Standards for CPAs - State-Specific Ethics

Important Ethical Concepts, Principles and the Rules for CPAs in Tennessee

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Important Ethical Concepts, Principles and the Rules for CPAs in Tennessee

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On-Site Ethics Training

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Standards for Tennessee CPAs
Important Ethical Concepts, Principles and the Rules for CPAs in Tennessee

Course Objectives:

Upon completion of this course you will:

- Understand the importance of complying with ethical standards.
- Understand the AICPA Code of Professional Conduct.
- Understand ethical behavior and how to respond to various situations.
- Understand the various sources of ethical guidance.
- Understand ethical responsibilities of the Tennessee CPA.

Introduction

Recent corporate scandals have damaged the public's trust in our profession. As a result, the AICPA, Security and Exchange Commission (SEC), Public Companies Oversight Board (PCAOB) federal and state government regulators, state societies and others have promulgated rules and regulations designed to eliminate (or at least limit) such situations in the future. Accordingly, CPAs face new rules and regulations that are to be followed in the performance of professional services in addition to pronouncements concerning accounting treatment for transactions and auditing standards. Our profession considers our commitment to a Code of Professional Conduct as one of our greatest hallmarks. The Code consists of principles, which set the standards for rules governing how members provide professional services. Our profession was founded on the principles of honesty, trustworthiness, doing what is right, remaining free of conflicts and delivering our services with integrity and reliability. Adherence to the Code of Professional Conduct is mandated by our license. It sets us apart from those who are non-certified.

The rules that apply depend on the client entity. For example, if you are providing attest services to a private entity requiring independence you are required to follow the rules of the AICPA, your state accountancy board and your state society. If your client is a publicly traded entity you are required to follow the rules of the AICPA, the SEC, the PCAOB, your state board of accountancy and your state society.

Your integrity and objectivity are called into question when your independence is impaired. Your services have value as long as your integrity is above reproach and your reputation for impartial views remains intact.

We are challenged with ethical issues throughout our professional career and often the path we should take may not always be apparent. In such situations, it is important to be knowledgeable with regard to our Code of Professional Conduct and its interpretations. The principles of the Code of Professional Conduct are designed to guide us in the performance of our professional responsibilities. They express the basic
tenets of ethical and professional conduct. The Principles call for an unswerving commitment to honorable behavior, even at the sacrifice of personal advantage.

Having a Code of Conduct is valuable only if it is communicated consistently throughout our profession. We must review our ethical culture regularly and insure that it deals with the issues currently facing our profession. Adherence with any code or set of rules must become a part of our normal behavior. We need to focus on it day by day as issues and situations challenge us. The spirit of the Code must become engrained in our decision process.

Organizational ethics are established by individual adherence within any organization. Management must set the example and should expect no less than complete compliance with the stated organizational ethics guidelines and its rules and regulations. The tone must be set within the organization and adherence to the rules should not be optional. We consider the integrity and ethics of our audit clients as part of our evaluation of internal control. It is reasonable to expect that the ethical standards of the management of our firms would have a similar impact on the quality of our work.

Some of the questions we might ask are, why do good people make bad decisions? What are the external forces that affect an individual’s decision-making process? What is professional skepticism, and how do I apply it in my auditing and accounting engagements? With so many rules and regulations to follow how do I keep up with them all? How do I develop and maintain a code of ethics in my organizations? How do I respond when I believe the actions of my colleagues are unethical? What resources are available to help me make the right ethical decisions?

One might ask, “Am I required to follow the AICPA’s Code of Conduct if I am not a member of the AICPA?” In most cases the answer is yes. Many state boards of accountancy (including Tennessee) have adopted the AICPA Code of Professional Conduct for its licensees, and most state societies (including Tennessee) have adopted the AICPA Code of Professional Conduct as the Code to be followed by their members. Whether one is a member or not, when faced with a challenge to one’s conduct, the AICPA’s Code of Professional Conduct is often the yard stick by which one’s behavior is measured. Therefore, all CPA professionals should be familiar with and adhere to an established Code of Conduct. If not for themselves, for the benefit and welfare of our profession.

A violation of professional ethics will make the CPA subject to disciplinary action. The CPA’s professional ethics affect the confidence of the public and the reputation of our profession.

In today’s climate all accountants must develop ethical competencies. Today’s challenges place each of us in an important role with unique opportunities. We must accept our role and make our contribution to foster an ethical environment for all CPAs. We must appreciate the ethical issues common to our engagements and know the proper value-oriented responses to our ethical dilemmas. The development of such an ethical basis for decisions is a personal task that requires conscious effort and thoughtful consideration. Each individual’s ethical behavior affects all CPAs, whether
such behavior is positive or negative. Because of this, we have a shared responsibility to see to it that all who call themselves CPAs conduct themselves in an ethical manner.

The AICPA and the Tennessee Society of Certified Public Accountants are committed to increasing awareness of ethical issues among their membership and assisting professionals in implementing the high ideals of our profession.

This course is designed to expand your knowledge and understanding so that you will know what to do when faced with ethical issues. It is designed to help answer some of those tough ethical challenges; to help you know where to turn; whom to consult and what resources are available; and what should be your next step when faced with an ethical dilemma.
Chapter 1: Introduction to Ethical Behavior

Objective:

- Understand the importance of complying with ethical standards.

Ethics involves more than compliance with policies, laws and regulations. Each of us has the ultimate responsibility for our actions. Ultimately, you are the person who must decide if and when your actions are ethical. Self-evaluation is a critical component of understanding ethics and even a more focused concept called Business Ethics.

Think about it – When is it ok or acceptable to be unethical? As S. J. Lewis stated, “Defining unethical is kind of like defining pornography: you know it when you see it.” What is the meaning of ethics? What does it mean to be ethical? These questions often present a real challenge. Any attempt to define ethics often leaves many questions unanswered. What rules or laws apply? Who decides under whose rules we shall be judged?

Simply stated, ethics involves learning the difference between right and wrong and then doing the right thing. Webster defines ethics as “standards of professional conduct and business practices adhered to by professionals in order to enhance their profession and maximize idealism, justice and fairness when dealing with the public, clients and other members of their profession.” Webster defines “laws” as “bodies of rules governing members of a community, state, organization, professional, etc., and enforced by authority or compelling legislation.”

Ethics has also been defined as the “science of morals.” A moral is defined as an accepted rule or standard of human behavior. The challenge is often who decides what is “accepted” or “acceptable.” Because standards of human behavior are as varied as the planet’s cultures and geo-political societies, what may be “acceptable” behavior in one culture might be morally reprehensible to another. Because of the existence of a moral element in any ethics discussion, it is easier to say what an ethical person will not do, rather than what an ethical person will do.

This “negative” type of definition leads to all sorts of rules that build an ethical “fence” around us, leading to the feeling that as long as we are within the bounds of the rules, we are acting in an ethical manner. Unfortunately, ethical behavior has many positive elements that require us to act in certain situations instead of sitting idly by, to take positions that might be considered controversial by others who don’t share our personal ethical view of a situation; or to call to task those whose actions we find unethical. Therefore, ethical behavior is not limited to following rules and regulations, but in putting moral restraints on our personal desires and acting in a manner that follows the spirit of the guidelines.
Ethics CPE is now a requirement in Tennessee, but for Tennessee CPAs, ethics-based training is more than just another regulatory mandate. According to the Tennessee State Board of Accountancy it an inspirational reminder of how important ethics and integrity are to the profession.

In 2006, the Tennessee State Board of Accountancy adopted new rules mandating that Tennessee CPAs devote at least four (4) hours of Continued Professional Education every two years in ethics training. Beginning in 2012, Tennessee licensees must take two (2) hours of state-specific ethics continuing education during each reporting period (two years) as part of the 80 hour continuing professional education requirement.

We as a profession should go beyond the minimal requirements and embrace ethics as a vital part of being the best at what we do. To be a good CPA, we must not only be technically competent, but also ethical in our professional responsibilities.

Of equal importance is a review of ethical rules and regulations which are involved in the delivery of accounting services. It is not simply enough to think about the laws and rules, but to go beyond. Until the accounting profession acknowledges that the standards establish the floor and not the ceiling of what is required, we will continue to struggle with this issue. We must embrace and accept ethics as an essential and vital part of being good at what we do. The profession must consider what we should be doing rather than just meeting the basic requirements.

When dealing with ethical dilemmas one may encounter two styles of recognizing and resolving ethical dilemmas, Ethic of Justice and Ethic of Care. An “ethic of justice” is based on principles such as justice, fairness, equality or authority. People with this style of dealing with ethical dilemmas tend to place a great deal of weight on rules, laws and policies, which they believe should be applied equally. They usually resist making exceptions based on special circumstances and are concerned about setting a precedent.

An “ethic of care” is founded on a sense of responsibility to reduce actual harm and suffering. People with this style generally struggle with a conflict of duties or responsibilities. They believe the focal point to every ethical dilemma is the person or people involved and the particular circumstances involved. Solutions are therefore tailored to the specific details of individual circumstances. In some circles, this concept is referred to as “situational ethics”. Making exceptions is easier and individuals with an ethic of care often feel constrained by rules that are supposed to be enforced without exception. Equity seems to be an objective, often doing what is appropriate under the circumstances. This often results in arbitrary results, focusing on decisions tailored to the individuals involved.
Imagine that one day a partner in the firm walks in with a copy of your chief competitor's bid on a large new client. He swears he got it legally, but you are not quite sure. (Your lack of confidence is likely founded in whether you have doubts about his honesty, suggesting his past behavior has been less than honorable.) Even if he did or did not come by it honestly, it still contains proprietary information. Are you going to use it in developing your bid? If you are successful in obtaining the work for the potential new client, you stand to receive a substantial increase in responsibilities and pay.

What if a salesman is up against some very tough year-end objectives, but he can make it if he creates a fictitious sales invoice. When the goods are delivered the next year and the customer calls to see why the order was received, he will just have them returned for a full credit. Should he do it? Is anyone harmed?

These dilemmas have two things in common; how they are handled can dramatically help or hurt your organization; and they are ethical issues. How would you want people in your company to handle these situations? What has the company done to let them know what they should do? What have you done to help them do the right thing? What should be the motivation for your employees’ actions?

Ethical problems are inevitable at all levels of your business. It is simply good sense for companies to take seriously the task of institutionalizing ethics within the company. Such tools as: Codes of Conduct, ethics training, anonymous employee hotlines, etc. are tools toward developing a corporate ethics program.

Let’s now explore what steps we can take to better understand our role when it comes to ethical behavior…
Chapter 2: The Value of a Professional Code of Ethics

Objectives:

- How does a professional code of ethics protect the public?
- To whom are we responsible?
- How does applying ethical rules and applying ethical concepts affect one’s thought processes?
- What about ethics in the workplace?

Business ethics is defined as “What is right or wrong in the workplace and doing what is right.” It goes beyond merely following the rules and laws. Following the rules, regulations and laws is better defined as obedience or being legalistic. Following all the traffic laws no more makes you an excellent driver, than following all the regulations and rules makes you an ethical person.

Ethical behavior is more about who you are, than what you do. Values such as respect, fairness, integrity, and honesty are considered moral values and how they are applied are sometimes called ethical principles. But can ethics be reduced to a series of laws or rules? If Roe v. Wade has taught us anything, it is that laws and rules may exist and be enforced, but people may still believe those laws and rules to be unethical.

The distinction between business ethics and personal ethics is not always clearly defined. Individuals bring their personal values to their work place and filter the challenges that confront them at work through their own ethical view. So then how would you define business ethics? It has come to mean different things to different people. Unfortunately there is no clear ethical compass to guide us through the complex dilemmas when choosing right from wrong.

Today's global economy and instant information have created even more questions and issues as we attempt to resolve and understand a broad spectrum of international issues. Events including the failures of Enron, WorldCom, and Adelphia have resulted in the passage of new rules and regulations and the creation of an oversight process in an attempt to get control of the ethics issue. In today’s post-Sarbanes-Oxley age, companies must achieve a heightened degree of oversight of their ethics programs. As they face greater scrutiny from regulators and investors and risk their personal liability if their program fails.

When you closely examine the underlying issues leading up to such failures, you begin to understand that it was not the failure of accounting rules and principles, or the failure of legal regulations and statutes, but rather a failure of a moral standard. Some would argue that no laws or rules were broken until the moral code was broken. However, less attention is being given to ethical behavior. Andrew Sigler, CEO of Champion puts
it this way, “an ethical company will in the short run and in the long run be a better institution….Ethical behavior is simply good business.”

