



AUD

Auditing and Attestation

CPA Exam Review

2026
Edition

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Auditing and Attestation

Auditing & Attestation

INTRODUCTION	5
Area I: Ethics, Professional Responsibilities, and General Principles	
AUD 1 ETHICS, INDEPENDENCE AND PROFESSIONAL RESPONSIBILITIES	17
AUD 2 PROFESSIONAL SKEPTICISM AND JUDGMENT	71
AUD 3 AUDIT ENGAGEMENTS	77
AUD 4 TERMS OF ENGAGEMENT	99
AUD 5 REQUIREMENTS FOR ENGAGEMENT DOCUMENTATION	113
AUD 6 COMMUNICATION WITH MANAGEMENT AND THOSE CHARGED WITH GOVERNANCE	123
Area II: Assessing Risk and Developing a Planned Response	
AUD 7 ENGAGEMENT QUALITY	137
AUD 8 PLANNING AN ENGAGEMENT	147
AUD 9 UNDERSTANDING AN ENTITY AND ITS ENVIRONMENT	155
AUD 10 UNDERSTANDING AN ENTITY'S CONTROLS	205
AUD 11 MATERIALITY	287
AUD 12 ASSESSING AND RESPONDING TO RISKS OF MATERIAL MISSTATEMENTS, WHETHER DUE TO FRAUD OR ERROR	297
AUD 13 PLANNING FOR AND USING THE WORK OF OTHERS	333
AUD 14 SPECIFIC AREAS OF ENGAGEMENT RISK	345
Area III: Performing Further Procedures and Obtaining Evidence	
AUD 15 USE OF DATA AND INFORMATION	367
AUD 16 SUFFICIENT APPROPRIATE EVIDENCE	393
AUD 17 SAMPLING TECHNIQUES	401
AUD 18 PROCEDURES TO OBTAIN SUFFICIENT APPROPRIATE EVIDENCE	419
AUD 19 SPECIFIC MATTERS THAT REQUIRE SPECIAL CONSIDERATION	441
AUD 20 MISSTATEMENTS AND INTERNAL CONTROL DEFICIENCIES	473
AUD 21 WRITTEN REPRESENTATIONS	485
AUD 22 SUBSEQUENT EVENTS	493
Area IV: Forming Conclusions and Reporting	
AUD 23 REPORTING ON AUDIT ENGAGEMENTS	507
AUD 24 REPORTING ON ATTESTATION ENGAGEMENTS	555
AUD 25 ACCOUNTING AND REVIEW SERVICE ENGAGEMENTS	597
AUD 26 REPORTING ON COMPLIANCE	629
AUD 27 OTHER REPORTING CONSIDERATIONS	635



Introduction

Introduction

Introduction	7
HOW TO BEST USE YOUR COURSE	7
AICPA BLUEPRINTS	9
THE CPA EXAM	10

Introduction

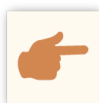
How to Best Use Your Course

Welcome to the UWorld CPA Review course! Our expert team is passionate about helping you succeed and has developed an award-winning program that is proven to yield results. Before you get started, please read through this guide on how to best use your course so that you can master all of the topics laid out for you in the AICPA Blueprints and ultimately pass the CPA Exam. At UWorld, our passion is to make the hard stuff easy to learn and understand.

Plan Your Studies

When preparing for the CPA Exam, half the battle is setting yourself up for success with a solid plan from the get go. This includes establishing short- and long-term goals to ensure you're staying on track.

To get started, use the Study Plan in your course. Start your plan by setting the beginning and ending dates for your schedule. Then select your pace (Fast Track versus Customize) and set the number of hours per day you will study. The system will create your plan based on your choices. It is important to follow your plan steadily so that you can ensure you hit your goals. If you miss a day, make it up!



Tip!

Download the app; this gives you access to everything your course offers even while on the go.

Master the Concepts through Active Learning

With this program, you will build your foundational knowledge and mastery of core exam topics through **active learning**. This evidence-based learning methodology centers around the principle that students retain information best when they actively participate in answering questions.

- **Begin with the Representative Task.** Read through each representative task carefully. (The Representative Tasks are from the AICPA Blueprints and are presented in our books and videos to guide you through the materials.) Pay particular attention to the words at the beginning of the task; they provide guidance on level and focus
- **Scan the book chapter.** Do you feel confident with the material? If you do, you might want to move directly to the questions and begin to practice. If you find that you are hesitant about an area, read the book or watch the video to solidify your understanding before you practice on some questions
- **Watch the videos.** If you prefer to absorb material on video rather than by reading the book, you will notice that the videos are deliberately set up in small segments. Our team created these segments so you can review what you need, either as part of the whole topic or for specific review of a smaller area
- **Practice the questions.** In our question bank (our QBank) we have taken great care to provide you with very high-quality questions and explanations. Each explanation not only tells you why the concept tested is important to understand but also teaches you why the answer is correct and why the other answer choices are not correct. Images, tables, definitions, and TBS Mastery videos also help fill in gaps as you use the questions and explanations to learn by doing

Track Your Progress and Performance

As you complete each chapter, track your progress and performance using our signature **SmartPath Predictive Technology™**. SmartPath is a data-driven platform that provides recommended targets based on those of previous students who have passed the CPA Exam. This is an important tool to help you study efficiently and gauge whether you are *exam-ready*. Your goal is to hit both your progress target (Questions Attempted) and performance target (Score) for each chapter.

As you work through the material, don't worry about hitting your "Score" target right away and focus your efforts on hitting the "Questions Attempted" target first. This approach may feel uncomfortable, but trust that you are building your knowledge as you absorb the answer explanations.

Once you've completed all the topics in a chapter, you can go back and focus your efforts on hitting the "Score" target. If you are falling short, drill down in the Performance tab to see which topics need extra attention.



Tip!

Don't over-study. **SmartPath™** helps determine when you can move on to the next topic.

Solidify the Concepts

Need extra help mastering the concept? Take advantage of the additional learning tools that are integrated into your course. For example, you could be working through a difficult question and find you need further explanation. No problem! There's a link to the supporting lecture right there in the question. Want to remember something for later review? You can easily transfer content directly from the question to a digital flashcard. These are just a few ways we make it easy for you to navigate to and access the right tools at the right time.

These additional tools are designed to enhance your studies—**you do not necessarily need to read or watch all of this material!** Rather, use these tools as a means to improve on any weak areas you might have:

- **Video Lectures** – From the Lectures tab or from the direct link at the bottom of each practice question, you have access to the profession's most motivating and effective lecturers. The lectures break down difficult topics into simplified concepts and provide helpful memory aids. These are especially recommended for visual and auditory learners
- **Textbooks** – The video lectures are accessible side by side with the digital eTextbooks or, in some of our course packages, a printed format. These guides can be used as a reference if you need further explanation of a concept. Many students also find it beneficial to follow along in the textbook while watching the lectures and taking notes, either directly in the physical books or by using the Notes feature and highlighting tool in the platform
- **Digital Flashcards** – Create custom flashcards directly from your practice questions by clicking on the lightning bolt symbol. Depending on your program package, your course may also be pre-loaded with an "Expert Deck" of flashcards covering the most heavily tested topics. You can review all your cards in Study Mode or by using our **spaced-repetition technology**. This is an evidence-based learning method that presents cards you've marked as *difficult* more frequently and cards you've marked as *easy* less frequently. The spacing of how and when the flashcards are introduced has been proven to increase retention and strengthen memory recall

Get Exam-Ready

The final days leading up to the exam are a critical time in which you're going to want to review your SmartPath data and ask, "Am I *exam-ready*?" If you have hit all the targets, you are in a really good spot. However, if any areas are still marked "Needs Improvement," now is the time to focus your efforts on meeting those targets.

We recommend you **take at least one full practice exam before exam day** (click on the "Exam Sim" tab in the QBank). This allows you to hone your test-taking skills in an exam-like environment that follows the same 5-testlet, 4-hour structure as the exam. The Exam Sim pulls questions from the QBank, and there is no limit to the number of times you can create an Exam Sim.

As a final step to assess your exam day readiness, we recommend you take the full-length mock exam. Curated with a unique set of questions not featured in the regular QBank, these practice tests are directly aligned to the content allocation and difficulty level of each CPA exam testlet. We recommend using this feature about 1–2 weeks before exam day.

