-type: none"> • should provide for a significance evaluation by the member of the nature and extent of a COTS customization service, should not preclude such judgment outright (para.12) • Unclear whether paragraphs .11 and .12 should apply to customization that is unrelated to financial reporting; definition of “customize” in paragraph .11 should include similar language as paragraph .09's definition of "configuration" • revise the guidance to address the impact of non-financial modifications/customizations to COTS Financial Information Systems • Consider updating paragraph .12 to be consistent with the extant interpretation which allows for members to make insignificant modifications to source code underlying an attest client’s existing financial information system. • Guidance in first sentence of paragraph is too broad-appears to allow configuration of revenue recognition rules. 	<ul style="list-style-type: none"> • CL2 • CL7 • CL9 • CL14 • CL19
<p>Interface a COTS Financial Information System Software Solution (.13-.15)- <u>Should include more than API, as this may be the right term as it is too narrow- (6 comments for paragraphs .13-.18 on API)</u></p>	<ul style="list-style-type: none"> • Suggest clarifying in that API (paragraph .15 and .18) means that the API must be unaltered and auditable in how it is used and how it processes data that is moved through that API protocol through the interpretation or in non-authoritative guidance • more than just APIs should be scoped out for purposes of paragraphs .13 through .15. Data is not being created when performing these services, rather, just moving data and so safeguards should be able to be put in place. For example, with advances in machine learning, some interfaces could be bot to bot that has machine learning on each side of the application. This would not be considered an API and safeguards should be able to be put in place to reduce threats to independence to an acceptable level. • Consider also referring to “data translation” services as “data conversion” services. • Concerned that specifically referencing application programming interfaces (APIs) may be inappropriately narrow and should be 	<ul style="list-style-type: none"> • CL7 • CL12 • CL14 • CL17

	<p>revised in the Proposal.</p> <ul style="list-style-type: none"> • proposed interpretation defines “API” as “application program interface,” but we understand the “P” is generally understood by practitioners to mean “programming” rather than “program • believe that the subtitle “interface a COTS financial information system software solution” could imply an ongoing relationship suggest removing the subsection on “Interface a COTS Financial Information System Software Solution” in paragraphs .13-.15, and incorporate paragraph .15 behind paragraph .04, as part of “Designs or Develops a Financial Information System” section 	<ul style="list-style-type: none"> • CL22 • CL22
<p>Data Translation Services Related to a COTS Financial Information System Software Solution (.16-.18)- <u>Should include more than API, as this may be the right term as it is too narrow- (6 comments for paragraphs .13-.18 on API)</u></p>	<ul style="list-style-type: none"> • suggest clarifying in that API (paragraph .15 and .18) means that the API must be unaltered and auditable in how it is used and how it processes data that is moved through that API protocol via the interpretation or in non-authoritative guidance • API may not be the right term to use, as a program for data translation purposes is usually used for these services (could use a third party) • In certain cases, data transformation would be a normal threat that could be overcome with certain safeguards and should not result in an automatic threat to independence, and not considered an API (export to CSV) this situation should be clarified for purposes of this ED • Consider using “data conversion” instead of “data translation” • Concerned that specifically referencing application programming interfaces (APIs) may be inappropriately narrow and should be revised in the Proposal. Suggests revision such as “members may use any generally available technique or technology, including application programming interfaces (APIs), to interact or provide data translation services for a COTs provided the member’s work does not alter how the COTS financial information system functions, processes data or produce results. • API may not be used correctly in this paragraph. A member could use a third-party tool that performs data translation services (that is, it’s not usually an API connector but rather a 	<ul style="list-style-type: none"> • CL7 • CL12 • CL12 • CL14 • CL17 • CL18

	program for data translation purposes.	
System and Network Maintenance, Support, and Monitoring (.19-.20)- <ul style="list-style-type: none"> • <u>Add examples of permissible services (3 comments)</u> • <u>Language as written is narrow and does not represent value added services (5 comments)</u> • <u>Key distinction in the examples should be management making key decisions (5 comments)</u> • <u>Blanket independence impairment does not seem appropriate (2)</u> • <u>Should not depend on recurring or non recurring services to assess independence (4 comments)</u> • <u>Clarification on discrete vs ongoing functions (2 comments)</u> 	<ul style="list-style-type: none"> • Clarify the examples of permissible services described in paragraph .20b and .20c that appear to be part of the precluded services in paragraphs .19f and .19c, respectively • Suggest that PEEC consider whether further guidance could better distinguish the examples in pars. .19 and .20 especially with respect to what a discrete, nonrecurring project is. • Language as written is overly narrow and fails to recognize that the listed services delivered represent value added services. • A blanket independence impairment does not seem appropriate • The key distinction in the examples listed in section 19 should be management's decision-making status and involvement in the delivery process (CL6, CL13 and CL23 offer up proposed revised language). • Recurring or ongoing services would not much more likely to impair independence (as long as management takes responsibility(CL13) -(should not depend on recurring or non-recurring CL25) (CL6 and CL13 offer up proposed revised language). • more guidance is necessary to assist members in differentiating between ongoing and discrete activities (.19e vs. 20c) For example, if the member applies updates and patches only at the direction of the client and under their supervision, would that be considered a discrete activity since the member is executing each update as a separate occurrence and is not taking responsibly for performing ongoing maintenance? • Is the reference to "new software" (paragraph .20d) critical to the determination about whether this is an acceptable service? • Confirm that situations whereby a member licenses permissible software, as provided for under the Hosting Interpretation and under the proposed interpretation (when not related to a financial system) and such software requires certain bug fixes or other routine patches. • Clarification with respect to "Monitoring" activities, appears to 	<ul style="list-style-type: none"> • CL4 • CL4 • CL6, CL13, CL15, CL21, CL23 • CL6, CL15, • CL6, CL13, CL15, CL21, CL23 • CL6, CL13, CL15, CL25 • CL7 • CL7 • CL8 • CL8

	<p>be a potential inconsistency between the extant Code and the Proposed Interpretation with respect to “monitoring activities.”</p> <ul style="list-style-type: none"> • Forcing members to establish each instance of providing these services as “discrete” engagements places an unnecessary burden on the practitioner. • In paragraph .19, is there a concern if the firm is performing services at the client’s direction, but the firm bills the client according to a set monthly subscription service? • Confused as to why discrete functions could be overcome but ongoing functions, processes, and activities could not, should include specific examples rather than implying that performance of such services would be an automatic threat to independence that cannot be overcome. Believe there could be instances where ongoing maintenance, support and monitoring a • Consider defining “maintenance”, “support” and “monitoring”. • Provide additional clarification and example scenarios in which permissible services are being provided over multiple periods as separate and distinct projects that would not be considered outsourcing an ongoing management responsibility • The restrictions outlined would NOT allow members to perform cybersecurity monitoring for attest clients, which is a service we have discussed providing. 	<ul style="list-style-type: none"> • CL 11 • CL12 • CL 12 • CL14 • CL14 • CL16
Comments on Question 1		
<p><i>Is the terminology used in the proposal consistent with industry practice and will it be readily understood by members who do and do not practice in this arena?</i></p>	<ul style="list-style-type: none"> • Agrees with consistency and readily understood • Agrees with consistency and readily understood/ recommends clarification. • Agrees with consistency /recommends clarification <ul style="list-style-type: none"> ○ CL8 could there be a situation where a software package or solution designed and developed by a 3rd party (not the member) would not be considered a COTS solution? CL19 recommends .02c be clarified as a <i>financial</i> information system. CL22 notes that the P in API is “programming” not “program” and to add a “spreadsheet” as an example of a template. 	<ul style="list-style-type: none"> • CL16, CL24 (2) • CL 2 (1) • CL7, CL8, CL14, CL18, CL19, CL22 (6)

	<ul style="list-style-type: none"> • Agrees terminology will be readily understood • Agrees terminology will be readily understood/should avoid technology related terms (e.g., dashboard) that given the rapid evolution of technology, may fall out of use in a short period of time. • Agrees with consistency /not readily understood • Disagrees/ Not Consistent <ul style="list-style-type: none"> ○ CL3 believes inconsistent with GAS ○ CL13 believes it is too broad and implies any information system could have a material impact on financial decisions made by management and provides a number of examples. Suggest clarification or at least limited to direct financial information systems. ○ CL18 need to use more current technology and consider future technology (newer technology than API, there is bot-to-bot, virtual environments, various configurations on cloud systems and decentralized networks (blockchain) • Disagrees/Not readily understandable. • No comment 	<ul style="list-style-type: none"> • CL1, C16, CL21, CL26 (4) • CL4 (1) • CL10 (1) • CL3, CL9, CL12, CL18, CL25 (5) • CL11, CL20 (2) • CL5, CL6, CL13, CL15, CL17, CL23, CL27 (7)
Comments on Question 2a		
<i>Do you believe it is appropriate to allow members to use professional judgment to determine what is "significant"?</i>	<ul style="list-style-type: none"> • Agrees with proposed interpretation (no specific guidance) • Term Significant Should Be Defined. CL25 suggest the guidance included on page 6 that indicates information is significant if it is probable that it will be material to the financial statements. • Agrees Professional Judgment Appropriate. Suggest linking term to materiality/ including materiality in proposed interpretation/including guidance from the ED Explanation/ consider providing specific general application guidance or provide such details in an illustrative example <ul style="list-style-type: none"> ○ CL14 provides some suggestions regarding general application guidance and that might be helpful. Also, 	<ul style="list-style-type: none"> • CL1, CL2, CL3, CL7, CL16, CL19, CL20, CL21, CL26, CL27 (10) • CL10, CL25 (2) • CL4, CL8, C11, CL14 (4)

	<p>recommend the interpretation include a documentation requirement related to the member's evaluation regarding significant.</p> <ul style="list-style-type: none"> • Appropriate to provide some guidance such as the guidance included on page 6 that indicates information is significant if it is probable that it will be material to the financial statements. The added guidance should also note consideration of the nature of the information and the likelihood that it could be material or become material. Also, helpful to include examples of systems that may generate significant financial information in FAQs so that any updates necessary as a result of the fast pace of change can easily be done. • Believe the PEEC should replace "significant" with "material" • Consider replacing "significant" with "heavy" and clarify that independence should be considered for impairment if the member has heavy influence on the manner in which financial transactions are processed and recorded on the books and records of an entity. • No comment on definition- term can be interpreted to be more restrictive so clarify, add examples or issue FAQs. • No comment 	<ul style="list-style-type: none"> • CL24 (1) • CL22 (1) • CL 19 • CL12 (1) • CL5, CL6, CL9, CL13, CL15, CL17, CL18, CL23 (8)
Comments on Question 2b		
<p><i>By including the concept of "significant" it could be perceived as the proposal is less restrictive than extant. Is it appropriate to allow members to design and develop a financial information system that is not significant?</i></p>	<ul style="list-style-type: none"> • Appropriate exception <ul style="list-style-type: none"> ○ CL1 recommends documentation of conclusion that FIS is not significant. CL14 recommends this as well as provide examples in nonauthoritative guidance. CL24 notes that this scope is consistent with the SEC and IESBA. • Exception Appropriate/ add language that would clarify that design and development services should be looked at from an aggregated perspective as well and if significant then prohibited. • Not Appropriate 	<ul style="list-style-type: none"> • CL1, CL3, CL8, CL11, CL14, CL16, CL20, CL21, CL22, CL24, CL25 (11) • CL4 (1)

	<ul style="list-style-type: none"> Does not believe interpretation would support such conclusion (less restrictive) Makes sense in theory, not in practice since the evaluation would require ongoing consideration. No Comments 	<ul style="list-style-type: none"> CL9, CL10 (2) CL2, CL12 (2) CL7 (1) CL5, CL6, CL13, CL15, CL17, CL18, CL19, CL23, CL26, CL27 (10)
Comments on Question 2c		
<i>Is it clear that “financial processes” is intended to be applied broadly and would include “IT General Controls”?</i>	<ul style="list-style-type: none"> Clear Clear/ stronger language should be used/may be appropriate if such objective was explicitly stated within the interpretation/would be useful if the final Interpretation provided more examples. CL14 suggests using the phrase “financial consolidation and reporting process” Clear but add information technology controls as an example to the interpretation or issue a FAQ that provides this as an example. Unclear. CL7 recommends adding definition of page 6; CL8 should consider the scope of the attest service and whether the member is engaged to issue an opinion on internal control. CL9 members should be able to share expertise in financial processes and IT general controls when the client is implementing the system since they are likely to do so in connection with an audit when making recommendations on how to change or add controls. CL11 recommends an edit to definition of financial information system in its letter. CL12 says it would be clear if the definition from page 6 was carried forward. CL 25 believes the definition of a financial information system would be clearer if it was modified to state that the items included in i. through iv. of paragraph .02a would typically meet the definition of, or be part of, a financial information system. No Comment 	<ul style="list-style-type: none"> CL2, CL3, CL4, CL10, CL12, CL21, CL22 (7) CL1, CL14, CL16 (3) CL24 CL7, CL8, CL9, CL11, CL12, CL20, CL24, CL25 (7) CL5, CL6, CL13, CL15, CL17, CL18, CL19, CL23, CL26, CL27 (10)

Comments on Question 3		
<i>Is it clear that management level dash board reporting would be included in “systems that gather data to assist management in making decisions that directly affect financial reporting”?</i>	<ul style="list-style-type: none"> • No Decision- Multiple Dashboards; depends on dashboard reporting in question. CL7 does it only assist management with improving efficiency or effectiveness of operations? • Include. CL16 notes that members should stay away from implementation decisions that would have an effect on internal controls over financial reporting but assisting client to implement finance-related tools should be an acceptable service. • Include w/ clarification (FAQ that uses example in explanation as well as others) CL24 notes it would be helpful to: (a) include a dashboard as an example in paragraph .11 and (b) issue a FAQ regarding possible ways a member could determine if the dashboard reports would have a significant impact on management’s decision making. CL27 suggests “directly affect (or impact) financial reporting” • Exclude. CL20 believes you should be able to perform dashboard services since they only gather information that already exists and presents it differently than a typical financial statement. CL23 believes it is premature to include dashboards given the inconsistent application of this practice in the middle market today. • No Comment 	<ul style="list-style-type: none"> • CL1, CL7 (2) • CL3, CL8, CL10, CL16, CL22, CL25 (6) • CL4, CL14, CL24, CL27 (4) • CL2, CL11, CL12, CL17, CL18, CL19, CL20, CL21, CL23 (9) • CL5, CL6, CL9, CL13, CL15, CL26 (6)
Comments on Question 4		
<i>If the proposal is adopted as proposed, will the extended period of time be needed for members to adopt the revised guidance?</i>	<ul style="list-style-type: none"> • Proposed Implementation Sufficient. CL22 recommends early implementation be allowed. • No Extended time needed because the guidance is generally less restrictive than the current guidance. • More Time needed past the proposed implementation • No Comment 	<ul style="list-style-type: none"> • CL1, CL2, CL4, CL7, CL8, CL9, CL10, CL11, CL14, CL16, CL22, CL24, CL27 (13) • CL 25 (1) • CL12, CL18, CL20, CL21 (4) • CL3, CL5, CL6, CL13, CL15, CL17, CL19, CL23, CL26 (9)