If the established policies do not resolve the ethical dilemma, consider the following:

♦ Discuss the issue with the immediate supervisor. If this does not lead to a resolution, submit the issues to the next higher managerial level.
♦ Clarify relevant ethical issues with an objective advisor.
♦ Consult your own attorney as to legal obligations and concerns.
♦ If a satisfactory resolution cannot be reached, consider resigning from the organization and notify appropriate parties.

Companies must exercise an elevated degree of oversight of their compliance and ethics programs in this post Sarbanes-Oxley world. Business leaders face increased scrutiny from investors and regulators. They risk personal liability if their company’s program falters, putting increased pressure to ensure the program is effective.

For many years ethics has been a subject of philosophical study and debate. It was not until the 20th century that this modern concept we call “business ethics” truly emerged. As private enterprise has prospered and accumulated great wealth, it has become a powerful segment of our economy. At times, many have abused this power. The ethical foundations of these enterprises have had great influence upon their economy. It is no wonder that ethics has become a critical business issue.

The Human Resource Institute’s 2003-2004 Major Issues Survey found that among North American companies ranking 120 different issues, “ethics in business” was among the top three most important in terms of its impact on workforce management. Other conclusions included:

♦ The number one reason for running an ethical business, today and in the future, is protecting a company’s reputation.
♦ Maintaining an ethical business environment has become more important and more challenging in today’s fast-changing global marketplace.
♦ The pressure to meet unrealistic business deadlines or objectives is the factor most likely to cause people to compromise ethical standards in companies.
♦ Business scandals have had a major impact on business ethics issues in recent years but, in the future, globalization and competition will be the top business drivers of ethics.
♦ Laws and regulations are, and will remain, the most influential external drivers of corporate ethics, but issues related to the environment are expected to become considerably more important.
♦ As technologies grow ever more powerful and pervasive, they will raise difficult ethical questions with which companies will have to deal.
Globalization brings many ethical challenges, especially in developing nations where issues related to forced labor, child labor, and working conditions are top concerns.

Corporate culture is crucial to creating and maintaining an ethical environment, but culture is notoriously difficult to shape and change.

Leaders who support and model ethical behavior and communicate such values are critical to a company's ethics.

Establishing codes of conduct and training programs are seen as the most important corporate practices for contributing toward an ethical culture.

The best way of encouraging ethical conduct among suppliers is through codes of conduct and audits.

Business Ethics Survey 2005 found the factors likely to cause people to compromise ethical standards are:

1. Pressure to meet unrealistic business objectives/deadlines;
2. Desire to further one's career;
3. Desire to protect one's livelihood;
4. Working in environment with cynicism or diminished morale; and
5. Improper training/ignorance that the act was unethical.

Surveys have concluded that corporate culture is among the most important factors affecting the conduct of employees. On the other hand, the corporate culture created by companies can have an opposite effect. Surveys have found that employees of companies that have “strong ethical cultures and full formal programs are 36 percent less likely to observe misconduct than employees in organizations with weak culture and full formal programs” (Harned, Seligson & Baviskar, 2005).

It is the responsibility of everyone within the organization, not just the owners or managers, to act ethically. Ultimately, we are all responsible for our behavior. Setting the example can be a good place to start. Such behavior reflects on who we are and what we stand for. When it comes to integrity and ethics, everything is important, even the little things.

ETHICS – THE CORPORATE CHALLENGE

Setting the Tone at the Top

Management is not only responsible for the establishment of a culture of honesty and integrity, they must also set the example. Management has the ability to influence the behavior and activities of their employees. They must walk the walk and talk the talk. This concept is so important that the AICPA Quality Control Standards require that firms implement policies and procedures to set a proper quality tone at the top and to ensure that the firm follows relevant ethical guidelines.
In most engagements there are certain responses or actions that are discretionary and other areas where rules and procedures must be adhered to more precisely. We can see examples daily how someone made a poor ethical decision that caused disaster in a company. One decision can impact thousands of people. It is therefore critical to seek guidance and input from others and continually do what’s right and ethical.

The discretionary aspects of business include situations where there is room for compromise, bargaining or negotiation within traditional boundaries. It is often the boundaries which establish the non-discretionary aspects of business. It is in these, the non-discretionary areas, where codes of conduct, regulations, laws and rules offer guidance as to the proper response. In these situations, compromise is generally unacceptable.

When one examines companies with a strong commitment to ethics, one notices that the leaders are the strongest advocates of corporate integrity. Management is clear and vocal about their expectations for ethical actions. If commitment is displayed at the top, one of the first characteristics of companies strong on ethics is the existence of a formal and evident ethics program.

Successful programs communicate corporate values, describe acceptable behavior, provide resources, include codes of conduct, ethics workshops, hotlines and board level ethics committees. The central focus of such programs is a set of standards which defines acceptable behavior, conflicts of interest, and acceptable conduct in business affairs. Violations of such standards carry mandatory sanctions which range from warnings, demotions and temporary suspensions to discharge.

Don’t assume that everyone knows all the rules and regulations. Every employee should be informed of these standards and may participate in “ethics awareness workshops.” A critical part of the most successful programs is a hotline that employees can use to report unethical behavior.

An important part of implementing a successful ethics program is devising a statement describing a company’s standards. The most thorough ethics programs include a code of conduct and a corporate philosophy statement.

Codes of conduct are usually short, specific and simple. They set out dos and don’ts about specific problem areas and identify acceptable and unacceptable behavior. They should address conflicts of interest, proprietary information, gifts and entertainment, relations with customers, relations with vendors and confidential inside information. They may address what is clearly illegal and inappropriate behavior and what is acceptable behavior. It is critical that companies who establish codes of conduct enforce them. Otherwise everyone will assume that they are a charade.
What is not addressed in the code of conduct is generally covered in the corporate philosophy statement. The corporate philosophy statement generally expresses the company’s general values and thereby sets the tone.

Let’s now take a look at the AICPA Code of Professional Conduct.
Chapter 3: The Code of Professional Conduct

Objectives:

- The AICPA Code of Professional Conduct
- Understanding the difference between rules and principles
- How should CPAs respond to ethical dilemmas

AICPA CODE OF PROFESSIONAL CONDUCT

CPAs licensed or registered in Tennessee should be aware that where the law and rules are silent, the AICPA Code of Professional Conduct has been adopted. Therefore Tennessee CPAs should be familiar with the AICPA Code of Professional Conduct, even if they are not a member of the AICPA.

The AICPA ethics pronouncements can be thought of as a pyramid.

A. Principles

The six principles of the code of professional conduct provide the conceptual framework for the code. They are the cornerstone of ethical behavior.
B. Rules

The rules of the code of professional conduct are more specific than the six principles. Members must observe these rules.

C. Interpretations

Interpretations are issued by the AICPA to better explain the code of professional conduct. Only the principles and rules are considered part of the code of professional conduct. Interpretations explain the code but are not part of it.

D. Rulings

The rulings apply to the rules of conduct and interpretations to particular circumstances. AICPA members who depart from such rulings must justify their departure.

E. Your Behavior

The code. Interpretations and rulings are meaningless if they do not impact your behavior. For this reason, your behavior is at the top of the pyramid.

PRINCIPLES

The principles of the Code of Professional Conduct

I. Responsibilities
   In carrying out their responsibilities as professionals, members should exercise sensitive professional and moral judgments in all their activities.

II. The Public Interest
   Members should accept the obligation to act in a way that will serve the public interest, honor the public interest and demonstrate commitment to professionalism.

III. Integrity
   To maintain and broaden public confidence, members should perform all professional responsibilities with the highest sense of integrity.

IV. Objectivity and Independence
   A member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities. A member in public practice should be
independent on fact and appearance when providing auditing and other attestation services.

The principle of objectivity imposes the obligation to be impartial, honest and free of conflicts of interest. If a potential conflict of interest exists, you should consider the following:

1. Consider whether you believe you can perform the service with objectivity.
2. If the answer is no, you should decline the engagement. If yes, the next question you should consider is whether, in your professional judgment, other persons (client, third parties, employer) believe you can perform the service with objectivity.
3. If no, you should decline the engagement, if yes you must disclose the relationship with all relevant parties. You should note that you are required to maintain the confidentiality of your client’s information when making disclosures under this rule. If the relevant parties agree, then you can perform the services. If they do not agree, you should decline the engagement.

It should be noted this rule does not apply to attestation services that you or your firm provide. The impairment of independence cannot be eliminated by disclosure or permission.

V. Due Care
A member should observe the profession’s technical and ethical standards, strive continually to improve competence and the quality of services and discharge professional responsibility to the best of the member’s ability.

VI. Scope and Nature of Services
A member in public practice should observe the Principles of the Code of Professional Conduct in determining the scope and nature of the services to be provided.

When providing non-attest and attest services you are required to document your understanding with the client. Documentation can be in the form of an engagement letter or memo. Such documentation should include the scope of services being performed. While failing to document the understanding with the client would be considered a violation of Rule 202, Compliance With Standards, it generally would not impair independence as long as the understanding with the client was established.

These articles establish the basis for characterizing the responsibilities the CPA has to clients, colleagues and the public at large. The fundamental theme of the six articles is to be committed to honorable behavior, even at the sacrifice of personal advantage.
Public Trust - One of the Principles is to recognize our responsibilities to the public, who rely on our objectivity and integrity to make financial decisions. We run the risk of ignoring the public trust that is implied in all our services, even if we are dealing with so-called “private” businesses. For CPAs, the world of clients has now been divided into “registered” and “unregistered” companies, with the attendant rules and regulations that accompany those designations. Even for those “unregistered” companies, there is still a public trust element that must be considered. Comparative data between private companies is used for various purposes in accounting, for example.

Integrity - Integrity is another one of the Principles that we must consider in all our service to our clients. Integrity can be defined as wholeness, cohesiveness, or something’s purity, but these terms have to do with structural or mechanical integrity. In our discussion of a CPA’s professional ethics, we are dealing with a term that is harder to define.

As with objects, integrity for the person may be defined as a completeness of self, which is whole and cannot be corrupted by outside forces. This may sound hollow and empty, especially when one considers that there have been some very immoral things done by persons of integrity as defined here. Integrity defined this way requires the person to determine what course of action is most important and then pursue that course without deviation. To devote oneself in such a manner would constitute a completeness of self, and therefore could be interpreted as acting with integrity, no matter how immoral the act or consequences. For example, a salesperson could have a singular devotion to selling a product and become so focused on that goal that the person would do anything, including lying, to sell the product. That person may have a singleness of purpose, but most people would not refer to that person as having integrity.

Integrity may also be defined as being steadfast in one’s commitments, despite personal desires or changing opportunities. To limit integrity’s definition to this type of description eliminates some of the core fundamentals of character that we admire. Again, this approach can result in a singular focus on a person’s commitment to a cause or course of action, no matter how warped or immoral that course of action might be. Such blind devotion may not require significant thought or consideration of others, which is a hallmark of a person of integrity. Again, the authors would submit that most people do not limit their consideration of integrity to a blind commitment to a course of action.

Integrity can be looked at as putting moral restraints on a person’s commitments. This approach has merit, but doesn’t quite go far enough. Mark Halfon describes integrity in terms of a person’s dedication to the pursuit of a moral life and their intellectual responsibility in seeking to understand the demands of such a life. This leads Halfon to admit that, because morality can be different for different people, it is possible, for example, for a Nazi bent on genocide of the entire Jewish people to be a person of moral integrity. Halfon thinks it possible, but not at all likely (Halfon 1989, pp. 134-36).

As used in the Code of Professional Conduct, however, integrity includes a balancing of many of the attributes discussed above. It balances the desires of the individual with the best interests of others. It has a moral element that considers honest differences of
opinion, but not deceit, subordination of principle, or elevation of personal gain or advantage above the public trust. It therefore has a moral element, which makes it easier to say what a person of integrity will not do, rather than what a person of integrity will do.

Article III of the Rules of Professional Conduct says that “integrity requires a member to observe both the form and the spirit of technical and ethical standards; circumvention of those standards constitutes subordination of judgment.” Included in this mix of attributes are objectivity, independence and due professional care.

