Ethics, Professional Responsibilities, and General Principles

AICPA Code of Professional Conduct

Introduction and Preface

Code of Professional Conduct

New Electronic Version

- Effective (mostly) 12/15/14
- Conceptual Framework effective 12/15/15

Features:

- Searchable
- Easily updated
- Located: http://pub.aicpa.org/codeofconduct

Preface

Preface (Part 0) Divides Code into Three Major Parts:

1. Members in Public Practice (MIPPs)
2. Members in Business (MIBs)
3. Other Members (OMs)

   • If multiple roles, use strictest rules
Principles and Rules
Supplemented by:
- Interpretations
- Definitions
- Applications
- Where applicable, standards promulgated by bodies such as:
  - State CPA Societies
  - SEC
  - PCAOB
  - GAO
  - DOL
  - Etc.

Six Principles of Professional Conduct

1. **Responsibilities principle:** “In carrying out their responsibilities as professionals, members should exercise sensitive professional and moral judgments.” Members should cooperate to:
   - improve the art of accounting,
   - maintain the public's confidence, and
   - carry out the profession's special responsibilities for self-governance.

Six Principles of Professional Conduct

2. **Public Interest principle:** “Members should accept the obligation to act in a way that will serve the public interest, honor the public trust, and demonstrate a commitment to professionalism.”
   - “A distinguishing mark of a profession is acceptance of its responsibility to the public.”
Six Principles of Professional Conduct

3. **Integrity principle**: “To maintain and broaden public confidence, members should perform all professional responsibilities with the highest sense of integrity.”
   - Integrity is measured in terms of what is right and just.
   - Members should always ask “Am I doing what a person of integrity would do?”

Six Principles of Professional Conduct

4. **Objectivity and Independence principle**: “A member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities. A member in public practice should be independent in fact and appearance when providing auditing and other attestation services.”

**Objectivity** is a state of mind that requires:
- impartiality,
- intellectual honesty, and
- freedom from conflicts of interest.
**Independence**: applies only to MIPPs, but all members performing all services must act with objectivity and integrity.

<table>
<thead>
<tr>
<th></th>
<th>Audit</th>
<th>Compilation</th>
<th>Tax</th>
<th>Consulting</th>
</tr>
</thead>
<tbody>
<tr>
<td>Integrity</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Objectivity</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Independence in Fact</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Independence in Appearance</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

---

**Six Principles of Professional Conduct**

5. **Due Care principle**: “A member should observe the profession's technical and ethical standards, strive continually to improve competence and the quality of services, and discharge professional responsibility to the best of the member's ability.”
   - Perfection is not required.
   - Competence requires a commitment to continued learning—hence, CPE.
   - Competence can come from:
     - Research or
     - Consultation with experts
   - Due care entails:
     - Adequate planning of engagements
     - Supervision of professional activities for which members are responsible

---

6. **Scope and Nature of Services principle**: “A member in public practice should observe the Principles of the Code of Professional Conduct in determining the scope and nature of services to be provided.”
   - At a minimum, members should:
     - practice in firms with good internal quality control procedures,
     - use their individual judgments to determine whether the scope and nature of services provided to an attest client would create a conflict of interest, and
     - individually assess whether a contemplated activity is consistent with their role as professionals
Definitions
Part 0 contains 50 or so…

Ex: **Partner Equivalent:** Someone who is not a partner but who either has ultimate responsibility for the conduct of an attest engagement or the authority to bind the firm to conduct an attest engagement.
Part 1 (MIPPs) also applies to government auditors within a government audit organization.

Three Steps to Applying Conceptual Framework

1. Identify threats

2. Evaluate the significance of the threats (acceptable level?)

3. Identify and apply safeguards
Seven Types of Threats

1. **Adverse interest threats**
   - Client sues or threatens to sue
   - Subrogee makes claim against firm to recover payment made to client

2. **Advocacy threats**
   - Member provides forensic accounting services to client in lawsuit with third party
   - Firm acts as investment adviser, underwriter, promoter, or registered agent for a client

3. **Familiarity threats**
   - Member’s spouse or parent is employed by the client
   - Former firm partner joins client in a key position
Seven Types of Threats

4. **Management participation threats**
   - Member takes on role of client management

---

Seven Types of Threats

5. **Self-interest threats**
   - Member has a financial interest in a client that may be affected by the outcome of a professional services engagement
   - Excessive reliance on revenue from a single client

---

Seven Types of Threats

6. **Self-review threats**
   - Member relies on work product of the member’s firm
   - Member performs bookkeeping services for a client
Seven Types of Threats

7. Undue influence threats
   - Client threatens to fire firm or to withhold future business
   - Major shareholder of client threatens to terminate a professional service unless the member reaches certain judgments or conclusions

Three Kinds of Safeguards Exist

1. Created by the profession, legislation, or regulation
   - Education and training requirements, including CPE
   - Professional standards and the threat of discipline
   - External reviews firm’s quality control system
   - Legislation establishing prohibitions and requirements for a firm or its professionals
   - Competency and experience requirements for licensure
   - Professional resources such as hotlines for consultation on ethical issues

Three Kinds of Safeguards Exist

2. Implemented by the client
   - The client has personnel with suitable skills, knowledge, or experience to make managerial decisions about the delivery of professional services.
   - The tone at the top emphasizes the client’s commitment to fair financial reporting and legal compliance.
   - Policies and procedures are in place to achieve fair financial reporting and compliance.
   - Policies and procedures are in place to address ethical conduct.
   - A governance structure, such as an active audit committee, is in place to ensure appropriate decision making, oversight, and communications regarding a firm’s services.
   - Policies are in place that bar the entity from hiring a firm to provide services that do not serve the public interest or would impair independence.
Three Kinds of Safeguards Exist

3. Implemented by the firm
   - Firm leadership stresses rule compliance and acting in the public interest
   - Policies and procedures designed to implement and monitor engagement quality control
   - Designation of someone from senior management to oversee the functioning of the firm’s quality control system
   - A disciplinary mechanism that is designed to promote compliance with policies and procedures
   - Rotation of senior personnel who are part of the engagement team
   - Policies that preclude audit partners or partner equivalents from being directly compensated for selling Nonaudit Services (NAS) to the attest client
   - And so on….
MIPPs Nonindependence Rules
Conflicts of Interest, Directorships, and Gifts

Conflicts of Interest
Pose a threat to objectivity and integrity
Two types:
1. Client A versus Client B
2. Firm and Members versus Client

Examples:
- Providing litigation services in connection with a lawsuit filed against a client
- Providing tax services to both members of a couple embroiled in a divorce
- Suggesting that a client invest in a business in which the member has a financial interest
- Suggesting that a client hire an insurance broker who refers clients to the member under an exclusive arrangement to do so
Conflicts of Interest
Threats to objectivity are reduced to an acceptable level if:
- There is full disclosure to the client
- The client consents

Director Positions
Objectivity is threatened when a member serves as a director of a client entity, so the Conceptual Framework should be applied to determine whether the threat is unacceptably high.
Better: Simply serve as a consultant to the board.

Gifts and Entertainment Rules
Objectivity and integrity are threatened if MIPPS receive gifts or entertainment from (or give to) client or its:
- Officers
- Directors
- 10% shareholders
Gifts and Entertainment Rules

A violation is presumed if:

- The member receives gifts or entertainment from a client that violate the member’s or client’s policies or applicable laws and regulations; and
- The member knows of the violation or is reckless in not knowing.

Gifts and Entertainment Rules

If no rules are violated, gifts and entertainment must still be: reasonable in the circumstances.

In deciding reasonableness, the following factors, among others, should be considered:

- Nature of the gift or entertainment
- Occasion giving rise to the gift or entertainment
- Cost or value
- Whether the entertainment was associated with the active conduct of business directly before, during, or after the entertainment
Reporting Income and Subordination of Judgment

Preparing and Reporting Income
Members have violated the Code if they have:

- Made, permitted or directed another to make, materially false and misleading entries in an entity’s F/S or records,
- Failed to correct an entity’s F/S or records that were materially false and misleading when they had the authority to record the entries, or
- Signed, permitted or directed another to sign, a document containing materially false and misleading information.

Subordination of Judgment
If members have disagreements with a superior over how to record potential earnings (or some other issue), they are not to simply accept the superior’s judgment.
Proper Procedure

1. Evaluate the significance of the threat that a material misrepresentation will occur or that applicable laws or regulations will be violated. If the threat is not significant, then nothing further need be done.

2. But, if there is such a significant threat, the member should discuss the matter with the superior.

3. If discussion with the superior does not resolve the difference of opinion, the member should go over the superior’s head.

Proper Procedure

4. If, after discussion with people up the chain, the member is still worried that the right thing is not going to be done, the member should, in no particular order, invoke the following safeguards:
   - Determine whether the organization’s internal policies and procedures have any additional requirements for reporting differences of opinion.
   - Determine whether she is responsible for communicating to third parties, such as regulatory authorities or the organization’s external accountant.
   - Consult legal counsel regarding responsibilities.
   - Document her understanding of the relevant facts, principles, and conversations.

Proper Procedure

5. If MIPPs then conclude that the threat of a legal violation or misrepresentation of facts cannot be reduced to an acceptable level, they should consider quitting the firm and taking appropriate steps to eliminate exposure to subordination of judgment.

