

ETHICS FOR MARYLAND



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CHAPTER 1

ETHICS DEFINED

LEARNING OBJECTIVES:

After studying this chapter you will be able to:

1. Define ethics.
2. Differentiate between amoral and ethical values.
3. List and characterize two systems of ethics.
4. Differentiate between legal versus ethical codes.
5. Discuss the development of law and ethics.

Ethics is the “science of morals”. A moral is an accepted rule or standard of human behavior. The understanding of “accepted” is “accepted by society”, and accepted only insofar as the behavior in question being behavior that affects others in the society, even if only indirectly. The implication of this definition is therefore that private actions that have no impact on others are a matter for personal morality, which is not of business or organizational concern.

However, the distinction between personal morality and business morality may not always be so clearly defined. This is because individuals bring personal values to their jobs and to the real or perceived problems of moral choice that confront them at work. Moral choices sometimes must be made because of tensions within individuals, between individuals, or between individuals and what they believe to be the values that drive their organizations.

Furthermore, business organizations do not operate in a social vacuum. Because of the ways business organizations can and do affect the lives and livelihoods of society at large, some would argue that business organizations are kind of “moral agents” in society. Therefore managers and general public alike often wrestle with defining exactly what constitutes the ethical way of doing business, and what constitutes proper constraints on individual self-interests, and by whom shall these constraints be imposed.

A further complexity results from the fact that businesses are increasingly becoming global in nature. Different countries have or seem to have vastly different customs and values. Understanding and assessing whether and how these different cultural and ethical conflicts should be taken into account is often most difficult.

ATTITUDES TOWARD ETHICS

AMORAL:	Condone any actions that contribute to the corporate aim. Getting away with it is the key. No set of values other than greed.
LEGALISTIC:	Obey the letter of the law but not the spirit of

	it, especially if it conflicts with profits. Ethics ignored until it becomes a problem
RESPONSIVE:	Take the view that there is something to gain from ethical behavior, Using ethics as a tool to attain corporate aim.
EMERGING:	Ethical values becoming part of the culture. Codes of ethics being action documents, and likely to contain statements reflecting core value,
ETHICAL:	Total ethical profile. Everything done is ethical, and the right thing always done by everyone. The ideal.

In general, a key focus of ethics is the concept of integrity (or honesty). Integrity in broad terms will imply that no business-persons in the course of their business functions should be party to the falsification of any facts or information or make any statement which knowingly is misleading, false or deceptive in a material particular.

Another major focus of ethics is professional competence and due care, which implies that business professionals should always perform their functions in accordance with law and regulations. In other words, business transactions and professional functions should not be undertaken unless one possesses the required competence and technical skills.

A more controversial focus is the area of freedom from conflicts of interests. The preferred position of many is that one should always avoid concurrent involvement in any business, occupation or activity, which might result in the compromising of integrity, objectivity and independence of decision making.

ETHICAL SYSTEMS

Utilitarianism (teleological ethics)	The promotion that the best long-term interest of everyone concerned should be the moral standard: one should take those actions that lead to the greatest balance of good versus bad consequences
Deontology (Kantian ethics)	It deals with the concept of duty and the rightness of acts. It emphasizes maxims, duties, rules, and principles that are so important that they should be followed whatever the consequences.

In defining law and ethics and their relationship to each other it is necessary to distinguish between moral and legal rights and duties. Morally, a person's rights consist of claims that he can

justly make to the conditions of well-being; his duties consist of what he can justly contribute to well being. Legal rights and duties - that is, claims and obligations enforceable at law - may or may not be fully in harmony with prevalent moral opinion systems in which law and ethics and religion are closely interwoven. The impact of moral opinion on law varies with the type of political structure and influence of public opinion.

In free societies the ultimate justification of law is that it serves moral ends. But the dependence of law on moral principles must not be taken to imply that there is a set of moral principles which can be laid down for guidance. However, most free societies are coming to be more or less consistent in principles that draw the line between law and morals. The task of ethics becomes two-fold: to bring out what is involved in the notion of a principle or norm of action and to recognize ideals that serve as agencies of guidance and control.

