



Frequently Asked Questions:

Application of the independence
rules to affiliates of employee
benefit plans

As of May 18, 2017

AICPA Professional Ethics Division

Introduction

The [Client Affiliates](#) interpretation [AICPA, *Professional Standards*, ET sec. 1.224.010] under the Independence Rule” [AICPA, *Professional Standards*, ET sec. 1.200.001] provides guidance on which entities should be considered an [affiliate](#) [AICPA, *Professional Standards*, ET sec. 0.400.02] of a [financial statement attest client](#) [AICPA, *Professional Standards*, ET sec. 0.400.16] and, therefore, subject to the same independence provisions of the AICPA Code of Professional Conduct applicable to the financial statement attest client. This document will help members better understand how the definitions and guidance provided in the Client Affiliates interpretation apply to affiliates of employee benefit plans subject to the Employee Retirement Income Security Act (ERISA) through the use of answers to frequently asked questions (FAQ). These questions and answers do not apply to governmental employee benefit plan financial statement attest clients that would be covered by the [Entities Included In State and Local Government Financial Statements](#) interpretation [AICPA, *Professional Standards*, ET sec. 1.224.020] under the “Independence Rule”.

The answers to these questions are based on guidance the AICPA Professional Ethics Division staff provided in response to members’ inquiries concerning the Client Affiliates interpretation. The answers are not rules, regulations, or statements of the Professional Ethics Executive Committee and, therefore, are not authoritative guidance. Further, the answers do not address the requirements of other regulatory bodies, such as the state boards of accountancy, the U.S. Department of Labor (DOL), the SEC, and the U.S. Government Accountability Office whose positions may differ from and may be more restrictive than those of the AICPA.

In addition to this FAQ document, members may find the nonauthoritative [DOL and AICPA Independence Rule Comparison](#) developed by the Employee Benefit Plan Audit Quality Center of assistance in understanding where staff believes the DOL may be more restrictive than the AICPA.

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Plan affiliates

The Client Affiliates interpretation provides that certain entities should be considered affiliates of a plan that is a financial statement attest client. The interpretation further explains that, aside from four specified exceptions, members should apply any independence provisions that are applicable to the plan to affiliates of the plan. The following questions and answers are designed to assist you in understanding which entities are considered affiliates of a plan that is a financial statement attest client of your firm:

1. *When a single employer plan is a financial statement attest client of the firm, would the sponsor be considered an affiliate of the plan?*

Yes. The sponsor of a single employer employee benefit plan financial statement attest client is considered to be an affiliate of the plan because it is the sponsor that makes all business decisions related to the plan (such as when to create or terminate the plan, which employees may participate, and the vesting policies for the plan).

2. *When the plan sponsor of a single employer plan financial statement attest client is controlled by another entity, would the entity that controls the sponsor be considered an affiliate of the plan?*

Yes. The entity that controls the sponsor would be considered an affiliate of the plan if the plan was material to the controlling entity. When determining materiality, possible factors to consider include the following:

- a. Is the annual benefit expense paid by the sponsor for the client plan material to the controlling entity?
 - b. Is the unfunded liability for the client plan material to the controlling entity?
 - c. Does the client plan own a material amount of the controlling entity's stock?
 - d. Is the client plan's debt extended by or guaranteed by the controlling entity, material to the controlling entity?
3. *The Client Affiliates interpretation indicates that when a multiemployer employee benefit plan is a financial statement attest client, any entity, such as the union, participating-employers or a group association of employers will be considered affiliates of the plan when such entity has significant influence over the plan and the plan is material to such entity.*

- a. *Why are unions and participating employers identified as potential affiliates?*

Unions and participating employers are identified as potential affiliates because, based upon how these plans are typically structured, they are typically the entities that may have the most influence over the plan. *Another entity that might have significant influence is a group association of employers.*

- b. *How are multiemployer plans typically structured?*

A multiemployer plan includes pension or postretirement benefit plans to which two or more unrelated employers contribute, pursuant to one or more collective bargaining agreements. A characteristic of multiemployer plans is that assets contributed by one participating employer may be used to provide benefits to employees of other

participating employers because assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer.