6. MIPPs are not precluded from resigning, but that will not necessarily shield them from liability if there is a legal duty to report to external authorities.
Advocacy, Third-Party Service Providers (TSPs), General Standards, and Accounting Principles

Client Advocacy
MIPPs may not advocate for their attest clients.
Members providing advisory and tax services may advocate for their clients, but should not threaten objectivity or integrity by:
- Stretching the bounds of performance standards,
- Going beyond sound and reasonable professional practice, or
- Compromising credibility

Use of a Third-Party Service Provider
Outsourcing work to TSPs, at home or abroad, threatens compliance with integrity and objectivity rules.
Mere administrative support (ex: record storage or software application hosting) is no problem.
But when professional services are outsourced, clients should be notified, preferably in writing, before any confidential information is provided to the TSP.
If the client objects, either don’t outsource or decline the engagement altogether.
General Standards

Members must follow the rules set by appropriate bodies, meaning in part:

- **Professional Competence**: undertake only the professional services that the member or firm can reasonably expect to complete with professional competence
- **Due Professional Care**: exercise due professional care in performance of professional services
- **Planning and Supervision**: adequately plan and supervise the performance of professional services
- **Sufficient Relevant Data**: obtain relevant data to afford a reasonable basis for conclusions or recommendations in relation to any professional services performed

Competence

**Competence**: Means that the member or member’s staff possesses appropriate technical qualifications and member can supervise and evaluate the quality of work performed.

- If members cannot obtain necessary knowledge through *additional research or consulting with experts*, they should decline the engagement.
- If members employ a specialist for consulting services, they should possess the ability to define the tasks and evaluate the end product.

Use of a TSP

Before using a TSP, members should ensure that the TSP has the required professional qualifications, technical skills, and other resources.

Members must adequately plan and supervise the TSP’s services and obtain the data necessary to evaluate them.
Compliance with Standards
Members performing any professional services shall:

1. Comply with professional standards promulgated by bodies designated by the AICPA, and
2. Apply the Conceptual Framework where appropriate.

Accounting Principles
Members shall follow GAAP and other relevant accounting principles.
Exceptions: Departure from GAAP is appropriate if the member:

• Demonstrates that due to unusual circumstances, following GAAP would have been misleading; and
• Describes:
  • the departure,
  • its approximate effects, and
  • the reasons why compliance with the usual principle would result in a misleading statement.

Departure from GAAP
Circumstances that might justify a departure from GAAP:

• New legislation, or
• Evolution of a new form of business transaction.

Circumstances that do not justify:

• An unusual degree of materiality, or
• Conflicting industry practice.
Departure from GAAP

Departure from GAAP is permitted when other accounting principles apply, such as:

- Financial reporting frameworks generally accepted in another country;
- Financial reporting frameworks prescribed by an agreement or contract; or
- Other special purpose frameworks, including statutory financial reporting provisions required by law or a U.S. or relevant foreign governmental body.
Discreditable Acts

MIPPs shall not engage in **Discreditable Acts**, including:

- Discrimination and harassment in Employment
- Solicitation or disclosure of CPA Exam questions and answers
- Failure to file a tax return or pay a tax liability
- Negligence in the preparation of F/S or records

- Material departure from the audit standards of government bodies, commissions, or Other regulatory agencies
- Failure to follow additional government standards over and above GAAS where applicable
- Improper use of indemnification and limitation of liability provisions
- Disclosing confidential information obtained from employment or volunteer activities
Discreditable Acts

- False advertising
- Improper use of the CPA credential
- **Records requests**
  - Removing client files or proprietary information from a firm after termination
  - Use of confidential information obtained from a prospective client or nonclient without consent

Records Requests

There are four categories of records:

1. **Client-provided records** are records given by the client to the member.
2. **Member-prepared records** are those the member was not specifically engaged to prepare and are not in the client's books and records, rendering the client's financial information incomplete. Ex: adjusting, closing, combining or consolidating journal entries and supporting schedules and documents that the member proposed or prepared as part of an engagement.
3. **Member's work products** are deliverables set forth in the engagement letter. Ex: a tax return.
4. **Working papers** are all other items prepared solely for purposes of the engagement, including both items prepared by the member (Ex: audit programs, analytical review schedules, and statistical sampling and analysis) and by the client (Ex: papers prepared at the member's request and reflecting testing or other work done by the member).

Proper Treatment of Requests from Client

**Client-provided records:** return upon request, even if the client has not paid its bill to the member

**Member-prepared records:** deliver upon request when related to a completed and issued work product, except that they may be withheld if fees are due for that specific work product
Proper Treatment of Requests from Client

**Work Products:** provide upon request, except that they may be withheld if:
- fees are due for the specific work product
- the work product is incomplete
- to comply with professional standards (ex: withholding an audit report because of unresolved audit issues)
- if threatened or outstanding litigation exists concerning the engagement or the member’s work

Proper Treatment of Requests from Client

**Working papers:** are the member’s property and need not be provided to the client, *unless* some regulation or contractual provision requires production

Records Requests
Sometimes state laws are more demanding of accountants, and those laws must be followed.

Generally, requests should be honored within 45 days.
Contingent Fees

MIPPs shall not receive **contingent fees** for any service performed for a client for whom the MIPP performs any of the following attest services:

- An audit or review of a financial statement
- A compilation of a financial statement where the member reasonably expects a third party will use it and the compilation report does not disclose a lack of independence
- An examination of prospective financial information

A MIPP may not prepare an original or amended tax return or claim for a tax refund for a contingent fee for *any client*, even one for whom no attest work is done.

Contingent Fees defined: “a fee established for the performance of any service pursuant to an arrangement in which no fee will be charged unless a specified finding or result is attained, or in which the amount of the fee is otherwise dependent upon the finding or result of such service.”

- Exclusion: “fixed by courts or other public authorities, or, in tax matters, if determined based on the results of judicial proceedings or the finding of government agencies.”
Contingent Fees

Members may sometimes do tax work for non-attest clients on a contingent fee basis if IRS rules are not to the contrary (which they sometimes are).

Permitted Contingent Fees in the Tax Area

- Representing a client in a revenue agent's examination of the client's return
- Filing an amended return claiming a tax refund based on a tax issue that is the subject of a test case involving a different taxpayer or with respect to which the taxing authority is developing a position
- Filing an amended return (or refund claim) claiming a tax refund in an amount greater than the threshold for review by the Joint Committee on Taxation or the state taxing authority
- Representing a client in connection with obtaining a private letter ruling or influencing the drafting of a regulation or statute

Contingent Fees Not Permitted in the Tax Area

A contingent fee is not permitted if a member prepared an amended return claiming a refund because of an error in the originally filed return.
Commissions and Referral Fees

Referral fees and commissions are prohibited for attest clients.

For nonattest clients, they are permitted, but must be disclosed.

A member’s spouse may receive a commission from the member’s attest client, as long as the spouse’s activities are separate from the member’s practice and the member is not significantly involved in the spouse’s activities.

Members taking title to a product and assuming risks of ownership may resell the product to a client at a profit without disclosure.

Similarly, members may subcontract a service to another person and mark-up the cost of the services to the client without this being considered a commission.
Advertising and Confidentiality

Advertising and Other Forms of Solicitation

Members are responsible for third parties' promotional efforts as well as their own. Promotional efforts are considered false, misleading, or deceptive if they:

- Create false or unjustified expectations of favorable results,
- Imply the ability to influence any court or regulatory agency, or
- Claim that services will be performed for a stated fee when it is likely that it will be substantially increased.

Confidential Information

**General Rule:** Do not disclose confidential client information without specific consent of client.

Definition: “any proprietary information pertaining to the employer or any organization for whom the member may work in a voluntary capacity that is not known to be available to the public and is obtained as a result of such relationships”

It is a discreditable act either:

- To disclose client confidential information without permission, or
- To use the information for personal benefit.

Members should take reasonable steps to ensure that staff members do not improperly disclose.

Confidentiality duty survives the employment relationship.
Confidential Information—Exceptions

Even confidential information may be disclosed if:
- The client consents
- Disclosure is permitted by law and authorized by the employer
- Disclosure is required by law. Ex:
  - Comply with a validly issued and enforceable subpoena or summons
  - Inform the appropriate public authorities of violations of the law that have been discovered

Confidential Information—Exceptions

- There is a professional responsibility or right to disclose information, when not prohibited by law, to:
  - Initiate an ethics complaint with the AICPA, a state board of accountancy, etc.;
  - Protect the member’s professional interests in legal proceedings;
  - Comply with professional standards and other ethics requirements; or
  - Report potential concerns to the employer’s confidential complaint hotline or those charged with governance.

Confidential Information—Exceptions

- Disclosure is permitted on behalf of the employer to:
  - Obtain financing with lenders,
  - Communicate with vendors, clients, and customers, or
  - Communicate with the employer’s external accountant, attorneys, regulators, and other business professionals.
Additional Concepts

Be particularly sensitive to confidentiality when providing services to clients who are also competitors.

When accepting a new client would likely lead to disclosure of confidential information from an existing or previous (and identifiable) client, don’t take on the new client without obtaining informed consent from the previous client.

When withdrawing from an engagement due to, say, irregularities in a client’s tax return, if contacted by a potential successor firm, suggest that the firm contact the client to ask permission for you to discuss all matters freely.

Additional Concepts

When both spouses are tax clients and involved in a divorce, seek legal guidance if given conflicting directions.

When outsourcing work to TSPs, before disclosing confidential information, a member should:

- Enter into a contract with the TSP to maintain confidentiality and provide reasonable assurance that the TSP has procedures in place, or
- Obtain specific consent from the client for the disclosure.