AICPA Blueprints

The UWorld CPA Review course is based on the AICPA Blueprints, which show candidates what skills and content topics will be tested on the CPA Exam. You don't have to make tough decisions about what concepts to focus on. If you follow our methodology, you will be well on your way to passing the exam.

Let's take a look at what we mean by starting with the AICPA Blueprints. The Blueprints have four levels:

- Area
- Group
- Topic
- Representative Task

Each Representative Task also has a Skill level.

- Remembering & Understanding
- Application
- Analysis
- Evaluation (used only in AUD)

The Table of Contents of the book shows how each UWorld textbook is set up to follow the order of the AICPA Blueprints, with

- Area
- Group
- Topic

In the pages of each book, we provide the Representative Tasks from the AICPA Blueprints. We did that to make a direct connection between the exam and our content. Our team deliberately focused on what the Tasks say and wrote study materials that match with each Task. There is no closer connection between what will be tested and what you are studying.

Beyond connecting to the topics of the AICPA Blueprints, our team also differentiated the textbook content to match the Skill Levels of the Tasks.

- **Remembering & Understanding** tasks require you to understand the definitions and fundamentals of the topic. We have presented the information in these areas with an eye to creating clear explanations of the topics
- **Application** tasks are more about using your knowledge in scenarios to indicate that you understand the concepts. Our authors have therefore provided examples that show you how to apply your knowledge in specific situations. Many of these examples are similar to questions that you will find on the exam
- **Analysis** tasks require a higher level of thinking, many times requiring you to choose one outcome over another or to make a decision. On the exam, these tasks will always be addressed in Task-Based Simulations, or TBSs. The AICPA intentionally makes these more challenging to determine if you really know the material and can work with it as a professional. In our materials, our authors often guide you through the critical thinking required to work with TBSs
- **Evaluation** tasks are only in the AUD section of the exam and are at the highest level of thinking. They go a step further than the Analysis level and require you to evaluate or judge different approaches or outcomes

The CPA Exam

Within the AICPA Blueprints, there is information about how much time candidates have for each section and how many questions each section contains, categorized by question type. Question types include Multiple-Choice Questions (MCQs) and Task-Based Simulations (TBSs).

Section	Section Time	Multiple-Choice Questions (MCQs)	Task-Based Simulations (TBSs)
AUD – Core	4 hours	78	7
FAR – Core	4 hours	50	7
REG – Core	4 hours	72	8
BAR – Discipline	4 hours	50	7
ISC – Discipline	4 hours	82	6
TCP – Discipline	4 hours	68	7

Scoring Weight by Exam Section

The AICPA also shows candidates how the question types for each section are weighted and account for their overall score.

Section	Score Weighting	
	Multiple-Choice Questions (MCQs)	Task-Based Simulations (TBSs)
AUD – Core	50%	50%
FAR – Core	50%	50%
REG – Core	50%	50%
BAR – Discipline	50%	50%
ISC – Discipline	60%	40%
TCP – Discipline	50%	50%

Skill Allocations

As mentioned earlier, each Representative Task is tested at a specific Skill Level, and each part of the exam has its own weighting of the Skill Levels, as seen here.

Section	Remembering & Understanding	Application	Analysis	Evaluation
AUD – Core	30–40%	30–40%	15–25%	5–15%
FAR – Core	5–15%	45–55%	35–45%	–
REG – Core	25–35%	35–45%	25–35%	–
BAR – Discipline	10–20%	45–55%	30–40%	–
ISC – Discipline	55–65%	20–30%	10–20%	–
TCP – Discipline	5–15%	55–65%	25–35%	–

Content Allocations

The AICPA Blueprints address how coverage of the various content areas is allocated in each exam. Using the UWorld system that ties directly to the Blueprint structure, it is easy to see the extent to which each topic is covered.

AUD

Content Area		Allocation
Area I	Ethics, Professional Responsibilities, and General Principles	15–25%
Area II	Assessing Risk and Developing a Planned Response	25–35%
Area III	Performing Further Procedures and Obtaining Evidence	30–40%
Area IV	Forming Conclusions and Reporting	10–20%

FAR

Content Area		Allocation
Area I	Financial Reporting	30–40%
Area II	Select Balance Sheet Accounts	30–40%
Area III	Select Transactions	25–35%

REG

Content Area		Allocation
Area I	Ethics, Professional Responsibilities, and Federal Tax Procedures	10–20%
Area II	Business Law	15–25%
Area III	Federal Taxation of Property Transactions	5–15%
Area IV	Federal Taxation of Individuals	22–32%
Area V	Federal Taxation of Entities (including tax preparation)	23–33%

BAR

Content Area		Allocation
Area I	Business Analysis	40–50%
Area II	Technical Accounting and Reporting	35–45%
Area III	State and Local Governments	10–20%

ISC

Content Area		Allocation
Area I	Information Systems and Data Management	35–45%
Area II	Security, Confidentiality, and Privacy	35–45%
Area III	Considerations for System and Organization Controls (SOC) Engagements	15–25%

TCP

Content Area		Allocation
Area I	Tax Compliance and Planning for Individuals and Personal Financial Planning	30–40%
Area II	Entity Tax Compliance	30–40%
Area III	Entity Tax Planning	10–20%
Area IV	Property Transactions (disposition of assets)	10–20%

Exam Testlets

Each section of the exam is divided into five testlets. Two testlets cover MCQs and three testlets cover TBSs. Not all sections have an equal number of MCQs and TBSs, as the following chart shows.

Section	Testlet					Total	
	1	2	3	4	5	MCQ	TBS
	MCQ	MCQ	TBS	TBS	TBS		
AUD – Core	39	39	2	3	2	78	7
FAR – Core	25	25	2	3	2	50	7
REG – Core	36	36	2	3	3	72	8
BAR – Discipline	25	25	2	3	2	50	7
ISC – Discipline	41	41	1	3	2	82	6
TCP – Discipline	34	34	2	3	2	68	7

Finally, to manage your time effectively in the exam, we recommend that you:

- Use 75 seconds per multiple-choice question as a benchmark,
- Allocate 15–20 minutes per task-based simulation, depending on complexity, and
- Take the standard 15-minute break after the third testlet; it doesn't count against your time.

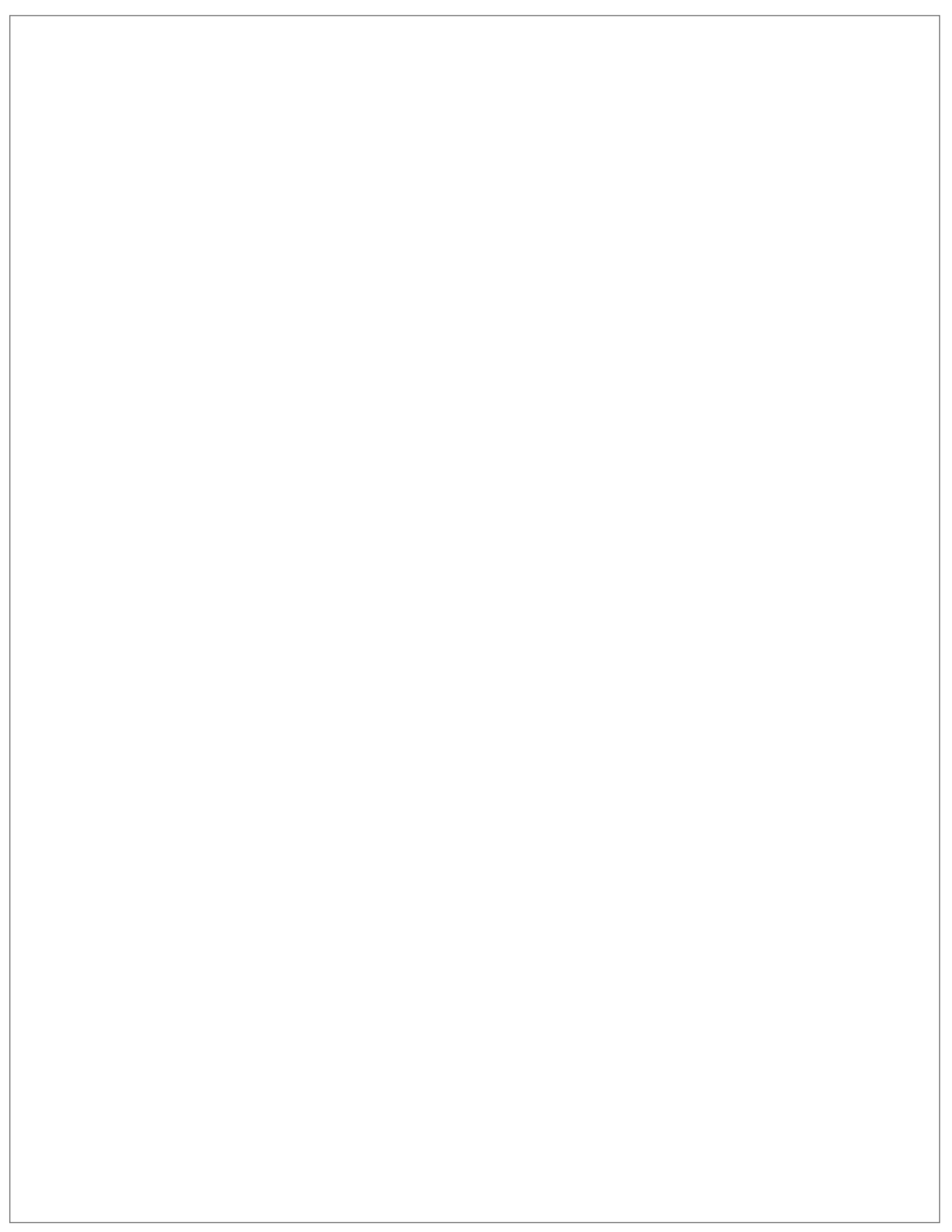
To see the full AICPA Blueprints, visit the AICPA website.