Objectivity – According to the Code, this attribute requires a CPA to be “impartial, intellectually honest, and free of conflicts of interest.” This objectivity should permeate a member’s dealings with clients or the member’s employer if not in public practice. This objectivity calls for us to be candid and tell the truth, no matter how uncomfortable that may be. This is especially true in the audit and other attest functions, which are the main services for which a CPA is licensed.

Independence – Without an independent attitude, objectivity becomes much more difficult, if not impossible. So much has been written about independence of mind and action in the wake of the corporate accounting scandals that we should all be familiar with the issues. However, as is so often the case when such scandals happen, rules have been implemented to assist the CPA in determining whether or not the CPA is independent. These rules have specific application in specific circumstances, but there are many other times when CPAs do not have specific guidance to rely on when determining whether or not they are independent. A narrow reading of the specific rules that is designed to find some sort of “loophole” that would allow a desired behavior violates the integrity requirement that requires us to “observe both the form and the spirit of technical and ethical standards”.

Creditors, investors and financial decision makers rely on our profession to provide objective and independent decisions concerning financial information. It is our responsibility to make sure we provide an objective assessment of a client’s circumstances. Your firm’s policies and procedures should help you maintain independence. Compliance with the independence requirements depends primarily on your understanding and interpretations of the policies and rules and your willingness to follow them.

Ultimately it is your responsibility to comply with the various independence rules. One objective of this course is to give you a better understanding and appreciation of the independence rules so you can better apply these rules in practice.

Due Care – In a professional setting, the requirement for due professional care sets a high standard, especially since it is not necessarily an objective measurement. According to the Code, competence and diligence are hallmarks of due care. Competence refers to a “mastery of the common body of knowledge”, “a commitment to learning and professional involvement” throughout one’s career, and the ability to recognize when consultation or referral is required to best serve the client and the public. We are all responsible to evaluate our own competence. “Diligence imposes the
responsibility to render services promptly and carefully, to be thorough, and to observe applicable technical and ethical standards."

Scope and Nature of Services – Our services are to be consistent with our abilities and in accordance with the principles discussed above. Judgment is required to determine the appropriate scope and nature of services consistent with professional standards. This is a subjective area by design. It is clear, however, that the scope and nature of our services must first be in compliance with the principles discussed above.

RULES

The following definitions are used in the Rules of Professional Conduct:

Practice of Accounting – The practice of accounting consists of a performance for a client, by a member or a member’s firm, while holding out as CPA(s), of the professional services of accounting, tax, personal financial planning, litigation support services and those professional services for which standards are promulgated by bodies designated by Council.

However, a member or a member’s firm, while holding out as CPA(s), is not considered to be in practice of public accounting if the member or the member’s firm does not perform, for any client, any of the professional services described in the preceding paragraph.

Professional services – Professional services include all services performed by a member while holding out to be a CPA.

Below is a list of applicable rules:

Rule 101 Independence
Rule 102 Integrity and Objectivity
Rule 201 General Standards
Rule 202 Compliance with Standards
Rule 203 Accounting Principles
Rule 301 Confidential Client Information
Rule 302 Contingent Fees
Rule 501 Acts Discreditable
Rule 502 Advertising and Other Forms of Solicitation
Rule 503 Commissions and Referral Fees
Rule 505 Form of Organization and Name

Do You Understand Your Ethical Responsibility?
Have you ever shared your copy of a software disc with a colleague? Was this an unethical act?

Technology has complicated ethical issues. Few CPA would enter a music store and pilfer a CD and walk out without paying. Would the same person have an ethical problem illegally downloading an entire album via the internet? The technological imperative drives the feeling that if we can do it, it must be ok. We often justify our actions by saying, ‘Well everybody else is doing it.” The new technology and the information revolution has made it easier to do this privately.
Chapter 4: Understanding Professional Conduct

Objective:

- How does the Code of Professional Responsibility apply to engagements

Stop and think what would happen if we did not obey laws and regulations. The stakes in behaving unethically are very high. One decision may impact thousands of people.

Some important focal points of ethics are the concept of integrity (honesty) and conflict or interest. Integrity suggests that individuals should always conduct themselves in accordance with law and regulations. To the CPA this suggests that they should not undertake engagements unless they possess the required competence and technical skills. To avoid conflict of interest issues, one should always avoid simultaneous involvement in any activity which might result in the compromising of their integrity, their independence or their objectivity.

The management of ethics in the workplace provides noteworthy benefits for today’s business leaders. This is particularly true in light of today’s highly motivated and diverse business environments.

It is rare and difficult to find business ethics literature which provides a “how-to” approach to solving many of the ethical issues encountered in today’s business world. There are plenty of examples that demonstrate the lack of managers to adequately manage ethics in the workplace.

Keep ethics at the top of your priority list. Make sure there are resources available within your organization that provide guidance and assistance with ethical issues – resources that individuals will use and trust.

Carter McNamara, MBA, PhD, identified 10 Myths about Business Ethics:

1. Business ethics is more of a religion than management.
2. Our employees are ethical so we don’t need attention to business ethics.
3. Business ethics is a discipline best led by philosophers, academics and theologians.
4. Business ethics is superfluous – it only asserts the obvious: “do good!”
5. Business ethics is a matter of good guys preaching to the bad guys.
6. Business ethics is the new policeman on the block.
7. Ethics cannot be managed.
8. Business ethics and social responsibility are the same thing.
9. Our organization is not in trouble with the law, so we are ethical.
10. Managing ethics in the workplace has little practical relevance.
We are expected to do the right thing.
Chapter 5: Ethical Rulings and Pronouncements

Objectives:

- Understanding the difference in Pronouncements and Rulings
- Understanding how rulings affect your practice
- Where to find ethical guidance

Regulatory and legislative bodies issue both pronouncements and rulings. In considering pronouncements and rulings, one could describe the pronouncements issued as general guidelines that apply to all parties. They are naturally broad in scope and are meant to convey the regulatory or legislative body’s intent for the conduct of those under its authority. Interpreting the pronouncements can lead to disagreements as to how those broad standards of behavior are to be adhered to in particular circumstances. In order to help implement the pronouncements, the regulatory or legislative body may issue rulings that deal with specific circumstances and how a particular pronouncement should be interpreted in those specific circumstances.

In considering the AICPA’s approach to regulating the practice of public accountancy in the United States, we note that the Code of Professional Conduct (discussed in Chapter 3) contains six principles that are broad in scope and designed to provide an overall sense of how CPAs are to conduct themselves. The rules that flow from those broad pronouncements seek to implement the spirit of those principles, but even those rules have not provided sufficient guidance by themselves. Interpretations of the rules have also been issued to provide even more specific guidance. Some would argue that the interpretations still are not adequate in some circumstances. That feeling of uncertainty requires the CPA to exercise professional judgment in dealing with such ethical dilemmas. And because each CPA brings different backgrounds, experience, education and creativity to their reading of this information, judgment varies from person to person.

A broad principle in the Code of Professional Conduct is that –

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

Rule 102 Integrity and Objectivity flows from that broad principle and states that –

“In the performance of any professional service, a member shall maintain objectivity and integrity, shall be free of conflicts of interest, and shall not knowingly misrepresent facts or subordinate his or her judgment to others.”

In order to help CPAs follow the principle and the rule, the AICPA has issued Ethics Interpretations concerning integrity and objectivity designed to address specific situations that involve integrity and objectivity. CPAs should be familiar with the principles in the Code of Professional Conduct and should be prepared to research the rules and associated interpretations to determine if a situation has already been
addressed. The AICPA Code of Professional Conduct, along with the rules and interpretations, are available on the AICPA web site and are also published in a single volume annually, usually as of June 1st. The AICPA also seeks comment on proposed ethics interpretations through its web site and includes recently issued ethics interpretations in the Journal of Accountancy.

Since the Code cannot anticipate any and all possible ethical dilemmas for CPAs, there could be situations involving relationships or circumstances that are not discussed in rules or interpretations. The Professional Ethics Executive Committee (PEEC) of the AICPA uses a conceptual framework to analyze independence issues and the standards that are issued. This framework is designed to evaluate a member’s relationship with a client and determine if that relationship poses an unacceptable risk to independence. The PEEC has issued ET Section 100.01 – Conceptual Framework for AICPA Independence Standards, which describes the risk-based approach CPAs are to use in evaluating threats to independence. The framework is to be used when considering independence matters not covered by the Code of Professional Conduct.

Independence is defined as:

- Independence of mind – acting with integrity and exercising objectivity and professional skepticism.
- Independence in appearance – avoiding circumstances that would cause a reasonable third party (already described above) to conclude that independence of mind had been compromised.

Independence is thus described as an absolute term, i.e., there are no degrees of independence. One is either independent or is not independent.

The standard contains the following concerning risk to independence:

ET 101.01.01 – “Risk is unacceptable if the relationship would compromise (or would be perceived as compromising by an informed third party having knowledge of all relevant information) the member’s professional judgment when rendering an attest service to the client. Key to that evaluation is identifying and assessing the extent to which a threat to the member’s independence exists and, if it does, whether it would be reasonable to expect that the threat would compromise the member’s professional judgment and, if so, whether it can be effectively mitigated or eliminated.”

In order to use this risk-based approach described by the framework, you evaluate the risk that you would not be independent or would be perceived as not being independent by a reasonable and informed third party who has knowledge of the issues and all the relevant information. The risk has to be reduced to an “acceptable” level, which is described as being when threats to independence are at an acceptable level. (It’s not reasonable to expect that the threat would compromise professional judgment.)

The evaluation of independence risk involves:

- Identifying and evaluating threats to independence;
- Evaluating the significance of a threat;


- Determining whether safeguards eliminate or mitigate threats or potential threats; and,
- Recognizing that if safeguards do not eliminate a threat or reduce it to an acceptable level, independence would be impaired.

In the standard, there is an acknowledgement that it is impossible to identify every situation that creates a threat to independence. However, the standard lists seven broad categories of threats that should be evaluated during the identification and assessment of threats:

- **Self-review** – using your own non-attest work as audit evidence without proper review or preparing source documents (audit evidence) used to generate client financial statements:
- **Advocacy** – promoting an attest client’s interest or position, such as in IPO’s, representation in US tax court
- **Adverse interest** – opposite interests between the client and the member, such as litigation between the parties
- **Familiarity** – close or long-term client relationships with the client or those that perform accounting services for the client that affect professional skepticism
- **Undue influence** – the client or interested parties attempt to coerce the member to ignore standards and principles
- **Financial self-interest** – potential benefit to the member from a financial relationship with the client
- **Management participation** – performing management functions on behalf of a client, such as serving as an office or director, establishing or maintaining internal controls, or hiring, supervising, or terminating the client’s personnel

In dealing with the above-listed threats, the standard describes safeguards as controls that mitigate or eliminate threats to independence. The safeguards are described in broad categories as:

- Safeguards created by the profession, legislation, or regulation;
- Safeguards implemented by the client; and,
- Safeguards implemented by the firm, including policies and procedures to comply with professional and/or regulatory requirements.

When evaluating and assessing risk, the CPA must also evaluate the effectiveness of the safeguards, which may be influenced by some factors noted in the standards:

- The facts and circumstances of the particular situation;
- The proper identification of threats;
- Whether or not the safeguard (as designed) meets its objectives;
• The party/parties that are subject to the safeguard;
• How the safeguard is applied in each particular situation;
• The consistency of application of the safeguard; and,
• Who applies the safeguard.

The standard includes examples of safeguards for each broad category, but the listing is not intended to be all-inclusive, nor will all the safeguards be present in every instance.

**Safeguards created by the profession, legislation or regulation**

- Education and training for independence and ethics for all CPAs and staff;
- Professional standards, monitoring, and disciplinary processes;
- Peer review;
- Legislation concerning independence; and,
- Licensing requirements for competency and experience.

**Safeguards implemented by the client**

- Client personnel with suitable skill, knowledge and/or experience who make managerial decisions with respect to the delivery of nonattest services by the member to the client;
- A tone at the top that emphasizes the client’s commitment to fair financial reporting;
- Policies and procedures that are designed to achieve fair financial reporting;
- A governance structure designed to ensure appropriate decision-making, oversight, and communications; and,
- Policies that dictate the types of services that the entity can hire the member to provide without impairing independence.