Additional Concepts

Members involved in a peer review of another’s practice must keep the information confidential and not use it for their advantage.

Disclosing clients’ names is permissible, unless to do so discloses confidential information, such as where the member does primarily bankruptcy work and disclosure of clients’ identities signals that the clients are in financial difficulty.
Form of Organization and Names

Form of Organization

Basic Rules
- MIPPs may practice only in a form of organization permitted by law
- MIPPs may not practice under a firm name that is misleading
- Names of one or more past owners may be included in the firm name of a successor organization
- A firm may not designate itself as “Members of the AICPA” unless all its CPA owners are members of the AICPA

Ownership of a Separate Business
- A member may own an interest in a separate business that provides Nonaudit Services, but if the member controls the separate business, then its owners and professional employees must comply with the Code. Regarding an attest client, independence rules would have to be complied with it as well.
- But if the member’s interest is not a controlling one, then the Code’s provisions apply to him but not to the separate firm or its employees.
Form of Organization

Partner Designation
- Only members of a firm who are legally partners should use the designation “partner.”

Responsibility for Nonmember Practitioners
- If a member becomes an employee of a firm made up of one or more nonmembers:
  - she must still comply with the Code, and
  - if she is a partner in the firm, she is responsible for the firm’s professional employees.

Form of Organization

Attest Engagement Performed with a Former Partner
- Two former partners may continue to jointly perform an attest engagement, but should present their report on plain paper (no letterhead).

Firm Name

If two firms merge, they may use in the newly formed firm’s name the name of retired or other partners in either or both of the former firms.

A CPA member who is in partnership with non-CPAs may nonetheless sign reports in the firm’s name and also affix the designation “CPA” to his own signature.

Firm names may not mislead as to the legal form of the firm or who its owners are.
Firm Name

Firms within a network may share a common brand or common initials as part of their firm name without misleading. To be part of a network, the firms should share one or more of the following characteristics with other firms in the network:

• Common control among the firms
• Profits or costs
• Common business strategy
• Significant portions of professional resources
• Common quality control policies and procedures
MIPPs Independence Rules

Introduction to MIPPs Independence Rules

Introduction

MIPPs shall be independent when performing attest services.

If the Code and its interpretations do not resolve independence issues, the Conceptual Framework should be applied.

Threats and Safeguards

Threats to independence are quite similar to the threats to integrity and objectivity discussed elsewhere:

- Adverse interest threats
- Advocacy threats
- Familiarity threats
- Management participation threats
- Self-interest threats
- Self-review threats
- Undue influence threats
Threats and Safeguards

The safeguards that may be applied to reduce the threats to independence come from the same three sources as those relevant to integrity and objectivity:

- The profession, legislation, or regulation
- The attest client
- The firm

Threats and Safeguards

The threats to independence (adverse interest, advocacy, etc.) are concentrated in four areas:

1. **Financial relationships**—Ex: an attest partner should not own stock in an audit client
2. **Employment relationships**—Ex: an attest partner should not be on an audit client’s board of directors
3. **Family relationships**—Ex: an attest partner should not audit a client whose CEO is the partner’s spouse
4. **Consulting relationships**—Ex: an attest firm should not provide internal audit services to an attest client

Time Period

Independence rules must be followed when relationships exist during:

- The period covered by the financial statements, and/or
- The period of the professional engagement.
<table>
<thead>
<tr>
<th>Covered Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>Covered Members (CMs) who must comply with the independence rules for financial interests (and others) are:</td>
</tr>
<tr>
<td>1. An individual on the attest engagement team (team member);</td>
</tr>
<tr>
<td>2. An individual in a position to influence the attest engagement (PTI);</td>
</tr>
<tr>
<td>3. A partner, partner equivalent, or manager who provides more than 10 hours of nonattest services to the attest client within any fiscal year (10-hour person);</td>
</tr>
<tr>
<td>4. A partner or partner equivalent in the office in which the lead attest engagement partner or partner equivalent practices in connection with the attest engagement (OPIO—other partner in office);</td>
</tr>
<tr>
<td>5. The firm, including the firm's employee benefit plans; and</td>
</tr>
<tr>
<td>6. An entity whose operating, financial, or accounting policies can be controlled by any of the individuals or entities described in items 1 through 5 or two or more such individuals or entities if they act together.</td>
</tr>
</tbody>
</table>
Network Firms and Affiliates

Network Firms

Network firms are firms that cooperate to enhance their capabilities to provide professional services and share one or more of the following:

- a common brand name,
- common control,
- profits or costs,
- a common business strategy,
- professional resources, or
- common quality control policies and procedures.

Must comply with independence rules with respect to clients of other network firms if the use of the audit or review report for the client is not restricted. For all other attest clients, network members should apply the Conceptual Framework.

Use of a Nonindependent Firm

Independence is impaired if partners or professional employees (POPEs) of another, nonindependent firm participate on the attest engagement team.

Members of another firm may work in a manner similar to internal auditors without creating an independence problem so long as the firm complies with AU-C Section 610 (which sets out the rules for the proper relationship between internal and external auditors).
Affiliates
Independence problems can obviously arise if covered members while not having a disqualifying relationship with the attest client, have such a relationship with an affiliate of the client.

Examples of Affiliates
- Client controls the entity
- Client has direct and material financial interest in the entity
- Entity controls the client (which is material to the entity)
- Entity has material and direct investment and significant influence over the client
- A sister entity of a client if the client and sister entity are each material to the entity that controls both

Affiliates
Although there are significant exceptions (which we do not cover here), in general covered members must abide by independence rules for both their attest clients and their clients’ affiliates. There are similar rules (and exceptions) when a firm audits some units, but not all, of related governmental agencies.
Reissues, Engagement Letters, ADR, and Unpaid Fees

Reissued Reports
Covered members or their firms that were independent when they first issued an audit report may reissue that report or consent to its incorporation by reference, even if they are no longer independent.

- Not OK: Performing new procedures that would require updating the date of the original report.
- OK: Making inquiries of successor auditors, reading subsequent financial statements, or undertaking other procedures necessary to assess the effect of new facts on the original report.

Engagement Contractual Terms
Although the SEC and other regulators disapprove of engagement contracts that indemnify auditors for the effects of their own mistakes, it is OK for an engagement letter to require an attest client to indemnify or hold harmless a member firm for liability and costs resulting from the client’s management’s knowing misrepresentations.

But, it is an independence violation for a covered member to agree to indemnify the attest client for losses resulting from the client’s own acts.
**Alternative Dispute Resolution (ADR)**

Engagement letters may require ADR in lieu of litigation to resolve disputes relating to past litigation.

However, like litigation, ADR could place the MIPP and the client in positions of *material adverse interests* and thereby impair independence.

---

**Unpaid Fees**

A MIPP may not sign a current-year audit report if it has unpaid fees from the client for services provided *more than one year prior*.

Fees are “unpaid” even if they are unbilled or if the client has issued to the firm a note receivable.

Exception: Client in bankruptcy.
Financial Interests
Overview and Unsolicited Financial Interests

Overview
If a covered member has or is committed to acquire any direct (whether or not material) or any material indirect financial interest in an attest client, independence is impaired. Only if interests are both indirect and immaterial is independence not impaired.

<table>
<thead>
<tr>
<th>Direct</th>
<th>Material</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indirect</td>
<td>Immaterial</td>
</tr>
</tbody>
</table>
Overview and Unsolicited Financial Interests

Definitions

Financial interest: includes ownership (or an obligation to obtain ownership) in equity, debt or derivatives issued by an entity.

Definitions

Direct financial interest:
- An interest owned directly (even if managed by others)
- An interest under one’s control (even if managed by others)
- An interest beneficially owned through an investment vehicle, estate, trust, or other intermediary when the beneficiary either:
  - controls the intermediary, or
  - has the authority to supervise or participate in its investment decisions.
Definitions

**Indirect financial interest**: A financial interest beneficially owned through an investment vehicle, estate, trust, or other intermediary when the beneficiary *neither*:

- controls the intermediary, *nor*
- has the authority to supervise or participate in its investment decisions.

Definitions

**Beneficial ownership**: Occurs when an individual or entity is not the record owner but has a right to some or all of the underlying benefits of ownership, such as to direct the voting or disposition of the interest or to receive its economic benefits.

Overview

Even if a partner or professional employee (POPE) of a firm is not a covered member, that person (and his or her immediate family, or any group of such persons acting together) cannot own >5% of a client’s ownership interests.
Unsolicited Financial Interests
If covered members receive or learn they will receive an unsolicited financial interest in an attest client (perhaps through gift or inheritance), independence will not be impaired if they dispose of the interest as soon as practicable but within 30 days.

Unsolicited Financial Interests
If CMs do not yet have the right to dispose of the interest (perhaps a relative who wrote a will is still alive), independence will not be impaired if:

- The member does not participate on the attest engagement team, and
- The interest is not material to the covered member.
Mutual Funds and Retirement Plans

Mutual Funds
If a CM owns shares in a mutual fund,
- Interest in fund itself is: direct.
- Interest in underlying investments if own ≤5% of diversified fund: indirect.

