

## **Ethics Interpretation No. 101-3, *Performance of Nonattest Services***

### **Proposed Revisions Clarify Independence Requirements**

---

On February 28, 2011, the AICPA Professional Ethics Executive Committee (PEEC) issued an omnibus exposure draft containing proposed revisions to Interpretation No. 101-3, “Performance of nonattest services,” under Rule 101, *Independence* (AICPA, *Professional Standards*, ET sec. 101 par. .05). The PEEC believes these revisions will add clarity to the nonattest services guidance and enhance practitioners’ understanding of the interpretation’s requirements. An overview of the proposed revisions follows.

#### ***Establishing or maintaining internal control***

One of the proposed revisions relates to a general activity that would impair a member’s independence: establishing or maintaining internal controls, including performing ongoing monitoring activities for a client. The PEEC recognized that an inconsistency existed within the current interpretation in that certain bookkeeping and other nonattest services permitted under the interpretation could be viewed as maintaining internal controls for the client and, as such, may appear to be prohibited by the general activity. For example, under the proposed revisions to the interpretation, a practitioner could prepare monthly bank reconciliations for an audit client without impairing independence provided the general requirements of the interpretation are met, such as ensuring that the client reviews and approves the bank reconciliations and sufficiently understands the services performed to oversee them. However, preparing bank reconciliations for a client is also considered to be maintaining an internal control for the client. Because it was never the PEEC’s intent to have the permitted activities listed in the interpretation be considered as impairing independence, the committee agreed to revise the general activity to state accepting responsibility for designing, implementing or maintaining internal control. The PEEC believes the phrase “designing and implementing” is not only clearer than “establishing,” but is more reflective of the language used in the professional standards (for example, auditing standards) and the *Code of Ethics for Professional Accountants* issued by the International Ethics Standards Boards for Accountants (IESBA Code). The addition of the phrase “accepting responsibility for” is intended to clarify that practitioners are able to assist their clients by performing services to design, implement, or maintain certain aspects of internal control when management accepts responsibility for such services and the other general requirements of the interpretation are met.

Even if client management accepts responsibility for internal control related services, threats to independence (for example, self-review and management participation threats) may still exist. The general requirements of the interpretation serve as safeguards to mitigate these threats to an acceptable level and, therefore, are necessary in order to maintain independence.



Copyright © 2011 by  
American Institute of Certified Public Accountants, Inc.  
New York, NY 10036-8775

All rights reserved. For information about the procedure for requesting permission to make copies of any part of this work, please e-mail [copyright@aicpa.org](mailto:copyright@aicpa.org) with your request. Otherwise, requests should be written and mailed to the Permissions Department, AICPA, 220 Leigh Farm Road, Durham, NC 27707-8110.

Specifically, in addition to accepting responsibility for the services, management must make all significant judgments and decisions in connection with the engagement and must also designate an individual who has the skill, knowledge, and or experience to oversee the services and evaluate the adequacy and results of the services performed. While the general requirements are generally sufficient to safeguard independence, there could be situations in which the practitioner may cross the line and impair independence due to the scope and extent of internal control services performed. For example, as discussed in the proposed revisions to the interpretation, the management participation threat created when a practitioner performs ongoing monitoring procedures is so significant that no safeguards could reduce the threat to an acceptable level. In addition, management is responsible for designing and maintaining the company's internal control process and, therefore, should not rely on the practitioner's work as the primary basis for its assertion regarding the effectiveness of its internal control over financial reporting. Accordingly, in cases in which the practitioner's involvement in the client's internal control process is so extensive that it results in management relying on the practitioner's work as the primary basis for its assertion, no safeguards could reduce the threats to independence to an acceptable level, and independence would be impaired. Practitioners should use judgment in determining whether services performed would constitute ongoing monitoring activities or whether management appears to be relying on its work as the basis for its assertion on internal control effectiveness.

#### ***Defining management responsibilities***

In addition to the proposed revision to the general activity, the PEEC is proposing several other clarifications to enhance the guidance in the interpretation. For example, the PEEC believes the term *management responsibilities* is clearer than *management functions* and, therefore, proposes certain revisions to reflect this change. The revised interpretation also incorporates a description of the term *management responsibilities* as well as additional examples of management responsibilities. The examples previously referred to as *general activities* have also been merged into the examples of management responsibilities because the reason they impair independence is because they are deemed to be responsibilities of management. The proposed language is consistent with the IESBA Code, and, therefore, it aligns the AICPA Code closer with international standards. The PEEC does not consider these revisions to be more restrictive than the existing independence requirements of Interpretation No. 101-3, and, therefore, such changes are not expected to change current practice.

#### ***Performing ongoing monitoring versus separate evaluations***

One proposed revision to the interpretation may be viewed as more restrictive. Specifically, the PEEC is proposing to include a requirement that members evaluate the significance of the management participation threat created by performing separate evaluations on the client's internal control system. The PEEC believes that an inconsistency in the interpretation exists by prohibiting a member from performing ongoing monitoring procedures for a client while permitting separate evaluations because, depending on the scope or extent of the controls being tested and frequency of the separate evaluations, the member may be performing services equivalent to ongoing monitoring procedures. Accordingly, the PEEC is proposing that the significance of the threat created by performing separate evaluations should be evaluated and safeguards applied when necessary to eliminate the threat or reduce it to an acceptable level.

#### ***Incorporating nonauthoritative guidance***

Other proposed revisions to the interpretation involve incorporating certain nonauthoritative guidance contained in the Ethics Division's answers to [\*Frequently Asked Questions: Performance of Nonattest Services\*](#). One such revision relates to clarifying the difference between performing bookkeeping services and performing activities that are considered to be part of the attest engagement. For example, proposing adjusting journal entries or making suggestions about the form or content of the financial statements for a client (subject to management's review and approval) as part of an audit engagement would generally not be considered a nonattest service subject to the requirements of Interpretation No. 101-3. However, the practitioner is expected to use judgment in determining whether his or her involvement has become so extensive that it would constitute performing a separate service which would be subject to the interpretation's general requirements. A client's books and records should be substantially complete and current in order to perform an audit or review of those books and records. If practitioners find themselves performing a service to bring those books and records current or complete, the service may be considered outside the scope of the normal audit or review process and, therefore, a bookkeeping service subject to Interpretation No. 101-3.

To learn more about these and other proposed revisions to Interpretation No. 101-3, view the [exposure draft](#). Comments on revised Interpretation No. 101-3 and other proposals contained in the exposure draft are due by May 31, 2011.