Above all, start the study process with confidence! As Roger always says, "You do not have to be a genius to pass the CPA Exam. If you study, you will pass!" You've got this.



AUD

**Area I: Ethics, Professional
Responsibilities, and
General Principles**





AUD 1
**Ethics, Independence
and Professional
Responsibilities**

AUD 1: Ethics, Independence and Professional Responsibilities

1.01 AICPA Code of Professional Conduct	19
OVERVIEW	19
PREFACE	20
PART 1: MEMBERS IN PUBLIC PRACTICE	21
CONCEPTUAL FRAMEWORK	22
INTEGRITY AND OBJECTIVITY (TOPIC 1.100)	25
INDEPENDENCE (TOPIC 1.200)	29
GENERAL STANDARDS (TOPIC 1.300)	43
ACTS DISCREDITABLE (TOPIC 1.400)	43
FEES AND OTHER TYPES OF REMUNERATION (TOPIC 1.500)	45
ADVERTISING AND OTHER FORMS OF SOLICITATION (TOPIC 1.600)	46
CONFIDENTIAL INFORMATION (TOPIC 1.700)	46
FORM OF ORGANIZATION AND FIRM NAME (TOPIC 1.800)	47
PART 2: MEMBERS IN BUSINESS	48
PART 3: OTHER MEMBERS	49
1.02 Requirements of the SEC and PCAOB	50
OVERVIEW	50
INDEPENDENCE REQUIREMENTS	52
PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD (PCAOB) OVERVIEW	57
PCAOB RESPONSIBILITIES	58
SARBANES-OXLEY (SOX)	58
INDEPENDENCE AND ETHICS RULES	60
1.03 Requirements of the GAO and DOL	64
GOVERNMENT ACCOUNTABILITY OFFICE (GAO) GOVERNMENT AUDITING STANDARDS	64
DEPARTMENT OF LABOR (DOL) AND EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974 (ERISA)	69

1.01 AICPA Code of Professional Conduct

Overview



Representative Task (Remembering & Understanding): Understand the principles, rules, and interpretations included in the AICPA Code of Professional Conduct.



Representative Task (Application): Apply the principles, rules and interpretations included in the AICPA Code of Professional Conduct to situations (eg, maintaining integrity and objectivity and compliance with standards, maintaining the confidentiality of client information when using automated or third-party tools and techniques including artificial intelligence).

CPAs are subject to various regulators such as the SEC or the PCAOB. Each of these agencies, organizations, regulators, and societies has rules and guidelines that affect the behavior of CPAs. One of the most comprehensive is the **AICPA Code of Professional Conduct (Code)**. Many sets of rules and codes of ethics related to accountants are largely based on the Code, which is regularly tested on the CPA exam.

The most severe consequence of violating the Code is losing membership in the AICPA. The rules and guidelines in the Code are obligations specifically for AICPA members.

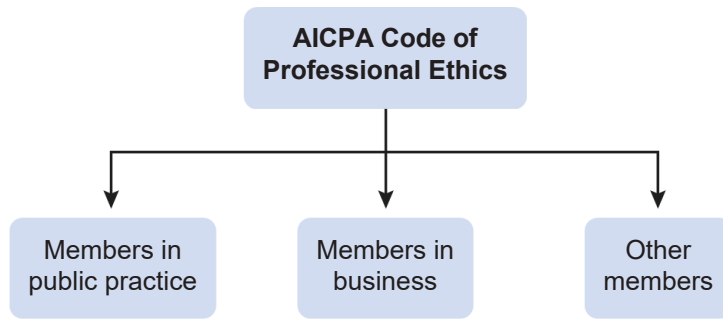
Note that violations of other codes of conduct (state board of accountancy) may result in a prohibition against performing certain types of services, the inability to serve certain regulated clients, or, in some cases, the suspension or loss (revocation) of the CPA certificate. This could result from the commission of a felony or the filing of a fraudulent tax return, whether for the CPA or for a client.

In addition to the Code, a CPA will consider the ethical requirements of all applicable bodies and agencies, which may include:

- State societies
- State boards of accountants and related regulatory agencies
- The SEC, PCAOB, GAO, and DOL
- Taxing authorities

The Code is organized in four parts:

- The Preface, which is applicable to all members
- Part 1, which is applicable to members in public practice
- Part 2, which applies to members in industry
- Part 3, which applies to all other members, including those retired or unemployed



Preface

The Preface is applicable to *all members* and consists of six topics:

Topic 100—Provides:

- An overview, including an explanation of the structure of the Code
- A requirement that members adhere to the Code's rules based on an understanding of the rules and the voluntary actions of the CPA
- An indication that CPAs are expected to follow interpretations, and may be required to justify departures from them
- An indication that, when a CPA has multiple professional roles, the highest and most restrictive level of standards should be applied.

Topic 200: Describes the structure of the **Code** and indicates its **applicability** to the services performed by a CPA. It indicates that, with few exceptions, the Code applies to **all professional services** performed by a CPA, except when rules identify services to which they do not apply.

AICPA Code of Professional Conduct

Topics and Subtopics	Applicable to Members In		
	Public Practice	Business	Other
Preface	X	X	X
Introduction	X	X	X
Integrity and Objectivity	X	X	
Independence	X		
General Standards	X	X	
Acts Discreditable	X	X	X
Fees and Other Types of Remuneration	X		
Advertising and Other Forms of Solicitation	X		
Confidential Information	X		
Form of Organization and Name	X		

Topic 300: Describes the **principles** embedded in the Code. In the preamble, it reminds CPAs of their **responsibility of self-discipline** exceeding the simple compliance with applicable laws and regulations; responsibilities to the public, to clients, and to colleagues; and a commitment to act with honor despite the possibility of personal sacrifice that may result.

- **Responsibilities:** Requires the application of sensitive professional and moral judgment at all times and cooperation with other members of the profession to improve the art of accounting, to maintain the public's confidence in the profession, and to carry out the profession's responsibility for self-governance.
- **Public Interest:** Requires a commitment to professionalism and acting in a manner that serves the public interest and honors the trust that the public has in the accounting profession. The public interest is the collective well-being of the community of people and institutions that are served by the accounting profession, which requires the accountant to act with integrity when confronted by conflicts among various stakeholders and perform services applying integrity, objectivity, and due professional care.
- **Integrity:** Requires that the highest level of integrity be applied through the CPA's honesty and candor, within the constraints of client confidentiality, and an unwillingness to subordinate service or the public trust to personal gain or advantage.
- **Objectivity and Independence:** Requires independence, both in *fact* and in *appearance*, when performing auditing and other attestation services, for which standards require independence, and that the CPA remain free of conflicts of interest and exercise impartiality and intellectual honesty in the performance of all professional services.
- **Due Care:** Requires compliance with technical and ethical standards while continuing to endeavor to improve the CPA's competence and quality of services, which is accomplished through a commitment to learning throughout the CPA's professional life, and diligence in the provision of professional services enabling performance to the best of the CPA's ability. Due care also requires a CPA to remain competent and to understand the limitations to that competence, which may result in consultation or the referral of services, and to adequately plan and supervise all professional activities for which the CPA is responsible.
- **Scope and Nature of Services:** Requires the CPA to evaluate whether or not services can be performed in a manner consistent with the principles of the Code by practicing in a firm with appropriate quality control policies and procedures commensurate with the services being performed; by making certain that services performed for an audit client do not create a conflict of interest; and by making certain that activities in which the CPA participates are appropriate for members of the CPA profession.