Mutual Funds
However, if covered members own >5% of a diversified fund’s shares or own a financial interest in an undiversified fund, then they must evaluate the fund’s underlying investments to determine whether their indirect financial interest in any of the underlying investments is material.
Mutual Funds - Example

*If a nondiversified mutual fund owns shares in attest client Company A, and:

- the mutual fund's net assets are $10,000,000,
- the covered member owns 1% of the outstanding shares of the mutual fund, having a value of $100,000, and
- the mutual fund has 10% of its assets invested in Company A,
- then the indirect financial interest of the covered member in Company A is $10,000 and this amount should be measured against the covered member's net worth (including the net worth of his or her immediate family) to determine if it is material.*

Retirements, Savings, Compensation, or Similar Plans

If covered members or their IFMs self-direct their investments into such a plan or have the ability to supervise or participate in the plan's investment decisions, then the financial interests held by the plan are: direct

Examples

When covered members or their IFMs are a trustee of a plan or otherwise have the authority to supervise or participate in the plan's investment decisions (including through the selection of investment managers or pooled investment vehicles), the underlying investments are: direct.

For self-directed or participant-directed plans (that is, the covered members or their IFMs select the underlying plan investments or select from investment alternatives offered by the plan), the underlying investment interests are: direct.
**Examples (continued)**

If covered members (or their IFMs) do not self-direct or supervise or participate in plan’s investment decisions, the underlying investments are: *indirect.*

When a *defined benefit plan* is involved, interests held by the plan are not considered to be interests held by the covered members unless the covered members (or their IFMs) are trustees of the plan or otherwise have the ability to supervise or participate in the plan’s investment decisions.
Partnerships, 529s, Trust and Estates, Employee Benefit Plans

Partnerships

**General Partnership (GP):** A GP’s interests in a GP and its investments are considered direct financial interests because GPs have authority to influence those investments.

**Limited Partnership (LP):**
- GP interests: both interests are direct, as in GP-ship
- LP interests:
  - In LP-ship: direct
  - In LP-ship’s investments: indirect, unless
    - LP has authority (acting alone or together with firm or other partners) to supervise or participate in investment decisions or,
    - LP has ability to replace the GP.

Limited Liability Company

**Member-managed LLCs:** are much like partnerships and are treated the same for independence purposes.

**Agent-managed LLCs:** interests in investments are indirect, unless the member or members have authority to control the LLC or to supervise or participate in its investment decisions.
Section 529 Plans

**Prepaid tuition plans.** Owner has a direct financial interest in the plan, but only an indirect interest in its underlying investments.

**Savings plans.** Owner has a direct financial interest in both the plan and its investments because he or she decides in which sponsor’s section 529 plan to invest and can determine before investing which firms the plan has invested in.

Trusts and Estates

The fact that a covered member is asked to serve as trustee of a trust or executor of an estate does not by itself create an independence problem just because an attest client’s shares are owned by the trust or estate. However, there is a problem if:

- The covered member has the authority to make investment decisions for the trust or estate;
- The trust or estate owns or is committed to acquiring more than 10% of the client’s equity ownership interest; or
- The value of the trust’s or estate’s holdings in the client exceeds 10% of its total assets.

Grantor

If a covered member acts as a grantor to set up a trust, then its investments are treated as direct financial interests if:

- A covered member has the ability to amend or revoke the trust,
- A covered member has authority to control the trust,
- A covered member has the ability to supervise or participate in the trust’s investment decisions, or
- the underlying trust investments will ultimately revert to covered member as the grantor of the trust,
- If none of these four factors is present, interest underlying investments is indirect.
### Beneficiary

If a covered member is a *beneficiary* of a trust, then:

- **General Rule**: Covered member’s interest is considered direct and his interest in the trust’s underlying investments is indirect.

- **Exception**: If a covered member controls the trust or supervises or participates in the investment decisions, then the underlying investments are considered to be direct.

### Blind Trust

Because the investments will ultimately revert to the grantor and the grantor usually retains the right to amend or revoke the trust, both a blind trust and its underlying investments are considered to be *direct* financial interests of the covered member.

### Participation in Employee Benefit Plans

Independence is impaired if a covered member participates in an employee benefit plan that is an audit client or is sponsored by an audit client.
Participation in Employee Benefit Plans

Two exceptions apply:

1. First, when a covered member is an employee of a government organization that sponsors a benefit plan and the covered member is required by law to audit the plan, then it acceptable to do so if:
   - The covered member is required to participate in the plan as a condition of employment;
   - The plan is offered to all employees in comparable employment positions;
   - The covered member is not associated with the plan in any prohibited capacity [director, officer, employee, promoter, etc.]; and
   - The covered member has no influence or control over the investment strategy, benefits, or other management activities associated with the plan.

2. Second, when the covered member formerly was associated with the audit client but is no longer and has met the requirements, (discussed later in these materials) for preserving independence when making an employment change from attest client to audit firm.
Depository Accounts, Brokerage Accounts, and Insurance Policies

**Depository Accounts**

**Firm**: Firms may maintain depository accounts at a bank that is an attest client if they conclude that the likelihood is remote that the bank will experience financial difficulties.

**Individual**: Individual covered members may maintain such accounts if:
- The balance in the depository account is fully insured, or
- Any uninsured amounts are not material to the covered member’s worth, or
- If uninsured accounts are material, they are reduced to an immaterial amount within 30 days.

**Brokerage Accounts**

A covered member’s brokerage account at an attest client broker-dealer would impair independence unless:
- The attest client’s services were rendered under the attest client’s normal terms, procedures and requirements, and
- Any covered member’s assets subject to the risk of loss* are immaterial to the covered member’s net worth.

*In determining risk of loss, the question is not whether the assets’ market value might decline but whether the client might become insolvent or commit fraud. Protection by regulators and insurance are relevant factors in determining risk of loss.
Insurance Accounts

An insurance policy is not a financial interest unless it offers an investment option. If there is an investment option, then there still would not be an independence problem if the covered member bought the policy under normal terms and conditions.

- Exception: if the covered member had the ability to select the policy’s underlying investment or the authority to supervise or participate in the investment decision, and the covered member invested in an attest client.
Loans, Leases, and Business Relationships

Loans
There may be a problem if a covered member loans to or borrows from:

• Attest client
• Its officers or directors
• 10% holder
• especially if client is not a lending institution

Loans
If the attest client is a lending institution, however, then a loan to covered members (or their IFMs) is permissible if it is an immaterial unsecured loan, a home mortgage, or a secured loan, if:

• Normal lending procedures, terms, and requirements applied;
• The loan was obtained before the lending institution became an attest client, or from a lending institution for which independence was not required and later sold to an attest client;
• The loans are kept current and are not changed (ex: extended maturity dates or lowered interest rate); and
• Estimated FV of the collateral for a mortgage or other secured loan equals or exceeds the outstanding balance during the term of the loan.
• If there is a deficit in the value of the collateral, it cannot be material to the covered member’s net worth.
Loans

If a covered member complies with the loan or lease terms, for example, keeping payments current, then each of the following would also not impair independence:

- Auto loans and leases collateralized by the car
- Loans fully collateralized by the cash surrender value of an insurance policy
- Loans fully collateralized by cash deposits at the same lending institutions (e.g., passbook loans)
- Aggregate outstanding balances from credit card and overdraft reserve accounts of $10,000 or less

Leases

**Capital leases** (leases-to-own) impair independence.

**Operating leases** do not, if:

- The lease meets the GAAP criteria for an operating lease;
- The terms and conditions are comparable with other leases of a similar nature; and
- All amounts are paid in accordance with the terms of the lease.

Business Relationships

**Cooperative Ventures.** Cooperating with an attest client to provide services to 3P is problematic. “Cooperative venture” does not exist if:

- Participation of firm and client are governed by separate contracts that don’t create obligations between them;
- Neither assumes responsibilities for the other’s activities or results;
- Neither has authority to act as other’s agent.
## Business Relationships

Joint financial investments may create an independence problem also.

- **OK:** Firm and attest client both own the stock of a widely-held public company.
- **Not OK:** Both owned material stakes in a small company.
- **Not OK:** A covered member and an officer of an attest client jointly purchased a vacation home.
Family Relationships

Introduction
Two categories of family relationships create potential independence problems

1. Immediate Family Members: spouses, spousal equivalents, and dependents
2. Close Relatives: parents, siblings, and nondependent children

Immediate Family Members
With substantial exceptions that are about to be spelled out, immediate family members of covered members must comply with the same independence rules as covered members themselves.

Irrespective of exceptions below, immediate family members may not cumulatively own >5% of an attest client.
Immediate Family Members Employed by Attest Client
A covered member’s immediate family members may work for an attest client, just not in a key position such as one in which an employee has:
- Primary responsibility for significant accounting functions that support material components of the F/S;
- Primary responsibility for the preparation of the F/S; or
- The ability to exercise influence over the contents of the F/S.
- Can’t be: a member of the BOD, CEO, president, CFO, COO, general counsel, CAO, controller, director of internal audit, director of financial reporting, treasurer, or any equivalent position.

Immediate Family Members Participation in an Employee Benefit Plan
Immediate family members may participate in an employee benefit plan that is an attest client or is sponsored by an attest client, so long as all of the following safeguards are followed:
- The plan is offered to all employees in comparable employment positions,
- Immediate family members do not serve in a position of governance,
- Immediate family members does not have the ability to supervise or participate in the plan’s investment decisions or in the selection of the investment options.