**Safeguards implemented by the firm**

- Leadership that stresses the importance of independence and the expectation that members will act in the public interest;
- Policies and procedures that implement and monitor quality control;
- Documented independence policies concerning identification and evaluation of threats and the identification and application of safeguards;
- Monitoring compliance with independence policies and procedures;
- Policies and procedures to identify interest or relationships between the firm and/or its personnel and clients and/or client personnel;
• Using different partners and engagement teams for non-attest services;
• Training and communication of firm policies and procedures;
• Consideration of concentration of revenue from a single client and how to deal with that situation;
• Appointment of senior personnel to be responsible for the performance of the firm’s quality control system;
• Communication of attest clients and related entities for which independence is required;
• Disciplinary procedures to promote compliance with policies and procedures;
• Empowering staff to communicate engagement issues to senior firm management, without fear of retribution;
• Policies and procedures relating to independence communications with those charged with client governance, including discussing independence issues with them, describing the nature of services and the amount of fees charged;
• Involving another CPA (within the firm or an outsider) or another CPA firm to review the work done or advise the engagement team concerning independence issues;
• Rotation of senior personnel on the attest engagement team;
• Policies and procedures designed to ensure that members of the attest engagement team do not make or assume management responsibilities;
• Removing members of attest engagement teams whose relationships pose a threat to independence;
• Establishing a consultation function to assist engagement teams in resolving accounting, auditing, independence, and reporting matters;
• Client acceptance and continuation policies designed to prevent association with clients that might pose a threat to independence; and,
• Policies and procedures to preclude attest partners from being directly compensated for increasing non-attest services to attest clients.

To resolve an ethical conflict, consider the following factors and then select the best course of action that would best enable you to follow the rules:

• The relevant facts and circumstances (including applicable rules, laws or regulations);
• The ethical issues involved in the situation;
• Established procedures already established by –
  o The profession, legislation, or regulation;
  o The client; and
Alternative courses of action.

It would be advisable to document the substance of the issue and details of any discussions held or decisions made concerning the ethical issue.

If the ethical conflict remains unresolved, you could be considered to be in noncompliance with the rules if you remain associated with the matter that caused the conflict. That may lead you to withdraw from the engagement team, withdraw from a specific assignment, cease work for a client or resign from your firm or organization.

The principles, rules and interpretations are applicable to all professional services, except where the wording of the rule/interpretation indicates otherwise or where the CPA is practicing outside the United States and is following the applicable rules in that country. Departures from these rules can result in disciplinary action and CPAs must be prepared to justify departure from the rules.

In addition to the oversight provided by the Tennessee State Board of Accountancy, the Tennessee Society of CPAs has a Professional Ethics Committee that deals with complaints about TSCPA members. The Committee determines if the complaint can be resolved directly by the efforts of the Committee or if the situation requires further investigation, in which case, the AICPA Joint Ethics Enforcement group investigates the situation. The AICPA group recommends a resolution to the TSCPA Committee which authorizes the action. The AICPA then requests consent to the resolution from the CPA, such as additional CPE or review of future workpapers or reports.

Tennessee CPAs have significant information and assistance available when dealing with ethical matters from the AICPA, the Tennessee State Board of Accountancy and the Tennessee Society of CPAs.
Please consider these scenarios and decide what you should do:

**Case 1 –**

Your supervisor tells you that one of your staff members is among several employees to be laid off soon, but you are not to tell anyone. Meanwhile you hear that he plans to enroll his child in private school and the tuition is due.

What should you do?

**Case 2 –**

Mom and Pop have quit their jobs and mortgaged everything they own to start a new business to fulfill a lifelong dream. Things did not go as planned and they were forced to borrow money from family and friends. It is now time to renew the business loan and the bank has asked for a current financial statement. They have asked you to assist them in preparing the financial statement and make it look good enough to get the loan renewed.

What should you do?

**Case 3 –**

You are preparing a tax return for one of your clients. You ask the client to provide you with the total amount of revenue received for the year. The client responds, “I only received 1099’s totaling $310,000, so that is all I want to report.”

What should you do?

**Case 4 –**

Your firm is performing the annual audit for one of your largest clients. The client is concerned about a required disclosure you have included in the notes to the financial statements. They ask you to omit the disclosure.

What should you do?

**Case 5 –**

One of your firm’s clients is negotiating to sell their business. A potential buyer is also one of your clients. The potential buyer has come to you requesting your opinion about the value of the business and if you think he should make the purchase. He promises this is just between you and him.
What should you do?

**Case 6 –**

A couple, who are tax clients, are in the process of getting a divorce. One spouse asks you to assist in disputing the value placed on the other spouse’s business and to provide advice concerning the tax consequences of the divorce.

What should you do?
Chapter 6: The Tennessee Accountancy Act

Objectives:

- Knowledge and understanding of the Tennessee Accountancy Law

The Tennessee Accountancy Act

The Tennessee Accountancy Act is a product of the legislative process. After the act has passed the legislature and is signed by the Governor it becomes law. It is often amended by the legislative process over time. Our current accountancy law was last amended, substantively, in 1998.

The current accountancy law can be found in the Tennessee Code Annotated, Title 62 Professions, Business and Trade, Chapter 1. A full version of the law can be found at www.lexisnexis.com. A link to this website can be found at the home page of the Tennessee State Board of Accountancy: www.tn.gov/commerce/boards/tnsba/.

What’s New-

New Ethics CPA requirements for Tennessee CPAs

New and updated ethics CPE requirements are effective for CPAs who renew in 2012 and after. The new ethics requirements reduce the total number of ethics CPE from 4 hours to 2, and establish that both of the required two (2) hours be Tennessee state-specific. This replaces the original requirement of a total of 4 hours with a minimum of 1 hour of Tennessee state-specific.

All qualifying Tennessee specific ethics course must be approved by the Board.

Mobility

Starting in 2009 the National Association of State Boards of Accountancy (NASBA) started an effort to get all 55 jurisdictions to adopt a concept called Mobility. Under Mobility CPA’s could practice across state lines without having to notify the various state boards in advance. On August 17, 2011, New York became the 48th state to adopt Mobility. A Mobility internet tool can be found at CPAmobility.org for more details. The site works by posing three targeted questions to CPAs interested in exercising cross-border practice privileges. Those are:

- Where is your principal place of business?
- Where are you going to perform services (target state)?
- What type of services will you perform?

Mutual Recognition Agreements (MRA)
The International Qualifications Appraisal Board (IQAB) has currently established mutual recognition agreements with the following professional bodies:

Institute of Chartered Accountants in Australia  
Canadian Institute of Chartered Accountants  
Canada, Mexico and United States Memorandum of Understanding  
Charted Accountants Ireland  
Irish Institute of Chartered Accountants  
Instituto Mexican de Contadores Publicos  
New Zealand Institute of Charted Accountants

Through a mutual recognition agreement, qualified professional accountants from another country can practice in the United States without having to completely re-credential. Similar recognition is given to United States CPAs who wish to practice in that same country.

Professional bodies that are substantially equivalent to those of the United States CPA in the areas of education, examination and experience (as stated in the Uniform Accountancy Act) are invited to apply for a Mutual Recognition Agreement.

Each United States jurisdiction will have to adopt the agreement if its wishes to be part of the agreement.

**International Financial Reporting Standards (IFRS)**

The future of the International Financial Reporting Standards in the United States is yet to be decided. A recent practice analysis conducted by the American Institute of Certified Public Accountants (AICPA) – Board of Examiners determined that knowledge of IFRS was entry level practice. As a result, the standards are now included on the Uniform CPA Exam.

**Accountancy Licensing Database (ALD)**

The ALD is a central repository of current licensee and firm information. It was conceptualized to assist boards of accountancy with their regulatory mission. Ideally, the database will continue to grow to include the current and accurate licensing information for individual accountants and firms in each of the 55 jurisdictions. ALD is hosted by NASBA and access to the system is free to state boards of accountancy.

A public version of this database is being planned.

**International Testing Sites of the CPA Exam**

In conjunction with the AICPA, Prometric and NASBA, the Uniform CPA Examination is now offered in Japan, Bahrain, Kuwait, Lebanon and the United Arab Emirates. Applications were accepted starting in May 2011 with the first opportunity to test occurring in August of 2011. The U.S. CPA exam is being offered internationally for the
first time as a service to foreign nationals in response to rapidly escalating international demand for U.S. CPA licensure.

The CPA Examination application process is basically the same for U.S. and international candidates. In order to qualify to take the CPA Examination outside the U.S., candidates will have to establish their eligibility through a State Board participating in the International CPA Examination Administration program.

Prospective candidates must select the participating U.S. jurisdiction to which they will apply, contact the Board of Accountancy (or its designee) in that jurisdiction to obtain application materials, submit completed applications and required fees as instructed and once deemed qualified, register for the examination. After receiving the Notice to Schedule, they may then register to take the examination in an international location through a participating state board.

The information below represents a summary of pertinent sections of the law:

Section 62-1-102 states the legislative intent as follows: “It is the policy of this state, and the purpose of this chapter, to promote the reliability of information that is used for guidance in financial transactions or for accounting for or assessing the financial status or performance or commercial, noncommercial, and government enterprise. The public interest requires that persons professing special competence in accountancy or offering assurance as to the reliability or fairness of presentation of such information shall have demonstrated their qualifications to do so, and that persons who have not demonstrated and maintained such qualifications not be permitted to represent themselves as having such special competence or to offer such assurance; that the conduct of persons licensed as having special competence in accountancy be regulated in all aspects of their professional work; that a public authority competent to prescribe and assess the qualifications and to regulate the status or competence of the persons using such titles be prohibited.”

The law provides in Section 62-1-104 for a State Board of Accountancy (Board). It states, “The Board shall be composed of eleven (11) members appointed by the governor.” It provides for the composition of the board to consist of nine (9) members who shall be certified public accountants holding a certificate issued by the Board and shall reside within the State of Tennessee representing the three (3) grand divisions or the state. As a result three members are appointed from each division of the state, east, middle and west. Terms of these members are staggered such that one (1) member is appointed each year to a three year term from each of the three (3) grand divisions. The members of the board are appointed by the Governor from a list of qualified certified public accountants submitted by the Tennessee Society of Certified Public Accountants.

The additional two members of the board, which are also appointed by the Governor include an attorney, licensed to practice in the highest court of the state and one (1) public member possessing expertise in one (1) or more significant portions of the board’s regulated activities who resides in the state and is at least 18 years of age. The
law prohibits either the attorney or public member from holding a certified public accountant certificate or a license as a public accountant.

The term of a board member is three (3) years and members shall not be eligible to serve more than three (3) consecutive terms. The board elects a Chair, Vice-Chair and a Secretary annually and generally meets at least quarterly.

The Board is charged with the responsibility to hire an Executive Director and two investigators, who shall be a certified public accountant with an active certificate in Tennessee. The Board is also staffed by additional personnel employed by the State, who work under the direction of the Executive Director and the Board.

The Board operates under a committee structure. The current Board committees are (1) Probable Cause; (2) Executive; (3) Finance & Administrative; (4) Licensing; and (5) Laws and Rules.

The current law allows the Board to, “adopt rules governing its administration and enforcement ... and the conduct of licensees.” Rules address such things as board meetings; procedures governing the conduct of investigations and hearings of the board; educational and experience qualifications; professional conduct; use of the title “Certified Public Accountant”; peer review; substantial equivalency; examination and other rules deemed necessary for implementing the provisions and purposes of the Accountancy Law.

The Board currently meets quarterly with committee meetings taking place on the first day and the Board meeting on the following day. Meetings of the Board are conducted under the Sunshine Law, which requires advance notice and publication of the time, place and date of the meeting. All meetings of the Board are open to the general public and the Board invites anyone to attend.

The primary responsibility of the Accountancy Board is to protect the Public. The Board and its staff fulfill this responsibility through its regulatory powers. Individuals who violate the accountancy law and rules are investigated by the board and are subject to disciplinary actions deemed appropriate by the Board. The Board has an attorney on staff, which assists and advises the Board in the interpretation and enforcement of the law and rules.

The Boards staff oversees licensing, renewals, maintains files, answers questions, investigates complaints among some of its duties. Contact information for the Board and its staff can be found at www.tn.gov/commerce/boards/tnsba/.

Once the Board receives a complaint, a case number is assigned and the file referred to the Board’s attorney. The Attorney determines if any law or rule has been violated and advises the Board of the specific law or rule. The case may then be assigned to the Board’s investigator who performs a thorough investigation of the alleged violation(s) and prepares a report. The report and the attorney’s recommendation are then provided to the Probable Cause Committee; however, the names of all involved parties are withheld. The Committee then makes its recommendation to the full Board for final
disposition. The Board has adopted guidelines to insure fair and consistent disciplinary action.