	General Comments on Overall Interpretation	
<u>Guidance in interpretation should be principles based vs. rules based (2 comments)</u>	<ul style="list-style-type: none"> • Final interpretation should expressly state that such use of a member's electronic practice aids software to aid in the preparation of a client's financial statements is permitted, as it has been heretofore pursuant to ET sec. 1.295 and does not constitute a threat to independence. • Does not address the impact these services have on other types of attestation engagements. Suggests that PEEC broaden the scope of the interpretation to go beyond financial reporting considerations. (e.g., should a member be able to install a non-financial system and issue a SOC 2 or 3 report on the same system?) • Support the ED as drafted and happy to discuss the implications for education or additional feedback we require. • Interpretation should specifically state that a member cannot provide implementation, installation, configuration or customization services for a system the member designed or developed since the definition of COTS refers to third party, and members could be designing systems that are COTS. • Interpretation should address that design or development may include various methods such as custom solutions/products, modules/components for COTS systems; components for commercially available platform; or a framework solution such as SharePoint. • The ED 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 • PEEC should review this current proposal and the hosting FAQs to ensure they are consistent with the previously issued guidance because 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. Also, developing FAQs that address particular current fact patterns that are relevant to current technology and update these as new 	<ul style="list-style-type: none"> • CL2 • CL4 • CL5 • CL7 • CL7 • CL9 • CL12

	<p>technologies evolve.</p> <ul style="list-style-type: none"> • Is there a concern that subscriptions and bundling of services regarding the appearance of impairing independence, suggest clarification here or perhaps Q&As that walk through particular fact patterns and whether they might impair independence? • Concerned that the conclusions reached in the bookkeeping interpretation are not dependent upon who is the software licensee is yet paragraph .04c of the Hosting Services interpretation and discussions with Ethics Staff seems to imply it is dependent upon who the software licensee is. • Recommend that this interpretation be moved to a FAQ or put all technology examples in an FAQ leaving only a principles-based interpretation; • concerned that this theory (CPA's code a threat to independence that cannot be overcome) is conceptually flawed, especially if IT services in conjunction with assurance services are not specifically scoped out; • concerned that the interpretation does not take into consideration other sources and uses of code that could be then attributed to the CPA as they are not specifically addressed in the current rules-based interpretation • Believe this interpretation penalizes the use of technology • Proposing such rules-based interpretive guidance could lead to more confusion and additional questions, especially in an area of professional services that is continually changing as new technologies and business practices are developed • Commercial Off-The-Shelf (COTS) financial information systems-concept is used throughout the exposure draft and it seems to ignore what is happening more and more in practice • Increased clarity could be achieved for members who do and do not practice in this arena if examples were provided delineating between common activity causing and not causing concern • We request an exception for systems like UAN that are required by law, cannot be customized by the client, has broad use, and 	<ul style="list-style-type: none"> • CL12 • CL12 • CL18 • CL18 • CL18 • CL18 • CL19 • CL19 • CL20 • CL26
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	has substantial safeguards in place be immune from the 'design and development' criteria	
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1.295.145 Information Systems Services (Marked Changes from Exposure Draft)**Introduction**

.01 Self-review and management participation *threats* to the *member's* compliance with the "Independence Rule" [1.200.001] may exist when a *member* provides **nonattest** services related to an *attest client's* information systems.

Terminology

.02 The following terms are defined solely for the purpose of applying this interpretation:

- a. Financial information system (**FIS**) is a system that aggregates source data underlying the *financial statements* or generates information that is significant to the *financial statements* or financial processes as a whole. To determine whether a nonattest service is related to a **FIS** financial information system, *members* may **should** consider **all relevant** factors, such as whether the nonattest service will affect the following:
 - i. System controls or system output that will be subject to attest procedures
 - ii. A system that generates data that are used as an input to the *financial statements*
 - iii. A system that gathers data that **is significant to** assist management's **decision** in making decisions that directly impacting financial reporting **matters, such as analytical and reporting tools**
 - iv. A system that is part of the *attest client's* internal controls over financial reporting
- b. 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.
- c. Developing an information system entails creating software code, for individual or multiple modules, and testing such code to confirm it is functioning as designed.
- d. *Commercial off-the-shelf* (COTS) refers to a software package developed, distributed, maintained and supported by a third-party vendor, sometimes simply referred to as an "off the shelf" package or solution. COTS solutions have generally referred to traditional on-premise software that runs on a customer's own computers or on a vendor's "cloud" infrastructure. COTS solutions range from software packages that require only installation on a computer and are ready to run to large scale, complex enterprise applications.

Design, Development, or Implementation Services Not Related to a Financial Information System

.03 When performing design, development, or implementation services described in this interpretation for an *attest client* that are not related to a **FIS** financial information system, *threats* to compliance with the "Independence Rule" [1.200.001] would be at an *acceptable level* provided:

- a. *the information system doesn't aggregate source data underlying the **subject matter of the attest engagement** or generates information that is significant to the subject matter of the attest engagement; and*
- b. all the requirements of the "Nonattest Services" subtopic [1.295] of the "Independence Rule" are met, including that the *attest client* has not outsourced a function, process, or activity to the *member*, which in effect would result in the *member* assuming a management responsibility.

Designs or Develops a Financial Information System

- .04 When a *member* designs or develops an *attest client's* ~~FIS financial information system~~, *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*. Designing and developing a tool that performs a discrete calculation such as a tax provision or depreciation calculation does not constitute designing or developing a ~~FIS financial information system~~ and will not *impair independence*, provided the ~~tool~~ template does not perform an activity that, if performed directly by the *member*, would *impair independence* and the *member* complies with all the requirements of the "Nonattest Services" subtopic [1.295] of the "Independence Rule".

Implementation of a COTS Financial Information System Software Solution

- .05 Implementation services involve activities related to an *attest client's* information systems after the design and development of the system. Implementation ceases when the system is available on a regular basis to the client for its intended use. For example, implementation services can include activities such as installing, configuring, interfacing, customizing, and data translation. Services that are performed post-implementation, such as the maintenance, support, and monitoring of the system, are not considered to be implementation services.
- .06 *Threats* created by certain COTS implementation services related to the *attest client's* ~~FIS financial information system~~ may be reduced to an *acceptable level* by the application of *safeguards*; however, in other situations *threats* to compliance with the "Independence Rule" would be significant and could not be reduced to an *acceptable level* by the application of *safeguards*.

Install a COTS Financial Information System Software Solution

- .07 To install a COTS ~~FIS financial information system~~ software solution means the initial loading of software on a computer, normally onto a customer's server. Software configuration, integration, and conversion activities may follow installation.
- .08 When a *member* installs a COTS ~~FIS financial information system~~ software solution, *threats* to compliance with the "Independence Rule" would be at an *acceptable level*, provided all the requirements of the "Nonattest Services" subtopic of the "Independence Rule" are met.

Configure a COTS Financial Information System Software Solution

- .09 To configure a COTS ~~FIS financial information system~~ software solution means selecting the software features, functionality options, and settings provided by the vendor that will determine how the software will perform certain transactions and process data. Configuration options may also include selecting the predefined format of certain data attributes and the inclusion or exclusion of such attributes. For purposes of this interpretation, configuring a COTS ~~FIS financial information system~~ software solution does not involve developing new

software code or features to modify or alter the functionality of the COTS software solution in ways not pre-defined by the vendor.

- .10 When a *member* configures a COTS ~~FIS financial information system~~ software solution, *threats* to compliance with the "Independence Rule" would be at an *acceptable level*, provided all the requirements of the "Nonattest Services" subtopic of the "Independence Rule" are met.

Customize a COTS Financial Information System Software Solution

- .11 To customize a COTS ~~FIS financial information system~~ software solution means altering or adding to the features and functions provided for by the vendor, that go beyond all options available when configuring the COTS software solution. For purposes of this interpretation, customizing can involve both modification and enhancements:
 - a. Modification involves altering the COTS software solution code to change or add to the functionality provided by the vendor.
 - b. Enhancements involve developing new code, external to the COTS software solution, that works in concert with the COTS software solution to provide altered or additional functionality.
- .12 If a *member* customizes an *attest client's* COTS ~~FIS 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*.

Interface a COTS Financial Information System Software Solution

- .13 Providing interface services for a COTS ~~FIS financial information system~~ software solution means connecting two or more systems by designing and developing software code that passes data from one system to another. Interfaces may flow in one direction or be bidirectional. Interfaces may involve the performance of an end-to-end transaction or they may pass data from one system to another.
- .14 If a *member* provides interface services for a COTS ~~FIS 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.
- .15 If a *member* uses an application program interface (API) that is developed by a third party to interface legacy or third-party COTS ~~FIS financial information system~~ software solutions, *threats* to *independence* would be at an *acceptable level*, provided the *member* will not be designing or developing code for the API to work and all the requirements of the "Nonattest Services" subtopic of the "Independence Rule" are met.

Data Translation Services Related to a COTS Financial Information System Software Solution

- .16 Performing data translation services for a COTS ~~FIS financial information system~~ software solution involves designing and developing the rules or logic necessary to convert legacy system data to a format that is compatible with that of the new system.
- .17 If a *member* performs data translation services for a COTS ~~FIS 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.
- .18 If a *member* uses an API developed by a third party to perform data translation services for a COTS ~~FIS financial information system~~ software solution, *threats* to *independence* would be

at an *acceptable level*, provided the *member* will not be designing or developing code for the API to work and all the requirements of the "Nonattest Services" subtopic of the "Independence Rule" are met.

System and Network Maintenance, Support, and Monitoring

.19 Maintenance, support, and monitoring services are activities that are provided after a financial or nonfinancial system or network is implemented. If post-implementation services involve the *attest client* outsourcing an ongoing function, process, or activity to the *member* that in effect would result in the *member* assuming a management responsibility, 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*. Examples of such services that involve an ongoing function, process, or activity that in effect would result in the *member* assuming a management responsibility would include a service whereby the *member* directly or indirectly does any of the following:

- a. Operates the *attest client's* network, such as managing the *attest client's* systems or software applications
- b. Supervises client personnel involved in the operation of the *attest client's* information systems
- c. Has responsibility for monitoring or maintaining the *attest client's* network performance
- d. Operates or manages the *attest client's* information technology help desk
- e. Has responsibility to perform ongoing network maintenance, such as updating virus protection solutions, applying routine updates and patches, or configuring user settings
- f. Has responsibility for maintaining the security of the *attest client's* networks and systems

.20 *Independence* will not be *impaired*, provided all the requirements of the "Nonattest Services" subtopic of the "Independence Rule" are met and the maintenance, support, and monitoring services are discrete nonrecurring engagements for which the *attest client* has not outsourced a function, process, or activity to the *member* that in effect would result in the *member* assuming a management responsibility. Examples of such services that do not *impair independence* may include being engaged for a discrete project to do any of the following:

- a. Analyze a network and provide observations or recommendations
- b. Apply virus protection solutions or updates that the *member* did not design or develop
- c. Apply certain updates and patches that the *member* did not design or develop
- d. Provide training or instruction on a new software solution
- e. Assess the design or operating effectiveness of an *attest client's* security over information technology systems
- f. Assess the *attest client's* information technology security policies or practices

Effective Date

.21 This interpretation will be effective one year after it appears in the *Journal of Accountancy*. Early implementation is allowed.

Nonauthoritative questions and answers regarding information systems design, implementation, and integration services are available at www.aicpa.org/InterestAreas/ProfessionalEthics/Resources/Tools/DownloadableDocuments/NonattestServicesFAQs.pdf.

Hosting services

1. **A member uses a third-party clearinghouse to issue attest reports. Would the clearinghouse be considered a member's portal under item e. in paragraph .04 of the Hosting Services interpretation (1.295.143)?**

No, the clearinghouse would not be considered a member's portal provided all of the following criteria are met:

- a. The platform is a document repository designed to facilitate document exchange between users.
 - b. The platform is hosted, run and controlled entirely by a third-party vendor that is not the member.
 - c. The member, attest client and other platform users have their own user agreements with the third-party vendor.
2. **A member prepares and transmits an attest client's income tax return and related schedules (return) in accordance with the Tax Services interpretation (1.295.160) and sends the filed return to the client using the member's portal. Must the member terminate the attest client's access to that return within a reasonable period after preparing and transmitting the return to avoid providing hosting services?**

Yes. Item e. in paragraph .04 of the interpretation indicates that to avoid providing hosting services, *members* should terminate an *attest client's* access to the data or records in the portal within a reasonable period after the conclusion of the engagement.

3. **Item e. in paragraph .04 of the interpretation indicates that to avoid providing hosting services, *members* should terminate an *attest client's* access to the data or records in the portal within a reasonable period after the conclusion of the engagement. What is a reasonable period?**

A reasonable period would be as soon as practicable but, absent extenuating circumstances, no later than 60 days after the completion of the engagement or provision of the information to the attest client through the portal, whichever is longer.

4. **Would a member who uses a third-party's general ledger software to perform bookkeeping services for an attest client be providing hosting services to the attest client if the software is solely located on the member's server (or server leased by the member)?**

Yes, the member would be providing hosting services because the member would be accepting responsibility to be the sole host of the attest client's financial information system. As such, the member has assumed responsibility for the attest client's internal control over financial reporting (that is, safeguarding and maintaining the client's data and records), which is a management responsibility that impairs independence (see 1.295.030.02(k)).

5. **Would the answer to question 3 change if the member provides the attest client with reports from the system so that the attest client's books and records are complete?**

No, the answer would not change and the member would still be accepting responsibility for being the sole host of the attest client's financial information system. In this situation, the system in question is not a software product that produces a discrete calculation (for example, depreciation). Rather, the member has assumed responsibility for the attest client's internal control over financial reporting, which is a management responsibility that impairs independence (see 1.295.030.02(k)).

However, the answer would change if *member* and the *attest client* maintain separate instances of the software on their respective servers, and the *member* provides updated financial information electronically to the *attest client*.

- 6. Would the answer change to question 3 if the software is located on a third-party's server (or server leased by the third-party) and the member has the software agreement with the third-party software provider?**

No, the answer would not change. The attest client does not have its own agreement with the third-party provider, making the attest client's access to its financial information dependent on its relationship with the member. Therefore, the member would still be accepting responsibility for being the sole host of the attest client's financial information system. As such, the member has assumed responsibility for the client's internal control over financial reporting, which is a management responsibility that impairs independence (see 1.295.030.02(k)).

However, the answer would change if the *attest client* enters into an agreement with a third-party service provider to maintain the software in a cloud-based solution and grants the *member* access to the software so that the *member* can perform the bookkeeping service for the *attest client*.

- 7. A member returned an attest client's original data or records used to perform a nonattest service but retained a copy as documentation in support of their service. Would the member be providing hosting services if the member complied with the attest client's subsequent request for a copy of its data or records?**

No. Item a. in paragraph .04 of the interpretation clearly allows a member to retain copies of an attest client's original data or records as documentation that supports the member's professional service. An occasional request by the client for copies of original data or records would not, in and of itself, mean that the member was providing hosting services. However, the member should be alert to a situation in which the client repeatedly requests copies of their data or records, which may signify that the member has become a de facto repository for the client's data or records.