Topic 400: Provides definitions of terms that are used throughout the Code.

Topic 500: Specifies that only the Code is authoritative and that guidance provided by the staff of the Professional Ethics Division of the AICPA is nonauthoritative guidance.

Topic 600: Indicates the status of new, revised, or pending interpretations and other guidance. It specifies that new or revised authoritative interpretations and other guidance are effective as of the last day of the month in which the pronouncement or notice is published in the *Journal of Accountancy*.

Part 1: Members in Public Practice

Part 1 is applicable to members in public practice (MIPP), including government auditors. When a CPA is serving both as a MIPP and as a member in business (MIB), both Parts 1 and 2 will apply.

Part 1 presents the **conceptual framework approach** to applying the Code. It provides a member with a means of evaluating compliance with the code when confronted with a decision or other circumstance that is not directly addressed. Applying the conceptual framework approach cannot overcome a clear violation of the rules or interpretations of the Code. It can, however, assist the CPA in determining if the Code has been violated when it is not necessarily clear.

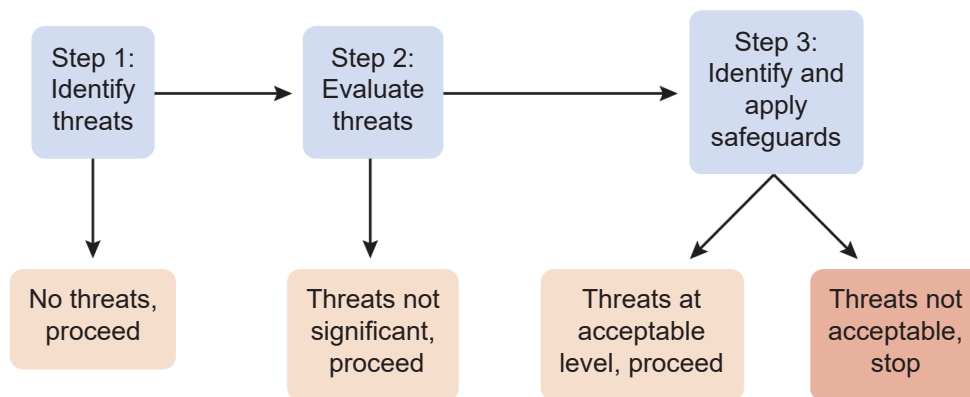
Conceptual Framework



Representative Task (Application): Apply the Conceptual Framework for Members in Public Practice and Members in Business included in the AICPA Code of Professional Conduct to situations that could present threats to compliance with the rules included in the Code.

The conceptual framework approach involves a **3-step process**. Applying the conceptual framework approach cannot *overcome* a clear violation of the rules or interpretations of the Code. It can, however, assist the CPA in determining if the Code has been violated when it is not necessarily clear.

Threats and Safeguards Approach



Threats

There are seven categories of threats identified in the Code. They are **not mutually exclusive** in that a single threat may fall under more than one category. Threats are evaluated both individually and in the aggregate. The threat categories are:

Self-review

The **threat of self-review**, which exists when the accountant performs **some form of evaluation** of matters that were previously influenced by the accountant's judgment, such as when an accountant is performing an attest service in relation to a client's financial statements when the accountant's firm performed bookkeeping services for that client.

The self-review threat is the threat that the **accountant will assume a level of reliability** without performing an appropriate level of testing or other due diligence.

Advocacy

An advocacy threat exists when the accountant's actions effectively **promote a client's interests** or position. For example, the accountant is:

- Providing forensic accounting services to the client in a conflict with third parties.
- Providing investment advice for an officer, director, or shareholder holding 10% or more of the client's shares.
- Endorsing the products or services of a client.

Adverse Interest

The threat of an adverse interest exists when the **interests of the client are in conflict** with the interests of the accountant, which may inhibit the accountant from applying objectivity. This would be the case, for example, if the client and the accountant were involved in, or anticipating, litigation against each other.

Familiarity

The threat of familiarity results from a **close and long-standing relationship** with a client, potentially causing the accountant to become too sympathetic to the client's interests or too trusting of the client's work or products. Examples of the types of relationships that create a familiarity threat include:

- The spouse, a family member, or a close friend of an engagement team member is employed by the client.
- The member has a close and significant business relationship with an officer, director, or significant shareholder of the client.
- Senior firm personnel have a long-standing relationship with the client.

Undue Influence

The threat of undue influence results from attempts by management or others to **exercise an excessive amount of influence** over the accountant. This may involve:

- A client's threat to replace the accountant as a result of a disagreement.
- A client exerting pressure to limit an engagement to reduce fees.

Self-Interest

The threat of self-interest occurs when the accountant has the **opportunity to obtain a potential benefit** from an interest in, or another relationship with, a client. This would be the case if:

- The accountant has a financial interest in the client, the value of which may be affected by the results of the service being performed.
- The accountant enters into an arrangement that involves a contingent fee rather than one that is predetermined.
- The accountant relies excessively on the fees earned from the client.

Management Participation

The threat of **management participation** occurs when the accountant **takes on the role** of management for the client or **performs management functions** on behalf of the client.

Identification of Threats to Auditors' Independence



Safeguards

Safeguards are **controls that eliminate or reduce threats**, ranging from prohibitions against circumstances that create threats to procedures that counteract the potential risk associated with a threat. Safeguards are considered effective if they eliminate a threat or reduce it to an acceptable level.

Three kinds of safeguards exist:

1. Safeguards created by the profession, legislation, or regulation. Examples include:
 - Ethics education, training requirements, and continuing professional education
 - Professional standards and threat of discipline
 - External reviews of a firm's quality controls
 - Legislation regulating firm's professionals
 - Licensure requirements
2. Safeguards implemented by the **client**. The client has, for example:
 - Knowledgeable and experienced managers
 - A tone at the top regarding ethical behavior and compliance
 - Effective policies and procedures for compliance and fair reporting
 - Appropriate ethics policies and procedures
 - Effective governance structure, including an active audit committee
 - Policies to prevent client from hiring a firm to provide services that would impair independence or objectivity

3. Safeguards implemented by the **firm**. Examples:

- Strong leadership emphasizing compliance and acting in the public interest
- Policies and procedures to implement and monitor engagement quality management
- Designation of qualified senior manager to oversee firm's quality control system
- Training and timely communication of firm policies and procedures
- An effective internal disciplinary system
- Rotation of engagement team senior personnel
- Policies precluding partners from being compensated for selling nonattest services to attest client

Integrity and Objectivity (Topic 1.100)

In performance of any professional service, a member shall maintain **objectivity and integrity**, avoid conflicts of interest, and not knowingly misrepresent facts or subordinate their judgment to others.

Conflicts of Interest

Conflicts of interest arise when a CPA is performing professional services related to a matter for two or more clients with conflicting interests or when the interests of the CPA or the CPA's firm conflict with those of the client.

Before accepting an engagement or a relationship, the CPA should **identify a potential conflicts** that threaten independence and objectivity, and should continue to monitor as engagement progresses.

When an **actual conflict is identified** by any member, the Conceptual Framework should be applied and engagements should be refused or terminated if the risk of violation is unacceptably high. In evaluating possible conflicts of interest, members should ask, *Would a reasonable and informed third party conclude that a conflict exists?*



Safeguards may reduce the threat of a conflict of interest to an acceptable level. For example, maintaining separate engagement teams with clear policies and procedures for maintaining confidentiality may be an adequate safeguard to reduce the threat of a conflict of interest to a reasonable level when the conflict arises from performing services for two or more clients with conflicting interests related to the subject matter of the engagements. Additional safeguards include a regular review by a senior manager not involved in the engagement and/or consulting with third parties, such as a professional body or legal counsel.

Conflicts should be **disclosed** to clients and affected third parties, even if threats to compliance are at an acceptable level.

