



441 G St. N.W.
Washington, DC 20548

August 15, 2013

Lisa A. Snyder
Director, Professional Ethics Division
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Subject: *Comments on the AICPA Professional Ethics Division's Document Entitled "Proposed Revised AICPA Code of Professional Conduct"*

Dear Ms. Snyder:

This letter provides the U.S. Government Accountability Office's (GAO) comments on the American Institute of Certified Public Accountants (AICPA) Professional Ethics Executive Committee's (PEEC) *Proposed Revised AICPA Code of Professional Conduct* (the Code or draft Code). In our view, the proposal's organization into separate parts for members in public practice and members in business separately represents a significant improvement in the Code's clarity. The proposed organization recognizes the Code's users' wide breadth of responsibilities and we expect that all users will find the new Code easier to implement at the individual and audit organization levels. We would like to call attention to a few areas where we believe the revised Code could go further in improving clarity, especially to the extent that the Code applies to accountants in government.

We have provided comments on draft revisions to the Code in prior letters. We will not repeat our prior comments here though we believe those comments remain valid to the extent that they still apply. For your reference, our most recent prior comments were sent to you on October 2, 2012 and November 20, 2012.

Numbering System

We suggest simplifying the numbering system used to identify sections and paragraphs within the Code. While the scheme proposed in the draft may be logical, it does not facilitate easily understandable referencing. Examples of numbering systems that we have found easy to use and that may serve as models include those in the International Ethics Standards Board for Accountants' *Handbook of the Code of Ethics for Professional Accountants* and the AICPA's clarified *Codification of Statements on Auditing Standards*. We also suggest that the Code include specific instructions for users on how to reference its sections and paragraphs in audit documentation. Finally, we suggest that the relevant section number be indicated at the top or bottom of each

page. The current Code is formatted in this way and as a result is much easier to navigate than the draft.

Identification of Principles and Rules

The proposed Code includes principles and rules that are fundamental to an understanding of the AICPA's ethics requirements. Because these principles and rules are so critical to proper application of the Code, we believe that they should be highlighted in a way that makes them easily identifiable and discernable from the remainder of the text. This could be done either by including in the Code a separate list of principles and rules or by printing the principles in boldface type, with the associated rules immediately following in the table of contents, similar to the table of contents in the current Code.

Use of "Should Consider," "Consider," "Evaluate," or "Determine"

The auditor's responsibility in response to the phrases "should consider," "consider," "evaluate," or "determine" is not discussed in the draft Code. The drafting conventions explanation that precedes the Code in the exposure draft does include such a discussion (pages 7 and 8). We suggest that a description of this convention be included in the Code itself or the language conformed to the drafting conventions in the document.

Definition of "Attest Client" (0.400.02)

The draft Code proposes the following definition:

"An attest client is a client that engages a member to perform an attest engagement or with respect to which a member performs an attest engagement."

As written, under some conditions two separate parties will meet the definition of "attest client" for the same engagement. These conditions are quite common in the government environment where, for example, a governmental auditor may perform an audit in response to a request by a legislative committee responsible for spending money in accordance with statutory requirements. As drafted, the "attest client" definition would make it difficult for an auditor working under these circumstances to determine how best to implement the Code's requirements. For example, draft Code section 1.295.040.01 addresses the member's responsibility for assessing the sufficiency of an attest client's skill, knowledge, and/or experience (SKE) to oversee a nonattest service provided by the member. The draft Code does not provide guidance as to which of the two attest clients should be subject to an SKE assessment. The PEEC may want to consider restricting use of "attest client" to refer only to those entities that engage a member to perform attest services. *Government Auditing Standards* uses "audited entity" to refer to an entity with respect to which an auditor performs an

engagement. A distinction between “attest client” and “audited entity” (or a similar term) in the Code would allow for the critical clarification that the auditor is required to assess SKE at the *audited entity*, not the attest client, in the event that the two parties are different and the audited entity is the subject of a nonattest service provided by the member.

Definition of “Client” (0.400.06)

As we have noted in previous letters, the Code’s definition of “client” is problematic, especially as it pertains to auditors in government. We recognize that the AICPA has initiated a project to address the problems with the definition and we look forward to working with the AICPA on a resolution.

Definition of “Threat”

The definitions section of the draft Code includes the definition of “safeguard” but not that of “threat.” We believe that the conceptual link between the two words and their specialized application in the conceptual framework justify the inclusion of both in the definitions. The draft Code appropriately defines “threats” as “Relationships or circumstances that could compromise a *member’s* compliance with the rules.” We suggest that this definition be moved to the “definitions” section of the Code.

Safeguards Implemented by the Firm (1.000.010.22)

We noted that the following safeguard has been added to the list of safeguards implemented by the firm in the draft Code:

“z. Policies and procedures addressing ethical conduct and compliance with laws and regulations.”

As we indicated in our letter dated November 20, 2012, GAO views adequate safeguards as proactive steps taken by an audit organization to eliminate threats to independence or to reduce them to an acceptable level. The proposed additional safeguard and the others on the list are directed at an accounting firm’s policies and procedures and do not emphasize management’s active role in responding to specific identified threats. While we recognize the value of passive safeguards such as documented policies and procedures, it is our view that they can augment but not take the place of active safeguards. From this perspective, providing examples of passive safeguards, without adequately explaining that in many cases such safeguards will not on their own eliminate threats to independence or reduce them to an acceptable level, can lead to misunderstandings by auditors that could result in application of insufficient safeguards. In our earlier letter we suggested that the PEEC revise the list of safeguards to identify those that are passive and therefore cannot be relied upon to eliminate or to reduce to an acceptable level any significant threats to auditor independence if they are not combined with active safeguards. That suggestion applies to the new proposed safeguard included in the draft Code.

Conceptual Framework for Independence (1.210.010)

Consideration of both aspects of independence expressed in the definition, independence in (1) fact and (2) appearance, is key to the appropriate application of the framework for independence. This point would be better made in the description of the conceptual framework by making the following revision to the first sentence of 1.201.010.01:

“It is impossible to enumerate all relationships or circumstances in which ~~the appearance of~~ *independence*, *either in fact or appearance*, *could* ~~might~~ be ~~questioned~~ *impaired*.”

We thank you for considering our comments on these important issues.

Sincerely yours,

A handwritten signature in black ink, appearing to read "James R. Dalkin". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

James R. Dalkin
Director
Financial Management and Assurance