- 8. A member uses payroll software that resides on the firm's server (or server leased by the firm) to prepare an attest client's monthly payroll using time records that the attest client has provided and approved. Would the member be providing hosting services?**

The member would not be providing hosting services if the member gives the payroll report to the attest client so that the attest client's books and records are complete. In this situation, the member would need to provide this information to the attest client each payroll period so

that the attest client is able to effectively oversee and take responsibility for the member's nonattest service.

This differs from a situation in which a member provides an attest client with bookkeeping services using general ledger software that resides on the firm's server (or server leased by the firm). In such situation, the member has assumed responsibility for maintaining the client's financial information, in total and become a part of the client's internal control over financial reporting, which is a management responsibility that impairs independence (see 1.295.030.02(k)).

- 9. A member provides an attest client access to sales tax computation software on the member's server. The attest client inputs its original data, the software calculates the sales tax and generates a tax return, which the attest client downloads and files. What actions could the member take to avoid providing hosting services?**

To avoid performing hosting services, the member may wish to consider the following:

- a. In obtaining an understanding with the attest client about the scope of the service (paragraph .01 of 1.295.050), specify that it is the attest client's responsibility to maintain its original data and records as well as the information produced by the system (information) and that the member has no responsibility to safeguard or maintain any of these data, records or information.
- b. Terminate the client's access to their data, records and information in the system after a reasonable period.

**Professional Ethics Executive Committee
Staff Augmentation Task Force**

Task Force Members

Lisa Snyder (Chair), Shelly Van Dyne, Coalter Baker, Jeff Lewis, Brian Lynch, Bill Mann
Staff: Brandon Mercer, CPA CGMA

Task Force Charge

The Task Force's charge is to study the issue of staff augmentation and independence, and determine whether additional guidance for members is warranted.

Reason for Agenda Item

The purpose of this agenda item is to discuss revisions made to the Task Force's draft proposal pursuant to feedback received from the Committee at its August 2018 meeting, and to request the Committee approve exposure of the revised draft proposal for comment.

Background

The Task Force presented a draft proposal and questions for the Committee at the Committee's August 2018 meeting. The Task Force held a conference call in October 2018 to consider the Committee's feedback and to make revisions to the draft proposal. Accordingly, the Task Force requests that PEEC consider the revisions made by the Task Force and approve exposure of the proposal for comment. The Task Force's revised proposal can be viewed at **[Agenda Item 4B](#)**.

Summary of Issues

In paragraph .02 of the draft interpretation proposed at the August PEEC meeting, members would be required, among other safeguards, to ensure that the "duration of the arrangement is temporary in nature" to reduce threats to an acceptable level. At the August Committee meeting, the Task Force indicated that it did not believe that the word "temporary" required a definition, but acknowledged that a question could be included in the exposure draft asking if commenters believed the meaning of "temporary" is clear. PEEC did not reach a consensus on the appropriate terminology, and suggested that the Task Force further deliberate regarding the proper terminology and intent of the safeguard. Some believed that "temporary" means "not permanent," while others had concerns that bright lines and prescribed time frames may be problematic in such scenarios. PEEC agreed that the duration or temporary nature should be a consideration in concept, but some expressed concern that attempting to define temporary would move the analysis further away from the use of professional judgment. PEEC suggested further deliberation on other terminology, and consulting the [SEC Investigation Report](#) and IESBA and other sources for appropriate contextual wording to address the duration of the arrangement. In addition, the Task Force was to consider whether the safeguard should be in both paragraph .02 and paragraph .03.

The Task Force's resulting recommendations and suggested revisions are discussed below. The referenced revisions are included at **[Agenda Item 4B](#)**.

Paragraph .02 – Required Safeguards for Staff Augmentation Arrangements

Paragraph .02 contains safeguards required for staff augmentation arrangements, which are similar to the requirements for other non-attest services. During its most recent call, the Task Force changed the polarity of the lead-in to this paragraph, from “independence is not impaired provided that the following safeguards are met...” to “independence is impaired unless the following safeguards are met.”

Paragraph .02 as presented at the August Committee meeting included a requirement that the “duration of the arrangement is temporary in nature.” At the August Committee meeting there were two questions raised regarding the concept of duration: 1) whether it should be included in both paragraph .02 and paragraph .03; and 2) the appropriate terminology to express the intended safeguard. The Task Force generally agreed that the notion of duration should be addressed in both paragraphs, but could be addressed using appropriate terminology for the appropriate context of the paragraphs.

During its recent conference call, the Task Force considered the related [SEC Investigative Report](#) and extant AICPA/IESBA provisions (**Agenda Item 4C**) and various terminology and concepts from those sources, (e.g. short term, short period of time, discrete, recurring, frequent, exclusive, continuous). After deliberation, the Task Force agreed that the phrase “for a limited period of time” better describes the intended safeguard compared to “temporary” or “short period of time.” As a result, the Task Force suggests revising “temporary in nature” to “for a limited period of time” in paragraph .02.

The Task Force continues to agree that a question should be included in the exposure draft regarding the duration terminology and the common views of the terms.

Action Needed:

See Agenda Item 4B. Does PEEC agree with the revised polarity of paragraph .02 to state that independence would be impaired unless all the safeguards are met?

Does PEEC agree that the concept of duration should be both a required safeguard in paragraph .02, and a factor for consideration in the evaluation of prohibited employment in paragraph .03?

Does PEEC agree that the term “for a limited period of time” is an appropriate phrase to describe the safeguard in paragraph .02?

Paragraph .03 – Appearance of Simultaneous Employment:

The concepts of exclusivity, continuity, and frequency are noted in the SEC Investigation Report as indicators related to the duration of an arrangement that may create the appearance of prohibited employment. For example, augmented staff working alongside client employees performing the same functions, or working at the client’s place of business exclusively and

continuously for an extended period of time were more indicative factors of appearing to be an employee of the client. The Task Force decided that paragraph .03 should provide a more detailed list to facilitate evaluating the duration of an arrangement and its impact on the appearance of prohibited employment. The Task Force agreed that the issues of exclusivity, continuity, and frequency should all be considerations included in the list and suggests revisions to reflect these concepts (see **Agenda Item 4B** and excerpt below):

.03 ...When evaluating the appearance of prohibited employment with the attest client, the member should consider factors such as:

- a.** the duration of the staff augmentation arrangement;
- b.** **whether the augmented staff will provide services to other clients during the period of the arrangement;** ~~the portion of the augmented staff's time spent performing augmentation activities for the specific attest client compared to time spent performing professional services or activities for other clients of the member's firm.~~
- c.** **the frequency with which the augmented staff will perform activities at the attest client's location (e.g. daily); and**
- d.** **whether the arrangement is discrete or recurring in nature, and if recurring, the frequency of such recurrence.**

Does PEEC agree with the itemized list of considerations that address the appearance of prohibited employment, as it relates to the concept of exclusivity, continuity, and frequency?

Does PEEC believe there are any other factors related to the appearance of prohibited employment that should be added to the itemized list?

Effective Date

The Task Force suggests a delayed effective date of six months after the last day of the month in which the pronouncement appears in the *Journal of Accountancy* to allow firms and clients to implement appropriate policies and procedures to comply with the draft proposal.

Does PEEC agree that a six-month delay in the effective date is appropriate?

Does PEEC believe that any additional questions for commenters should be included in the exposure draft?

Action Needed

The Task Force requests PEEC approve exposure of the draft proposal at **Agenda Item 4B** for comment, with a comment period of sixty days from the date of exposure.

Communication Plan

Upon exposure, the exposure draft will be posted to the AICPA website and distributed to both internal and external stakeholders and other interested parties.

Materials Presented

Agenda Item 4B – Draft Proposal

Agenda Item 4C – IESBA and AICPA Provisions

Staff Augmentation Task Force**Revisions to Draft Proposal**

Additions made since August 2018 PEEC meeting are bold underlined, deletions are struck through.

1.295.xxx Staff Augmentation Arrangements

.01 When a member or member's firm has a staff augmentation arrangement with an attest client, self-review and management participation threats to the member's compliance with the "Independence Rule" [1.200.001] may exist.

.02 Threats to compliance with the "Independence Rule" [1.200.001] would **not** be at an acceptable level, and independence would ~~not~~ be impaired, ~~provided that,~~ **unless,** in addition to the General Requirements of the "Nonattest Services" interpretation [1.295.000], all of the following safeguards are met:

- a. The member is satisfied that client management designates an individual or individuals who possess suitable skill, knowledge, and experience, preferably within senior management, to be responsible for:
 - i. determining the nature and scope of the activities to be provided by the individual performing the augmented staff services (the "augmented staff");
 - ii. supervising and overseeing the activities performed by the augmented staff; and
 - iii. evaluating the adequacy of the activities performed by the augmented staff and the findings resulting from the activities.
- b. The activities do not result in the augmented staff assuming management responsibilities as described in the "Management Responsibilities" interpretation [1.295.030] of the "Independence Rule" [1.200.001];
- c. The augmented staff only performs activities that would not otherwise be prohibited by the "Nonattest Services" interpretation [1.295.000] of the "Independence Rule" [1.200.001]; and
- d. The duration of the arrangement is **for a limited period of time.** ~~temporary in nature.~~

.03 In all circumstances, the member should consider whether the staff augmentation arrangement creates the appearance of prohibited employment with the attest client (See the "Simultaneous Employment or Association With an Attest Client" interpretation [1.275.005] of the "Independence Rule" [1.200.001]). When evaluating the appearance of prohibited employment with the attest client, the member should consider factors such as:

- a. the duration of the staff augmentation arrangement;
- b. **whether the augmented staff will provide services to other clients during the period of the arrangement;** ~~the portion of the augmented staff's time spent performing augmentation activities for the specific attest client compared to time spent performing professional services or activities for other clients of the member's firm.~~
- c. **the frequency with which the augmented staff will perform activities at the attest client's location (e.g. daily); and**
- d. **whether the arrangement is discrete or recurring in nature, and if recurring, the frequency of such recurrence.**

However, threats to compliance with the "Independence Rule" [1.200.001] would not be at an acceptable level and independence would be impaired if the augmented staff is held out or treated as an employee of the attest client, **such as being:** ~~as described below:~~

- a. ~~i. The augmented staff is **l**isted as an employee in the attest client's directories or other attest client publications;~~
- b. ~~ii. The augmented staff is **r**eferred to by title or description as supervising or being in charge of any business function of the attest client;~~
- c. ~~iii. The augmented staff is **i**dentified as an employee **of the attest client** in correspondence such as email, letterhead, or internal communications; or~~
- d. ~~iv. The augmented staff **Able to** participates in health, retirement, or other benefit plans that are normally only offered to employees of the attest client.~~

.04 The significance of any threats should be evaluated and safeguards applied when necessary to eliminate the threats or reduce them to an acceptable level. Examples of such safeguards may include:

- a. Not using the augmented staff on the attest engagement team, or not using the augmented staff to perform attest procedures on any areas for which the staff performed activities during the augmented staff arrangement;
- b. Discussion of the threats and any safeguards applied with those charged with governance;
- c. Rotation of individuals performing the staff augmentation activities; or
- d. Monitoring the scope of activities performed by augmented staff.

.05 This interpretation is effective [six months after issuance] with early implementation allowed.

Staff Augmentation Task ForceIESBA Ethics Handbook – Temporary Staff Assignments**Temporary Staff Assignments**

290.140 The lending of staff by a firm to an audit client may create a self-review threat. Such assistance may be given, but only for a short period of time and the firm's personnel shall not be involved in:

- a) Providing non-assurance services that would not be permitted under this section; or
- b) Assuming management responsibilities.

In all circumstances, the audit client shall be responsible for directing and supervising the activities of the loaned staff.

The significance of any threat shall be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level. Examples of such safeguards include.

- a) Conducting an additional review of the work performed by the loaned staff;
- b) Not giving the loaned staff audit responsibility for any function or activity that the staff performed during the temporary staff assignment; or
- c) Not including the loaned staff as a member of the audit team.

AICPA Code Sections 1.275, 1.295 (excerpts only)**1.275.005 Simultaneous Employment or Association With an Attest Client**

.01 In this interpretation, simultaneous employment or association with an *attest client* is serving as a director, an officer, an employee, a promoter, an underwriter, a voting trustee, a trustee for any pension or profit-sharing trust of the *attest client*, or in any capacity equivalent to that of a member of management of an *attest client* during the period covered by the *financial statements* or the *period of the professional engagement*.

.02 If a *partner* or professional employee of the *member's firm* is simultaneously employed or associated with an *attest client*, familiarity, management participation, advocacy, or self-review *threats* to the *member's* compliance with the "[Independence](#)"

[Rule](#)” [1.200.001] would not be at an *acceptable level* and could not be reduced to an *acceptable level* by the application of *safeguards*. Accordingly, *independence* would be *impaired*. [Prior reference: paragraph .02C of ET section 101]

.03 However, *threats* will be at an *acceptable level* and *independence* will not be *impaired* when either of the following situations exists:

- a. A *partner* or professional employee of a *firm* serves as an adjunct faculty member of an educational institution that is an *attest client* of the *firm*, and the *partner* or professional employee meets all of the following *safeguards*:
 - i. Does not hold a *key position* at the educational institution
 - ii. Does not participate on the *attest engagement team*
 - iii. Is not an *individual in a position to influence the attest engagement*
 - iv. Is employed by the educational institution on a part-time and non-tenure basis
 - v. Does not participate in any employee benefit plans sponsored by the educational institution, unless participation is required
 - vi. Does not assume any management responsibilities or set policies for the educational institution

Upon termination of employment, the *partner* or professional employee should comply with the requirements of the “[Former Employment or Association With an Attest Client](#)” interpretation [1.277.010] of the “Independence Rule” [1.200.001]. [Prior reference: paragraph .21 of ET section 101]

- b. A *member* in a government audit organization performs an *attest engagement* with respect to the government entity and the head of the government audit organization meets at least one of the following:
 - i. Is directly elected by voters of the government entity with respect to which *attest engagements* are performed
 - ii. Is appointed by a legislative body and is subject to removal by a legislative body
 - iii. Is appointed by someone other than the legislative body, as long as the appointment is confirmed by the legislative body and removal is subject to oversight or approval by the legislative body

.04 *Members* that are simultaneously employed or associated with an *attest client* should consider their obligations as a *member in business* under [part 2](#) of the code. [No prior reference: new content]

Effective Date

.05 [Paragraph .04](#) of this interpretation is effective December 15, 2014.