- General disclosure (eg, "We audit several firms in your industry sector") may suffice.
- Specific disclosure (eg, "We advise your closest competitor who would love to have access to your confidential information that we possess") may be needed, however.

Documenting the threat-reducing process is wise.

Members should always comply with federal (including Internal Revenue Service Circular 230), state, or local provisions that are more restrictive than the Code.



Serving as a director on the board of an entity may create a conflict of interest if the entity, such as a bank, enters into or considers transactions with the CPA's clients. The member may consider limiting the relationship to a consulting arrangement, excluding transactions that may involve the CPA's clients. If, however, the CPA does serve as a director, threats and safeguards should be evaluated to make certain that threats are at an acceptable level.

Gifts and Entertainment

Offering gifts or entertainment to a client or accepting gifts or entertainment from a client may create various threats to the CPA's compliance with the Code, including threats associated with self-interest, familiarity, and undue influence.

Objectivity and integrity are threatened if the client (including its officers, directors, and 10% shareholders) gives gifts or entertainment to the firm or its members (or vice versa).

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 or is reckless in not knowing of the violation.

If no rules are violated, then there is no problem if the gifts or entertainment are "reasonable in the circumstances." Factors in determining **reasonableness** include:

- The nature of the gift or entertainment
- The occasion giving rise to the gift
- The cost or value of the gift or entertainment
- The nature, frequency, and value of other gifts
- Whether the entertainment was associated with active conduct of the business

Preparing and Reporting Information

There would be a violation of the Code if a member has:

- Made, permitted, or directed another to make materially false and misleading entries in an entity's financial statements or records,
- Failed to correct misstatements when having the authority to do so,
- Signed, permitted, or directed another to sign misleading documents,
- Exercised discretion with the intent to mislead, or
- When relying on the work of others, either inside or outside the organizations, failed to ensure that the work was useful, honest, and accurate by taking into account such factors as the reputation, expertise, objectivity, and resources available to the third party.

When a member knows, or has reason to know, that information they are associated with is misleading, the member should apply appropriate safeguards to resolve the matter. This process may require talking to supervisors, consulting with professional bodies, and perhaps even considering resigning.

Subordination of Judgment

Differences of opinion between a member and supervisors or other individuals within the member's organization may threaten the member's ability to comply with the integrity and objectivity rule due to the potential subordination of the member's judgment.

A supervisor, for example, may take a position that the member believes is not in compliance with standards, represents a material misstatement of facts, or violates applicable laws or regulations. In this situation, the member should:

- **Evaluate** whether the threat is at an *unacceptable level*, which occurs if the position taken would result in a material misrepresentation or legal violation. If the threat is not significant, then nothing further need be done.
- Discuss the matter with the supervisor if there is a significant threat.
 - If the discussion does not resolve the difference of opinion, the member should go over the supervisor's head.
- 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 policies and procedures have any additional requirements for reporting differences of opinion.
 - Determine whether there is a duty to report to external authorities.
 - Consult legal counsel.
 - Fully document the situation.
- If the member ultimately concludes that the threat of misrepresentation or legal violation cannot be reduced to an acceptable level, **they should consider resigning from the firm and taking appropriate steps** to eliminate their exposure to subordination of judgment.
- Although the code does not require the member to resign, only to *consider it*, it goes on to say that "nothing in this interpretation precludes a member from resigning from the organization at any time."
- Resigning from the firm would not necessarily discharge all obligations, such as to report to regulatory authorities or an external auditor.

Pressure to Breach the Rules

Pressure to breach the rules or ethical conflicts may arise as a result of various circumstances, but most relate to a circumstance where:

- Internal or external pressures create obstacles that interfere with following an appropriate course of action
- Conflicts arise in applying relevant professional and legal standards, such as when reporting suspected fraud may be a violation of client confidentiality rules.

Examples of pressure that could result in breach of the Integrity and Objectivity Rule include the following:

- **Conflict of interest:** Joe is a member working for ABC Sales Co. and is charged with hiring a caterer for the company's events. Joe's supervisor's uncle is a caterer and attempts to convince Joe to accept his bid over similar bids by other caterers.
- **Presentation of information:** Miko is a member working for DEF Co. and her boss strongly urges her to treat personal expenses he has incurred as business expenses so that DEF will reimburse them.
- **Due care:** Member Carlos is an auditor for the GHI accounting firm and his superiors put him in charge of the audit of JKL Corporation. They give him such a small team and such a tight deadline that it will be impossible for him to do an audit that would comply with GAAS in time. When he protests, they say: "Just shut up and get it done."

- **Financial interests:** CFO Mandy, a member of the AICPA, is preparing the annual revenue numbers for MNO Corporation. Her CEO, Tina, reminds Mandy that Tina will receive a huge bonus if revenue targets are met and that there are lots of accountants out there with the qualifications to replace Mandy.
- **Gifts or entertainment:** Member Lia is a tax accountant for PQR Accounting. PQR hopes to be hired by Mega Corporation to prepare its tax returns. Mega's CFO, Tad, will make the hiring decision. Lia's superior, Pat, suggests strongly that Lia buy an expensive and rare vintage milk bottle that Tad collects, and to give it to him secretly.

If a member finds themselves under inappropriate pressure to violate the Code's rules, they may consult with superiors or legal counsel, escalate the matter within the organization, consider resigning, etc.

Client Advocacy

When performing certain nonattest services for a client, such as tax or consulting services, the member may be in **position to act as an advocate** for the client in supporting the client's position on accounting or financial reporting issues to other engagement team members or to standard setters or regulators. These services may **pose threats** to the member's ability to comply with the integrity and objectivity rules that should be evaluated.

Use of a Third-Party Service Provider

Use of a third-party service provider in a professional engagement may expose the third party to confidential information posing a threat to the member's ability to comply with the integrity and objectivity rules.

- Before disclosing confidential client information to a third-party service provider, the member should inform the client, preferably in writing. If the client objects, the member should either not outsource or decline the engagement.

There is no problem if the third-party service provider provides only administrative support (eg, record storage, software application hosting, authorized e-file transmittal services).

Responding to Noncompliance With Laws and Regulations (NOCLAR)

When a CPA becomes aware of or suspects noncompliance with laws and regulations while performing professional services, their ability to adhere to the *Integrity and Objectivity Rule* may be compromised.

Noncompliance, whether intentional or unintentional, includes violations of laws or regulations by a client, management, governance, or individuals acting under the client's direction. The AICPA Code of Conduct defines relevant laws as those that have a direct and material impact on financial statements or are essential to an organization's ability to operate and avoid significant penalties.

To address such situations, the Code establishes **specific responsibilities** based on the nature of the service provided.

Members providing F/S audit or review services are required to:

- Obtain an understanding of the NOCLAR.
- Discuss the matter with the appropriate level of management, and if appropriate, those in governance.
- Advise the client to take appropriate and timely actions to address the NOCLAR.
- Consider if the client understands the legal/regulatory responsibilities arising from the noncompliance and, if not, suggest information sources or obtaining legal advice.
- If required by law/regulation, report to authorities.
- If management's response is considered inappropriate, consider withdrawal.
- Consider whether additional communication may be required in group engagements.
- Document judgments made and actions taken.

Members providing other services:

- Are required to obtain an understanding of the NOCLAR.
- Are required to discuss the matter with the appropriate level of management, and, if appropriate, those in governance.
- Will communicate the matter within the firm if the member's firm is providing financial statement audit or review services to the client or a client component. If the member's firm is not providing financial statement audit or review services to the client or a client component, communication to the firm performing the audit/review is not allowed.
- Are encouraged to document judgments made and actions taken.

Independence (Topic 1.200)



Representative Task (Application): Apply the Conceptual Framework for Independence included in the AICPA Code of Professional Conduct to situations that could present threats to compliance with the rules included in the Code.

A member in public practice shall be independent in the performance of professional services when independence is required by applicable professional standards.

Independence is the ability to **act with integrity and objectivity** and applies to a *covered member and to the member's immediate family*, including the member's spouse or spousal equivalent, and all dependents, whether related or not.

Covered Members Include:

- Members of the attest engagement team
- Individuals in a position to influence the attest engagement
- Partners, partner equivalents, or managers providing 10 or more hours of nonattest services to the attest client within a fiscal year
- Partners or partner equivalents in the same office in which the lead engagement partner for the attest engagement practices
- The firm or the firm's employee benefit plan
- An entity controlled by any of the above or by two or more of the above acting together



For agreed-upon procedure engagements only, covered members are limited to those participating in or directly supervising the engagement and individuals consulting with the engagement team on technical or industry-related issues.