Generally, many employers participate in a multiemployer plan, and an employer may participate in more than one plan. The employers participating in multiemployer plans usually have a common industry bond, but for some plans the employers are in different industries and the labor union may be their only common bond. Some multiemployer plans do not involve a union. For example, local chapters of a not-for-profit entity may participate in a plan established by the related national organization. A multiemployer plan is usually administered by a Board of Trustees composed of an equal number of representatives from the union and participating employers. The Board of Trustees typically oversees the plan, is considered the plan sponsor, and makes all business decisions related to the plan.

c. When would an entity be considered to have significant influence over the plan?¹

Significant influence is defined as used in Financial Accounting Standards Board (FASB) *Accounting Standards Codification*TM (ASC) 323-10-15.² However, because neither the union nor a participating employer would have an equity interest in the plan called for by ASC 323-10-15-8, to satisfy this component members should look for other ways significant influence could be exerted (such as representation and corresponding voting interest that the entity has on the Board of Trustees).

For example, assume a plan has 10 participating employers and 1 union, and the Board of Trustees has 8 members, all with equal voting rights. If the union or a single participating employer is given 2 or more seats on the Board of Trustees, the entity typically will be considered to have significant influence over the plan because the entity will have 25 percent of the voting rights.

Any entity that is a member of the Board of Trustees but has less than 20 percent of the voting rights will not be considered to have significant influence over the plan unless some other factor gives it significant influence. Other factors to consider include the following:

- The ability to otherwise participate in the plan's policy-making processes
- The existence of material intra-entity transactions with the plan (such as when the entity employs a significant percentage of current plan participants and, as such, becomes the source of significant plan contributions)
- Overlap of managerial personnel between the Board of Trustees and the union or participating employer technological dependency (such as when a plan is reliant upon the union or participating employer's financial reporting system)

¹ This discussion concerning significant influence can also be used when determining if a multiemployer plan should be an affiliate of a financial statement attest client or an entity controlled by the financial statement attest client.

² See page 11 this document for an excerpt of FASB ASC 323-10-15 pertaining to this discussion.

4. *The Client Affiliates interpretation indicates a sponsor of a single employer employee benefit plan that is a financial statement attest client will be an affiliate of the plan, yet when the plan is a multiple-employer employee benefit plan financial statement attest client, only a participating employer that is the plan administrator (in other words, a the plan sponsor) will be considered an affiliate of the plan. What is a multiple-employer employee benefit plan?*

A multiple-employer employee benefit plan is a plan maintained by more than one employer. Multiple-employer plans generally are not collectively bargained and are intended to allow participating employers, commonly in the same industry, to pool their assets for investment purposes and reduce the costs of plan administration. A multiple-employer plan maintains a separate account for each employer so that contributions provide benefits only for employees of the contributing employer. In addition, some multiple-employer plans have features that allow participating employers to have different benefit formulas, in which the employer's contributions to the plan are based on the benefit formula selected by the employer.

For example, a multiple-employer 401(k) plan is set up by 10 medical practices in one geographic area. Although the employees of each practice participate in the plan, one practice will be selected by the participating employers to act as the plan sponsor or administrator who has overall responsibility for plan governance. That practice will oversee the day-to-day operations of the plan (for example, ultimate responsibility for the preparation of financial statements and hiring the auditor). It may perform these duties directly or outsource most of them and spend much of its time managing vendors. That practice will usually be viewed as having significant influence over the plan and consequently considered an affiliate of the plan.

5. *Would an entity in which a plan that is a financial statement attest client invests, other than the sponsor, be considered an affiliate of the plan?*

If the plan invests in an entity and the investment allows the plan to control the entity, as used in FASB ASC 810, *Consolidations*, for commercial entities and FASB ASC 958-805-20 for not-for-profit entities, then the entity would be considered an affiliate of the plan.

In addition, if the investment gives the plan significant influence over the entity, as used in FASB ASC 323-10-15, and the investment is material to the plan, then the entity would be considered an affiliate of the plan. For example, if a plan owns 30 percent of the voting stock of an investee, and that investment is material to the plan, the investee would be considered an affiliate of the plan.

6. *Would a service provider, such as a third-party administrator that is hired to administer (for example, recordkeeping, bookkeeping, payments) a plan that is a financial statement attest client, be considered an affiliate of a plan if the plan does not invest in the third-party administrator?*

No.

