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Draft – Independence Issues Committee Minutes of February 2, 1999 Meeting Public Session

Independence Standards Board. Independence Issues Committee

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February 2, 1999

Draft – These minutes have not yet been approved by the Independence Issues Committee and are subject to change.

**Independence Issues Committee
Minutes of February 2, 1999 Meeting
Public Session**

The Independence Issues Committee (IIC, or the Committee) held a public meeting on Tuesday, February 2, 1999.

The meeting began at approximately 10 AM and was attended by:

Committee Members

Barry Barber
Robert K. Bowen
Edmund Coulson
Kenneth E. Dakdduk
John M. Guinan
Charles A. Horstmann
Robert J. Kueppers
Frank J. Pearlman

Arthur Siegel, Executive Director of the Independence Standards Board (ISB, or the Board), served as Chairman.

Others present by invitation were:

William T. Allen – Chairman, Independence Standards Board (in part, via telephone)
W. Scott Bayless – SEC Staff (in part, via telephone)
Eric Jacobsen – SEC Staff (in part, via telephone)
Susan McGrath – ISB Staff
Richard H. Towers – ISB Staff

New Member

Mr. Siegel opened the meeting by asking the Committee to join him in welcoming Mr. Bowen as the IIC's newest member. Mr. Bowen is replacing Mr. O'Connell, whose term on the IIC recently expired. Mr. Bowen is from Hansen, Barnett & Maxwell, in Salt Lake City, and was nominated for Committee membership by the Executive Committee of the AICPA's SEC Practice Section, in accordance with ISB Operating Policies. The Board approved Mr. Bowen's nomination at its last meeting.

Mr. Siegel summarized Mr. Bowen's extensive experience serving the profession, and stated that Mr. Bowen currently serves on the SEC Practice Section Executive Committee.

Alternative Practice Structures

Mr. Allen joined the meeting via telephone to explain why he believes the Committee's project on alternative practice structures should be converted to a Board project. Mr. Allen stated that the issue was pressing and important. As there was not much literature on point, rather than have the Committee try to apply the existing literature to these structures by analogy, it would be best to have the Board take a fresh look at the issue to determine appropriate independence restrictions, in a fully-public process. Mr. Allen stated that the Board has a policy-oriented position towards open process with public participation.

Mr. Allen said the downside to a Board project would be that some individuals operating in a world of ambiguity would have to continue to do so for perhaps a year, while the Board deliberates the issue and issues documents for public comment. He had, however, balanced this cost against the good emanating from a public process – and that the larger good is having a process that is open in all respects. Mr. Allen urged the Committee to assist the Board and Staff in producing a neutral document outlining the issues for Board consideration.

Mr. Guinan questioned the IIC's charter if it were precluded from issuing timely guidance on emerging matters of current interest to firms and practitioners. Mr. Allen responded that the role of the IIC should not change since this specific matter could be dealt with as a special situation. Mr. Allen did intend to discuss the role of the IIC with the Board.

The IIC Chairman decided to form an IIC task force to assist the Staff in drafting the neutral discussion memo on alternative practice structures requested by Mr. Allen. A broad-based, project task force will also be formed, similar to those formed for other Board projects, to assist in ensuring that documents are balanced and comprehensive.

Minutes

The minutes of the December 15, 1998 meeting were approved unanimously.

Assisting Clients in the Implementation of FAS 133 – IIC Issue Summary 98-1

The Committee continued its discussion on the assistance that auditors could provide their audit clients in the implementation of the Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities*.

Mr. Bayless stated that Mr. Turner, the SEC's Chief Accountant, would like the document to note that the guidance provided is limited to FAS 133 assistance. In response, the Committee added the phrase "solely with respect to the implementation of FAS 133" to the last sentence of paragraph 3, so that it would read as follows:

This consensus provides guidance on the auditor independence implications of likely areas of requested assistance, solely with respect to the implementation of FAS 133.

Mr. Bayless said he was uncomfortable with the phrase "provided that the auditor concludes that management can accept responsibility for the results of the auditor's services," as it implied that the auditor could do anything as long as management accepts responsibility for the work performed. In response, the Committee deleted this language in paragraph 7, and similar language in 11g. The Committee concluded that the language in paragraph 4 on auditing one's own work, and in paragraph 8, which says that "[t]he auditor's independence would be impaired if....the auditor's level of assistance was tantamount to doing the work himself or herself," was sufficient to address the concern.