Independence in fact and in appearance is required. Independence in fact refers to independence in mind, the state of mind that enables the member to act with integrity and exercise objectivity and professional skepticism. Independence in appearance addresses the need to avoid circumstances that would make the member look like independence was lacking.

A covered member:

- Must maintain independence for attest services: examinations (including audits), reviews and agreed-upon procedure (ERA) engagements
- Does not need be independent for:
 - Compilations: Independence is expected, but not required; lack of independence must be disclosed
 - Taxes
 - Consultations
 - F/S preparation engagements
 - Other nonattest services, such as bookkeeping or payroll

When events, circumstances, or conditions that might impair independence *are not addressed* directly in the Code, *the member is required to apply the conceptual framework approach*, applied in the same manner as the conceptual framework approach related to the Code itself.



A CPA is considering whether to accept an engagement to prepare financial statements for a new client. Which of the following statements is correct regarding the independence of the CPA?

- The CPA should be independent of the client.
- The CPA is not required to make a determination of whether the CPA is independent of the client.
- The CPA is required to disclose in the engagement report any relationships with the client's personnel.
- The CPA should obtain management's understanding regarding the benefits of an accountant being independent of a client.

Required	Not Required
Attest services: <ul style="list-style-type: none"> • Audits • Reviews • Examinations • Agreed-upon procedures 	Nonattest services: <ul style="list-style-type: none"> • Financial statement preparation • Tax return preparation • Consulting • Compilations*

**Compilations do not require independence but a lack of independence must be disclosed.*

Preparation engagements are *nonattest* services in which CPAs put together financial statements (F/S) and are governed by SSARS. They do not require CPAs to form an opinion or conclusion about the F/S, issue a report, or disclose relationships with client personnel. Because CPAs do not attest to the accuracy or completeness of the F/S in a preparation engagement, they **do not need to be independent**.

Accounting Firms

When a firm is part of a network of firms, all firms within that network are required to comply with the independence rules in relation to an attest client of any of the firms within that network if the use of the audit or review report for the client is not restricted. In other cases, the covered member should consider any threats to independence that the covered member knows of or has reason to believe may be created by the interests or relationships of other firms within the network.

A firm is considered to be part of a network of firms if the **firms cooperate** to enhance their ability to provide professional services through cross referrals and other means **and** has **one or more** of the following characteristics:

Characteristics of Network Firms

- A common brand name or initials that are part of the firm name
- Common control through ownership or management
- Sharing of profit and costs with the exception of certain costs such as those of operating the association and other costs that are not material to the firm
- Collaboration to create a common business strategy that member firms are held accountable for implementing
- Sharing of significant professional resources, such as systems and staff
- Uniform quality control policies monitored and enforced by the association

A member whose independence becomes impaired after the issuance of a report may reissue the report provided the member or the member's firm does not perform procedures associated with updating or dual dating the report.

An indemnification clause in an engagement letter, in which an attest client holds the member harmless from liability resulting from knowing misrepresentations by management, does not impair independence. Independence would be impaired, however, if an attest firm indemnifies an attest client from liability arising directly or indirectly from the acts of the attest client. An alternative dispute resolution clause in an engagement letter would not impair independence.

Unpaid Fees

Unpaid fees for professional services rendered to an attest client can create **self-interest or undue influence threats** to the covered member's independence. Factors considered in evaluating these threats include the significance of unpaid fees, the length of time they have been due, and the attest client's agreement and ability to pay.

Threats are deemed acceptable if unpaid fees are clearly insignificant and relate to services provided **less than one year** before the current-year attest report. Conversely, threats are unacceptable if, when the current-year attest report is issued, the unpaid fees are significant and relate to services provided over a year prior to the report.

Safeguards should be applied to eliminate or reduce threats to an acceptable level (eg, obtaining partial payment before issuing the report or suspending further work for the client).

Determining Fees for an Engagement

The AICPA provides guidelines for determining engagement fees. It emphasizes that the determination of fees, whether for attest or other services, is a **business decision** influenced by the specific facts and circumstances of the engagement and compliance with technical and professional standards.

When nonattest services are also provided to an attest client, these additional services should **not** be considered when determining the attest engagement fee. If a covered member allows the attest engagement fee to be influenced by other services, it poses threats of self-interest and undue influence, potentially impairing independence.

Fee Dependency

When an attest client's total fees (from attest and nonattest services) constitute a *significant portion* of the firm's total revenue, covered members are required to evaluate the potential impact fees can have on independence. This can pose a **self-interest threat** and **undue influence threat** to independence.

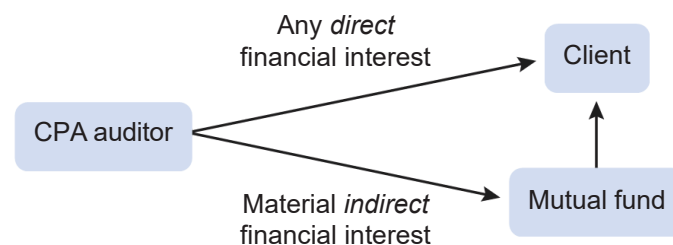
In addition, **long-term relationships** with attest clients with substantial total fees for over five consecutive years require additional safeguards. Safeguards involve external review of attest work either before the issuance of the fifth-year report or between the fifth and sixth-year engagements.

In cases where multiple firms participate in an attest engagement, the involvement of another firm may serve as an equivalent safeguard under certain conditions. These precautions aim to uphold the independence of covered members in the face of financial dependencies on attest clients.

Financial Interests: Overview

In general, a member who possesses or has a commitment to acquire a **direct or material indirect financial interest** in an attest client creates a **self-interest threat** that cannot be reduced to an acceptable level and the member's independence would be impaired.

The same would be true if a partner or professional employee of the firm, including the partner's immediate family or any group of those individuals acting together, owned more than 5% of an attest client during the period of the attest engagement.



Certain other financial interests may or may not create threats to independence that cannot be reduced to acceptable level, impairing independence.

Threats to independence may be reduced to an acceptable level when a member receives an unsolicited direct or indirect financial interest in an attest client, such as through a gift that is not material to the member, if the member applies two safeguards:

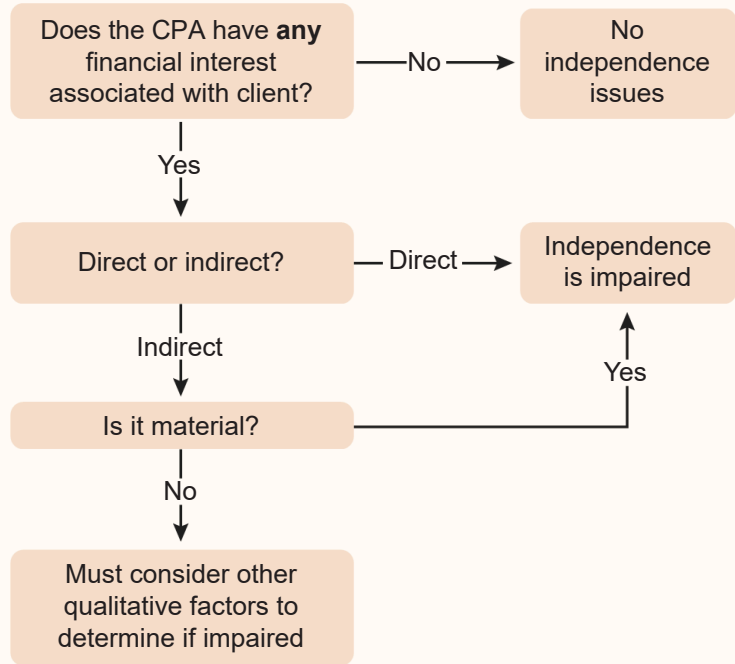
- The financial interest is disposed of **within 30 days** of learning about and gaining the ability to dispose of the interest, or sooner if practicable; and
- The member does not participate on the attest engagement team during the period in which the covered member does not have the right to dispose of a material financial interest.



A CPA in charge of the external audit of a nonissuer received an unexpected inheritance that includes 100 shares of the audit client's common stock. Which of the following actions should the CPA take to avoid violating independence rules?