If the licensee does not consent to and accept the action taken by the board, a formal hearing is set. This hearing is moderated by an Administrative Law Judge and the licensee is entitled to be represented by legal counsel. The full Board serves as the "trial board" and has the power to summon records and witnesses by subpoena and to compel their attendance. They may administer oaths and pass judgment upon those licensed under their jurisdiction. After having heard the testimony of the Board's investigator; statements by the Board's staff Attorney; testimony by the licensee and their attorney, the Board then renders its opinion and verdict. If the licensee wishes to appeal the Board's decision it can appeal to the Chancery Court of Davidson County.

The Board is responsible for assuring that individuals who apply to sit for the CPA exam meet the qualifications set forth. This procedure is currently contracted to the CPA Exam Services (CPAES), a division of National Association of State Boards of Accountancy (NASBA). They process applications and verify qualifications to allow qualified individuals to sit for the examination.

The current examination is computerized and offered during 8 months each year. Each calendar quarter provides for two (2) months of testing and one (1) "black out" month, during which the exam is not available.

The law provides for the issuance of a certificate of "certified public accountant" to "persons of good moral character who meet the education, experience and examination requirements" of the law. The law defines "good moral character" as the absence of a history of dishonest or felonious acts.

The education requirements are a minimum of one hundred and fifty (150) semester hours of college education including a baccalaureate or higher degree conferred by a college or university acceptable to the Board.

The examination requirements are set forth in more detail in the rules. The examination requirements further prescribe one (1) year of experience.

Once an individual has satisfied the requirements of education, examination and experience, the Board is empowered to issue them a certificate. Each certificate holder who desires to practice within the State is required to hold a license. The Board is authorized to grant and renew licenses to practice. Such licenses are issued for a period of two years, at which time the individual is required to renew their permit. Renewal requires the licensee with an active status to complete a minimum of 80 hours of continued professional education (CPE) every two years.

The law, under Section 62-1-108, further provides for the registration and regulation of each firm doing business in Tennessee. Firm permits are issued and renewed annually. Each CPA firm must be owned by at least a majority of certified public accountants licensed in some state. Any individual licensee who is responsible for supervising attest
services and signs or authorizes someone to sign the accountant’s report on financial statements on behalf of the firm shall meet certain experience requirements.

Section 62-1-111 authorizes the Board to revoke any license; suspend or fail to renew any license issued under its authority for a period of not more than 5 years; reprimand, censure or limit the scope of practice of any licensee; to impose a civil penalty; or place any licensee on probation, all with or without terms, conditions, and limitations. There are a variety of stated reasons, including fraud or deceit, actions taken against licensee by other states, failure to maintain compliance with requirements for renewal, violations of the law, rules or rules of professional conduct, conviction of a felony or of any crime of dishonesty or fraud, conduct reflecting adversely upon the licensee’s fitness to perform services, making false or misleading statements or verification in support of an application for license or violations or any lawful order entered by the board.

The law further provides for each firm who provides the attest function to obtain an acceptable peer review and licensees who perform attest services to satisfactory complete continued professional education specified by the Board.

Prohibited Activities – Section 62-1-113

The law authorizes that only licensees may issue a report on financial statements of any other person, firm, organization or governmental unit. Licensees performing attest services must provide such services pursuant to statements on standards related to those services adopted by reference or directly by the Board.

This section prohibits any person not holding a valid certificate to use or assume the title “certified public accountant” or the abbreviation “CPA” or any other title, designation, words, letters, abbreviation, sign, card, or device tending to indicate that such person is a certified public accountant.

It further prohibits any firm from providing attest services or to assume or use the title “certified public accountants” or the abbreviation “CPAs” or any other title, designation, words, letters, abbreviations, sign, card, or device tending to indicate such firm is a CPA firm unless it holds a valid permit issued by the Board and firm ownership is in accord with the law and rules promulgated by the Board. These limitations also apply to the use of the title “public accountant” or the abbreviation "PA".

Section 62-1-115, Accountant’s records as personal property

Subject to the confidential information provisions of Section 62-1-116, all statements, records, schedules, working papers, and memoranda incident to, or in the course of, rendering services to a client, made by a licensee or a partner, shareholder, officer, director, member, manager or employee of a licensee, except the reports submitted by the licensee to the client, and except for records that are part of the client’s records, shall be and remain the property of the licensee in the absence of an express agreement between the licensee and the client to the contrary.
Such records may not be sold, transferred or bequeathed, without the consent of the client. It requires the licensee to furnish the client or former client, upon request and reasonable notice, a copy of the licensee’s working papers, to the extent that such working papers include records that would ordinarily constitute part of the client’s records and are not otherwise available to the client. In addition, any accounting or other records belonging to, or obtained from or on behalf of the client removed from the client’s premises or received for the client’s account, the licensee may make and retain copies of such documents of the client when they form the basis for work done by the licensee.

Section 62-1-116, Confidential information

This section prohibits any licensee from divulging any information which is communicated to them or obtained by them by the reason of the confidential nature of their employment or engagement. Such information shall be deemed confidential; provided however, except for information required to be disclosed by the standards of the public accounting profession in reporting on the examination of financial statements or as disclosed in investigations or proceedings under the Accountancy Law.

Any disclosure of confidential information pursuant to this section shall not constitute a waiver of the confidential nature of such information for any other purpose.

Section 62-1-122 Payments to obtain clients or for referrals

This section prohibits a licensee from paying any consideration or commission either to obtain a client or to accept any consideration or commission for the referral of a client to others when the licensee or the licensee’s firm also performs for the client:

1) An audit or review of a financial statement;
2) A compilation of a financial statement when the licensee expects, or reasonably might expect, that a third party will use the financial statement and the licensee’s compilation does not disclose a lack of independence; or
3) An examination of prospective financial information.

This prohibition applies during the period in which the licensee is engaged to perform any of the services listed and the period covered by any historical financial statements involved in such services.

Any licensee, who is not prohibited by this section, shall disclose that fact in compliance with the requirements of this section to any person who the licensee recommends or refers a product or service to which a commission relates.

Any licensee who accepts consideration or a commission for the referral shall disclose such acceptance or payment to the client in writing in a clear and conspicuous manner disclosing the amount of consideration or the basis on which payment will be computed prior to the time of recommendation or referral or service for which consideration or commission is paid or prior to the client retaining the licensee.

Section 62-1-123 Contingent fee arrangements.
This section defines “contingent fee” as “a fee established for the performance of any service pursuant to an arrangement under which a fee will not be charged unless a specified finding or result is attained, or under which the amount of the fee is otherwise dependent upon the finding or result of such service.” It does not include a fee fixed by a court or other public authority, or a fee related to any tax matter which is based upon the results of a judicial proceeding or the finding of a governmental agency.

Any licensee is prohibited from receiving a contingent fee from a client for the following:

1) Performance of any professional services for a client for whom the licensee or person associated with the licensee performs any of the following:
   a. An audit or review of a financial statement
   b. A compilation of a financial statement when the licensee expects, or reasonably might expect, that a third party will use the financial statement and the licensee’s compilation does not disclose a lack of independence, or
   c. An examination of prospective financial information; or
2) Preparation of an original tax return.

This prohibition applies during the period in which the licensee is engaged to perform any of the services prohibited and the period covered by any historical financial statements involved related to such services.

The specific terms of the disclosure and the manner in which the disclosures shall be made as follows:

1) The disclosure must be in writing and be clear and conspicuous;
2) The disclosure must state the amount of the contingent fee or must state the basis on which the contingent fee will be computed; and
3) The disclosure must be made at or prior to the time the licensee undertakes representation of or performance of the service upon which a contingent fee will be charged.

Section 62-1-201 Peer review

This section states the Board shall require, by rule, as a condition to renewal of permits under this section, that applicants undergo, no more frequently than once every three (3) years, peer reviews conducted in such manner as the Board shall specify. The Peer Review shall include a verification that individuals in the firm who are responsible for supervising attest services and sign or authorize someone to sign the accountant’s report on the financial statements on behalf of the firm meet the experience requirements set out in the professional standards for such services.

It provides that the rules shall include a reasonable provision for compliance by an applicant showing that it has, within three (3) years undergone a satisfactory peer review. It shall require, that such peer reviews be subject to oversight by an oversight body established or sanctioned by board rule, which body shall periodically report to the board on effectiveness of the review program under its charge and provide to the board
a listing of firms that have participated in a peer review program that is satisfactory to the board.

It further provides with respect to peer review, that the peer review process be operated and documents maintained in a manner designed or preserve confidentiality and neither the board nor any third party, other than the oversight committee, shall have access to documents furnished or generated in the course of the review.

Section 62-1-202 Review Committees – Confidentiality and proceedings - Scope of confidentiality

This section provides that “The proceedings, records and work papers of a review committee shall be privileged and confidential and shall not be subject to discovery, subpoena or other means of legal process or introduction into evidence in any civil action, arbitration, administrative proceeding or state board of accountancy proceeding, and no member of the review committee or person who as involved in the peer review process shall be permitted or required to testify in any such civil action, arbitration, administrative proceeding or state board of accountancy proceedings as to matters produced, presented, disclosed or discussed during or in connection with the peer review process, or as to any findings, recommendations, evaluations, opinions, or other actions to such committees, or any member thereof; provided, that recommendations, documents or records that are publicly available are not to be construed as immune from discovery or use in any civil action, arbitration, administrative proceedings or state board of accountancy proceeding merely because they were presented or considered in connection with the peer review process.”

62-1-203 Accountants serving on review committee – Immunity

This section provides immunity from liability for any certified public accountant or public accountant who serves on any review committee with respect to any action taken in good faith as a member of the review committee.

The members of the committee are immune from liability for furnishing information, data, reports or records to any review committee or for damages resulting from any decisions, opinions, actions, and proceedings rendered, entered or acted upon by committee member undertaken or performed with the scope or functions of the duties of the review committee, if made or taken in good faith, and without malice and on the basis of facts reasonably known or reasonably believed to exist.
Chapter 7 – The Rules of the Tennessee State Board of Accountancy

The Rules of the Tennessee State Board of Accountancy (Rules) are adopted by the Board to provide for fair application and understanding of the Law. The discussion of the Rules which follows includes selected statements taken verbatim from the Law and statements which are paraphrased. The complete Rules can be found at www.tn.gov/commerce/boards/tnsba/, the website of the Tennessee Accountancy Board. Everyone is encouraged to access and read the Rules in their entirety.

The Table of Contents of Chapter 0020-1, Board of Accountancy, Licensing and Registration Requirements

20-1-.01 Definitions
20-1-.02 Board Meetings
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20-1-.09 Denial of Certificates
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20-1-.11 Application and Renewal of CPA and PA Firm Permits
20-1-.12 Notification of Firm Changes
20-1-.13 Interstate Practice
20-1-.14 International Reciprocity

The Rules are proposed by the Board. Once Rules have been proposed, including any changes a public hearing is announced and the public has an opportunity to comment either in writing or in person at the public hearing. After receiving and considering any comments the Board adopts the Rules and they are then submitted to the Attorney General’s office for review and approval. This process usually takes about six (6) months. Once the Board receives the approval of the Attorney General, the Rules are submitted to the Secretary of State. After “sitting” with the Secretary of State for a period of 45 days, the Rules become final and effective.

Rule 0020-1-.02

This rule provides that the Board shall meet at least four (4) times a year. It provides that the chair or a quorum of the Board shall have the authority to call a meeting and that the Board shall follow and apply the rules of the Administrative Procedures Act of the State of Tennessee regarding notice and conduct of meetings.
Comment: Meetings of the Board and its committees are open to the public and are appropriately announced under the Sunshine provisions of meetings. Consequently all discussions and deliberations by any two or more members of the Board must be in open to the public after adequate notification.

Section 0020-1-.04 Fees

This section provides fees charged by the Board

a) Initial issuance of a certificate  $100
b) Replacement of a certificate  $ 25
c) Renewal of certificate or registration  $120 biennially
d) Initial firm permit  $ 50
e) Penalty for firm permit,  $ 50
f) Renewal of firm permit  $ 50
certificate or registration renewal application
g) Application for reinstatement  $200, plus past due late fees and $50 penalty
h) Notification of intent to practice  $ 50 per year or part year fee, sent to the Board and not the Board’s designee under rule 0020-1.13(a)
i) Change of address late fee  $ 25

0020-1-.05 Applications – addresses applications to take the Uniform CPA Examination and the due date for filing such applications. The Board’s designee for this process is CPA Exam Services (CPAS), a subsidiary of the National Association of State Boards of Accountancy.