A nonauthoritative question and answer regarding independent contractors retained by the firm who are simultaneously employed or associated with an attest client is available

1.295.040 General Requirements for Performing Nonattest Services

.01 When a member performs a nonattest service for an *attest client*, *threats* to the member's compliance with the "Independence Rule" [1.200.001] may exist. Unless an *interpretation* of the "Nonattest Services" subtopic [1.295] under the "Independence Rule" states otherwise, *threats* would be at an *acceptable level*, and *independence* would not be *impaired*, when all the following *safeguards* are met:

- a. The member determines that the *attest client* and its management agree to
 - i. assume all management responsibilities as described in the "Management Responsibilities" interpretation [1.295.030].
 - ii. oversee the service, by designating an individual, preferably within senior management, who possesses suitable skill, knowledge, and/or experience. The member should assess and be satisfied that such individual understands the services to be performed sufficiently to oversee them. However, the individual is not required to possess the expertise to perform or re-perform the services.
 - iii. evaluate the adequacy and results of the services performed.
 - iv. accept responsibility for the results of the services.
- b. The member does not assume management responsibilities (See the "Management Responsibilities" interpretation [1.295.030] of the "Independence Rule") when providing nonattest services and the member is satisfied that the *attest client* and its management will
 - i. be able to meet all of the criteria delineated in item a;
 - ii. make an informed judgment on the results of the member's nonattest services; and
 - iii. accept responsibility for making the significant judgments and decisions that are the proper responsibility of management.

If the *attest client* is unable or unwilling to assume these responsibilities (for example, the *attest client* cannot oversee the nonattest services provided or is unwilling to carry out such responsibilities due to lack of time or desire), the member's performance of nonattest services would *impair independence*.

- c. Before performing nonattest services the member establishes and documents in writing his or her understanding with the *attest client* (board of directors, audit committee, or management, as appropriate in the circumstances) regarding
 - i. objectives of the engagement,
 - ii. services to be performed,
 - iii. *attest client's* acceptance of its responsibilities,
 - iv. member's responsibilities, and
 - v. any limitations of the engagement.

.02 The *safeguards* in [paragraph .01](#) and the “[Documentation Requirements When Providing Nonattest Services](#)” interpretation [1.295.050] of the “Independence Rule” [1.200.001] do not apply to certain routine activities performed by the member, such as providing advice and responding to the *attest client's* questions as part of the *attest client*-member relationship. However, in providing such services, the member must not assume management responsibilities, as described in the “[Management Responsibilities](#)” interpretation [1.295.030] of the “Independence Rule.” [Prior reference: paragraph .05 of ET section 101]

Nonauthoritative questions and answers regarding suitable skill, knowledge, and experience are available at www.aicpa.org/interestareas/professionalethics/resources/tools/downloadabledocuments/nonattestservicesfaqs.pdf.

1.295.150 Internal Audit

.01 For purposes of this interpretation, internal audit services involve assisting the *attest client* in the performance of its internal audit activities, sometimes referred to as “internal audit outsourcing.” When a member provides internal audit services to an *attest client*, self-review and management participation *threats* to the *covered member's* compliance with the “[Independence Rule](#)” [1.200.001] may exist.

.02 The *attest client's* management is responsible for directing the internal audit function, including the management thereof. Such responsibilities include, but are not limited to, designing, implementing and maintaining internal control. *Threats* to compliance with the “[Independence Rule](#)” [1.200.001] would not be at an *acceptable level*, cannot be reduced to an *acceptable level* by the application of *safeguards*, and *independence* would be *impaired* if the *attest client* outsources the internal audit function to the member, whereby the member, in effect, manages the *attest client's* internal audit activities.

.03 However, except for the outsourcing services discussed in [paragraph .02](#), *threats* to compliance with the “[Independence Rule](#)” [1.200.001] would be at an *acceptable level* and *independence* would not be *impaired* if the member assists the *attest client* in performing financial and operational internal audit activities, provided that, in addition to the “[General Requirements for Performing Nonattest Services](#)” interpretation [1.295.040] of the “Independence Rule,” the member is satisfied that management

- a. designates an individual or individuals who possess suitable skill, knowledge, and experience, preferably within senior management, to be responsible for the internal audit function.
- b. determines the scope, risk, and frequency of internal audit activities, including those the member will perform in providing the services.
- c. evaluates the findings and results arising from the internal audit activities, including those the member will perform in providing the services.
- d. evaluates the adequacy of the audit procedures performed and the findings resulting from the performance of those procedures.

.04 For example, if the member applies the *safeguards* in [paragraph .03](#), the member may assess whether performance is in compliance with management’s policies and procedures, identify opportunities for improvement, and recommend improvement or further action for management consideration and decision making.

.05 The member may assist the individual responsible for the internal audit function in performing preliminary audit risk assessments, preparing audit plans, and recommending audit priorities. The member should also be satisfied that *those charged with governance* are informed about the member’s and management’s respective roles and responsibilities in connection with the engagement. Such information should provide *those charged with governance* a basis for developing guidelines for management and the member to follow in carrying out these responsibilities and monitoring how well the respective responsibilities have been met.

.06 *Threats* to compliance with the “[Independence Rule](#)” [1.200.001] 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*, if, for example, in addition to those activities listed in the “[Management Responsibilities](#)” interpretation [1.295.030] of the “Independence Rule,” a member

- a. performs ongoing evaluations (see [paragraph .10](#) that follows) or control activities (for example, reviewing *loan* originations as part of the *attest client*’s approval process or reviewing customer credit information as part of the customer’s sales authorization process) that affect the execution of transactions or ensure that transactions are properly executed or accounted for, or both, and performs routine activities in connection with the *attest client*’s operating or production processes that are equivalent to those of an ongoing compliance or quality control function.

- b. performs separate evaluations on the effectiveness of a significant control such that the member is, in effect, performing routine operations that are built into the *attest client's* business process.
- c. has *attest client* management rely on the member's work as the primary basis for the *attest client's* assertions on the design or operating effectiveness of internal controls.
- d. determines which, if any, recommendations for improving the internal control system should be implemented.
- e. reports to the board of directors or audit committee on behalf of management or the individual responsible for the internal audit function.
- f. approves or is responsible for the overall internal audit work plan, including the determination of the internal audit risk and scope, project priorities, and frequency of performance of audit procedures.
- g. is connected with the *attest client* as an employee or in any capacity equivalent to a member of management (for example, being listed as an employee in the *attest client's* directories or other *attest client* publications, permitting himself or herself to be referred to by title or description as supervising or being in charge of the *attest client's* internal audit function, or using the *attest client's* letterhead or internal correspondence forms in communications).

.07 *Monitoring activities.* Designing, implementing, or maintaining the *attest client's* monitoring activities are management responsibilities. Accordingly, *independence* would be *impaired* if a member accepts responsibility for performing such activities. Monitoring activities are procedures performed to assess whether components of internal control are present and functioning. Monitoring can be done through ongoing evaluations, separate evaluations, or some combination of the two. Ongoing evaluations are generally defined, routine operations built in to the *attest client's* business processes and performed on a real-time basis. Ongoing evaluations, including managerial activities and everyday supervision of employees, monitor the presence and functioning of the components of internal control in the ordinary course of managing the business. A member who performs such activities for an *attest client* would be considered to be accepting responsibility for maintaining the *attest client's* internal control. Accordingly, the management participation *threat* created by a member performing ongoing evaluations is so significant that no *safeguards* could reduce the *threat* to an *acceptable level*, and thus *independence* would be *impaired*.

.08 Separate evaluations are conducted periodically and generally not ingrained within the business but can be useful in taking a fresh look at whether internal controls are present and functioning. Such evaluations include observations, inquiries, reviews, and other examinations, as appropriate, to ascertain whether controls are designed, implemented, and conducted. The scope and frequency of separate evaluations is a matter of judgment and vary depending on assessment of risks, effectiveness of ongoing evaluations, and other considerations. Because

separate evaluations are not built into the *attest client's* business process, separate evaluations generally do not create a significant management participation *threat* to *independence*.

.09 Members should refer to the Committee of Sponsoring Organizations of the Treadway Commission's (COSO's) *Internal Control—Integrated Framework*, for additional guidance on monitoring activities and distinguishing between ongoing and separate evaluations.

.10 Members should use judgment in determining whether otherwise permitted internal audit services performed may result in a significant management participation *threat* to *independence*, considering factors such as the significance of the controls being tested, the scope or extent of the controls being tested in relation to the overall *financial statements* of the *attest client*, as well as the frequency of the internal audit services. If the *threat* to *independence* is considered significant, the member should apply *safeguards* to eliminate or reduce the *threat* to an *acceptable level*. If no *safeguards* could reduce the *threat* to an *acceptable level*, then *independence* would be *impaired*.

.11 *Attest-related services*. Services considered extensions of the member's audit scope applied in the audit of the *attest client's financial statements*, such as confirming accounts receivable and analyzing fluctuations in account balances, are not considered internal audit services and would not be subject to this interpretation even if the extent of such testing exceeds that required by generally accepted auditing standards (GAAS). In addition, engagements performed under the attestation standards would not be considered internal audit services and, therefore, would not *impair independence*.

.12 When a member performs internal audit services that would not *impair independence* under this interpretation and is subsequently engaged to perform an attestation engagement to report on management's assertion regarding the effectiveness of its internal control, *independence* would not be considered *impaired*, provided the member is satisfied that *attest client* management does not rely on the member's work as the primary basis for its assertion. [Prior reference: paragraph .05 of ET section 101]

State and Local Government Task Force

Task Force Members: Nancy Miller (Chair), James Curry, John Good, Lee Klumpp, George Dietz, Flo Ostrum, Anna Dourdourekas, Jack Dailey, Randy Roberts, Barbara Romer (Observer), E. Gorla (Staff), J. Kappler (Staff), M. Powell (Staff)

Task Force Objective

Consider incorporating the threats and safeguards approach into the Entities Included in State and Local Government Financial Statements interpretation [1.224.020] and determine if a conceptual framework assessment could be utilized to determine when a member needs to be independent of state and local governmental entities for which he or she is not providing financial statement attest services. The Task Force will also clarify who at the firm and which immediate family members the interpretation should extend to and if the interpretation should contain any exceptions. The Task Force will also determine if the final guidance could be extended to the federal government environment.

Reason for Agenda

Discuss the revisions made for upstream entities (**Agenda Items 5B.1 and B.2**) and investments (**Agenda Item 5C**) and next steps.

Summary of Issues***Upstream Entities***

During the August meeting there was significant discussion about what the evaluation would entail for upstream entities. While the Committee seemed agreeable that the evaluation would require members identify if there are any upstream entities meeting the required criteria, the Committee agreed that it wasn't clear what was expected of the member once such an entity was identified. A number of theoretical suggestions were noted for possible consideration by the Task Force.

After discussing these suggestions and related strawmen the Task Force agreed to recommend to the Committee that the interpretation not contain any specific requirements for upstream entities. Rather, the Task Force recommends that examples¹ of relationships or circumstances that members may have with upstream non-affiliates that could result in the member consulting the Conceptual Framework for Independence be added to the interpretation. The Task Force believes that adding these examples strikes an appropriate balance between cost of compliance for upstream entities and providing adequate guidance that will help members operationalize the interpretation. The Task Force is also recommending that this approach be used to address downstream entities that are not affiliates and investments that are not affiliates.

Question for the Committee

1. Does the Committee agree that that adding the examples in paragraph .04 strikes an appropriate balance between cost of compliance and providing adequate guidance that will help members operationalize the interpretation?

¹ The Task Force believes that there is precedence for including examples (e.g., Paragraph .03 of the [Retirement, Savings, Compensation, or Similar Plans](#) interpretation; Paragraph .03 of the [Insurance Policies With Investment Options](#) interpretation; Item c. in paragraph .01 of the [Immediate Family Member Participation in an Employee Benefit Plan With Financial Interests in an Attest Client](#) interpretation; Paragraph .09 of the [Actual or Threatened Litigation](#).)

Investments

The Task Force was asked to consider if the intent of the interpretation was for members to consider as affiliates, investments held by just the financial statement attest client or, if they should also consider investments held by affiliates. The Task Force is recommending that members not monitor investments that affiliates ii. (entity that is material to the client that the client has MTMI over and the member makes reference to another auditor's report) or iii. (materially excluded entity that the client has MTMI over) have, because that the cost of compliance outweighs the threats to independence. To clarify this position, the Task Force recommends the following additions be made to affiliate iv.

- iv. the **financial statement attest client or an affiliate under item b. i. of this definition** has an investment **in an investee** that either
 - 1. is not trivial and clearly inconsequential to the **financial statement attest client's** financial statements as a whole and gives the **financial statement attest client control** over the **investee** or
 - 2. is material to the **financial statement attest client's financial statements** as a whole and gives the **financial statement attest client significant influence** over the **investee**.

Question for the Committee

- 1. Does the Committee agree the cost of compliance outweighs the threats to independence for affiliates ii and iii?

Impact Analysis and Other Training or Educational Material

Staff updated the impact analysis (**Agenda Item 5D**) for the proposed revisions and seeks the Task Force's input on whether there are other areas of impact that should be highlighted.

The Committee is asked to discuss if there are other types of training and educational material that should be developed, including whether a detailed comment letter summary would be beneficial at this point or if the impact analysis is adequate.

Questions for the Committee

- 1. Does the Committee have any suggestions or changes to the impact analysis?
- 2. What other training or educational material should be developed and are there any members of the Committee that are interested in being involved with these projects?

Re-Exposure

The Task Force believes that the substantive revisions made to the proposal are supported by the comments received and by themselves would not be significant enough to warrant re-exposure. However, if the Committee believes re-exposure is necessary since the proposal was significantly re-written to address simplification and clarity concerns, the Task Force would recommend a targeted re-expose wherein the proposal would seek feedback limited to input regarding whether any unintended consequences were caused by: (1) the simplification and clarity changes; and (2) the substantive changes made to the initial exposure draft. The exposure draft should make it clear that input on the original issues proposed is not requested.

Question for the Committee

1. Does the Committee believe the proposal needs a targeted re-exposure to determine whether there are any unintended consequences that were caused by the revisions?

Materials Presented

Agenda Item 5B.1	Proposed Revised SLG Interpretation (Changes from Exposure Draft Un-Marked)
Agenda Item 5B.2	Proposed Revised SLG Interpretation (Changes from Exposure Draft Marked)
Agenda Item 5C	Proposed Revised Affiliate Definition
Agenda Item 5D	Revised Impact Analysis

1.224.020 State and Local Government Entities (Un-Marked)**Applicability**

- .01 This interpretation applies to state and local governmental entities. State and local governmental entities are entities whose GAAP standard setter is GASB. Examples of state and local governmental entities include general purpose governments such as states, counties, cities, towns, villages, and special purpose governments that perform limited activities. Examples of special purpose governments include, but are not limited to, cemetery districts, school districts, universities and colleges, utilities, hospitals or other health care organizations, public airports, public housing authorities, financing authorities, public transportation systems, public employee retirement systems (PERSs), post-employment benefit plans, pension plans, public entity risk pools, external investment pools, Indian tribes, state tuition programs, and other special districts.