Additional final language changes were made to the draft consensus on the issue; these changes will be circulated among Committee members following the meeting. The Committee unanimously approved the consensus, subject to clearance of the final language. The consensus, the Committee's first, will be posted to the ISB website in the near future, and presented to the Board for ratification at its next meeting.

New Projects for the Committee's Agenda

The Committee discussed various issues for possible addition to its agenda.

One such issue was whether the auditor should observe independence restrictions with respect to *all* mutual funds in a "fund family," when the auditor audits one or more, but not all, of the funds. (This was referred to as the "sister fund" issue, and often relates to investments by firm benefit plans, such as 401k plans.) Mr. Bayless stated that the SEC Staff had addressed this issue and that the Chief Accountant, in a letter dated January 7, 1999, requested that further consideration of the matter be at the Board level.

After further discussion, the Committee voted unanimously to add the sister fund project to its agenda, subject to Board approval.

Another issue involved the question of *when* a professional other than a partner or manager, after completing work on an engagement, loses his or her “member” status under the independence rules with respect to the client. The Committee voted to add this project to its agenda, as long as the SEC Staff has not expressed a definitive view on the subject (to be determined). There was one vote opposed to the project, and one abstention.

In addition, the Board will be considering a project on the nature of legal services, if any, the auditor can provide to a client without impairing auditor independence. Mr. Siegel called for three volunteers to help determine the scope of such a project. He received several offers, and subsequently appointed Messrs. Coulson, Dakdduk, and Guinan. Input, however, would be sought from all interested IIC members.

ISB Staff Report

Update on Board Activities

Mr. Siegel stated that the Board’s project task force on the conceptual framework was scheduled to meet on Friday to review two draft sections of a neutral conceptual framework discussion memo. The sections cover the objectives of an audit and the objectives of auditor independence.

Mr. Siegel also stated that the Board had issued its first standard, “Independence Discussions with Audit Committees,” which is now available on the website. The Board had also approved, for public exposure, a neutral discussion memo on employment with audit clients, which would be issued shortly. In addition, the Board directed the Staff to prepare an invitation to comment on independence and family relationships between audit firm and client personnel. The Staff will attach a new proposed standard to the invitation to comment, as well as an alternative proposal which the SEC Staff will prepare.

ISB Staff Consultation Activity

At Mr. Siegel’s request, Mr. Towers summarized Staff consultation activity. Since the Committee’s December 15th meeting, 39 informal consultations have been completed, for a cumulative total of 101. These informal consultations are classified by subject as follows:

Family relationships	5
Bookkeeping	5
Other services	4
Unpaid fees	3
Former partners	2

Business relationships	2
Other	<u>18</u>
Total	39

Mr. Towers added that the three formal consultation interpretations issued to date are now available on the website, including the recent interpretation on alternative practice structures.

Mr. Towers then summarized one informal inquiry and the related Staff response that may be of current interest to Committee members, practitioners generally, and to the public. The SEC currently requires certain broker-dealers and others to file a “Year 2000 Plan” with the Commission. This plan must be the subject of an accountant’s report prepared under the Auditing Standards Board’s Statement of Position 98-8 on Year 2000 agreed-upon procedures attestation engagements (SOP 98-8). The specific question was whether an auditor would be independent in performing the agreed-upon procedures, if the auditor had also been previously engaged to *prepare* the subject plan.

The ISB Staff had concluded that independence would be impaired under SEC rules if the auditor both prepared the plan and issued the SOP 98-8 report. The Staff’s threat analysis addressed the questions of whether the auditor would be reviewing his or her own work, or be placed in the position of making management decisions or taking on management responsibilities. In addition, AICPA Ethics Interpretation 101-11, on agreed-upon procedures and attestation engagements, raises a concern when the auditor contributes to the development of the subject matter of the engagement.

Mr. Towers stated that in the future, he will summarize on a generic, “no-name” basis, selected information about informal independence inquiries received and the related Staff responses for the IIC members and for incorporation in the minutes.

Change in December Meeting Date

Due to a conflict with the AICPA’s Annual SEC Conference, the meeting previously scheduled for December 7, 1999 was changed to December 16, 1999. The meeting will begin at 10 AM and will be held at the AICPA’s New York offices.

Next Meeting

The Committee’s next meeting will be held on Tuesday, March 16, 1999 at 10 AM, in the New York offices of the AICPA.

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The meeting was adjourned at approximately 12:15 PM.

Respectfully submitted,

Susan McGrath