IFM Participation in an Employee Benefit Plan with Financial Interests in an Attest Client
An immediate family member might work for a company that is not an attest client but participate in its employee benefit plan and learn that the plan holds stock of an attest client.
An immediate family member may hold a direct financial interest or material indirect financial interest in an attest client if:
- The covered member is neither on the attest team nor a PTI. [So, an immediate family member could be a 10-hour person or an OPIO];
- Such investment is an unavoidable consequence of such participation; and
- If the plan creates an option that would allow the immediate family member to invest in a nonattest client, the immediate family member should select that option and dispose of the attest client shares as soon as practicable but within 30 days.
Close Relatives
Generally, close relatives of covered members must follow the same independence rules as the covered members themselves, but the restrictions are looser than for immediate family members and they are looser for close relatives of covered members who are not on the engagement team.

Close Relatives
Independence is impaired if the close relative of an audit team member has either of the following:

- A key position with the attest client, or
- A financial interest in the attest client that:
  - The team member knows or has reason to know was material to the close relative, or
  - Enabled the close relative to exercise significant influence over the attest client.

Close Relatives
Independence is impaired if the close relative of a PTI or a OPIO has either of the following:

- A key position with an attest client, or
- A financial interest that:
  - The PTI or OPIO has reason to believe was material to the close relative, and
  - Enabled the close relative to exercise significant influence over the attest client.

There are no restrictions on CRs of 10-hour people.
The focus of the employment rules is upon partners or professional employees (POPEs) of attest firms.

- Can’t work for attest client as: director, officer, employee, promoter, underwriter, voting trustee, or trustee for any pension or profit-sharing trust of the client’s, or in any equivalent management position.

Professors

POPEs may serve as adjunct faculty members at an educational institution that is an attest client so long as these safeguards all apply:

- Does not hold a key position with the client
- Is not on the attest team
- Is not a PTI
- Is on a part-time and non-tenure basis
- Does not participate in any employee benefit plan sponsored by the school, unless participation is required
- Does not assume any management responsibilities or set policies
Honorary Director or Trustee of a Not-for-Profit Organization

POPEs may lend the prestige of their names to a not-for-profit organization that is an attest client if:

- the position is clearly honorary,
- the POPE cannot vote and takes no management role in the organization, and
- all externally circulated materials identify the position as “honorary”.

Campaign Treasurer

Assume a firm’s POPE is campaign manager for a political campaign.

- Can’t audit: the campaign.
- Can audit: the political party of the candidate or the governmental unit which the candidate will head if successful.

Member of Federated Fund-Raising Organization

Assume that a firm’s POPE serves as director or officer of a federated fund-raising organization such as United Way which gives funds to a particular local charity.

- If United Way also controls the charity: can’t audit.
- If United Way does not control: should apply Conceptual Framework.
Former Employment or Association with an Attest Client

Concerns arise when people who are employed by attest clients or who were associated with them as officers, directors, promoters, underwriters, voting trustees, or trustees for a pension fund or profit sharing fund of the clients join the firm as covered members.

Former Employment or Association with an Attest Client

Independence is impaired if one of these people participated on the attest engagement team or became a PTI when the engagement covers any period of time when the person was employed by or associated with the audit client.

Former Employment or Association with an Attest Client

However, if the people become merely OPIOs or 10-hour people, then independence is not impaired so long as they dissociate themselves from the client prior to becoming a covered member.
Dissociation

Dissociation includes all of the following five steps:

1) Ceasing to participate in all employee health and welfare benefit plans sponsored by the attest client, unless the client is legally required to allow the covered member to participate in the plan (e.g., COBRA), and the covered member pays 100% of his or her portion of the cost.

2) Ceasing to participate in all other employee benefit plans by liquidating or transferring all vested benefits in the client's defined benefit plans, defined contribution plans and similar arrangements at the earliest date permitted under the plan.

3) Disposing of any direct or material indirect financial interest in the client.

4) Collecting or repaying any loans to or from the client other than those specifically permitted or grandfathered by the Code.

5) Assessing other relationships with the client to determine if they create threats to independence that would require the application of safeguards to reduce threats to an acceptable level.
Subsequent Employment

Considering Subsequent Employment with an Attest Client
When an attest team member or PTI is considering employment with the attest client, independence is impaired unless the team member:

- promptly reports such consideration or offer to an appropriate person in the firm, and
- removes himself from the engagement until the offer is rejected or the position is no longer sought.

Considering Subsequent Employment with an Attest Client
When a covered member learns that a team member or a PTI is considering employment with a client and has not taken the steps listed above, then that covered member should alert the firm, which must then consider additional procedures needed to provide reasonable assurance of no problems.
Subsequent Employment with an Attest Client

A firm's independence will be considered impaired when a partner or professional employee (POPE) goes to work for an attest client in a key position, unless all of the following conditions are met:

- Amounts due the former employee for previous interest in the firm and for unfunded, vested retirement interests are not material to the firm, and the underlying formula used to calculate payments remain fixed during the payout period. The firm may adjust the retirement benefits for inflation and pay interest on amounts due.
- The former employee is not in a position to influence the accounting firm's operations or financial policies.

Subsequent Employment with an Attest Client (continued)

- The former employee does not participate or appear to participate in the firm's business and is not otherwise associated with the firm, whether or not compensated for such participation. The Codes states that an appearance of participation results from such actions as:
  - The individual provides consultation to the firm.
  - The firm provides the individual with an office and related amenities (for example, secretarial and telephone services).
  - The individual's name is included in the firm's office directory.
  - The individual's name is included as a member of the firm in other membership lists of business, professional, or civic organizations, unless the individual is clearly designated as retired.

Subsequent Employment with an Attest Client (continued)

- The team considers modifying the engagement procedures to adjust for the risk that, by virtue of the former POPE's knowledge of the audit plan, audit effectiveness could be reduced. Additionally, if the individual will have significant interaction with the attest engagement team, the firm should evaluate whether existing team members have appropriate experience and stature.
Subsequent Employment with an Attest Client (continued)

- If the former employee joins the client in a key position within one year of dissociating from the firm, and has significant interaction with the attest team, an appropriate professional in the firm should review the subsequent engagement to determine whether team maintained skepticism. Relevant factors include:
  - the position that the former employee assumed at the attest client,
  - the position that the individual held at the firm, and
  - the nature of the services that the former employee provided to the attest client.

SOX

SOX imposes stricter rules for public companies

- Applies to? Lead partner, concurring partner, or any other member of the attest team who provides >10 hours of attest services.

- Positions to avoid?
  - CEO, CFO, controller, CAO or any equivalent officers
  - any financial oversight role, and
  - any position preparing F/S.

- How long? One-year cooling off period preceding the beginning of the audit.
Other Associations and Relationships

Member of Social Club
If a covered member belongs to a social club, such as a country club, that is an attest client, there should be no independence problem if the membership is primarily a social matter.

Member of a Trade Association
Independence is impaired if:
- A covered member belongs to a trade association that is an attest client, or
- A POPE of a firm is employed by or associated with a trade association in an important role (director, trustee, etc.).
Member of a Common Interest Realty Association (CIRA)

If a covered member buys an interest in a condominium, cooperative or other CIRA, his or her firm may nonetheless audit the CIRA, but only if all of the following safeguards are met:

- The CIRA performs functions similar to local governments, such as public safety, road maintenance, and utilities
- The covered member’s annual assessment is not material to either the CIRA or to her
- The liquidation of the CIRA or sale of common assets would not result in a distribution to the covered member
- The CIRA’s creditors would not have legal recourse to the covered member’s assets if the CIRA became insolvent

Member of a Credit Union

A covered member is eligible to join only because of provision of professional services? Not independent.

A covered member is eligible to join because of individual qualifications? Is independent.

Gifts

Independence is impaired if the firm, a team member, or a PTI accepts a gift from an attest client, unless the value is *clearly insignificant* to the recipient.
Entertainment
May be accepted without impairing independence so long as it is reasonable in the circumstances. The circumstances to be considered include:
• The nature of the gift or entertainment
• The occasion giving rise to the gift or entertainment
• The cost or value of the gift or entertainment
• The nature, frequency, and value of other gifts and entertainment offered or accepted
• Whether the entertainment was associated with the active conduct of business directly before, during, or after the entertainment
• Whether other attest clients also participated in the entertainment
• The individuals from the attest client’s and member’s firm who participated in the entertainment

Actual or Threatened Litigation
Litigation Between Client and Firm/Member. If the client (or its management) sues the audit firm (or vice versa), the key question is whether the firm and client are in threatened or actual positions of material adverse interests. A minor dispute or one not related to the engagement (such as a billing dispute) would not impair independence.

Independence
Independence is impaired if:
• An attest client’s present management sues firm (or probably will), alleging deficiencies in audit work.
• A covered member commences litigation against an attest client’s present management alleging management fraud or deceit.
Actual or Threatened Litigation

Litigation by Client Security Holders. Lawsuits filed by shareholders who claim securities fraud or some other wrong by both the client and the audit firm presumptively do not impair independence unless there are cross-claims with a significant risk of material settlements or judgments.

Other Third Party Litigation. Lawsuits by non-shareholder third parties, such as lenders, are treated similarly.

Actual or Threatened Litigation

Final resolution of the litigation or dispute eliminates the independence threat.
Nonaudit Services
Code Provisions

The Code governs NAS provision to non-public attest clients and to public non-attest clients. Communications about the following topics relate to the audit and are not NAS:

- The client’s selection and application of accounting standards or policies and F/S disclosure requirements;
- The appropriateness of the client’s methods used in determining accounting and financial reporting;
- Adjusting journal entries that the member has prepared or proposed for client management consideration; and
- The form or content of F/S.

Firms should monitor the total amount of NAS provided.
Firms shouldn’t assume management responsibilities.