A number of consistent principles recognized in modern society are the individual, responsibility and equity. The end of law is to secure the greatest possible general individual self-assertion. In the Judeo-Christian ethic responsibility is a given: the best ordering of human society in which the individual may come to full manhood and satisfying existence. On the basis of equitable doctrine we can say confidently that morality is inseparable from the legal order; that right and wrong is part of the legal order.

HISTORICAL FOUNDATIONS OF LAW AND ETHICS

The great religions of the world gave birth to several concepts that evolved into structural precepts for society. A commonality of precepts evolved with the passing of tribal customs and tribal belief systems and the rise of the great religions of the world.

"The monotheistic idea of God unifies and coordinates the spiritual goods of the race. The unity of GOD involves the unity of all classes of men. This is a long step toward equality. The sense of sin became part and parcel of the common consciousness. It is a leveler and equalizer." For the good of the tribal society now becomes for the good of the individual. It must come to pass that a given society, if it is to retain the right to exist, must be continually extending the experience of its best things to men who were at one time outside, the pale of the best. The principle of individuality, once established, draws after it the principle of progress." "If it amounts to this, that wherever you find man, you find the eternal goods, and therefore the highest worth. The scale of market prices for the common man is forever disarranged by the discovery in him of something that is above price."

Two of the primary maxims in ethics are the utilitarian rule "Each man is to count for one, nobody for more than one". The second is Kant's--Always treat humanity, whether in yourself or another, as a person, and never as a thing."

"The only ground for counting every body as one, and nobody as more than one is the presence in all men of a something or other which possesses such value that existing social forms and economic

accumulations cannot bid against it."

"The social question is the moral question, first, because its ultimate root is a choice between divergent ideals of the state, that , between different ways of viewing and organizing the total human life in time and space; and secondly, because, as a consequence, the question concerning the worth of the labor turns into the question concerning the worth of the laborer". The history of conscience is the history of the individual where 'conscience' means knowing along with " ...nothing can be good for one man that is not law for all men."

CONCLUSIONS

In the historical development of law there are many different points of view. It is for this reason that the law is unable to accept without modification many of the results of ethical inquiry. In modern terminology law creates a duty "...there are no properties of goodness and badness that states of affairs an inherently possess, and no properties of rightness or wrongness that inhere in actions."

Value judgment in a broad sense compares contrasted ways of life; rationality, prudence and stability, (one of pleasure and happiness) versus the state of anxiety, confusion, inner turmoil and impulsive rashness. The first is a "good" way of life; the other is a "bad" way in terms of value. The best way of life involves the guidance of reason, and also the way of knowledge, of understanding, of relative freedom from error.

Moral responsibility rests solely on the attitude displayed in so-called "choice". The act of choosing is essentially a proper and stringent expression of the ethical. Whenever in a stricter sense there is a question of an either/or one can always be sure that the ethical is involved.

An ethic must first decide upon the kind of social effects which it desires to achieve and the kind which it desires to avoid. It must then decide, as far as our knowledge permits, what acts will promote the desired consequences; these acts it will praise, while those having a contrary tendency it will condemn. To the extent to which man has freedom, he needs a personal morality to guide his conduct. "Good and evil grow up together and are bound in an equilibrium that cannot be surrendered. The most we can do is try to tilt the equilibrium toward the good." The least we can do is be aware of our standards of conduct least "...the habit of being amoral should make the immoral come to seem right."

CHAPTER 2

AICPA ETHICS

LEARNING OBJECTIVES:

After studying this chapter you will be able to:

1. Differentiate between rulings and principles of the AICPA' Code of Professional Conduct.
2. Briefly describe the six principles.
3. List the eleven rules.
4. Outline ethics rulings on independence.
5. List consulting services prohibited by the Sarbanes-Oxley (SOX) Act of 2002.
6. Outline the standards for tax services
7. Explain disciplinary mechanisms within the profession.
8. List the key features of corporate responsibility law (Sarbanes-Oxley act).