- Decline to accept the inheritance.
- Petition the AICPA for an independence exception from unforeseen circumstances.
- Resign from the audit firm.
- Sell or donate the stock within 30 days after receipt of ownership rights.

Is Independence Impaired?



CPAs assigned to an attest engagement should not participate in the engagement if they become aware of a material (direct or indirect) unsolicited financial interest related to that client when they do not have the right to dispose of it. CPAs who become aware of—and have the rights to **dispose** of—the interest must dispose of it as soon as practical but **no later than 30 days** after receiving it.

Financial Interests: Mutual Funds

Ownership of shares of a **mutual fund** constitutes a **direct financial interest** in the mutual fund. Ownership of the underlying investments of the mutual fund are indirect. The response to these interests varies depending on the proportion of the mutual fund owned by the member and the diversity of the mutual fund's holdings.

- Ownership of 5% or less of a diversified mutual fund results in an immaterial indirect financial interest in its investments.
- Ownership of more than 5% of a diversified fund, or an ownership interest in an undiversified fund, should be evaluated to determine if the member holds a material indirect financial interest.

Financial Interests: Other

Financial interests in retirement, savings, compensation, or similar firm-sponsored plans may be direct or indirect financial interests, based on circumstances.

A partnership interest is a direct financial interest in a general or a limited partnership.

- A general partner has a direct financial interest in the partnership's financial interests.
- A limited partner has an indirect financial interest in the partnership's financial interests unless the limited partner controls the partnership, supervises or participates in the partnership's investment decisions, or has the ability to replace the general partner or participate in investment decisions, in which case the interest is direct.

An ownership interest in a limited liability company (LLC) is a direct financial interest in the LLC.

- The managing member and those with the ability to control, supervise, or participate in the LLC's investment decisions have direct financial interests in the LLC's financial interests.
- Others without the ability to control, supervise, or participate in the LLC's investment decisions have indirect financial interests.

The account owner of a Section 529 Prepaid Tuition Plan has a direct financial interest in the plan and an indirect financial interest in the underlying investments. The owner of a Section 529 Savings Plan has a direct financial interest in both the plan and its investments due to the ability to view the investment options of different plans prior to selection.

Trusts and Estates

If an estate or trust has any direct or any material indirect financial interest in an attest client, a threat to the member's independence would not be at an acceptable level if the member served as trustee of the trust, or executor or administrator of the estate, during the period of the professional engagement if any of the following also applied:

- The member had the authority to make investment decisions for the trust or estate;
- The trust or estate either owned, or was committed to acquire, an equity interest in excess of 10% of the attest client's outstanding equity securities; or
- The value of the equity interest in the attest client exceeded 10% of the total assets of the trust or estate.

When the CPA is the grantor of a trust, the trust and its investments are considered direct financial interests of the CPA, even if the trust is a blind trust, if the trust's investments ultimately revert to the CPA, or if the CPA:

- Can amend or revoke the trust;
- Has the authority to control the trust; or
- Has the ability to participate in, or supervise, the trust's investment decisions.

If none of those circumstances apply, the CPA has a direct financial interest in the trust and an indirect financial interest in the trust's underlying investments.

Participation in Employee Benefit Plans

When a CPA is a participant in an employee benefit plan that is either sponsored by an attest client or is, itself, an attest client, independence is generally impaired due to the self-interest threat. The threat would be reduced to an acceptable level, however, when the CPA is a participant in a public employee retirement plan that is sponsored by more than one governmental organization, one of which is the employer of the CPA, and the following requirements are met:

- The CPA is required as an employee to participate in the plan, which is offered to all employees in comparable positions
- The CPA does not influence or control key aspects of the plan such as investment strategy, benefits, or other management activities
- The CPA may not serve in a role prohibited by ET 1.275 *Current Employment or Association with an Attest Client*.

When, as a result of an immediate family member's employment, that family member is a participant in a plan that is an attest client or is sponsored by an attest client, the requirements of ET 1.270 *Family Relationships with Attest Clients* are to be complied with.

Depository, Brokerage, and Other Accounts

A firm may have funds on deposit at an attest client that is a bank or similar depository institution without impairing its independence as long as the firm concludes that the likelihood that the institution will experience financial difficulties is remote.

An individual's independence would not be impaired as long as:

- The balance on deposit is fully insured
- The aggregate of uninsured amounts is not material to the individual
- Uninsured amounts that are considered material are reduced to an amount that is not material within 30 days of when it became, or becomes, material to the individual.

When a CPA maintains **brokerage or other accounts** with an attest client that is an insurance company, investment advisor, broker-dealer, bank, or other member of the financial services industry, impairment of independence may be avoided if certain safeguards are in place:

- The attest client is providing services applying its normal terms, procedures, and requirements
- Any risk of loss, such as from the client's bankruptcy, insolvency, fraud or illegal acts, or other circumstances, is not material to the individual after considering protections from federal, state, or other insurers or from other sources.

An **insurance policy** from a stock or mutual life insurance company is not considered a financial interest unless the policy offers the policy holder an investment option. Holding such a policy would create a self-interest threat to independence only if the policy was not obtained under the issuing entity's normal terms, procedures, and requirements.

When a CPA holds an insurance policy with an investment option, independence may be impaired:

- If not obtained under the insurer's normal terms, procedures, and requirements, threats to independence would not be at an acceptable level
- When obtained under the insurer's normal terms, procedures, and requirements, a direct financial interest would be created if the CPA participates in or oversees investment decisions and the self-interest threat would be at an unacceptable level

Loans, Leases, and Guarantees

Loans to or from an attest client, an officer or director of an attest client with decision-making ability or influence, or an individual with a beneficial ownership interest providing significant influence create a *self-interest threat* that may not be at an acceptable level. Unsecured loans that are not material to the CPA's net worth, home mortgage loans, secured loans, and student loans will not raise the threat to an unacceptable level if certain safeguards are all in place:

- The loan was obtained under the institution's normal terms, procedures, and requirements.
- The loan was obtained prior to the institution becoming an attest client; from a lender that was not an attest client but was subsequently sold to an attest client; or prior to the CPA becoming a covered member.
- The loan has been maintained as current at all times as long as the borrower has been a covered member and there have been no changes to the terms of the loan not provided for in the original agreement.
- The estimated value of collateral at least equals the outstanding balance of the home mortgage or secured loan.

Obtaining one of the following from a lending institution under its normal lending procedures, terms, and requirements would *not impair* a CPA's independence as long as the CPA is in compliance with the terms of the agreement at all times:

- Automobile loans or leases collateralized by the automobile;
- Loans fully collateralized by the cash surrender value of an insurance policy or cash deposits at the same institution; or
- Credit cards, retail installment loans, home improvement loans, and overdraft protection with an aggregate balance of no more than \$10,000 after payment of the most recent monthly statement, made within the grace period.

A *lease arrangement* with an attest client would not raise threats to an unacceptable level if all the following safeguards are in place:

- The lease meets the criteria to be accounted for as an operating lease under GAAP.
- The terms and conditions are comparable to other similar leases.
- All payments are made in accordance with the lease terms.

Family Relationships with Attest Clients

Two categories of family relationships can create potential independence problems.

Family Members

- Immediate family members = spouse, spousal equivalent, dependent
- Close relatives = parents, siblings, nondependent children



Immediate Family

In general, members of a CPA's immediate family, which include the CPA's spouse or spousal equivalent, and all dependents, whether related or not, are required to comply with the independence rules to avoid impairing the independence of the CPA. Any financial interests of immediate family members are attributed to the CPA, including when determining the materiality of an indirect financial interest.

Without impairing a CPA's independence, an immediate family member may:

- Be employed by an attest client provided it is not in a key position, which would create the threats of management participation, familiarity, and self-interest.
- Participate in an employee benefit plan that is an attest client or is sponsored by an attest client as long as the family member is not in a key position with the client, the plan is offered to all employees in comparable positions, the family member is not part of the plan's governance, and the family member does not participate in or oversee investment decisions.
- Participate in a retirement plan that is not an attest client or sponsored by an attest client but that holds an investment in an attest client provided:
 - The CPA does not participate in, and cannot influence, the attest engagement;
 - The family member has no other investment options available; and
 - If given the opportunity to invest in a nonattest client or a nonclient, the family member disposes of financial interests in the attest client as soon as is practicable, no later than 30 days after the option becomes available.