7. *An entity sponsors multiple single employer employee benefit plans. If the entity offers these plans to its employees and a member audits only one plan (client plan), would the other plans (nonclient plans) that the entity sponsors be considered affiliates of the client plan?*

For the nonclient plans to be considered affiliates of the client plan, both the control and materiality conditions contained in (e) of the affiliate definition must be met. Because the term control as used in the ASC would include having the direct or indirect ability to determine the direction of management and policies through ownership, contract or otherwise, the control component would be considered met because the sponsor has the ability to control all plans. However, a nonclient plan would only be considered an affiliate of the client plan if the client plan and nonclient plan are material to the sponsor. Therefore, it is possible that certain nonclient plans may be material to the sponsor and, accordingly, considered an affiliate whereas others may not. When determining if plans are material to the sponsor, possible factors to consider include the following:

- Is the annual benefit expense paid by the sponsor for the client plan and nonclient plan material to the sponsor?
- Is the unfunded liability for the client plan and nonclient plan material to the sponsor?
- Do the client plan and nonclient plan own a material amount of the sponsor's stock?
- Is the client plan and nonclient plan's debt extended by or guaranteed by the sponsor, material to the sponsor?

8. *A parent entity has three subsidiaries. Each subsidiary sponsors a single employer employee benefit plans. If a member only audits the plan of one subsidiary, would the other two plans be affiliates of the plan that the member audits?*

No. The other two plans would not be considered affiliates of the plan that the member audits as the sponsors of each plan are different entities.

Exceptions to the client affiliates interpretation

Question. May a [member](#) make a political contribution to the campaign of an individual that is The Client Affiliates interpretation requires that members apply any independence provisions that are applicable to a plan that is a financial statement attest client to affiliates of the plan. However, the interpretation does provide four specific exceptions. The following questions and answers are designed to assist you in understanding how to apply these exceptions in the context of a financial statement attest engagement for a plan.

1. *When a plan is a financial statement attest client of a member, would independence be impaired if the member provides nonattest services to an affiliate of the plan, as defined in (c)–(l) of the Client Affiliates interpretation?*

Independence would not be impaired provided the member complies with the requirements of [Nonattest Services](#) subtopic [AICPA, *Professional Standards*, ET sec. 1.295] of the Independence Rule. However, if the member provides nonattest services to an affiliate of the plan, as defined in (c)–(l), that is not in compliance with the Nonattest Services subtopic (that is, provides nonattest services that would impair independence), independence would not be impaired if it is reasonable to conclude that the services do not create a self-review or management participation threat because the results of the services will not be subject to attest procedures. Any other threats that are created by the provision of the nonattest service are eliminated or reduced to an acceptable level by the application of safeguards.

2. *When a plan is a financial statement attest client of the firm, would independence be impaired if an immediate family member or close relative of a covered member is employed in a key position at an affiliate of the plan, as defined in (c)–(l) of the Client Affiliates interpretation?*

Independence would not be impaired provided the position does not place the immediate family member or close relative in a key position with respect to the plan. For example, the immediate family member or close relative should not be a member of the Board of Trustees of the plan, nor should he or she sign the management representation letter for the plan audit.

3. *When a plan is a financial statement attest client of the firm, would independence be impaired if a former partner or professional employee of the firm becomes associated or employed with an affiliate of the plan, as defined in (c)–(l) of the Client Affiliates interpretation?*

Independence would not be impaired, provided the position does not place the former partner or professional employee in a key position with respect to the plan. For example, the former partner or professional employee would be in a key position with respect to the plan if he or she is a member of the Board of Trustees of the plan or signs the management representation letter for the plan. If the former partner or professional employee is in a key position with respect to the plan, for independence not to be impaired the safeguards in paragraph .02 of the [Subsequent Employment or Association With an Attest Client](#) interpretation [AICPA, *Professional Standards*, ET sec. 1.279.020] of the Independence Rule must be met.

4. *When a plan is a financial statement attest client of the firm, would independence be impaired if a covered member has a loan to or from an individual who is an officer, director, or a 10 percent or more owner of an affiliate of the plan?*

Independence would not be impaired, provided the covered member does not have knowledge that the individual is in such a position with an affiliate. However, if the covered member knows or has reason to believe the individual is in such a position, independence may be maintained if, after applying the [Conceptual Framework for Independence](#) [AICPA, *Professional Standards*, ET sec. 1.210.010], the covered member concludes that threats are at an acceptable level.

Difficulty in identifying affiliates of a plan

1. *When a plan is a financial statement attest client of the firm, what should members do if they are unable to identify all affiliates of the plan?*

Members must expend best efforts to obtain the information necessary to identify a plan's affiliates. If, after expending best efforts, members are unable to obtain the information to determine which entities are affiliates of the plan, members should (a) discuss the matter, including the potential impact on independence, with those charged with plan governance (for example, the plan administrator, employee benefit committee, or board of trustees); (b) document the results of that discussion and the efforts taken to obtain the information; and (c) obtain written assurance from the client that it is unable to provide the information necessary to identify the client's affiliates.