0020-1-.06 Examinations – establishes that the test shall test the knowledge and skills required for performance as an entity-level certified public accountant. It prescribes the examination shall include the subject areas of accounting and auditing and related knowledge and skills as the Board may require.

Comment: The examination currently used for Tennessee applicants is the national exam developed by the Board of Examiners and offered through Prometric facilities throughout the country. Tennessee applicants make application to CPA Examination Services, which notifies the applicant of their acceptance to sit for the exam. The content of the examination is determined through a Practice Analysis conducted every five years.

Candidates must pass all four (4) parts of the examination within six (six) three-month exam cycles (18 months). Candidates cannot retake a failed test section in the same examination window (three month cycle). Candidates are also required to pass an examination covering the rules of ethics and professional conduct obtained from the American Institute of Certified Public Accountants (AICPA).
0020-1-.11 Application and Renewal of CPA and PA Firm Permits

These rules outline the requirements for each CPA and/or PA firm providing accounting services or engaged in the practice of public accountancy in Tennessee. Firms organized as a sole proprietorship, partnership or corporation of certified public accountants and/or public accountants shall obtain a permit from the Board for each office location for the ensuing calendar year.

**Comment:** Currently firm registration is available on-line, or a firm may request a written application.

All permits expire December 31. Initial applications and renewals for each office location shall be signed by the resident manager of the office and disclose the following:

- a) The name of the firm;
- b) The firm's organizational structure;
- c) The address of the office location;
- d) The name and address of each individual with an equity or voting interest in the firm;
- e) A listing of the percentage of equity ownership and voting rights of each owner of the firm;
- f) The percentage of the firm's nominal business hours that each non-CPA owner spends working for the firm;
- g) The name, address and certificate number of each certified public accountant or public accountant employed at the office location;
- h) The name, address and certificate number of the resident manager of the office location;
- i) The name and certificate number of each person responsible for supervising or providing attest services as contemplated by T.C.A. §62-1-108(c)(2). The firm's initial application must include a completed experience affidavit for each of these individuals; and
- j) The type of peer review program in which the firm participates along with proof of compliance in a manner acceptable to the Board.

0020-1-.12 Notification of Firm Changes

Any firm registered with the Board must file with the Board a written notification of any of the following events concerning the practice of public accountancy within Tennessee within 30 days after its occurrence:

- a) Formation of a new firm;
- b) Addition of a partner, member or shareholder;
- c) Retirement, withdrawal or death of a partner, member, manager or shareholder;
- d) Any change in the name of the firm;
- e) Establishment of a new office location providing accounting services in Tennessee or the closing or change of address of an office registered in Tennessee; and
f) The occurrence of any event or events which would cause such firm not to be in conformity with the provisions of the Act or these Rules.

0020-1-.13 Interstate Practice

These rules provide two distinct routes for an individual already licensed in another state to be authorized to practice in Tennessee. The applicable route depends upon whether the individual will establish a principal place of business in Tennessee. An individual establishing a principal place of business in Tennessee may qualify for a reciprocal license if the applicant has met the requirements of T.C.A. §62-1-107. An individual with a principal place of business in another state may offer or render services in Tennessee if the applicant has met the requirements of T.C.A. §62-1-117.

Any individual intending to practice public accountancy in Tennessee who does not intend to establish a principal place of business and who holds a valid license from a state who provides for CPA inter-state mobility, as outlined in Section 23 of the Uniform Accountancy Act, may provide services without notice or fee. This method is often referred to as, No Notice, No Fee, No Escape. The individual CPA who practices in Tennessee under Mobility does not have to provide notice to the Board or pay a fee. However, the actions imply their consent to the authority of the Tennessee Accountancy Act, thus no escape. If they are found to be in violation of our accountancy act, the Board has the authority to discipline the CPA.

Currently 48 of the 50 states, and one of the territories who license CPAs, have adopted Mobility. California and Hawaii are supportive of the efforts to adopt mobility legislation in their states, however, there are some special interest groups which are hesitant to adopt mobility, and so discussions are continuing with them.

An application for a reciprocal certificate shall be accompanied by a nonrefundable fee of one hundred dollars ($100). The fee for issuance of an initial reciprocal certificate is one hundred dollars ($100). The fee for biennial renewal of a reciprocal certificate shall be one hundred twenty dollars ($120).

Individuals holding reciprocal certificates shall comply with the continuing education requirements contained in Chapter 0020-5, and shall comply with all other requirements of the statutes and rules governing the practice of public accountancy within the State of Tennessee.

Chapter 0020-2 Education and Experience Requirements

0020-2-.01 Recognized Colleges and Universities
0020-2-.02 Education
0020-2-.03 Experience

0020-2-.01 Recognized Colleges and Universities

This chapter defines “semester hour” as the conventional college semester hour. Quarter hours may be converted to semester hours by multiplying them by two-thirds.
The remainder of this section defines what colleges and university credits are approved by the Board for qualifications to sit for the Uniform CPA Examination.

**0020-2-.02 Education**

This rule establishes the educational requirements for an applicant. The applicant must earn a baccalaureate or higher degree from an accredited educational institution and obtain a minimum number of hours including:

a) At least twenty-four (24) semester or thirty-six (36) quarter hours of accounting education including the elementary level;

b) Not more than three (3) semester or four (4) quarter hours may be internship programs which may be applied to twenty-four (24) semester or thirty (36) quarter hours in accounting; and

c) At least twenty-four (24) semester or thirty-six (36) quarter hours in general business education in one (1) or more of the following:

   i. Algebra, Calculus, Statistics, Probability
   ii. Business Communication
   iii. Business Law
   iv. Economics
   v. Ethics
   vi. Finance
   vii. Management
   viii. Technology/Information
   ix. Marketing

**0020-2-.03 Experience**

Experience may consist of providing any type of service or advice using accounting, attest, management advisory, financial advisory, tax or consulting skills. Experience must be verified to the Board by a licensee and shall include employment in industry, government, academia or public practice.

One (1) year of shall consist of full or part-time employment that extends over a period of no less than one (1) year and no more than three (3) years and includes no fewer than two thousand (2,000) hours of performance of services described above.

Any individual licensee, who is responsible for supervising attest services and signs or authorizes another person to sign the accountant’s report on behalf of the firm, shall meet the competency requirements and shall have no less the two (2) years of experience satisfactory to the Board in the preparation of financial statements or reports on financial statements.

Experience must be earned within the ten (10) periods immediately preceding the latest application for a certificate.
Evidence of an applicant’s experience may be requested by the Board and failure or refusal to comply with such requests must be explained to the Board in writing or in person explaining the basis for such refusal.

Chapter 0020-3, Rules of Professional Conduct

0020-3-.01 Definitions
0020-3-.02 Applicability
0020-3-.03 Independence
0020-3-.04 Integrity and Objectivity
0020-3-.05 Contingent Fees, Commissions and Other Considerations
0020-3-.06 Disclosures
0020-3-.07 Competence
0020-3-.08 Compliance and Standards
0020-3-.09 Accounting Principles
0020-3-.10 Confidential Client Information
0020-3-.11 Records
0020-3-.12 Discreditable Acts
0020-3-.13 Acting Through Others
0020-3-.14 Advertising and Other Firm Solicitation
0020-3-.15 Firms
0020-3-.16 Notification to the Board
0020-3-.17 Retention of Records

0020-3-.02 Applicability

The provisions of this Chapter shall apply to all professional services performed in the practice of public accountancy or in the provision of accounting services, and shall apply to all licenses except where the wording of a rule indicates otherwise and that a licensee who is practicing outside the United States shall not be subject to disciplinary action by the Board for departing from any of the provisions of this chapter as long as the licensee’s conduct is in accord with the standards of professional conduct applicable to the practice of public accountancy in that country.

This Chapter adopts the AICPA Code of Professional Conduct when the rules are silent on any matter.

0020-3-.03 Independence

This chapter provides that licensees, in performing professional services, shall conform to the independence standards established by the AICPA, the United States Security Exchange, the General Accounting Office and other regulatory or professional standards setting bodies.

0020-3-.04 Integrity and Objectivity
In the performance of any professional service, a licensee shall maintain objectivity and integrity, free of any undisclosed conflicts of interest and shall not knowingly misrepresent facts or subordinate his or her judgment to others.

0020-3-.05 Contingent Fees, Commissions and Other Consideration

This chapter echoes the language of in the law regarding the acceptance and payment of contingent fees.

0020-3-.06 Disclosures

This chapter provides that when not prohibited from receiving consideration or a commission, the licensee shall disclose that fact in compliance with this rule. Any licensee who accepts consideration or a commission for a referral shall disclose such acceptance or payment to the client. The disclosure must:

a) Be in writing and be clear and conspicuous;
b) State the amount of the consideration or commission or the basis on which it will be computed;
c) Be made at or prior to the time of the recommendation or referral of the product or service for which consideration or commission is paid or prior to the client retaining the licensee to whom the client has been referred for which a referral fee is paid; or
d) Be made prior to the time the licensee undertakes representation or performance of the service upon which a contingent fee will be paid.

A sample statement is included in the rules.

0020-3-.07 Competence

This chapter provides that a licensee shall comply with standards and interpretations of bodies designated by the AICPA or similar entities having generally recognized authority. Standards identified specifically include:

a) Professional Competence - Undertake only those professional services that the licensee or the licensee’s firm can reasonably expect to be completed with professional competence.
b) Due Professional Care – Exercise due professional care in the performance of professional services.
c) Planning and Supervision – Adequately plan and supervise the performance of professional services.
d) Sufficient Relevant Data – Obtain sufficient relevant data to afford a reasonable basis for conclusions or recommendations in relation to any professional services performed.

0020-3-.08 Compliance With Standards
This chapter provides that a licensee who performs attest, management advisory, tax or other professional services shall comply with standards promulgated by the AICPA or other entities have similar authority as recognized by the Board.

Such groups include, but are not limited to the Security and Exchange Commission, General Accounting Office and the Public Company Accounting Oversight Board.

0020-3-.09 Accounting Principles

This chapter states that a licensee shall not express or state affirmatively that the financial statements or other financial data of any entity are presented on conformity with generally accepted accounting principles; or that he or she is not aware of any material modifications that should be made to such statements or data in order for them to be in conformity with generally accepted accounting principles if such statements or data contain any departure from accounting principles promulgated by bodies designated by the AICPA to establish such principles, which departure as a material effect on the statements or data taken as a whole.

0020-3-.10 Confidential Client Information

This chapter prohibits a licensee from disclosing any confidential information without the specific consent of the client. Licensees of a recognized investigative or disciplinary body and professional practice reviewers shall not use to their own advantage or disclose any licensee’s confidential client information that comes to their attention in carrying out their official responsibilities.

0020-3-.11 Records

A licensee shall, upon request made within a reasonable time, furnish to his or her client or former client:

a) A copy of any report or other documentation belonging to, or obtained from or on behalf of, the client, which the licensee removed from the client’s custody.

b) Any accounting or other documents belonging to, or obtained from or on behalf of the client, which the licensee removed from the client’s premises or received from the client’s custody.

c) A copy of the licensee’s working papers, to the extent that such working papers include records with would ordinarily constitute part of the client’s books and records and are not otherwise available to the client, to include but not limited to general ledgers, general journals, fixed assets and depreciation records.

0020-3-.12 Discreditable Acts

A licensee shall not commit any act that reflects adversely on the profession. A licensee or a candidate for licensure, who solicits, discloses and/or uses information obtained through violation of any nondisclosure statement of the Uniform CPA Examination shall be considered to have committed an act discreditable to the profession.
0020-3-.13 Acting Through Others

A licensee shall act to prevent others from acting on his or her behalf, when the service or task performed would violate the Code of Professional Conduct, the Accountancy Act or the accompanying rules.

0020-3-.14 Advertising and Other Forms of Solicitation

A licensee shall not seek to obtain clients by advertising or other forms of solicitation in a manner that is false, misleading or deceptive. The use or coercion, over-reaching or harassing conduct is prohibited.