- **Definition:** “leading and directing an entity, including making significant decisions regarding the acquisition, deployment, and control of human, financial, physical, and intangible resources.”
Examples

- Setting policy or strategic direction for the attest client
- Authorizing, executing, or consummating transactions for client
- Preparing source documents
- Having custody of client’s assets
- Deciding which recommendations of the member or third party to implement

General Requirements

Unless otherwise provided, NAS = OK for attest client if all these general requirements are met:

Client agrees to:

- Assume all management responsibilities.
- Oversee the service, by designating an individual, preferably within senior management, who possesses the skill, knowledge and/or experience to do the job. The member should assess the situation to ensure that the individual is up to the task.
- Evaluate the adequacy and results of the services performed.
- Accept responsibility for the results of the services.

General Requirements

MIPPs do not assume management responsibilities and satisfy selves that management is able to:

- Meet the criteria listed in the previous slide;
- Make an informed judgment on the results of the member’s NAS; and
- Accept responsibility for making the significant judgments and decisions that are the proper responsibility of management.
General Requirements

Before performing NAS, MIPPs establish and document in writing their understanding with the client regarding:

- Objectives of the engagement
- Services to be performed
- The attest client’s acceptance of its responsibilities,
- The member’s responsibilities
- Any limitations on the engagement

Sarbanes-Oxley

SOX limits NAS by saying that MIPPs may not provide certain advisory services to audit clients that are public companies:

Key: MIPPs should not:

- Audit their own work
- Advocate for attest clients
- Serve as client’s managers

Sarbanes-Oxley

MIPPs can’t provide:

- Bookkeeping or other services related to the accounting records or financial statements;
- Financial information systems design and implementation;
- Appraisal or valuation services, fairness opinions, or contributions-in-kind reports;
- Actuarial services;
- Internal audit outsourcing services;
- Management functions or human resources;
- Broker or dealer, investment adviser, or investment banking services;
- Legal services and expert services unrelated to the audit; and
- Any other service that the PCAOB determines is impermissible.
Sarbanes-Oxley
PCAOB: Independence is impaired in tax area if:
- the firm enters into a contingent fee arrangement with an audit client;
- the firm provides marketing, planning, or opinion services in favor of the tax treatment of a “confidential transaction,” or if the transaction is based on an “aggressive” interpretation of tax law; and/or
- the firm provides tax services to members of management who serve in a financial-reporting oversight role for a client (or to their immediate family).

SOX Process
Independent audit committee selects, evaluates and compensates auditor.
Audit committees must pre-approve any permitted NAS (such as tax services) purchased by a company from its auditor.
Specific Services

The Code gives guidance for these NAS:

- Internal Audit
- Appraisal, Valuation and Actuarial Services
- Benefit Plan Administration
- Bookkeeping, Payroll and Other Disbursements
- Business Risk Consulting
- Corporate Finance Consulting
- Executive or Employee Search
- Forensic Accounting Services
- Information Systems Design, Implementation and Integration
- Investment—Advisory or Management
- Tax Services

Example: Internal Audit

Do not impair independence:

- Assessing whether performance complies with management policies
- Identifying opportunities for improvement
- Recommending improvement for mgmt. consideration
Example: Internal Audit

**Do** impair independence:
- Performing ongoing monitoring activities or control activities that affect execution of transactions
- Performing separate evaluations of a significant control such that member is, in effect, performing routine operations built into client's business process
- Having management rely on member's work as primary basis for client's assertions on design of operating effectiveness of internal controls
- Determining which, if any, recommendations for improving internal control system should be implemented
- Reporting to the board or audit committee on behalf of management regarding internal audit affairs
- Approving or being responsible for the overall internal audit work
- Being connected with the client as an employee or in any management position

**Remember**

The **general requirements** must always be met, and **Sarbanes-Oxley** restrictions must always be respected if public companies are involved.
Members in Business

Members in Business (MIBs) are members who are "employed or engaged on a contractual or volunteer basis in an executive, staff, governance, advisory, or administrative capacity in such areas as industry, the public sector, education, the not-for-profit sector, and regulatory or professional bodies."

Generally, MIBs do not need to worry about independence rules, but must follow the other guidelines for MIPPs (objectivity, integrity, etc.)

Threats

Six of the seven types of threats that apply to MIPPs also apply to MIBs:
1. Adverse interest threats
2. Advocacy threats
3. Familiarity threats
4. Self-interest threats
5. Self-review threats
6. Undue influence threats
Safeguards

Safeguards derive from:

- the profession, legislation or regulation, and
- the employer

Integrity and Objectivity

Offering or Accepting Gifts or Entertainment. MIBs should not accept any gifts or entertainment that would violate the law or the policies of the other firm or their own employer. Gifts or entertainment not reasonable in the circumstances would create a violation of the integrity and objectivity rule.

Preparing and Reporting Information. MIBs must never make or direct another to make a false entry, fail to correct inaccurate financial statements or entries, or sign or permit another to sign a document containing materially false information.

Integrity and Objectivity (continued)

Subordination of Judgment. MIBs must follow essentially the same rules that forbid subordination of judgment that MIPPs must obey.

Obligation of a Member to His or Her Employer’s External Accountant. MIBs must be candid and truthful with their employers’ external auditor.

Educational Services. When teaching at a university or performing other educational services, MIBs must act with integrity and objectivity.
General Standards
Like MIPPs, MIBs must:
- Act with professional competence
- Exercise due professional care
- Adequately plan and supervise professional services
- Have sufficient relevant data for any conclusions or recommendations

General Standards
MIBs must also:
- Comply with applicable standards from IRS, SEC, etc.
- Not falsely imply that:
  - F/S submitted to third parties were prepared in accordance with independence rules
  - F/S were prepared in accordance with GAAP

Acts Discreditable
Like MIPPs, MIBs must not engage in discreditable acts, including:
- discrimination and harassment in employment practices,
- solicitation or disclosure of CPA exam Q&A’s,
- failure to file a tax return or pay a tax liability,
- negligence in preparing F/S or records,
- failure to follow applicable standards,
- entering into prohibited indemnification agreements and limited liability provisions,
- improperly disclosing confidential information,
- false advertising
- improper (misleading) use of the CPA credential.
Other Members

OMs are:
- unemployed,
- retired, or
- otherwise not working in the profession.

Other Members

At a minimum, OMs should not act discreditably by:
- Discriminating and harassing in employment
- Soliciting CPA Exam Q&A’s
- Failing to file tax return or pay a tax liability
- Improperly disclosing confidential info
- Falsely advertising
- Improperly using CPA credential
Requirements of SEC and PCAOB

Securities and Exchange Commission (SEC)

SEC Ethics and Independence Rules

How closely do the SEC’s ethics and independence rules resemble those of the AICPA?
Very closely. These two sets of rules usually lead to the same answer.

What qualifications does the SEC require for a CPA to be able to audit a public company?
Must be registered and in good standing under the laws of his or her state
Must be and appear to be independent and capable of exercising objective and impartial judgment
SEC Ethics and Independence Rules

What are the SEC’s primary concerns regarding ethics and independence?
Whether a relationship with or provision of a service to an audit client:

- Creates a conflict of interest for the auditor
- Results in the CPA auditing his or her own work
- Results in the CPA acting as an audit client’s manager or employee
- Places the CPA in a position of being an advocate for an audit client

SEC Ethics and Independence Rules

Does the SEC use the same definitions of “family relationships” as the AICPA?

No, but close.
It defines “immediate family members” (IFMs) the same—spouse, spousal equivalent, and dependents.
But instead of using the term “close relative” (CR), the SEC speaks of “close family members” (CFMs), which include “spouse, spousal equivalent, parent, dependent, nondependent child, and sibling.”
SEC Ethics and Independence Rules

Does the SEC use the AICPA's concept of "covered members" to determine who must follow independence rules?

Close, but the SEC uses slightly different terminology.

AICPA

"Covered Members":
- Audit team members
- PTIs
- 10-hour persons
- OPIOs
- The firm itself
- Any entity controlled by the first five
“Covered Persons”
- Audit team members
- “Chain of command” (PTIs)
- 10-hour persons
- OPIOs

[Not specifically listed, but would undoubtedly be covered:]
- The firm itself
- Any entity controlled by the first five

Financial Relationships

Do direct financial investments in an audit client impair independence?
Yes; the firm, CPs, and their IFMs may not, e.g., own stock in an audit client, even in immaterial amounts.

And a “direct investment” includes one through an intermediary if:
- the firm, CPs, or IFMs either supervise or participate in the intermediary’s investment decisions, or
- the intermediary is a nondiversified mutual fund that has invested 20% or more of its money in an audit client.
### Financial Relationships

**Do investments by someone who is not a CP impair independence?**

Sometimes. Independence is impaired if any partner, principal, shareholder, or professional employee of the accounting firm (and any of their CFMs) own 5% or more of an audit client’s stock.

---

**May the firm, its CPs, or their IFMs serve as trustees of trusts or executors of estates that hold securities of an audit client?**

Not unless they have no authority to make investment decisions for the trust or estate.