Affiliate definition

Affiliate. The following entities are affiliates of a *financial statement attest client*:

- a. An entity (for example, subsidiary, partnership, or limited liability company [LLC]) that a *financial statement attest client* can *control*.
- b. 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*.
- 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.

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/fags-application-independence-rules-affiliates-of-employee-benefit-plans.pdf.

Client affiliate interpretation – 1.224.010

- .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 *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].
 - 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*.
 - 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*.
 - 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*.
- .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/fags-application-independence-rules-affiliates-of-employee-benefit-plans.pdf>.

FASB ASC 323-10-10 [Except for significant influence]

- 15-6 Ability to exercise significant influence over operating and financial policies of an investee may be indicated in several ways, including the following:
- a. Representation on the board of directors
 - b. Participation in policy-making processes
 - c. Material intra-entity transactions
 - d. Interchange of managerial personnel
 - e. Technological dependency
 - f. Extent of ownership by an investor in relation to the concentration of other shareholdings (but substantial or majority ownership of the voting stock of an investee by another investor does not necessarily preclude the ability to exercise significant influence by the investor).
- 15-7 Determining the ability of an investor to exercise significant influence is not always clear and applying judgment is necessary to assess the status of each investment.
- 15-8 An investment (direct or indirect) of 20 percent or more of the voting stock of an investee shall lead to a presumption that in the absence of predominant evidence to the contrary an investor has the ability to exercise significant influence over an investee. Conversely, an investment of less than 20 percent of the voting stock of an investee shall lead to a presumption that an investor does not have the ability to exercise significant influence unless such ability can be demonstrated. The equity method shall not be applied to the investments described in this paragraph insofar as the limitations on the use of the equity method outlined in paragraph 323-10-25-2 would apply to investments other than those in subsidiaries.
- 15-9 An investor's voting stock interest in an investee shall be based on those currently outstanding securities whose holders have present voting privileges. Potential voting privileges that may become available to holders of securities of an investee shall be disregarded.
- 15-10 Evidence that an investor owning 20 percent or more of the voting stock of an investee may be unable to exercise significant influence over the investee's operating and financial policies requires an evaluation of all the facts and circumstances relating to the investment. The presumption that the investor has the ability to exercise significant influence over the investee's operating and financial policies stands until overcome by predominant evidence to the contrary. Indicators that an investor may be unable to exercise significant influence over the operating and financial policies of an investee include the following:
- a. Opposition by the investee, such as litigation or complaints to governmental regulatory authorities, challenges the investor's ability to exercise significant influence.
 - b. The investor and investee sign an agreement (such as a standstill agreement) under which the investor surrenders significant rights as a shareholder. (Under a standstill agreement, the investor usually agrees not to increase its current holdings. Those agreements are commonly used to compromise disputes if an investee is fighting against a takeover attempt or an increase in an investor's percentage ownership. Depending on their provisions, the agreements may modify an investor's rights or may

increase certain rights and restrict others compared with the situation of an investor without such an agreement.)

- c. Majority ownership of the investee is concentrated among a small group of shareholders who operate the investee without regard to the views of the investor.
- d. The investor needs or wants more financial information to apply the equity method than is available to the investee's other shareholders (for example, the investor wants quarterly financial information from an investee that publicly reports only annually), tries to obtain that information, and fails.
- e. The investor tries and fails to obtain representation on the investee's board of directors.

15-11 The list in the preceding paragraph is illustrative and is not all-inclusive. None of the individual circumstances is necessarily conclusive that the investor is unable to exercise significant influence over the investee's operating and financial policies. However, if any of these or similar circumstances exists, an investor with ownership of 20 percent or more shall evaluate all facts and circumstances relating to the investment to reach a judgment about whether the presumption that the investor has the ability to exercise significant influence over the investee's operating and financial policies is overcome. It may be necessary to evaluate the facts and circumstances for a period of time before reaching a judgment.

Changes in Level of Ownership or Degree of Influence

15-12 An investment in common stock of an investee that was previously accounted for on other than the equity method may become qualified for use of the equity method in accordance with paragraph [323-10-15-3](#) by an increase in the level of ownership described in that paragraph (that is, acquisition of additional voting stock by the investor, acquisition or retirement of voting stock by the investee, or other transactions). See paragraph [323-10-35-33](#) for guidance on all changes in an investor's level of ownership or degree of influence.