0020-3-.15 Firms

This rule prohibits the use of a CPA or PA firm name that is misleading. It defines a firm name is misleading if its name:

a) Implies the existence of a corporation when the firm is not a corporation;
b) Implies the existence of a partnership when the firm is not a partnership;
c) Is similar to or the same as existing fictitious names within the State of Tennessee;
d) Tends to mislead regarding the nature of the business or the affiliation of the trade name user with another business entity;
e) Contains more than one (1) fictitious name;
f) Includes the name of an individual whose license has been suspended or revoked by the Board;
g) Includes the name of the person who is neither a present nor a past partner, member or shareholder of the firm; or
h) Includes the name of a person who is not a CPA, if the title “CPAs” is included in the firm name.

A fictitious firm name may not be used by a CPA firm unless such name has been registered with and approved by the Board, and is not false or misleading.

The Board may disapprove of the use of any fictitious name that is used within one (1) year of the prohibitions listed above or if it determines after notice and hearing that the trade name is deceptive.

A CPA or PA may practice under his/her own name or that of inactive or deceased partners or shareholders who were certified public accountants or public accountants. A partner or shareholder surviving the death or withdrawal of all other partners or shareholders may continue to practice under the partnership or professional association name for up to two (2) years after becoming a sole proprietorship.

0020-3-.17 Retention of Records
A licensee shall maintain copies, or other obtainable facsimile records, or computer records, in whatever manner kept, of all work papers and work product used to render or support rendering public accounting services to a client for a period of five (5) years, commencing at the end of the fiscal period in which the engagement is conducted. The premature destruction of these records shall subject the licensee to disciplinary action.

Chapter 0020-4 Disciplinary Actions and Civil Penalties

0020-4-.01 Definitions
0020-4-.02 Civil Penalties
0020-4-.03 Grounds for Discipline Against Licensees
0020-4-.04 Return of Certificate Registration or Permit
0020-4-.05 Review of Professional Work Product
0020-4-.06 Safe Harbor Language

0020-4-.02 Civil Penalties

The Tennessee Board of Accountancy may assess civil penalties in addition to other disciplinary action. The Board may assess civil penalties up to $1,000 for violations to the law and rules. The rule further states that each day of a continued violation may constitute a separate violation.

In assessing penalties the Board may consider whether the amount of the penalty imposed will be a substantial economic deterrent to the violator; the circumstances leading to the violation; the severity of the violation and the risk of harm to the public; the economic benefits gained by the violator as a result of non-compliance; and what is in the best interest of the public.

0020-4-.03 Grounds for Discipline Against Licensee

The grounds for disciplinary action against licensees are set forth in Tennessee Code Annotated §62-1-111 in both specific and general terms. The general terms of that provision include but are not limited to the following grounds:

a) Fraud or deceit in obtaining a certificate, registration or firm permit.
b) Dishonesty, fraud or gross negligence, making misleading, deceptive or untrue representations in the performance of services.
c) Violations of the Accountancy Act or of its Rules, including but not limited to:
   1) Using the CPA or PA title or providing attest services in Tennessee without a certificate, registration or permit to practice;
   2) Using or attempting to use a certificate, registration or permit which has been surrendered, suspended or revoked;
   3) Making a false or misleading statement in support of an application for a certificate, registration or a permit filed by another;
   4) Failure to provide any explanation requested by the Board;
   5) Failure to furnish for inspection upon request by the Board or its representative documentation relating to any evidence submitted in support of an application;
6) Failure to satisfy the continued professional education requirements set out in the Law and Rules;
7) Failure to comply with professional standards as to the attest experience requirement for those who supervise or sign financial statements in the performance of the attest service; and
8) Failure to comply with the peer review requirements set out in the Law and Rules.

Conduct reflecting adversely upon the licensees’ fitness to perform services includes but is no limited to adjudication as mentally incompetent; fiscal dishonesty of any kind; presenting as one’s own a certificate, registration or permit issued to another; concealment of information regarding violations by another licensee of the Law or Rules when questioned or requested by the Board; and willfully failing to file a report or record required by state or federal law or impeding or obstructing the filing of such, or inducing another person to impede or obstruct such filing of which one know to be false.

0020-4-.04 Return of Certificate, Registration or Permit

Any licensee whose certificate, registration or permit is subsequently suspended, revoked or expired shall promptly return them to the Board unless otherwise notified by the Board.

Chapter 0020-5 Continued Education

0020-5-.01 Definitions
0020-5-.02 Purpose
0020-5-.03 Basic Requirement
0020-5-.04 Qualifying Programs
0020-5-.05 Sponsors
0020-5-.06 Control and Reporting System
0020-5-.07 Extension of Time
0020-5-.08 Failure to Meet CPE Requirements

0020-5-.02 Purpose

The Law mandates compliance with continuing education requirements as a prerequisite for renewal of licenses issued by the Board.

0020-5-.03 Basic Requirements

A license holder shall, every two years, show they have completed no less than eighty (80) hours of qualified CPE during the two (2) year period, with a twenty (20) hour per year minimum immediately preceding renewal.

In satisfying the eighty (80) hours of CPE, all licensees shall complete at least forty (40) hours in accounting, accounting ethics, attest, taxation or management advisory services. All license holders are further required to complete a board-approved two (2) hour state-specific ethics course designed to familiarize the licensee with the
accountancy law and rules as well as professional ethics. Any licensee engaged in the attest function must complete at least (20) hours in attest, accounting theory and practice in fulfilling these requirements.

When engaged to testify as an expert witness in a Tennessee court in the areas of accounting, attest, management advisory services or tax, license holders must have completed within the current and most recent renewal period, at least twenty (20) hours in the subject areas concerning such expert testimony.

The rules allow for a carryover of up to twenty (24) CPE hours taken in excess of the eighty (80) hour requirement, every two years. Any carryover hours may be applied to the requirements of the next succeeding two year renewal period. Records must be maintained by the licensee and submitted to the Board if requested. Failure to maintain adequate documentation and records will result in the disallowance of carry-forward hours.

The Board, upon application, may exempt licensees not practicing in Tennessee, and who do not perform or offer to perform for the public services requiring accounting or auditing skills, including the issuance of reports on financial statements or one or more services including management advisory or consulting services, or the preparation of tax returns or advise on tax matters, from CPE requirements. Licensees granted this exemption must place the words “inactive” adjacent to their CPA or PA title.

Individuals who have been exempted under this rule who wish reactivate a license must complete eighty (80) hours of CPE in the areas of accounting, accounting ethics, attest, taxation, or management advisory services during the 24 months preceding the date of their request for reactivation.

Licensees who surrender their licenses in good standing may reactivate their license in the same manner.

The Board, upon application supported by such evidence, may exempt individuals age seventy (70) and over, disabled for more than six (6) months or in active military service, from payment of license fee and/or CPE requirements, so long as they do not practice public accountancy or offer accounting services to the public.

If a licensee allows their license to lapse and wishes to reinstate their license, the licensee must complete no less than eighty (80) hours of CPE in the same areas as listed above during the six (6) months preceding the date of reapplication. These CPE hours necessary to reinstate are considered penalty hours and may not be used to satisfy CPE hours required for the renewal of their license.

Non-resident licensees are deemed to be in compliance with this rule, if they are in compliance with the CPE requirements in the state in which their principal office is located. Such compliance is evidenced by signing a statement certifying to that effect.

0040-5-.04 Qualifying Programs
In order to be in compliance with the above rule, a CPE program must be a program of learning which contributes directly to the professional competence of the licensee and which meets the Statements on Standards for CPE Programs jointly approved by NASBA and AICPA.

Live seminars may be considered for credit if an outline is prepared and preserved, is at least one (1) credit hour [one (1) credit hour = fifty (50) minute period], is conducted by a qualified individual and a record of registration is maintained.

The following programs are deemed to qualify for this rule:
   a) CPE programs of the AICPA, state accounting societies and their chapters;
   b) Technical sessions of the AICPA, NASBA and state societies and their chapters;
   c) University and college courses;
   d) Organized in-firm or in-house educational programs presented to employees and others without charge; and
   e) Programs of other organizations recognized by the Board.

Formal correspondence and other individual programs which met specific criteria (set out in 0020-5-.04 (4)) may qualify for CPE credit.

Instructors, discussion leaders or speakers who are involved in CPE programs eligible for CPE credit may claim CPE credit for the first presentation only, unless the program has been substantially revised. The amount of credit awarded shall not exceed three (3) times the number of class hours and the total hours claimed under this rule shall not exceed fifty percent (50%) of the total number of credit hours required by this chapter within any two (2) year period.

CPE credit may be allowed for the reading of professional journals and successful completion of an examination thereon. Credit hours under this rule are limited to twenty percent (20%) of the total number of credit hours required within any two (2) year period.

CPE credit may also be available for the successful completion of exams for Certified Management Accountant (CMA), Certified Information Systems Auditor (CISA), as well as other similar exams approved by the Board. Credit is awarded at a rate of five (5) times the length of the exam taken and limited to fifty percent (50%) of total CPE hours required.

The Board has the right to approve or disapprove credit for any CPE claimed under this rule.

0020-5-.05 Sponsors

Sponsors who are registered with the NASBA National Registry or Tennessee Roster of CPE Sponsors are accepted by the Board as qualified sponsors. In addition the following organizations are exempt from registering: American Institute of CPAs (AICPA), Tennessee Society of CPAs (TSCPA), Tennessee Association of Accountants (TAA), Institute of Management Accountants (IMA), or other similar organizations.
approved by the Board; universities and colleges; firms offering in-firm for their employees or clients without charge and government agencies.

Sponsors who are not exempt from registration must register with the Board.

0020-5-.06 Control and Reporting System

Every two years each licensee must submit a signed statement that he or she has complied with the CPE requirements during the reporting period. Supporting documentation must be maintained for at least five (5) years from date of submission.

On a random basis the Board will audit licensees and request submission of verification for CPE credits claimed.

0020-5-.07 Extension of Time

Upon request the Board may extend for up to six (6) months the time to comply with the CPE requirements for reasons of poor health, military service, foreign residence or good cause. Requests filed after the deadline will automatically be denied.

0020-5-.08 Failure to Meet CPE Requirements

If a licensee fails to meet the twenty (20) hour one (1) year minimum or the eighty (80) hour two (2) year minimum, the licensee shall be assessed a penalty of eight (8) hours unless an extension is granted by the Board. Any penalty assessed under this rule must be completed within one hundred eighty (180) days of the end of the notification of the deficiency.

0020-6 Peer Review

0020-6-.01 Definitions
0020-6-.02 Purpose
0020-6-.03 Review Committee
0020-6-.04 Basic Requirements
0020-6-.05 Reviewers and Reviews
0020-6-.06 Peer Review Results

0020-6-.02 Purpose

The purpose of the Peer Review Program is to improve the quality of financial reporting and to assure that the public can rely on the fairness of presentation of financial information on which licensees issue reports.

0020-6-.03 Review Committee

The Board appoints a peer review oversight committee (the Committee) to assist it in the implementation of this program. The Committee is comprised of three licensees in
good standing representing each of three grand divisions of the state. Committee members serve for a term of three (3) years but may be reappointed.

The responsibilities of the Committee include monitoring and approving peer review programs and reporting periodically to the Board that the rules are being satisfied and other such duties as may be deemed necessary.

**0020-6-.04 Basic Requirements**

Each firm required to hold a permit must undergo an on-site peer review every three (3) years if they perform one (1) or more audit engagements. Firms that perform only compilations or reviews must have either an on-site or off-site peer review.

Each firm must have their peer review conducted through an approved peer review program. Firms who fail to comply with this rule may have their firm permit denied.