---

**May the firm, CPs, or their IFMs own material indirect interests in an audit client?**

No, only interests that are both indirect and immaterial are permitted. Ex: ownership of 5% or less of a diversified mutual fund = immaterial.
Financial Relationships

May the firm, CPs, or their IFMs invest in an entity that an audit client either
(a) has a material investment in, or (b) has the ability to exercise control
over? And vice versa:

Audit
Client ➔ Invests or contro ls ➔ Entity

Entity ➔ Invests or controls ➔ Audit
Client

Financial Relationships

May the firm, CPs, or their IFMs borrow money from or loan money to an
audit client, its officers and directors, or its 10% shareholders?
No, with exceptions:
May borrow from a financial institution under normal procedures and terms:
Auto loan collateralized by the car
Loans fully collateralized by:
  • surrender value of an insurance policy
  • cash deposits at that same institution
Mortgage collateralized by borrower’s primary residence if obtained when
borrower was not a CP

Financial Relationships

May the firm, CPs, or their IFMs have a savings or checking account at a
financial institution client?
Yes, but only if:
• The account balance is fully insured ($250,000 limit) by the FDIC and
• If there is an uninsured balance, the likelihood of the institution
  experiencing financial difficulties is remote.
Financial Relationships
May the firm, CPs or their IFMs have a credit card issued by an audit client? Yes, if the account balance is < $10,000.

Financial Relationships
May the firm, CPs, or their IFMs buy insurance products from an audit client? No. Insurance policies are permitted only if:
• They were obtained before the person became a CP, and
• The likelihood of the insurer becoming insolvent is remote.

Financial Relationships
What about unsolicited financial interests acquired by the firm, CPs, or the IFMs? An unsolicited gift or an inheritance that would normally impair independence is permitted so long as it is disposed of:
• As soon as practicable
• But no later than 30 days after the person learns of the interest and has the right to dispose of it.
Employment Relationships

May a current partner, principal, shareholder, or professional employee of the accounting firm be employed by the audit client or serve as a member of the board of directors?

No!!!!!!!!!!

Employment Relationships

How about family members?
A CFM of a CP may not work at an audit client in:
An accounting role, or
- A Financial Responsibility Oversight Role (FROR)
## Employment Relationships

May an accounting firm employee go to work for an audit client in an accounting or FROR?

No, unless two requirements are met.

1. The individual:
   - Does not influence the accounting firm’s operations or financial policies;
   - Has no capital balances in the accounting firm; and
   - Has no financial arrangement with the accounting firm other than one providing for regular payment of a fixed dollar amount.

2. The individual has served a one-year “cooling-off” period.

## “Cooling-Off” Period

How does the “cooling-off” period work?

It does not apply to:

- Persons who provided 10 or fewer hours of attest services,
- Persons employed by the client as a result of a merger, or
- Persons employed by the client as a result of an emergency.

And the cooling-off period is an entire year before the audit cycle begins.

## Example Question

ABC Co’s audit cycle runs from May 1 through April 30. Bib is on the audit team for ABC and wants to go to work for ABC in an accounting role.

- If he leaves the audit team on February 1, 2020:
- If he leaves the audit team on June 14, 2020:
“Cooling-Off” Period
Can an audit client employee come to work for an accounting firm?
Yes, but only if he or she does not participate in, and is not in the chain of command, the audit of F/S covering any period he or she was employed by the audit client.

Business Relationships
May a CP have a direct or material indirect business relationship with an audit client?
No. But providing services to a client or buying goods and services from a client in the ordinary course of business ≠ a business relationship.
Non-Audit Services (NAS)

May an auditor provide NAS to a public company that is not an audit client or to a private company that is an audit client?
Yes.

Not the following services:
- Bookkeeping services
- Financial information systems design and implementation
- Appraisal or valuation services
- Actuarial services
- Internal audit outsourcing services
- Management functions
- Human resources
- Broker-dealer, investment adviser, or investment banking services
- Legal services
- Expert services unrelated to the audit
Exam Question

According to SEC regulations, each of the following non-audit services will impair an auditor’s independence, except
A. Designing a management information system that aggregates source data underlying the financial statements.
B. Performing an internal audit function.
C. Preparing the audit client’s financial statements that are filed with the SEC.
D. Preparing the audit client’s tax return.

Copyright © 2016 by the American Institute of Certified Public Accountants, Inc., is reprinted and/or adapted with permission.

SEC Ethics and Independence Rules

May an accountant accept contingent fees or a commission from a public company audit client?
No, not for any service or product.

SEC Ethics and Independence Rules

Must public companies rotate their outside audit firms from time to time?
No, but accounting firms must rotate:
• Lead and concurring audit partners every five years (five on, five off).
• Other partners providing more than 10 hours of attest services every seven years (seven on, two off).
• There are exemptions for firms with fewer than five audit clients and fewer than ten audit partners.
SEC Ethics and Independence Rules

What is the role of the audit client’s audit committee? Among other things, it must preapprove:

- Hiring of the auditor and
- The auditor’s provision of NAS.

SEC Ethics and Independence Rules

Does SOX address auditor compensation? Only to say that a firm is not independent if any audit partner earns or receives compensation based on selling NAS to the audit client.

SEC Ethics and Independence Rules

What about firm quality controls? SOX and the SEC provide that an accounting firm’s independence will not be impaired solely because a covered person is not independent, provided:

- The covered person did not know of the circumstances giving rise to the lack of independence;
- The covered person’s lack of independence was corrected as promptly as possible once it became known;
- The accounting firm has a quality control system in place that provides reasonable assurance that independence rules will be complied with.
SEC Ethics and Independence Rules

What does a quality control system look like?

For firms annually auditing more than 500 companies, their quality control system provides such reasonable assurance only if it has the following features:

- Written independence policies and procedures
- An automated system tracking investments of partners and manages that might impair independence
- For all professionals, a system that provides timely information about entities from which the accountant is required to maintain independence
- Firm-wide training on independence

SEC Ethics and Independence Rules (continued)

- An annual internal inspection and testing program to monitor adherence to independence rules
- Notification to all firm employees of the name and title of the member of senior management responsible for compliance with independence rules
- A disciplinary mechanism to ensure compliance
Ethics Requirements of the PCAOB

Sarbanes-Oxley (SOX) enacted several provisions relating to auditor independence (including audit partner rotation, cooling-off periods, etc.) that are covered elsewhere in these lessons.

All PCAOB rules must be approved by the SEC, so its ethics and independence rules are consistent with SEC rules.

AICPA rules are generally consistent with SEC and PCAOB rules, but if the latter are stricter than AICPA rules, they govern for public companies.

Ethics Requirements of the PCAOB

Must auditors of public companies be independent?

Yes. Rule 3520: “A registered public accounting firm and its associated persons must be independent of the firm's audit client throughout the audit and professional engagement.”
Ethics Requirements of the PCAOB

Do contingent fees and commissions impair independence?
Yes. Rule 3521 says that independence is impaired if a firm or any affiliate provides “any service or product” to an audit client in exchange for a contingent fee or a commission.

- A contingent fee is an arrangement where the amount of a fee is “dependent upon a specified finding or result being obtained.”
- Fees fixed by courts or other public authorities and not dependent on a particular finding or result are not viewed as contingent.

Ethics Requirements of the PCAOB

May public company auditors provide tax services to audit clients?
Yes, with limits. Rule 3522 forbids services related to marketing, planning, or opining in favor of tax transactions that are:

- Confidential—a transaction that is offered to a taxpayer under conditions of confidentiality and for which the taxpayer has paid the advisor a fee, or
- Aggressive—a tax transaction position initially recommended by the accounting firm and a “significant purpose” of which is tax avoidance, unless the proposed tax treatment is at least more likely than not to be allowable under applicable tax laws.

Ethics Requirements of the PCAOB

May an auditor provide tax services to an audit client’s FRORs?
No. Rule 3523 provides auditors forfeit independence if they provide “any tax service” to a person in a “financial reporting oversight role” (FROR) at the audit client or to an IFM of such a person.
Ethics Requirements of the PCAOB

Who are FRORs?
People who can or do exercise influence over the contents of financial statements or anyone who prepares them.
Ex: directors, CEOs, presidents, CFOs, COOs, general counsel, CAOs, controllers, directors of internal audit, directors of financial reporting, treasurers, or other equivalent positions

Ethics Requirements of the PCAOB

Are there any exceptions to this FROR rule?
Yes, three. Independence is not impaired if:
1. The person is in an FROR only because he or she is a member of the client’s board of directors.
2. The person is in an FROR only because of a relationship to an affiliate of the entity being audited where the affiliate’s financial statements are not material to the consolidated financial statements of the audit client or are audited by a different audit firm.
3. The person was not in an FROR before a hiring, promotion, or similar change in employment and the tax services are:
   - Provided pursuant to an engagement in process before the change in employment; and
   - Completed on or before 180 days after the employment event.

Ethics Requirements of the PCAOB

Are there any requirements for provision of tax services to an audit client?
Yes. SOX requires preapproval by the client’s audit committee, and Rule 3524 sets out a three-step procedure for seeking such approval, requiring that the accounting firm to:

- **Describe** in writing:
  - The scope of the service, the fee structure for the engagement, and any other related agreement between the firm and the audit client; and
  - Any compensation arrangement or other agreement, such as a referral fee or fee-sharing arrangement between the firm and any person (other than the audit client) regarding the promoting, marketing, or recommending of a transaction covered by the service.

- **Discuss** with the audit committee the potential effects of the services on the firm’s independence; and

- **Document** the discussion.

The three Ds:
- Describe
- Discuss
- Document
Ethics Requirements of the PCAOB

Are the requirements for getting preapproval of other permitted NAS similar to the tax requirements?

Yes. Rule 3525 says that the accounting firm should:

- **Describe** in writing to the audit committee the scope of the service;
- **Discuss** with the audit committee the potential effects of the service on the firm’s independence; and
- **Document** the discussion.