Interpretation

- .02 *Financial Interests* in, and other relationships with, *affiliates* of a *financial statement attest client* that is a state or local government entity may create *threats* to a *member's* compliance with the "Independence Rule" [1.200.001].
- .03 *Members* should apply the "Independence Rule" and related *interpretations* applicable to a state or local government *financial statement attest client* to their *affiliates* except as provided for in paragraph .07 of this interpretation.
- .04 Examples of circumstances or relationships that could result in the *member* consulting the *Conceptual Framework for Independence* [1.210.010] include:
- A *covered member's immediate family* is in a *key position* with a non-affiliate that includes the *financial statement attest client* in its *financial statements* and the non-affiliate provides accounting staff, shares financial information systems or establishes internal controls over financial reporting for the *financial statement attest client*.
 - The *member* is considering providing financial information system design services to a non-affiliate where the financial information system would also be used by the *financial statement attest client*.
 - A *covered member* has a *financial interest* in a non-affiliate that includes the *financial statement attest client* in its *financial statements* and the non-affiliate prepares the *financial statements* for the *financial statement attest client*.
 - The *financial statement attest client* participates in a public private partnership or joint venture that does not meet the definition of an investment in paragraph .06b of this interpretation. A *covered member* has a financial interest in an organization that is also involved with the public private partnership or joint venture.
 - A *covered member* owns utility bonds issued by a non-affiliate and the *financial statement attest client* is responsible for payment of the utility bond debt service.
 - A *covered member* owns defeased debt issued by the *financial statement attest client*. The defeased debt is not accounted for on the *financial statements* of the *financial statement attest client* and the *financial statement attest client* has funded the debt service to be paid from a bank trust account.
 - A *covered member* owns conduit debt issued by the *financial statement attest client* on behalf of a non-affiliate. The conduit debt is not accounted for on the

financial statements of the *financial statement attest client* and the debt service is paid by the non-affiliate.

- .05 When an *interpretation* of the “*Independence Rule*” is applied in a state or local government environment and the *interpretation* uses terminology that is not applicable in this environment, the *member* should use professional judgement to determine if there is an equivalent term. For example, certain *interpretations* use the phrase “officer, director, or owner of the *attest client*.” In some state or local government environments, it may be necessary for the *member* to extend these *interpretations* to officials of the *financial statement attest client* when the individual has governance responsibilities or control over financial reporting.

Terminology

- .06 The following terms are defined here solely for use with this interpretation:

- a. **Entity.** An entity is intended to be broadly defined and can include, but is not limited to funds, component units, departments, agencies, programs, organizational units, fiduciary activities, custodial activities, employee benefit plans and sub-organizational units of the preceding entities.
- b. **Investment.** An investment is a security or other asset that the *financial statement attest client* holds primarily for the purpose of income or profit and has a present service capacity based solely on its ability to generate cash or to be sold to generate cash. This includes investments and ownership of an equity interest in common stock accounted for using the equity method of accounting as provided for in GASB Codification Section 150. The following interests are not considered investments for purposes of this interpretation:
 - i. Interests obtained by a *financial statement attest client* as a result of an action by a third party, such as through a bequest or a grant, and that the entity does not intend to retain (temporary investments).
 - ii. Equity interests in joint ventures partnerships, limited liability companies, or other types of entities in which the intent of the *financial statement attest client* is to directly enhance its ability to provide governmental services
 - iii. Equity interests in component units in which the intent of the *financial statement attest client* is to directly enhance its ability to provide governmental service
 - iv. Entities that would otherwise be considered an entity as defined in item a above.

Exception

- .07 The *member* and *member's firm* may provide prohibited nonattest services to entities described under items b.ii. and b.iii. of the definition of *affiliate*, during the *period of the professional engagement* or during the period covered by the *financial statements*, provided that it is reasonable to conclude that the services do not create a self-review *threat* with respect to the *financial statement attest client* because the results of the nonattest services will not be subject to the *covered member's financial statement* attest procedures. For any other *threats* that are created by the provision of the nonattest services that are not at an *acceptable level* (in particular, those relating to management participation), the *member* should apply *safeguards* to eliminate or reduce the *threats* to an *acceptable level*.

Best Efforts

.08 A *member* must expend best efforts to obtain the information necessary to identify *affiliates* of a *financial statement attest client*. If, after expending best efforts, a *member* is unable to obtain the information to determine which entities *are affiliates of a financial statement attest client*, *threats* would be at an *acceptable level* and *independence* would not be *impaired* if the *member* does all of the following:

- a. Discusses the matter, including the potential impact on *independence*, with *those charged with governance* at the *financial statement attest client*.
- b. Documents the results of that discussion and the efforts taken to obtain the information
- c. Obtains written assurance from the *financial statement attest client* that it is unable to provide the *member* with the information necessary to identify the *affiliates* of the *financial statement attest client*.

More Than Minimal Influence Over Accounting and Financial Reporting Process

.09 The overall facts and circumstances should be considered when evaluating the level of influence the *financial statement attest client* has over the accounting or financial reporting process of *an entity* in the financial reporting entity. The targeted analysis is applied solely to the accounting and financial reporting process of the entity as opposed to the analysis of what entities are included in the financial reporting entity. Factors such as the following may assist *members* with this evaluation. The extent:

- a. of involvement the *financial statement attest client* has in preparing the *financial statements* of an entity.
- b. of operational control the *financial statement attest client* has over an entity.
- c. to which both the *financial statement attest client* and an entity have the same
 - i. accounting or finance staff
 - ii. accounting systems
 - iii. internal control over financial reporting systems
- d. to which the *financial statement attest client*
 - i. is able to direct the behaviors or actions of the governing board of the entity
 - ii. has the ability to add or remove members of the governing board of the fund or component unit
 - iii. issues or pays for the entity's debt
 - iv. finances the entity's deficits
 - v. uses or takes the entity's financial resources

.10 Whereas some factors may indicate influence, others may indicate little to no influence. Some factors may be weighted differently depending on the circumstances and the subject matter of any potential impairment. *Members* should take a substantive approach to evaluating the factors (for example, the entity exercises a right) rather than merely

considering form (for example, the *financial statement attest client* has a right that is not exercised). The consideration of these factors will require the *member* to exercise professional judgement when reaching the determination of whether more than minimal influence exists.

Material To the Financial Statement Attest Client's Financial Statements As a Whole

- .11 Determination of materiality is a matter of professional judgment. *Members* should consider both quantitative and qualitative factors when determining whether an entity *or investment* is material to a *financial statement attest client's* financial reporting entity. For purposes of this interpretation, materiality is intended to be applied at the *financial statement attest client's* financial reporting entity as a whole, rather than individual opinion units in circumstances where there may be more than one opinion unit.

Effective Date

- .12 This interpretation will be effective for engagements covering periods beginning on or after [insert date that would be 1 year after adoption]. Early implementation is allowed.

1.224.020 State and Local Government Entities (Marked)**Applicability**

This interpretation applies to state and local governmental entities. State and local governmental entities are entities whose GAAP standard setter is GASB. Examples of state and local governmental entities include general purpose governments such as states, counties, cities, towns, villages, and special purpose governments that perform limited activities. Examples of special purpose governments include, but are not limited to, cemetery districts, school districts, universities and colleges, utilities, hospitals or other health care organizations, public airports, public housing authorities, financing authorities, public transportation systems. **Introduction**

~~.01 This interpretation provides guidance on which entities' members should be independent of because the entities have a relationship to public employee retirement systems (PERs), post-employment benefit plans, pension plans, public entity risk pools, external investment pools, Indian tribes, state tuition programs, and other special districts.~~

Interpretation

~~.04.02 *Financial Interests in, and other relationships with, affiliates of a financial statement attest client* that is a state or local government entity.—*may create threats to a member's compliance with the "Independence Rule" [1.200.001].*~~

~~.03 This interpretation applies to *financial statement attest clients* that are state and local governmental entities whose basic *financial statements* include funds and component units that are required to be included in a primary government's financial reporting entity under the applicable financial reporting framework. For purposes of this interpretation, the applicable financial reporting framework is as defined in the auditing standards (for example, governmental generally accepted accounting principles [GAAP], regulatory basis, cash basis, modified cash basis).~~

~~.03 *Members* should apply the "Independence Rule" and related *interpretations* applicable to a state or local government *financial statement attest client* to their *affiliates* except as provided for in paragraph .07 of this interpretation.~~

~~.04 Examples of circumstances or relationships that could result in the *member* consulting the Conceptual Framework for Independence [1.210.010] include:~~

- ~~a. *A covered member's immediate family* is in a *key position* with a non-affiliate that includes the *financial statement attest client* in its *financial statements* and the non-affiliate provides accounting staff, shares financial information systems or establishes internal controls over financial reporting for the *financial statement attest client*.~~
- ~~b. The *member* is considering providing financial information system design services to a non-affiliate where the financial information system would also be used by the *financial statement attest client*.~~
- ~~c. *A covered member* has a *financial interest* in a non-affiliate that includes the *financial statement attest client* in its *financial statements* and the non-affiliate prepares the *financial statements* for the *financial statement attest client*.~~

- d. The financial statement attest client participates in a public private partnership or joint venture that does not meet the definition of an investment in paragraph .06b of this interpretation. A covered member has a financial interest in an organization that is also involved with the public private partnership or joint venture.
 - e. A covered member owns utility bonds issued by a non-affiliate and the financial statement attest client is responsible for payment of the utility bond debt service.
 - f. A covered member owns defeased debt issued by the financial statement attest client. The defeased debt is not accounted for on the financial statements of the financial statement attest client and the financial statement attest client has funded the debt service to be paid from a bank trust account.
 - g. A covered member owns conduit debt issued by the financial statement attest client on behalf of a non-affiliate. The conduit debt is not accounted for on the financial statements of the financial statement attest client and the debt service is paid by the non-affiliate.
- .02.05** When an *interpretation* of the “Independence Rule” [ET sec. 1.200.001] is applied in a state or local government environment and the *interpretation* uses terminology that is not applicable in this environment, the *member* should use professional judgement to determine if there is an equivalent term. ~~For example, certain interpretations~~ For example, certain interpretations use the phrase “officer, director, or owner of the *attest client*.” In some state or local government environments, it may be necessary for the ~~member to extend these interpretations~~ member to extend these interpretations to officials of the *financial statement attest client* when the individual has governance responsibilities or control over financial reporting.

Terminology

.03.06 The following terms are defined here solely for use with this interpretation:

- a. ~~The primary government is a state and local governmental~~ **Entity.** An entity that includes the following:
 - ii. ~~The financial statement attest client and all entities that are required to be included in the financial statement attest client’s financial reporting entity (that is, downstream entities) under the applicable financial reporting framework~~
 - iii. ~~The financial reporting entity (that is, upstream entity) in which the attest client’s financial statements are required to be included under the applicable financial reporting framework~~
- d. ~~State and local governmental entities are entities whose GAAP standard setter is GASB. Examples of state and local governmental entities include general purpose governments such as states, counties, cities, towns, villages, and special purpose governments that perform limited activities. Examples of special purpose governments include, but are not limited to, cemetery districts, school districts, universities and colleges, utilities, hospitals or other health care organizations, public airports, public housing authorities, financing authorities, public transportation systems, public utilities, public employee retirement systems (PERSs), post-employment benefit plans, pension plans, public entity risk pools, external investment pools, public colleges and universities, Indian tribes, state tuition programs, and other special districts.~~

~~e.a. Funds and component units are~~ intended to be broadly defined and can include, but ~~are~~ not limited to funds, component units, departments, agencies, programs, organizational units ~~administered by elected officials, grant reporting, organizational units within component units, employee benefit plans, and other~~, fiduciary ~~and~~ activities, custodial activities. ~~A component unit can also be a primary government in its standalone financial statements, employee benefit plans and sub-organizational units of the preceding entities.~~

~~f.b. Investment.~~ An investment is a security or other asset that the *financial statement attest client* holds primarily for the purpose of income or profit and has a present service capacity based solely on its ability to generate cash or to be sold to generate cash. This includes investments and ownership ~~in~~ of an equity interest in common stock accounted for using the equity method of accounting as provided for in GASB Codification Section 150. The following interests are not considered investments for purposes of this interpretation:

~~The following interests are not considered investments for purposes of this interpretation:~~

- ~~i. i.~~ Interests obtained by a ~~financial statement attest client~~ financial statement attest client as a result of an action by a third ~~party~~, such as through a bequest or a grant, and that the entity does not intend to retain (temporary investments).
- ~~ii. ii.~~ Equity interests in joint ventures partnerships, limited liability companies, or other types of entities in which the intent of the ~~financial statement attest client~~ financial statement attest client is to directly enhance its ability to provide governmental services
- ~~i.iii.~~ Equity interests in component units in which the intent of the ~~financial statement attest client~~ financial statement attest client is to directly enhance its ability to provide governmental ~~services~~ service

~~Independence of Funds and Component Units Required to Be Included in the Financial Reporting Entity (Downstream Entities) of the Financial Statement Attest Client~~

~~.02 Members should apply the "Independence Rule" [ET sec. 1.200.001] and related interpretations to all funds and component units included in the financial statement attest client's financial reporting entity in which the covered member does not make reference to another auditor's report on the fund or component unit.~~

~~.03 Members should apply the "Independence Rule" [ET sec. 1.200.001] and related interpretations to all material funds and component units included in the financial statement attest client's financial reporting entity in which the covered member makes reference to another auditor's report on the material fund or component unit, and the primary government has more than minimal influence over the accounting or financial reporting process over that fund or component unit.~~

~~.04 Members should apply the "Independence Rule" [ET sec. 1.200.001] and related interpretations to all material funds and component units excluded from the financial statement attest client's~~

~~financial reporting entity but required to be included under the applicable framework when the primary government has more than minimal influence over the accounting or financial reporting process over those funds or component units.~~

- ~~iv. In the situations identified in paragraphs .06–.07 of this interpretation, the Entities that would otherwise be considered an entity as defined in item a above.~~

Exception

~~.04.07 The member and member's firm may provide nonattest services that impair independence prohibited nonattest services to entities described under items b.ii. and b.iii. of the definition of affiliate, during the period of the professional engagement or during the period covered by the financial statements, provided that it is reasonable to conclude that the services do not create a self-review threat with respect to the financial statement attest client because the results of the nonattest services will not be subject to the covered member's financial statement attest procedures. For any other threats that are created by the provision of the nonattest services that are not at an acceptable level (in particular, those relating to management participation), the membermember should apply safeguards to eliminate or reduce the threats to an acceptable level to an acceptable level.~~

Independence When the Financial Statement Attest Client Is Required to Be Included in Another Financial Reporting Entity (Upstream Entity)

~~—When a material fund or component unit is a financial statement attest client and is required to be included in another financial reporting entity that is not a financial statement attest client, members should use the “Conceptual Framework for Independence” interpretation [ET sec. 1.210.010] to evaluate relationships and circumstances that a member has with a primary government that exerts more than minimal influence over the accounting or financial reporting process of the financial statement attest client.~~

Other Funds, Component Units, or Activities

~~—For funds, component units, or activities not specified in paragraphs .05–.09 of this interpretation, members should apply the “Conceptual Framework for Independence” interpretation [ET sec. 1.210.010] if the member knows or has reason to believe that a relationship or circumstance exists with the entity that would create threats to independence.~~

Investments

~~—Members should apply the “Independence Rule” [ET sec. 1.200.001] and related interpretations to an entity in which the financial statement attest client has the following:~~

- ~~—A controlling investment that is not de minimis to the financial statement attest client as a whole. De minimis amounts are dollar amounts that in the member's professional judgement are clearly inconsequential to the financial statement attest client as a whole.~~
- ~~—An investment that gives the financial statement attest client significant influence over the entity and that is material to the financial statement attest client as a whole.~~

~~—Members should use their professional judgement to determine if control or significant influence exists. Members should consider using the definitions for control [ET section 0.400.10] and significant influence [ET section 0.400.45], along with any applicable GASB guidance.~~

Best Efforts

~~.05.08~~ A *member* must expend best efforts to obtain the information necessary to identify ~~these investments~~ affiliates of a financial statement attest client. If, after expending best efforts, a ~~member-member~~ is unable to obtain the information to determine ~~the investments of the financial statement attest client, which entities are affiliates of a financial statement attest client,~~ *threats* would be at an *acceptable level* and *independence* would not be *impaired* if the ~~member-member~~ does all of the following:

- a. Discusses the matter, including the potential impact on ~~independence, independence,~~ with *those charged with governance* at the financial statement attest client.
- ~~b. Documents the results of that discussion and the efforts taken to obtain the information~~
~~b.a. Documents the results of that discussion and the efforts taken to obtain the information~~
- c. Obtains written assurance from the ~~financial statement attest client~~ financial statement attest client that it is unable to provide the ~~member-member~~ with the information necessary to identify the ~~investments~~ affiliates of the ~~financial statement attest client~~ financial statement attest client.