Close Relatives

Actions and circumstances related to close relatives, which are parents, siblings, and nondependent children, may also result in an impairment of a member's independence. This would be the case if a *member of the engagement team* has a close relative:

- In a key position with the attest client during the period covered by the engagement or during the period of the engagement
- With a financial interest in the attest client that is known or believed to be material to the relative or enables the relative to exercise significant influence over the attest client.

Independence will be impaired if an *individual in a position to influence the engagement team or any partner or partner equivalent in the office of the engagement partner* has a close relative:

- In a key position with the attest client during the period covered by the engagement or during the period of the engagement
- With a financial interest in the attest client that is known or believed to be material to the relative **and** enables the relative to exercise significant influence over the attest client

Family Relationships and Independence		
Immediate Family	<ul style="list-style-type: none"> • Spouse or equivalent • Dependent (related or not) 	Independence rules same as for CPA, except: <ul style="list-style-type: none"> • Employment by client OK if not in key position • Limited forms of compensation by, and investment in, client acceptable
Close Relative	<ul style="list-style-type: none"> • Parent • Sibling • Nondependent child 	Independence impaired if: <ul style="list-style-type: none"> • Relative in key position with client, or • Financial interest in client material to relative or gives significant influence over client



According to professional standards, which of the following circumstances will impair a CPA's independence?

- An employee at the CPA's firm who works in another state and does not work for the client that she has a material indirect financial interest in.
- The CPA has a car loan with a financial institution client.
- The CPA's dependent stepchild has a direct immaterial financial interest in the client.
- The client recently exceeded the 90-day limit for outstanding unpaid invoices due to the CPA

Independence between CPA and client can be affected by relationships between the CPA's immediate family or close relatives and the client. Close relatives include parents, siblings, and nondependent children (including stepchildren). Immediate family includes spouses and dependents (related or not). A **dependent stepchild** is therefore **immediate family**.

In determining independence, relationships between a CPA's immediate family (eg, dependents) and client are generally treated as if they existed between the CPA and client. **Direct financial interests**, even if immaterial, always **impair independence**.

Current Employment or Association with an Attest Client

When a member is employed or associated with an attest client as a director, officer, employee, promoter, underwriter, voting trustee, or trustee of a pension or profit-sharing plan during the period covered by financial statements or during the period of the professional engagement, the familiarity, management participation, advocacy, or self-review threats will be raised to an unacceptable level and independence will be impaired.



A member may serve as an adjunct faculty member for an attest client educational institution provided the member:

- Is not in a key position with the educational institution
- Does not participate on, nor can influence, the engagement team
- Is employed by the educational institution in a nontenured or part-time position
- Is not a participant in an employee benefit plan
- Does not assume management responsibilities or set policy for the institution

Threats would be at an acceptable level if a member's association with an attest client consisted of:

- Serving as an honorary director or trustee for an attest client not-for-profit organization provided the position is clearly honorary and held in name only
- Serving on the advisory board of an attest client provided the responsibilities are truly advisory in nature
- Serving as the treasurer for a mayoral campaign when the attest client is the candidate's political party or the municipality in which the candidate is running. Independence would be impaired, however, if the campaign organization itself was the attest client.

Independence will not be impaired if a CPA fails to disassociate from an attest client before becoming a covered member if certain safeguards are all met:

- The member discontinues participation in the client's employee health and welfare plans unless the client is legally required to allow the member to participate and the member pays 100% of the cost of participation on a current basis;
- The member discontinues participation in all other employee benefit plans and disposes of all vested benefits from the plan at the earliest date permitted by the plan;
- The member disposes of any direct and any material indirect financial interest in the client;
- The member collects or repays any loans to or from the client; and
- The covered member evaluates whether other relationships with the attest client create additional threats that must be addressed.

A member who leaves a CPA firm to take a key position with an attest client would potentially have created the threat of familiarity, self-interest, undue influence, or management participation. Independence will be impaired unless:

- Amounts due to the member from the firm are not material to the firm;
- The member cannot influence the firm's operations or financial position; and
- The member is not associated with the firm and does not participate, or appear to participate, in the firm's business once employed or associated with the attest client, even if compensated for doing so.

Employment with Audit Client

Prior to leaving:

- Must inform audit firm of conversations with client about possible employment
- Immediately be removed from the audit
- Once removed, the audit firm should consider whether additional work might be needed in the areas performed by the departed auditor

After employed by the audit client:

- Audit firm should consider modifying the audit plan
- Assure remaining audit team is objective
- The next annual audit should be separately reviewed by an audit firm professional uninvolved in the audit

Memberships

Although memberships do create or enhance threats associated with management participation, self-review, and self-interest, they do not necessarily impair independence.

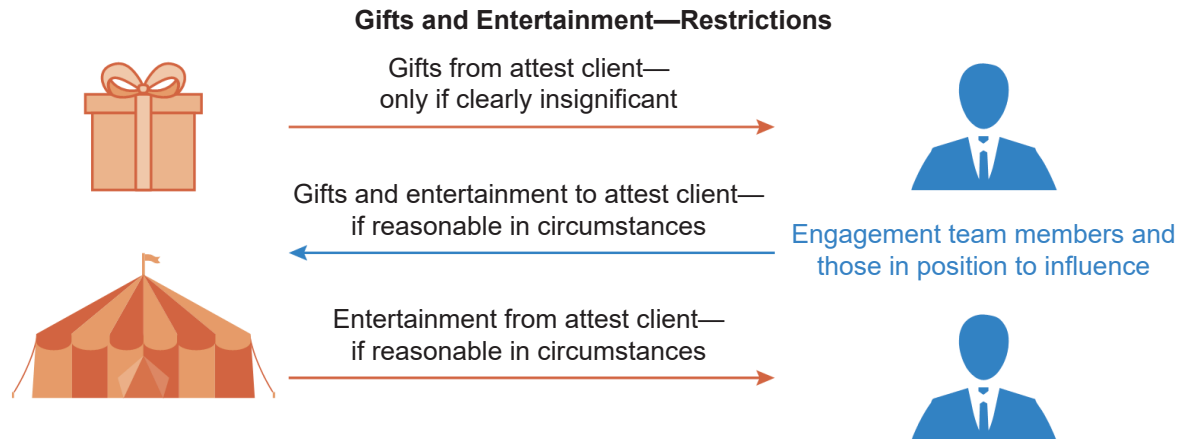
- A pro rata share of a club's equity or debt securities held by a CPA belonging to an attest client social club would not be considered a direct financial interest if the club membership is essentially a social matter.
- Membership in an attest client trade association would not impair independence unless the CPA serves in an inappropriate position, such as a director, officer, or employee during the period covered by the financial statements subject to the attest engagement or during the period of the engagement.

Subject to those restrictions related to depository accounts and loans, membership in an attest client credit union would not impair the CPA's independence if membership was based on the CPA's qualifications or characteristics other than providing professional services to the credit union.

Gifts and Entertainment

Offering a gift to, or accepting a gift from, an attest client, an individual in a key position with an attest client, or an individual with a beneficial ownership interest providing significant influence over the attest client may impair independence if the threats of undue influence or self-interest are increased to an unacceptable level.

To avoid impairing independence, the firm, a team member, or someone in a position to influence are subject to restrictions.



In determining whether "reasonable under the circumstances," the CPA will consider factors such as the nature of the item, the occasion giving rise to it, the cost or value, similarities with other gifts or entertainment offered or accepted, etc.

Actual or Threatened Litigation

Litigation, whether actual or the expressed intention to begin litigation, may create an adverse interest or a self-interest threat that could be at an unacceptable level. The materiality of such actual or threatened litigation to the CPA, the CPA's firm, and to the client should be evaluated by the CPA in making a determination. Whether or not independence is impaired will depend on the facts and circumstances surrounding each situation and will require the CPA to apply professional judgment.

Some, but not all, actual or threatened litigation between a CPA and an attest client will impair independence. Independence will not be impaired by litigation that is not related to the client's attestation engagement and is not material to either the CPA or the attest client.

Any threats to a CPA's independence due to actual or threatened litigation are eliminated when the parties reach final resolution and the matter no longer affects the relationship with the attest client. This is a matter of the CPA's professional judgment.

Performance of Nonattest Services

Many CPA firms provide a variety of nonattest services for their attest clients, the most common of which include bookkeeping, tax compliance, and nontax disbursement services such as payroll services. The performance of nonattest services may create *self-review*, *management participation*, or *advocacy threats to independence*.