Firms who receive inspections under the PCAOB program are also required to have a peer review under an approved peer review program covering the portion of the firms' practice not regulated by the U.S. Securities and Exchange Commission.
Review Questions

1. The AICPA’s Code of Professional Conduct is:
   a. applicable to all CPAs in the United States
   b. a list of specific rules that are to be followed by CPAs
   c. a set of principles that govern professional behavior
   d. not subject to interpretation

2. The most important function of organizational ethics is:
   a. to relieve the individual from personal responsibility
   b. to have a significant impact on the quality of a CPA’s work
   c. to prevent individuals from committing fraud
   d. to insure that the CPA will not be sued

3. Ethical standards consist of:
   a. rules of behavior that are acceptable to everybody
   b. laws and regulations designed to prevent bad decisions
   c. standards of behavior that result in the greatest good for the most people
   d. learning the difference between right and wrong and then doing the right thing

4. Ethical choices in business usually involve:
   a. research concerning the appropriate rules issued by the governing body
   b. two options that are easily distinguishable from each other
   c. money or other company assets
   d. each individual’s personal concept of ethical behavior

5. The recent corporate scandals involving Enron, WorldCom, Adelphia and others were caused by:
   a. failure of a moral standard
   b. Arthur Andersen & Co.
c. a lack of statutes and legal regulations  
d. a lack of accounting principles and rules

6. In the absence of established policies, ethical dilemmas may involve:
   a. consulting an attorney about your concerns and your legal obligations  
   b. discussing the situation and gathering advice from knowledgeable, objective advisors  
   c. releasing confidential company information to the press  
   d. discussing the situation with supervisory personnel that can resolve the issue  
   e. resigning from the organization  
   f. b and d only  
   g. a, c, and e only  
   h. a, b, d, and e only  
   i. all of the above  
   j. none of the above

7. As it pertains to business ethics, who is responsible for establishing the ethical culture in a CPA firm?
   a. the Federal and State law enforcement authorities  
   b. the American Institute of CPAs  
   c. the Tennessee State Board of Accountancy  
   d. the CPA firm’s management

8. Of the following principles, which one is not included in the Code of Professional Ethics?
   a. integrity  
   b. due care  
   c. accuracy  
   d. public trust  
   e. independence
f. scope and nature of services

g. objectivity

9. The principles, rules and interpretations of the Code of Professional Conduct are:
   a. applicable to U.S.-licensed CPAs practicing anywhere in the world
   b. available on the AICPA’s web site or in publications produced by the AICPA
   c. discussed and implemented by the AICPA without opportunity for public comment
   d. applicable only to attest engagements

10. Which of the following phrases best describes the importance of ethical behavior in the workplace?
    a. helps protect the company’s reputation
    b. may avoid financial crises that cost people their jobs
    c. attracts ethical employees to the business
    d. promotes teamwork and productivity
    e. may help deter criminal acts
    f. all of the above

11. The primary responsibility of the Accountancy Board is to protect the:
    a. guilty
    b. the accountancy profession
    c. the public
    d. clients

12. The law provides for the issuance of a certificate to an individual who has satisfied which requirements?
    a. experience
    b. examination
c. education
d. all the above

13. Any CPA licensed in Tennessee who has a permit to practice must obtain a minimum of ____ hours of continued professional education every two years to renew their permit to practice.
   a. 40
   b. 60
   c. 80
   d. 120

14. In order to renew a permit to practice a Tennessee licensee must undergo once every _____ years, a peer review conducted in such as manner as the Board specifies.
   a. 5
   b. 3
   c. 1
   d. 6

15. A Tennessee CPA may withhold a client’s record until all fees have been paid.

   True or False

16. Client records consist of
   a. documents obtained from or on behalf of the client
   b. documents belonging to the client
   c. copy of licensee’s working papers, to the extent they include records which ordinarily constitute books and records of client
   d. all the above
17. A licensee shall maintain copies, or other obtainable facsimile records, or computer records in whatever manner kept of all work papers and work product used to render or support rendering public accounting services to the client for a period of _____ years commencing at the end of the fiscal period in which the engagement was conducted.

a. 7 years
b. 15 years
c. 3 years
d. 5 years

18. When engaged to testify as an expert witness in a Tennessee court in areas of accounting, attest, management advisory or tax an individual is not required to have an active license or continuing professional education.

True of False

19. The minimum number of hours in continued professional education required to be obtain each year is?

a. None
b. 10 hours
c. 20 hours
d. 40 hours

20. Any firm registered with the Board and individual licensees must notify the Board with 30 days after the occurrence of:

a. Change of address
b. Addition of a partner, member or shareholder
c. Change in name of firm
d. Establishment of a new office
e. Formation of a new firm
f. All of the above
Appendix 1: Glossary of Ethical Terms

**Acceptance** – The taking or receiving of anything in good part.

**Business ethics** – Doing the right thing; what is right or wrong in the workplace

**Code** – A collection of laws, a system of laws, constitutions designed to regulate subjects to which they relate; promulgated by authority.

**Confidential** – Entrusted with the confidence of another; intended to be held in confidence or kept secret.

**Conflict** – Inconsistency or difference.

**Culture** – Our complete surroundings made by people, concepts and values; language, religion, law, politics, technology, education, social organizations, general values and ethical standards.

**Ethics** – Standards of professional conduct and business practices adhered to by professionals to enhance their profession.

**Fair** – Equitable as a basis of exchange; reasonable; just; equitable; even-handed; equal as between conflicting interest.

**Impair** – To weaken, to make worse, to lessen in power, diminish, or relax.

**Immoral** – Contrary to good morals; inconsistent with the rules and principles of morality; inimical to public welfare according to standards of a given community, as expressed in law or otherwise.

**Immoral conduct** – That conduct which is willful, flagrant, or shameless, and which shows a moral indifference to the opinions of the good and respectful members of the community.

**Independent** – Not dependent; not subject to control, restriction, modification, or limitation form a given outside source.

**Integrity** – Soundness of moral principle and character, as shown by one person dealing with others in the making a performance of contracts, and fidelity and honesty in the discharge of trust; synonymous with “honesty” and “uprightness”.

**Judgment** – A sense of knowledge sufficient to comprehend the nature of a transaction; an opinion, an estimate; the formation of an opinion or notion.

**Laws** – Bodies of rules laid down, ordained, or established. A rule or method according to which phenomena or actions co-exist or follow each other.
**Moral** – Pertains to character, conduct, intention, social relations; pertaining or relating to the general principles of good conduct; cognizable or enforceable only by conscience or by the principles of right conduct; an accepted standard of behavior.

**Penalty** – The sum of money which the obligator of a bond undertakes to pay in the event of omitting to perform or carry out conditions imposed upon him or her; punishment or penalty.

**Rule** – An established standard, guide, or regulation; a principle or regulation set up by authority, prescribing or directing action.

**True** – Conformable to fact; correct; exact; actual; honest.
Appendix 2: AICPA Ethical Decision Tree

No hallmark of the CPA profession is our commitment to a Code of Conduct. This Code details our responsibilities, and our CPA certificate demands compliance with it. Ethical conduct is never out of vogue in the CPA profession, and this professional code is what sets us apart from our non-certified colleagues. There is no compromise.

The Code of Conduct applies to all AICPA members whether employed in business and industry, public practice, government or academia. When faced with a work-related ethical issue, we have been taught to challenge the situation and if it is not resolved to our satisfaction (in the context of GAAP) we should resign. In establishing the Code of Conduct, the implications of resignation for a member in business & industry is not taken lightly; the fact that an employer is the member in industry’s only source of income, possibly the only source of health insurance for themselves and their family, is recognized. However, in situations where all efforts at resolution and GAAP compliance have been explored yet the situation is still not adequately resolved, then resignation is the only alternative — this is what we must do to comply with the high ethical standards of the CPA profession.

If you are challenged with an ethics issue at some point in your professional career, chances are you don’t know where to turn, whom to talk to, or what to do next. The AICPA, in consultation with the Business & Industry Executive Committee (BIEC), created the following decision tree to help walk you through a process of resolving an ethics issue that you might encounter. BIEC members, who are CPAs in companies of all sizes, contributed their experience in finalizing this decision tree. From their perspective, we offer the following points for you to think about:

- Do your best to resolve the issue within your own organization, whether that is your department in a larger organization or the company as a whole. Most issues are easily resolved.
- Be cognizant of your obligations to your employer’s external accountant. You must be candid and must not knowingly misrepresent facts or fail to disclose material information to them (Ethics Interpretation 102.3). The full text of the interpretation is provided on the fourth page of this document for your convenience.
- One of the most common ethics violations by CPAs in business & industry relates to Ethics Interpretation 102-4 on Subordination of Judgment. This interpretation may be especially relevant if the CPA has a disagreement or dispute with their manager on the preparation of financial statements or the recording of transactions. The full text of the interpretation is also provided herein for your convenience.
- Don’t overlook an ethics policy or statement in place at your company. In a smaller company you might need to rely on outside resources as ethics policies might not be fully developed or documented.
- Maintain professional skepticism; if you get an explanation for the situation think about whether it makes sense. Continue to observe over time to see if the situation plays out as expected.
- Maintain documentation of the issue—your thoughts and decisions all along the way, and the parties with whom you discussed these issues—to review later as may be necessary.
- Even if you are successful in a particular situation, you might find that there are other implications that make it impossible to continue working at a company. In this situation you should seek employment elsewhere.
- Depending on the severity of the issue, you may want to consult with people that you respect from outside the company. Also, consider whether you need to consult with an attorney.

Our hope for you is that you never need to use this decision tree. However, if you do, we hope you find it helpful. Share your comments with us at: BusIndNews@aicpa.org

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Ethics Decision Tree
For CPAs in Business & Industry

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ET Section 102
Integrity and Objectivity

.01—Rule 102—Integrity and objectivity. In the performance of any professional service, a member shall maintain objectivity and integrity, shall be free of conflicts of interest, and shall not knowingly misrepresent facts or subordinate his or her judgment to others.

[As adopted January 12, 1988.]

.04—102.3—Obligations of a member to his or her employer’s external accountant. Under rule 102 [ET section 102.01], a member must maintain objectivity and integrity in the performance of a professional service. In dealing with his or her employer’s external accountant, a member must be candid and not knowingly misrepresent facts or knowingly fail to disclose material facts. This would include, for example, responding to specific inquiries for which his or her employer’s external accountant requests written representation.

[Effective November 30, 1993.]

.05—102.4—Subordination of judgment by a member. Rule 102 [ET section 102.01] prohibits a member from knowingly misrepresenting facts or subordinating his or her judgment when performing professional services. Under this rule, if a member and his or her supervisor have a disagreement or dispute relating to the preparation of financial statements or the recording of transactions, the member should take the following steps to ensure that the situation does not constitute a subordination of judgment:

1. The member should consider whether (a) the entry or the failure to record a transaction in the records, or (b) the financial statement presentation or the nature or omission of disclosure in the financial statements, as proposed by the supervisor, represents the use of an acceptable alternative and does not materially misrepresent the facts. If, after appropriate research or consultation, the member concludes that the matter has authoritative support and/or does not result in a material misrepresentation, the member need do nothing further.

2. If the member concludes that the financial statements or records could be materially misstated, the member should make his or her concerns known to the appropriate higher level(s) of management within the organization (for example, the supervisor’s immediate superior, senior management, the audit committee or equivalent, the board of directors, the company’s owners). The member should consider documenting his or her understanding of the facts, the accounting principles involved, the application of those principles to the facts, and the parties with whom these matters were discussed.

3. If, after discussing his or her concerns with the appropriate person(s) in the organization, the member concludes that appropriate action was not taken, he or she should consider his or her continuing relationship with the employer. The member also should consider any responsibility that may exist to communicate to third parties, such as regulatory authorities or the employer’s (former employer’s) external accountant. In this connection, the member may wish to consult with his or her legal counsel.

4. The member should at all times be cognizant of his or her obligations under interpretation 102.3 [ET section 102.04].
Notes to Ethics Decision Tree
For CPAs in Business & Industry

1. When speaking with your manager or a more senior executive, carefully gauge your satisfaction with the response. Bear in mind that your manager or other executive might be a party to the situation that you have observed, so approach the response with the necessary degree of professional skepticism.

2. It appears you have successfully managed your way through this challenge. It is recommended that you maintain and secure all documentation related to this matter as described in your records retention policy or as recommended by your legal counsel in case the issue resurfaces. Has the organization’s processes, internal control system, and culture changed in response to this matter? Are these changes sufficient to minimize the recurrence of a challenge like this one? Evaluate your answers and consider consulting with management, an outside mentor or other neutral party whom you respect.

3. Consider whether it is appropriate for you to continue your employment at this company. Consider the severity and implications of the issue you have identified and whether it should be reported to the outside accountants, regulatory agency, bank or other lending institution, owner or investor committee, BoD, or another party.

ETHICS HOTLINE
The AICPA Professional Ethics Team maintains a hotline for members to make inquiries about the Code of Conduct, and for advice when facing situations that challenge their professional ethics. To access the Ethics Hotline dial 1-888-777-7077 and follow the prompts to be routed to the Ethics team.