Determination of Whether the Primary Government of the Financial Reporting Entity Has More Than Minimal Influence Over Funds or Component Units **Accounting and Financial Reporting Process**

~~.09~~ There is a rebuttable presumption that ~~The overall facts and circumstances should be considered when evaluating the level of influence the primary government has more than minimal influence~~ financial statement attest client has over the accounting or financial reporting process of a fund or component unit. To rebut this presumption, ~~an entity in the financial reporting entity. The targeted analysis is applied solely to the accounting and financial reporting process of the entity as opposed to the analysis of what entities are included in the financial reporting entity. Factors such as the following may assist members can consider factors, such as the following, that in the member's professional judgment demonstrate that the primary government with this evaluation. The extent:~~

~~.05~~ of involvement the financial statement attest client has only minimal influence:

- ~~b.a. Primary government does not prepare in preparing the financial statements for the fund or component unit of an entity.~~
- ~~a. Accounting or finance staff of the fund or component unit is not the same staff as the primary government.~~
- ~~b. Fund or component unit does not of operational control the financial statement attest client has over an entity.~~
- c. to which both the financial statement attest client and an entity have the same
 - i. accounting or finance staff

- ~~c.ii. accounting systems as the primary government.~~
- ~~d.iii. Fund or component unit does not have the same internal control over financial reporting systems as the primary government.~~
- ~~b. Primary government does not have a significant level of operational control over the fund or component unit.~~
- ~~d. Primary government does not to which the financial statement attest client~~
 - ~~e.i. is able to direct the behaviors or actions of the governing board of the fund or component unit.~~
 - ~~f.ii. Primary government does not have~~ has the ability to add or remove members of the governing board of the fund or component unit.
- ~~Primary government does not exert influence that results from issues or pays for the following:~~
 - ~~ii.iii. The primary government's issuance or full or partial payment of the fund's or component unit's~~ entity's debt
 - ~~iii.iv. The primary government's financing of some or all of~~ finances the fund's or component unit's entity's deficits
 - ~~iv.v. The primary government's actions to use or take the fund's or component unit's~~ uses or takes the entity's financial resources

.10 Whereas some factors may indicate influence, others may indicate little to no influence. Some factors may be weighted differently depending on the circumstances and the subject matter of any potential impairment. The overall facts and circumstances Members should be considered when using take a substantive approach to evaluating the factors in paragraph 14 to evaluate (for example, the entity exercises a right) rather than merely considering form (for example, the financial statement attest client has a right that is not exercised). The consideration of these factors will require the member to exercise professional judgement when reaching the determination of whether a primary government has more than minimal influence over the accounting exists.

Material To the Financial Statement Attest Client's Financial Statements As a Whole

~~06.11~~ Determination of materiality is a matter of professional judgment. *Members* should consider both quantitative and qualitative factors when determining whether an entity or investment is material to a financial statement attest client's financial reporting process of a fund or component entity. For purposes of this interpretation, materiality is intended to be applied at the financial statement attest client's financial reporting entity as a whole, rather than individual opinion units in circumstances where there may be more than one opinion unit. ~~Whereas some factors may indicate influence, others may indicate little to no influence. Some factors may be weighted differently depending on the circumstances and the subject~~

~~matter of any potential impairment. Thus, the consideration of these factors runs along a spectrum. The following illustrates one possible spectrum:~~

Less Influence	More Influence
a. Fund or component unit prepares its own financial statements.	A. Primary government prepares the fund or component unit's financial statements.
b. Accounting staff is separate from primary government staff.	B. Accounting staff is part of primary government finance staff.
c. Separate accounting system exists.	C. Same accounting system as primary government exists, with no fund or component unit subsystems that feed the primary government system.
d. Separate internal control over financial reporting exists.	D. Same internal control over financial reporting as primary government exists.
e. Primary government has no operational control.	E. Primary government has strong operational control.
f. Strong independent governing board exists.	F. Same governing body as primary government exists, with high level of involvement.
g. There is no level of financial dependence on primary government.	G. There is a high level of financial dependence (such as operating loss subsidies and payment for certain costs).
h. Board members are not otherwise associated with the primary government.	H. Board members are associated with the primary government, such as ex officio members that are employed by the primary government.
i. Fund or component unit financial statements is incorporated into primary government without modification (that is, either fund level or government wide level statements of primary government).	I. Fund component unit financial statements need adjustments or reclassifications (for example, significant adjustments made by primary government are necessary to include balances or notes to statements modified for differing accounting methods or reporting alternatives).

Effective Date

.12 This interpretation will be effective for engagements covering periods beginning on or after ~~June 15, 2019.~~[insert date that would be 1 year after adoption]. Early implementation is allowed.

0.400 Definitions**.02 Affiliate**

- a. ***When applying the Client Affiliate interpretation (1.224.010)*** The following entities are affiliates of a *financial statement attest client*:
- i. An entity (for example, subsidiary, partnership, or limited liability company [LLC]) that a *financial statement attest client* can *control*.
 - ii. An entity in which a *financial statement attest client* or an entity *controlled* by the *financial statement attest client* has a *direct financial interest* that gives the *financial statement attest client* *significant influence* over such entity and that is material to the *financial statement attest client*.
 - iii. An entity (for example, parent, partnership, or LLC) that *controls* a *financial statement attest client* when the *financial statement attest client* is material to such entity.
 - iv. An entity with a *direct financial interest* in the *financial statement attest client* when that entity has *significant influence* over the *financial statement attest client*, and the interest in the *financial statement attest client* is material to such entity.
 - v. A sister entity of a *financial statement attest client* if the *financial statement attest client* and sister entity are each material to the entity that *controls* both.
 - vi. A trustee that is deemed to *control* a trust *financial statement attest client* that is not an investment company.
 - vii. The sponsor of a single employer employee benefit plan *financial statement attest client*.
 - viii. Any entity, such as a union, participating employer, or a group association of employers, that has *significant influence* over a multiemployer employee benefit plan *financial statement attest client* and the plan is material to such entity.
 - ix. The participating employer that is the plan administrator of a multiple employer employee benefit plan *financial statement attest client*.
 - x. A single or multiple employer employee benefit plan sponsored by either a *financial statement attest client* or an entity *controlled* by the *financial statement attest client*. All participating employers of a multiple employer employee benefit plan are considered sponsors of the plan.
 - xi. A multiemployer employee benefit plan when a *financial statement attest client* or entity *controlled* by the *financial statement attest client* has *significant influence* over the plan and the plan is material to the *financial statement attest client*.
 - xii. An investment adviser, a general partner, or a trustee of an investment company *financial statement attest client* (fund) if the fund is material to the investment adviser, general partner, or trustee that is deemed to have either *control* or *significant influence* over the fund. When considering materiality, *members* should consider investments in, and fees received from, the fund.
- b. ***When applying the State and Local Government Entities interpretation [1.224.020]*** *an entity is an affiliate of a state or local government financial statement attest client in all of the following situations.*

- i. the entity is included in the **financial statement attest client's** financial statements and the **covered member** does not make reference to another auditor's report on the entity;
- ii. the entity is included in the **financial statement attest client's** financial statements and the **covered member** makes reference to another auditor's report on the entity, and
 - 1. the entity is material to the **financial statement attest client's** financial statements as a whole; and
 - 2. the **financial statement attest client** has more than minimal influence over the accounting or financial reporting process over the entity. There is a rebuttable presumption that the **financial statement attest client** has more than minimal influence over the accounting or financial reporting process of funds and blended component units.
- iii. the entity is a material excluded entity and the **financial statement attest client** has more than minimal influence over the entity's accounting or financial reporting process. A material excluded entity is an entity that is required to be included in the financial statements of the **financial statement attest client** but is excluded, and is material to the **financial statement attest client's** financial statements as a whole. There is a rebuttable presumption that the **financial statement attest client** has more than minimal influence over the accounting or financial reporting process of funds and blended component units.
- iv. the **financial statement attest client** or an affiliate under item b. i. of this definition has an investment in an investee that either
 - 1. is not trivial and clearly inconsequential to the **financial statement attest client's** financial statements as a whole and gives the **financial statement attest client control** over the investee or
 - 2. is material to the **financial statement attest client's financial statements** as a whole and gives the **financial statement attest client significant influence** over the investee.

Nonauthoritative questions and answers related to the application of the independence rules to affiliates of employee benefit plans are available at www.aicpa.org/interestareas/professionalethics/resources/tools/downloadabledocuments/faqs-application-independence-rules-affiliates-of-employee-benefit-plans.pdf.

Agenda Item 5D

Impact Analysis of Proposed Revisions to “Entities Included in State and Local Government Financial Statements” Interpretation

Color Key

Light Green: Clarifying change.

Yellow: Added guidance to the interpretation.

Red: Change in position based upon feedback.

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force’s Conclusion Regarding Change to The Revised Proposal
GASB Terms			
A. Certain terminology used in the extant interpretation is specifically defined by the Governmental Accounting Standards Board (GASB)	Some of the terminology used was in the proposed interpretation was GASB terminology but defined differently than GASB.	The proposed interpretation used the GASB term primary government but defined it differently than the GASB does so that the users of the interpretation would realize they need to look both up and downstream.	The change from the initial exposure draft was to respond to commenters request that GASB terms that had different definitions than GASB not be used because doing so was confusing. To respond to this concern, GASB terms were eliminated and replaced by more general terms such as “affiliate” and “entity”.
Affiliates (Downstream Entities)			
B. Members need to remain independent of funds and component units that are included in the financial statement attest client’s financial reporting entity in which the covered member does not make reference to another auditor’s report on a fund or component unit. <i>(Refer to paragraph .04 of the extant interpretation.)</i>	The requirement is the same under the proposed interpretation. <i>(Refer to paragraph .05 in the proposed interpretation.)</i>	Not applicable.	The requirement is the same as the extant and the initial exposure draft but instead of in the interpretation, it has been moved to the definition of affiliate found in paragraph .02 of ET 0.400. <i>(The requirement is now found in the proposed new affiliate definition under 0.400.02 item b. i.)</i>
C. Members do not need to remain independent of funds and component units that are included in the financial reporting entity of the financial statement attest client	When making reference to another auditor’s report, members will need to remain independent of material funds and	The Professional Ethics Executive Committee (PEEC) continues to believe that making reference to another auditor’s report will	The requirement is the same as the initial exposure draft but instead of in the interpretation, it has been moved to the definition of affiliate found in paragraph .02 of ET 0.400.

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force's Conclusion Regarding Change to The Revised Proposal
<p>when the member makes reference to another auditor's report. <i>(Refer to paragraph .04 of the extant interpretation.)</i></p>	<p>component units that are included in the financial reporting entity of the financial statement attest client when the primary government has more than minimal influence over the accounting or financial reporting process of the fund or component unit. <i>(Refer to provision paragraph .06 of the proposed interpretation.)</i></p>	<p>not always reduce threats to an acceptable level when the fund or component unit is material to the financial reporting entity, and the primary government has more than minimal influence over the accounting or financial reporting process of the fund or component unit.</p>	<p><i>(The requirement is now found in the affiliate definition under 0.400.02 item b. ii.)</i></p>
<p>D. The extant interpretation does not provide any independence guidance related to funds and component units that are excluded from the financial reporting entity but are required to be included under the applicable framework (for example, generally accepted accounting principles, regulatory, or cash basis).</p>	<p>Members should apply the independence rule and related interpretations to material funds and component units that are excluded from the financial reporting entity but required to be included under the applicable framework if the primary government has more than minimal influence over its accounting or financial reporting process. <i>(Refer to provision paragraph .07 of the proposed interpretation.)</i></p>	<p>It is not uncommon for a primary government to exclude a fund or component unit from the financial reporting entity for a variety of reasons, such as unavailability of a component unit's audited financial statements; therefore, PEEC incorporated guidance in its proposed interpretation related to a material fund or component unit that is excluded from the financial statement attest client's financial reporting entity but is required under the applicable framework to be included.</p>	<p>The requirement is the same as the initial exposure draft but instead of in the interpretation, it has been moved to the definition of affiliate found in paragraph .02 of ET 0.400.</p> <p><i>(The requirement is now found in the affiliate definition under 0.400.02 item b. iii.)</i></p>
<p>E. The extent interpretation does not specify how far downstream the member needs to continue looking when the independence rules needs to be applied.</p>	<p>N/A</p>	<p>N/A</p>	<p>Commenters asked for clarification regarding how far downstream they need to look. The Task Force believes the use of criteria in the definition of affiliate</p>

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force's Conclusion Regarding Change to The Revised Proposal
			<p>makes this clear and is not proposing any revisions.</p> <p><i>(The affiliate definition is found under 0.400.02 item b)</i></p>
Upstream Entities (Required Evaluation of Certain Relationships with Certain Upstream Entities)			
<p>F. Under the extant interpretation, members do not need to remain independent of entities that the member does not audit (for example, upstream entity), except covered members and their immediate family, and close relatives may not have a key position within the primary government. <i>(Refer to paragraphs .07–.08 of the extant interpretation.)</i></p>	<p>When certain upstream entities have relationships or circumstance that would create significant threats if a covered member was involved, members would be required to identify whether any covered members have such and evaluate the relationships and circumstances using the “Conceptual Framework for Independence” interpretation.</p> <p><i>(Refer to paragraph .09 of the proposed interpretation.)</i></p>	<p>PEEC believes that there could be circumstances in which a member could have a relationship that creates a threat(s) that is (are) not at an acceptable level.</p> <p>Furthermore, PEEC believes these situations are more likely to occur when a material fund or component unit is a financial statement attest client and is required to be included in another financial reporting entity and the primary government of that financial reporting entity can exert more than minimal influence over the accounting or financial reporting process of the financial statement attest client.</p>	<p>Requirement was eliminated. Examples of situations involving upstream entities that aren't affiliates where the Conceptual Framework for Independence (CFI) may need to be consulted were added.</p> <p><i>(The examples of situations involving upstream entities that aren't affiliates where the CFI may need to be consulted were added to paragraph .04.)</i></p>
<p>G. The extant interpretation only extends its limited independence restrictions to the primary government and does not address whether these restrictions could continue further upstream.</p>	N/A	N/A	<p>Commenters asked for clarification regarding how far upstream they need to look. Requirement was eliminated. Examples of situations involving upstream entities that aren't affiliates where the Conceptual Framework for Independence (CFI) may need to be consulted were added.</p>