The three Ds:
- Describe
- Discuss
- Document

Ethics Requirements of the PCAOB

How should a firm ensure independence when considering accepting a public company as a new audit client?

Rule 3526 says that it should:

- **Describe** in writing to the audit committee all relationships between the firm and its affiliates and between the client and its FROR employees that “may reasonably be thought to bear on independence”;
- **Discuss** with the audit committee these relationships and their potential effect on independence; and
- **Document** the discussion.

The three Ds:
- Describe
- Discuss
- Document

Ethics Requirements of the PCAOB

Is this independence review an ongoing obligation?

Yes. At least annually with respect to each public company audit client, a firm should go through this three-step procedure regarding existing relationships and affirm to the audit committee in writing that it remains independent.
Ethics Requirements of the PCAOB

Are there any other PCAOB independence rules to keep in mind?

Yes. Rule 3502 provides that public accountants have a responsibility to not—knowingly or recklessly, by action or omission—contribute to violations of:

- SOX provisions,
- PCAOB rules,
- Federal securities laws, or
- Professional standards.

Exam Question

The Public Company Accounting Oversight Board was established by which of the following?

A. The Financial Accounting Standards Board.
B. The American Institute of Certified Public Accountants.
D. The International Accounting Standards Board.
Requirements of GAO and DOL
Government Accountability Office (GAO)

GAO Yellow Book
Who must comply with the ethical and professional requirements of the GAO's Yellow Book?
Those who conduct GAGAS audits of:
• Government entities (e.g., federal, state and local), and
• Entities that receive government awards (e.g., colleges, trade schools, charities, local governments)

GAO Yellow Book
What does the Yellow Book require?
Those who audit pursuant to GAGAS are expected to audit:
1. Independently
2. In accordance with these key ethical principles:
   • The public interest
   • Integrity
   • Objectivity
### GAO Yellow Book

**What does the Yellow Book require?**

3. Proper use of government information, resources, and positions
   - Government information, resources, or positions are to be used for official purposes and not for an auditor's personal gain.

4. Professional behavior, including:
   - Complying with all relevant legal, regulatory, and professional obligations
   - Avoiding conflicts of interest
   - Sensitivity to appearance of impropriety, and
   - Putting forth an honest effort to meet technical and professional standards.

---

### GAO Yellow Book

**How does the Yellow Book differ from the AICPA Code of Conduct?**

- Generally, the two are very similar. If you understand the AICPA's rules and have some common sense, you shouldn't have any trouble with the GAO's Yellow Book.

---

### GAO Yellow Book

**What are the four key parts of the Yellow Book's provisions on ethics and independence?**

- **Conceptual framework for making independence determinations**
- **Requirements for and guidance on:**
  - Independence for audit organizations (AOs) structurally located within the entities they audit;
  - Independence for performing non-audit services (NAS); and
  - Documentation of the auditor's independence.
GAO Yellow Book

What does the GAO mean by “independence”?

Independence of Mind
- Ability to act with integrity, objectivity, and professional skepticism.

Independence in Appearance
- Objective third parties should have no reason to question integrity, objectivity, and/or professional skepticism.

Does the GAO’s “conceptual framework” for answering independence questions resemble the AICPA’s?
Yes.
For example, it involves three steps:
1. Identifying threats to independence;
2. Evaluating the significance of the threats identified, both individually and in the aggregate; and
3. Applying safeguards as necessary to eliminate threats or reduce them to an acceptable level.

Threats to Independence

What threats to independence does the GAO recognize?
1. Self-interest threat
   Ex: Auditor has a financial or other interest in the audited entity or program.
2. Self-review threat
   Ex: Auditor audits source documents she prepared.
3. Bias threat
   Ex: Auditor has political, ideological, or social convictions that could bias the audit.
4. Familiarity threat
   Ex: A close friend or family member is an official in the audited entity.
Threats to Independence

What threats to independence does the GAO recognize?

5. Undue influence threat
   Ex: External party’s threats undermine auditor’s objectivity.

6. Management participation threat
   Ex: Auditor takes management role in audited entity.

7. Structural threat
   Ex: Threat resulting from AO’s placement within a government entity, in combination with structure of the entity being audited.

Structural Threats

What else do we know about structural threats?

Example: Mei is an internal auditor of the Public Welfare Agency and reports her findings to the agency’s head.

Circumstances creating structural threats may also create undue influence and/or management participation threats.

Structural Threats

How is a structural threat reduced to an acceptable level?

Constitutional or statutory safeguards may mitigate the effects of structural threats. For external AOs, such safeguards may include governmental organizations under which the AO is:

- At a different level of government than the audited entity (e.g., federal auditors audit a state government program)
- Placed within a different branch of government (e.g., legislative auditors audit an executive branch program)
Structural Threats
If the head of an AO meets any of the following criteria:
- Directly elected by voters of the jurisdiction being audited
- Elected or appointed by a legislative body and accountable to it
- Appointed by someone other than a legislative body, but confirmed by
  and accountable to a legislative body
- Appointed by and accountable to a statutorily created governing body,
  the majority of whose members are independently elected or appointed
  and are outside the organization being audited

If neither of the above applies, then statutes should do **all** of the following:
- Prevent audited entity from abolishing the AO.
- Provide that if head of the AO is removed, the head of the agency reports
  this to the legislative body.
- Prevent audited entity from interfering with the initiation, scope, timing,
  and completion of any audit.
- Prevent audited entity from interfering with audit reporting, findings,
  conclusions or the manner, means, or timing of the AO's reports.

If neither of the above applies, then statutes should do **all** of the following:
- Require AO to report regularly to a legislative body or other independent
  governing body.
- Give AO sole authority over the selection, retention, advancement, and
  dismissal of its staff.
- Guarantee access to records and documents related to the agency,
  program, or function being audited and access to officials or others as
  needed to conduct the audit.
### Structural Threats

**What about the independence of an internal auditor?**

Internal auditors working under the direction of the audited entity’s management are considered independent if the head of the audit organization meets all of the following:

- Accountable to head of the government entity or to those charged with governance and
- Reports audit results both to the head of the government entity and to those charged with governance

<table>
<thead>
<tr>
<th>Structural Threats</th>
</tr>
</thead>
<tbody>
<tr>
<td>What about the independence of an internal auditor?</td>
</tr>
<tr>
<td>Internal auditors working under the direction of the audited entity’s management are considered independent if the head of the audit organization meets all of the following:</td>
</tr>
<tr>
<td>- Accountable to head of the government entity or to those charged with governance and</td>
</tr>
<tr>
<td>- Reports audit results both to the head of the government entity and to those charged with governance</td>
</tr>
</tbody>
</table>

---

**What about provision of non-audit services (NAS)?**

The Yellow Book has extensive guidelines, but they are very similar to AICPA rules that emphasize:

1. Don’t perform management functions.
2. Ensure that the entity to which you are providing NAS has the expertise to supervise, evaluate, and take responsibility for those services.

<table>
<thead>
<tr>
<th>Structural Threats</th>
</tr>
</thead>
<tbody>
<tr>
<td>What about provision of non-audit services (NAS)?</td>
</tr>
<tr>
<td>The Yellow Book has extensive guidelines, but they are very similar to AICPA rules that emphasize:</td>
</tr>
<tr>
<td>1. Don’t perform management functions.</td>
</tr>
<tr>
<td>2. Ensure that the entity to which you are providing NAS has the expertise to supervise, evaluate, and take responsibility for those services.</td>
</tr>
</tbody>
</table>
Structural Threats

Is documentation important to establishing independence?
Yes, extremely.

To establish independence, auditors should document:

- Threats to independence that require the application of safeguards, along with the safeguards applied.
- Safeguards required if an audit organization is structurally located within a government entity and is considered independent based on those safeguards.
- Consideration of audited entity management’s ability to effectively oversee a NAS to be provided by the auditor.
- The auditor’s understanding with an audited entity for which the auditor will perform a NAS.
Department of Labor (DOL)

Employee Benefit Plans
Employee Benefit Plans (plans) are broadly regulated by the Department of Labor’s (DOL’s) Employee Benefits Security Administration (EBSA) pursuant to the Employee Retirement Income Security Act (ERISA).

Independence: Department of Labor independence rules date to the 1970s and are old-fashioned.

Financial Ties
Independence will be considered to be impaired if during the period of the engagement, at the date of the opinion, or during the period covered by the F/S
Financial Ties

“The accountant or his or her firm or a member thereof had, or was committed to acquire, any direct financial interest or any material indirect financial interest in such plan, or the plan sponsor…”

Financial Ties

Because this provision covers any “member” of an accountant’s firm, its coverage is broader than that of current AICPA guidelines.

“Member”: all partners or shareholder employees in the firm and all professional employees participating in the audit or located in an office of the firm participating in a significant portion of the audit.

Employment Ties

During the same period, the same entities may not be connected to a plan or plan sponsors as:
1. Promoter
2. Underwriter
3. Investment advisor
4. Voting trustee
5. Director
6. Officer
7. Employee of the plan or plan sponsor
Non-audit Services (NAS)

- Rules are loose in this area
- Although an auditor should not audit what it has prepared and therefore may not maintain a plan's financial records, DOL rules do not prohibit provision of other NAS

Prohibited Transactions

Embezzlement has been a traditional problem with benefit plans, so an audit firm should take care not to violate 29 U.S.C. 1106(a)(1)(C), which prohibits certain transactions between a plan and a “party in interest”