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force's Conclusion Regarding Change to The Revised Proposal
			<div></div> (The examples of situations involving upstream entities that aren't affiliates where the CFI may need to be consulted was added to paragraph .04.)
Other Funds, Component Units, or Activities That Are Not Considered Affiliates or Upstream Entities (Possible Evaluation of Relationships Using Conceptual Framework)			
H. The extant interpretation does not have a reminder that members should consider the " Conceptual Framework for Independence interpretation " if they encountered situations not addressed by the extant interpretation that result in significant threats. requirement to evaluate threats to independence created by relationships or circumstances the member has with funds, component units, or activities that aren't covered by the interpretation.	If a member knows or becomes aware of relationships or circumstances with a fund, component unit, or activity that is not identified in rows A–E that would create threats to independence, the member would be required to evaluate the matter using the " Conceptual Framework for Independence interpretation ". (Refer to paragraph .10 of the proposed interpretation.)	Member may encounter circumstances or relationships with certain entities that could give rise to threats that are not at an acceptable level.	<div></div> Requirement was eliminated. Examples of situations involving upstream entities that aren't affiliates where the Conceptual Framework for Independence (CFI) may need to be consulted were added. (The examples of situations involving upstream entities that aren't affiliates where the CFI may need to be consulted was added to paragraph .04.)
Investments			
I. Under the extant interpretation, there is no guidance regarding when members should extend the "Independence Rule" and related interpretations to investments held by a state or local entity; therefore, members would use the Conceptual Framework for Independence interpretation when evaluation is required.	The proposed interpretation provides that members should apply the independence rules and related interpretations to certain entities that the financial statement attest client invests in.	The independence rules should be extended to: <ul style="list-style-type: none"> entities in which the financial statement attest client can control the entity and the investment in that entity is not de minimis to the financial statement attest client's 	<div></div> Some commenters thought it was unclear if they should only look downstream to investments the client and its affiliates held or if they should also look upstream to investments held by upstream entities. Affiliate iv was edited to clarify that investments of only the financial statement attest client and affiliate i. needed to be considered.

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force's Conclusion Regarding Change to The Revised Proposal
	<i>(Refer to paragraph .11 of the proposed interpretation.)</i>	<p>financial reporting entity.</p> <ul style="list-style-type: none"> include circumstances when a financial statement attest client has significant influence over an entity in which it has a material investment. <p>Furthermore, a de minimis threshold is applied because of the operational problems associated with determining which entities are controlled by a financial statement attest client when those entities are insignificant. Unlike in the commercial sector, state and local governments may not have systems in place to track this information, nor do they have regulatory requirements that might be applicable to commercial entities to monitor investment relationships.</p>	<p>The term “de minimis” was changed to “trivial and clearly inconsequential”. Instead of appearing in the interpretation, it has been moved to the definition of affiliate found in paragraph .02 of ET 0.400.</p> <p><i>(The requirement is now found in the affiliate definition under 0.400.02 item b. iv.)</i></p>
Not Subject to Attest Procedures Exception			
The extant interpretation does not have any exceptions for the provision of prohibited nonattest services.	Members may provide nonattest services that would impair independence to funds and component units identified in preceding rows B and C, provided it is reasonable to conclude that the services do not create a	The exception was incorporated so that the proposed interpretation would be conceptually consistent with the underlying principles of the “Client Affiliates” interpretation because	The requirement is the same as the initial exposure draft but instead of referring to the nonattest services as services that impair independence, these services are referred to as prohibited nonattest services which is consistent with the commercial affiliate guidance.

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force's Conclusion Regarding Change to The Revised Proposal
	self-review threat with respect to the financial statement attest client because the results of the nonattest services will not be subject to the covered member's financial statement attest procedures. For any other threats that are created by the provision of the nonattest services that are not at an acceptable level (particularly those relating to management participation), the member should apply safeguards to eliminate or reduce the threats to an acceptable level. <i>(Refer to paragraph .08 of the proposed interpretation.)</i>	PEEC did not identify a compelling reason to differ from those principles.	<i>(The requirement continues to be found in paragraph .07 of the revised interpretation.)</i>
Best Efforts Provision			
J. Under the extant interpretation, there is no guidance regarding best efforts.	Under the proposed interpretation, the best efforts provision was only applied to the identification of investments. <i>(Refer to paragraph .13 of the proposed interpretation.)</i>	Not specified in the explanation that accompanied the exposure draft.	The change from the initial exposure draft is that best efforts can now be applied to all affiliates not just to investments.. <i>(The requirement is now found in paragraph .08 of the revised interpretation.)</i>
Material to Financial Statements as A Whole			
K. Under the extant interpretation there is no materiality threshold.	Under the proposed interpretation, certain provisions are limited to material funds and component units.	Although .11 specifies that "An investment that gives the financial statement attest client significant influence over the entity and that is material to the financial	Application guidance was added to the interpretation to respond to comments on the ED.

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force's Conclusion Regarding Change to The Revised Proposal
	<i>(Refer to paragraph .06, .07, .09 and .11 of the proposed interpretation.)</i>	statement attest client as a whole”, the explanation to the exposure draft contains more clarification regarding how to measure materiality.	<i>(The requirement is now found in paragraph .11 of the revised interpretation.)</i>
Primary Government Has More Than Minimal Influence Over Accounting and Reporting Process			
L. The more than minimal influence provision is not used in the extant interpretation.	Under the proposed interpretation, application guidance was included for determining whether more than minimal influence existed. However, that application guidance did not specifically mention that this analysis is applied solely to the accounting and financial reporting process of the fund or component unit as opposed to the analysis that a member would perform to determine what entities are included in the financial reporting entity. <i>(Refer to paragraph .14 and .15 of the proposed interpretation.)</i>	PEEC believes the control and significant influence concepts used in the commercial affiliate guidance are not workable in the SLG environment since the SLG environment uses a financial accountability concept instead. PEEC believes that the concept of whether the primary government has more than minimal influence over the accounting and financial reporting process of the fund or component unit is the appropriate concept to use to determine whether independence should be applied to funds and component units that are required to be included in the financial reporting entity under the applicable framework	Added application guidance on applying the MTMI solely to the accounting and financial reporting process of the fund or component unit <i>(The requirement is now found in paragraphs .09-.10 of the revised interpretation.)</i>
M. The more than minimal influence provision is not used in the extant interpretation.	Under the proposed interpretation, application guidance in the form of examples was included to aid users in determining whether more than minimal influence existed.	PEEC believed including examples would be helpful to members when applying the revised interpretation.	The change from the initial exposure draft was to eliminate the redundancies in the examples. <i>(The requirement is now found in paragraphs .09-.10 of the revised interpretation.)</i>

Extant Interpretation	Additional Independence Requirements Under the Initial Exposure Draft	Rationale for The Exposed Change in The Initial Exposure Draft	Task Force's Conclusion Regarding Change to The Revised Proposal
	<i>(Refer to paragraph .14 and .15 of the proposed interpretation.)</i>		
N. Under the extant interpretation there is no rebuttable presumption.	<p>Under the proposed interpretation, the rebuttable presumption that the primary government has more than minimal influence over the accounting and reporting process was applied to all funds and component units.</p> <p><i>(Refer to paragraph .14 of the proposed interpretation.)</i></p>	PEEC believes there is a presumption that the primary government has more than minimal influence over its fund's and component unit's accounting or financial reporting process, it also believes that this presumption will often be rebutted depending upon the specific facts and circumstances.	<p>The only change to the rebuttable presumption from the initial exposure draft is that the rebuttable presumption was eliminated for discretely presented component unitsⁱ.</p> <p><i>(The requirement is now found in the definition of an affiliate 0.400.02bii.2. and 3.iii.)</i></p>
GASB Terms			
O. Certain terminology used in the extant interpretation is specifically defined by the Governmental Accounting Standards Board (GASB)	<p>Some of the terminology used was in the proposed interpretation was GASB terminology but defined differently than GASB.</p> <p><i>(Refer to items a, b and c in paragraph .04 of the proposed interpretation.)</i></p>	The proposed interpretation used the GASB term primary government but defined it differently than the GASB does so that the users of the interpretation would realize they need to look both up and downstream.	<p>The change from the initial exposure draft was to respond to commenters request that GASB terms that had different definitions than GASB not be used because doing so was confusing. To respond to this concern, GASB terms were eliminated and replaced by more general terms such as "affiliate" and "entity".</p> <p><i>(The requirement is now found in the affiliate definition under 0.400.02. and item a in paragraph .06 of the interpretation)</i></p>

ⁱ About a third of the commenters express concerns with the presumption that primary governments have more than minimal influence over funds and component units. The Committee included the rebuttable presumption in the exposure draft with discretely presented component units in mind. Since these entities are legally separate, the Committee believed that the rebuttable presumption would be operative more often when a discretely presented component unit was involved as opposed to when a fund or blended component

unit was involved. The Committee believed drafting the rebuttable presumption this way could result in members having to do less “work” since presumably the member wouldn’t go through the evaluation unless the member suspected factors existed that would lend to concluding that the primary government might not have more than minimal influence. However, given the concerns expressed by commenters, the Committee acknowledges that perhaps its desire to make the proposal easier to apply was not the best approach. As such, the Committee decided that the rebuttable presumption that the primary government has more than minimal influence over the accounting or financial reporting process should only cover funds and blended component units. The Committee believes that the limitation of the rebuttable presumption to funds and blended component units appropriately considers the reduced likelihood of threats to independence inherent in discretely presented component units. Members will still need to consider the impact of more than minimal influence by a primary government over a discretely presented component unit, but they do not need to rebut a presumption.

**Professional Ethics Executive Committee
External Directors Task Force**

Task Force Members

Bill McKeown (Chair), Bill Mann, Coalter Baker, David East, Brian Lynch, Chris Cahill
Staff: Brandon Mercer, CPA CGMA

Task Force Charge

The Task Force's charge is to evaluate the need to issue guidance for members in the application of the Independence Rule [1.200.001] to external members of the member's firm's board of directors or similar body.

Reason for Agenda Item

The purpose of this agenda item is to discuss the Task Force's direction and obtain the Committee's feedback regarding several discussion points as noted in this agenda item. The Task Force will utilize the feedback to prepare formal or informal guidance for consideration at the next Committee meeting.

Background

Large public accounting firms recruit external board members to improve corporate governance and the reliability of financial reporting as well as to enhance public trust. The primary question put to the Committee, and being considered by the Task Force, is the application of the Independence Rule [1.200.001] to these external board members with respect to attest clients of the firm, and whether guidance should be included in the form of a frequently asked question (FAQ) or other informal guidance.

Summary of IssuesBoard Members' Covered Member Status

In general, the Independence Rule and its interpretations apply to either covered members or all partners and professional employees of the firm, depending on the specific interpretation. Under the extant AICPA Code, a board member that is not a partner or professional employee of the firm may be considered a covered member under the definition below:

.12 Covered member. All of the following:

- a. an individual on the attest engagement team.
- b.** an individual in a position to influence the attest engagement.
- c. a partner, partner equivalent, or manager who provides 10 or more hours of nonattest services to the attest client within any fiscal year. Designation as covered member ends on the later of (i) the date that the firm signs the report on the financial statements for the fiscal year during which those services were

provided or (ii) the date he or she no longer expects to provide 10 or more hours of nonattest services to the attest client on a recurring basis.

d. a partner or partner equivalent in the office in which the lead attest engagement partner or partner equivalent primarily practices in connection with the attest engagement.

e. the firm, including the firm's employee benefit plans.

f. an entity whose operating, financial, or accounting policies can be controlled by any of the individuals or entities described in items a–e or two or more such individuals or entities if they act together. [Prior reference: paragraph .07 of ET section 92]

Specifically, the individual may be considered to be an *individual in a position to influence the attest engagement*, which is defined as one who:

- a. evaluates the performance or recommends the compensation of the *attest engagement partner*;
- b. directly supervises or manages the *attest engagement partner*, including all successively senior levels above that individual through the *firm's* chief executive;
- c. consults with the *attest engagement team* regarding technical or industry-related issues specific to the *attest engagement*; or
- d. participates in or oversees, at all successively senior levels, quality control activities, including internal monitoring, with respect to the specific *attest engagement*.

It should be noted that any "entity whose operating, financial, or accounting policies can be controlled" by a covered member or "two or more such individuals or entities if they act together" would also be considered a covered member, and would be subject to the "Independence Rule" [1.200.001]. For example, if a covered member owned a separate bookkeeping company that provided bookkeeping services to an attest client with respect to which he/she is a covered member, the separate bookkeeping business may be required to comply with the "Nonattest Services" interpretation [1.295] with respect to the bookkeeping activities.

In addition, immediate family members of the covered member would be subject to the requirements unless specifically exempt by the "Immediate Family Members" interpretation [1.270.010] of the "Independence Rule" [1.200.001].

Questions for PEEC:

Does the Committee agree with an approach that considers whether external members of a firm's board members may be considered to be covered members as individuals in a position to influence the attest engagement, and thus subject to the Independence Rule and interpretations as a covered member?

Does PEEC agree that separate entities or businesses controlled by the board member may be subject to the Code, if the board member is considered a covered member?

Does the Committee believe any safeguards, such as recusal from the board matters related to the attest client, or from activities noted in a-d above, would mitigate any threats created with respect to the attest client?

Should external members of a firm's board of directors or similar body be subject to the basic independence requirements applicable to all partners and professional employees of a firm?

Does the Committee agree, based upon its discussion, that it is not necessary to revise the AICPA Code, but that guidance should be provided as a supplement, potentially in the [Plain English Guide to Independence](#) or the [General Ethics Questions FAQ](#) documents on the Division's website?

Effective Date

N/A

Action Needed

The Task Force requests PEEC discuss the preliminary direction of the Task Force as noted above, and provide feedback. The Task Force will report on its progress at the February 2018 PEEC meeting.

Communication Plan

Communications plan will be formulated based upon the guidance issued, if any.

Materials Presented

N/A

**AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS
DIVISION OF PROFESSIONAL ETHICS
PROFESSIONAL ETHICS EXECUTIVE COMMITTEE
OPEN MEETING MINUTES
August 8, 2018**

The Professional Ethics Executive Committee (Committee) held a duly called meeting on August 8-9, 2018 at the AICPA offices in New York, NY. The meeting convened at 9:00 a.m. and concluded at 5:00 p.m. on August 8, 2018. The meeting reconvened at 8:30 a.m. on August 9, 2018 and concluded at 9:00 a.m. on August 9, 2018.

<u>Attendance:</u> Samuel L. Burke, Chair Coalter Baker Carlos Barrera Stanley Berman Chris Cahill Tom Campbell *Robert E. Denham Anna Dourdourekas Brian S. Lynch *Greg Guin *participated by phone	William Darrol Mann *Steven Reed James Smolinski *Shelly Van Dyne Lisa Snyder Kelly Hunter Stephanie Saunders <u>Not in attendance:</u> William McKeown Sharon Jensen Martin Levin
<u>Staff:</u> James Brackens, VP - Ethics & Practice Quality Sue Coffey, EVP – Public Practice Toni Lee-Andrews, Director Ellen Gorla, Associate Director Brandon Mercer, Senior Manager *participated by phone	*April Sherman, Manager *Shannon Ziemba, Manager *James West, Manager *Michele Craig, Manager *Jennifer Kappler, Manager *Jennifer Clayton, Senior Manager *John Wiley, Manager *Melissa Powell, Manager *Henry Grzes, Lead Manager – Tax Practice & Ethics
<u>Guests:</u> Jeff Lewis, Chair, Independence/Behavioral Standards Subcommittee Ian Benjamin, Chair, Technical Standards Subcommittee Nancy Miller, KPMG Kimberly Kuhl, KPMG Elaine Cahoon, KPMG Debra Hahn, Grant Thornton Lori West, Grant Thornton Jason Evans, BDO Kelly Hnatt, External Counsel Dan Dustin, NASBA	

Catherine Allen, Audit Conduct

*David East, PwC

Sonia Araujo, PwC

Paula Tookey, Deloitte

*George Dietz, PwC

Jennifer Kary, Crowe Horwath

*Vassilios Karapanos, SEC

*Lynette Linder, Connecticut Society of CPAs

*Dan Nugent

*Leise Faircloth

*Brian Dayes, Michigan Institute of CPAs

*Lisa Brown, Ohio Society of CPAs

*Pam Hill, Missouri Society of CPAs

*Jessica Mytrohovich, Georgia Society of CPAs

Kari Hipsak

*Dennis Bushnell

*TeriAnn Kruse

*Flo Ostrum

*Sharon Elston

*Matt Ryan

*Laura Hyland

*Heather Acker

*Gary Zeune (Day 2 only)

*Participated via phone

1. **Welcome and Introductions**

Mr. Burke welcomed the Committee.

2. **Leases**

Ms. Snyder led the discussion of the Task Force's proposed draft for possible adoption. Ms., Snyder noted that she and staff held a call with a task force member after the agenda was distributed and suggested additional revisions, which were presented on screen for meeting participants. PEEC discussed the application of safeguards in paragraph .02, specifically; paragraph .02b stipulates that, when entering the lease, all amounts must be paid in compliance with the lease terms. However, Mr. Cahill noted that this safeguard would not be operational at lease entry, and the proposal is not sufficiently clear in that regard. The Committee revised paragraph .02 by deleting the safeguard from the lettered list of safeguards, and copying the language from paragraph .03 regarding payment compliance. In addition, the change would note that the safeguard applied after entering the lease and on an ongoing basis. This revision resolved the issue of clarity regarding when the payment safeguard applies. PEEC also agreed that the lead-in to paragraph .02 should continue to only reference a member who enters into a lease and not a member who has a lease. Paragraph .03 would contain a reference to a member who has a lease.

A second aspect to the revisions were made to paragraph .03, as PEEC ultimately agreed that paragraph .03 should address any leases that were in compliance with .02 at entry, but where there has been a change in the circumstances (e.g. the lease subsequently becomes material after being immaterial at entry) that creates threats to independence. PEEC's agreed by a straw poll of 17-1 that if a lease becomes material subsequent to entering the lease, that the Conceptual Framework should be applied to the lease, rather than being automatically impaired.

PEEC agreed that paragraph .04 did not add anything that was not already in the Conceptual Framework approach, and added confusion. As a result, PEEC agreed that paragraph .04 should be removed and that the interpretation should only specifically address leases of the specific covered members noted in paragraphs .02 and .03. The AICPA Code and application of the Independence Rule would require the member to use the Conceptual Framework in situations that are not specifically addressed in the Independence Rule and its interpretations, and would apply to all other leases without the interpretation specifically addressing them.

PEEC discussed the proposed paragraph regarding leases between covered members specified in .02 with affiliates of the attest client, and agreed with the approach that such leases should be allowed provided any threats are at an acceptable level, and that the covered member should use the Conceptual Framework if any threats are not at an acceptable level. Minor revisions to the Task Force's proposed language were made to accurately reflect this position.

Given the number of revisions made during the meeting and time constraints, there was no motion made for adoption; the Task Force agreed that it would finalize the revisions suggested by PEEC and distribute before bringing a potential draft for adoption to the November 2018 PEEC meeting.

3. Disclosing Information in Connection with a Quality Review

Mr. Mercer updated the Committee on the status of the exposure draft, which had a comment deadline of August 20, 2018. Mr. Mercer noted that several comment letters had come in but more were expected before the upcoming deadline. Mr. Mercer noted that there were no significant issues raised in the comment letters received to date, and that a draft for possible adoption should be ready for the November PEEC meeting.

4. Minutes of May 2018 PEEC Open Meeting

It was moved, seconded and unanimously agreed to adopt the minutes from the May 2018 open meeting.

5. Staff Augmentation

Ms. Snyder presented the agenda item to the Committee. Ms. Snyder noted that the Task Force presented a draft proposal at the May 2018 PEEC meeting and held a conference call in July 2018 to consider the feedback received and make conforming revisions to the proposal. The Task Force requested that PEEC consider the revisions made by the Task Force and approve exposure of the proposal.

Paragraph .02

Ms. Snyder noted that in paragraph .02, the proposal applies the same standard for skill, knowledge, and experience that is applied to non-attest services under the Non-attest Services interpretation [1.295]. The Task Force agreed, but suggested adding the words “by the augmented staff” to parts of the passage to clarify that the member is under the supervision of the client. Additionally, the Task Force suggested clarifying that the services should be “not otherwise prohibited” rather than “otherwise permitted” under Section 1.295. PEEC agreed with the suggested revisions.

.02 Threats to compliance with the “Independence Rule” [1.200.001] would be at an acceptable level, and independence would not be impaired, provided that, in addition to the General Requirements of the “Nonattest Services” interpretation [1.295.000], all of the following safeguards are met:

- a. The member is satisfied that client management designates an individual or individuals who possess suitable skill, knowledge, and experience, preferably within senior management, to be responsible for:*
 - i. determining the nature and scope of the activities to be performed **provided by the individual performing the augmented staff services (the “augmented staff”)**;*
 - ii. supervising and overseeing the activities performed **by the augmented staff**; and*
 - iii. evaluating the adequacy of the activities performed **by the augmented staff** and the findings resulting from the activities.*
- b. The activities do not result in the **augmented staff** member assuming management responsibilities as described in the Management Responsibilities” interpretation [1.295.030] of the “Independence Rule” [1.200.001];*
- c. The augmented staff only performs activities that would **not** otherwise be ~~permitted~~ **prohibited** by the “Nonattest Services” interpretation [1.295.000] of the “Independence Rule” [1.200.001]; and*
- d. The duration of the arrangement is temporary in nature.*

Ms. Snyder noted that item d. of paragraph .02 above requires that the arrangement be temporary in nature. The Task Force did not believe that the word “temporary” required defining, but acknowledged that a question could be included in the exposure draft asking if commenters believed the meaning of “temporary” is clear. Ms. Snyder noted that IESBA does not define the terms “temporary” or “short period of time” which are used in the IESBA provisions. Some PEEC members felt that “temporary” simply means “not permanent,” while others had concerns that bright lines and prescribed time frames may be problematic in such scenarios. The following additional comments / questions were noted:

- Consider use of the term “discrete projects” as an alternative.
- Do not necessarily need to define the term “temporary” before exposure, but have something close to defining it.
- Consider using a reasonableness test.

- Mr. Burke asked if frequency really the primary issue, given that firm quality controls are more geared around the project and activity itself, rather than the frequency of the activity.
- One member asked how this was any different from bookkeeping arrangements; Mr. Lynch noted that the issue of simultaneous employment, or the appearance of such, would still remain an issue even in the case of bookkeeping, if there was a staffing arrangement in place.

After discussion, PEEC agreed that the Task Force should further deliberate regarding suggestions for the use of the term temporary or alternatives, and bring recommendations to the November PEEC meeting for the Committee to consider.

Paragraph .03 – Appearance of Simultaneous Employment

Ms. Snyder noted that the Task Force suggests changing “member” to “augmented staff” in paragraph .03, to clarify that the augmented staff, rather than the member, is subject to the parameters in paragraph .03 regarding the appearance of simultaneous employment. For example, the augmented staff should not be listed as an employee of the attest client, whether or not that individual is a member. PEEC agreed with the recommended revision.

While discussing paragraph .03 the question was raised as to whether the concept of duration of the arrangement (i.e. temporary) should be included in paragraph .03 as well as paragraph .02. One member believed duration should be a consideration, however others expressed concerns that attempting to define temporary would move the analysis further away from the use of professional judgment. PEEC suggested consulting the SEC language and consider whether a similar language should be included in paragraph .03 to address the duration of the arrangement.

Paragraph .04 – Examples of Safeguards

Ms. Snyder noted that paragraph .04 presents examples of safeguards that can be applied, which were based upon feedback received at the May 2018 PEEC meeting. PEEC agreed with the revisions presented by the Task Force.

Effective Date

Mr. Burked noted that the effective date should be longer to provide ample implementation time for small firms.

6. State & Local Government

Ms. Miller reminded the Committee that the reason for the proposed change was because (1) the commercial affiliate interpretation had been adopted and so the SLG interpretation needed to be evaluated to determine what changes were necessary in order to keep pace with the latest thinking regarding what related entities members should be independent of; and (2) the extant interpretation was adopted in 2001 and there had been changes to the GASB standards and in the SLG environment (e.g., some governmental entities function more like commercial entities). Ms. Miller also reminded the Committee that, during the February 2018 meeting, the Task Force’s sole request of the Committee was whether the project should proceed given that approximately one third of the commenters either didn’t believe the project should proceed because changes to the interpretation were not

necessary or believed that the proposal should be clarified or simplified. During this meeting the Committee agreed the project should proceed.

Ms. Miller went on to explain that the Task Force was seeking input on: (1) how far downstream members should look when determining whether investments should be considered affiliates; and (2) what the independence evaluation would entail when looking at upstream affiliates and other entities. For investments, there was general agreement that investments would be considered affiliates until one of the two criteria [1] was no longer met. The Committee did not agree on what the upstream evaluation would entail. Rather, the Task Force was asked to consider a number of possible ways the evaluation could be conducted including but not limited to, applying a pure conceptual framework approach to upstream entities or including upstream entities as affiliates. For other entities, the Task Force was asked to consider whether the reminder to apply the conceptual framework was needed or if this could be accomplished through the issuance of non-authoritative guidance such as a FAQ.

Ms. Miller noted that although the substantive changes to the exposure draft seem to make the proposal less restrictive the Committee may want to consider if a targeted re-exposure might be helpful to determine whether the re-write was clear enough that members will be success when implementing. The Task Force was asked to consider how it could provide the Committee with assurance that all matters raised by commenters were considered.

7. Information Technology Services

Ms. VanDyne reported that the Information System Services Exposure Draft had received a significant number of comment letters and that the Task Force planned to provide the Committee with a report at the November meeting. Ms. VanDyne also asked for input on several frequently-asked-questions (FAQs) drafted to address the previously-released Hosting Services interpretation. Staff has received numerous questions from smaller firm practitioners about the interpretation and concerns about meeting the September 1, 2018 effective date.

Mr. Brackens briefed the Committee about some concerns raised related to the hosting services interpretation. Mr. Brackens explained that the AICPA's Technical Issue Committee (TIC) believed that some vendors used by members to provide bookkeeping services to attest clients may need some additional time to modify their operational processes so that members would not be hosting an attest client's financial information system.

Mr. Brackens also noted that a member who teaches ethics CPE reached out to him seeking clarification regarding how the hosting services interpretation (specifically, FAQs 4, 5 and 6 of the FAQs included in the PEEC's agenda) would change how bookkeeping services are provided when a member wants to maintain their independence. Specifically, up until now when providing bookkeeping services, some members obtain the records from their attest clients and enter the approved information into a financial information system that resides on the member's server or on a vendor's server that the member has a contract with. As part of complying with the General Requirements interpretation members would provide their attest client with a copy of the trial balance or general ledger. However, under the hosting services interpretation it seems as though this practice would impair

independence and thus require a change in practice. This member also noted that this position seemed inconsistent with how the Hosting Services interpretation treats the preparation of depreciation and similar schedules since independence would not be impaired if the member provided the attest client with the schedule and calculation so that attest client's books and records are complete.

The Chair of the Committee suggested the Committee discuss delaying the effective date, primarily to give the market (software vendors) additional time to allow members to adhere to the current standard, but table the technical discussion. He noted that the standard went through due process so if members or others had issues with the proposal they should have stated so during that process. He also suggested tabling discussion of the FAQs (as a whole) to allow the Task Force to consider the questions raised. **The Committee unanimously agreed to extend the effective date for the interpretation to July 1, 2019.**

The Task Force was asked to consider whether the FAQs are consistent with the hosting services interpretation; whether the interpretation is consistent in terms of how it addresses working on the client's general ledger vs. depreciation schedules; what cutting off access to a portal means (i.e., document vs portal system) and if there are differing views within the Task Force, to share the differing views with the Committee.

8. NOCLAR

Mr. Denham reported on task force activity since the May PEEC meeting. The task force, including the UAA co-chairs observing, has been meeting monthly to discuss comment letters received. The task force thus far has discussed comments that would likely not be considered by the UAA committee and revised certain language based on those discussions. The task force has also discussed whether or not there should be distinctions made between audit and non-audit services for certain areas, but no specific conclusions have been reached as these matters will be discussed in a more broader sense after the UAA Committee has begun its meetings. Mr. Denham, Ms. Hnatt, Mr. Brackens, and Ms. Lee-Andrews will be attending a combined UAA meeting to discuss NOCLAR on September 12-13th. Stavros Thomadakis, IESBA Chairman will also be attending this meeting. Mr. Denham also indicated that several jurisdictions reported on NOCLAR at the National Standards Setters meeting in May, which was attended by Mr. Burke and Ms. Lee-Andrews. Certain jurisdictions have adopted the standard and reported having challenges in implementation. Ms. Lee-Andrews has reached out to those jurisdictions to obtain additional information regarding such challenges.

9. IESBA Update

Ms. Gorla reported that at the May meeting the Board received preliminary feedback provided regarding the two roundtables that were held regarding (1) approaches to redefining professional skepticism so that it is appropriate for all types of professional activity; and (2) consideration of the impact that Non-Assurance Services (NAS) has on independence. She noted that the Board agreed the Fees Working Group should develop a proposal on fees and bring a draft to the Board in September and the NAS Task Force should try to put terms of reference together that included how the NAS project will cover this topic. Ms. Gorla also noted that the Basis for Conclusion document for the Inducements, Including Gifts and Hospitality would be given to the PIOB in June.