This chapter covers the AICPA's *Code of Professional Conduct*, Statements on Standards for Consulting Services, and the disciplinary systems within the accounting profession. This chapter has six subunits. The first section is a condensed but comprehensive summary of the AICPA Code of Conduct. The second section contains summaries of AICPA Ethics Interpretations and Professional Ethics Rulings under the 11 Rules of Conduct. The third section addresses Statements on Standards for Tax Services. The fourth section lists some of the consulting services prohibited by the Sarbanes-Oxley (SOX) Act of 2002. The fifth section covers disciplinary systems within the profession. The final section outlines the key features of the SOX.

AICPA's CODE OF PROFESSIONAL CONDUCT

It consists of two sections: Principles and Rules. The six principles, which provide the framework for the rules, are goal-oriented and aspirational but nonbinding.

Synopses of the Six Principles

1. *Responsibilities.* Members should exercise sensitive professional and moral judgments when carrying out their professional responsibilities. Members should accept the obligation to act in a way that will serve the public interest, honor the public trust, and demonstrate commitment to professionalism. A distinguishing mark of a profession is acceptance of its responsibility to the public.
2. *The Public Interest.* Members should act to benefit the public interest, honor the public trust, and demonstrate commitment to professionalism. The AICPA adopted the ethical

standards because a distinguishing mark of a profession is an acceptance of responsibility to the public.

3. *Integrity.* Members should perform all professional responsibilities with the highest sense of integrity to maintain public confidence.
4. *Objectivity and Independence.* A member should maintain objectivity and be free of conflicts of interest. A member in public practice should be independent in fact and appearance when providing attestation services. Objectivity is a state of mind, a quality that lends itself to a member's services. It is a distinguishing feature of the profession. The principle of objectivity imposes the obligation to be impartial, intellectually honest, and free of conflicts of interest.
5. *Due Care.* A member should follow the profession's technical and ethical standards, strive for improved competence and quality services, and discharge professional responsibility to the best of the member's ability. Members must adequately plan and supervise any activity for which they are responsible.
6. *Scope and Nature of Services.* A member in public practice should follow the Principles of the *Code of Professional Conduct* in determining the nature and scope of services.

Synopses of the Eleven Rules

Rule 101 — Independence. A member in public practice should be independent when performing professional services as required by standards-setting bodies.

- (1) In this context, rules of the state boards of accountancy, state CPA societies, the Independence Standards Board, the SEC, the General Accounting Office, and other bodies may be relevant.
- (2) Relevant AICPA standards-setting bodies are the Auditing Standards Board (ASB), Accounting and Review Services Committee, and Management Consulting Services Executive Committee. The foregoing bodies are all authorized to promulgate attestation standards.
- (3) The ASB issues Statements on Auditing Standards. Thus, SAS 1 is consistent with the requirement for auditors to maintain an independence in mental attitude. To inspire public confidence, an auditor must not only be independent (intellectually honest) but also be recognized as independent (free of any obligation to, or interest in, the client).
- (4) The fourth general attestation standard likewise requires practitioners to maintain an independence in mental attitude when performing attest engagements.

- (5) Under Statements on Standards for Accounting and Review Services, an accountant may not report on a review of the financial statements of a nonpublic entity if (s)he is not independent.
- (6) According to the AICPA's Statements on Standards for Attestation Engagements, a practitioner must also be independent to examine or apply agreed-upon procedures to prospective financial statements.
- (7) SEC independence regulations were revised in accordance with the Sarbanes-Oxley Act of 2002.
- (a) Audit committees must preapprove the services performed by accountants (permissible nonaudit services and all audit, review, and attest engagements). Approval must be either explicit or in accordance with detailed policies and procedures. If approval is by the latter, the audit committee must be informed, and no delegation of its authority to management is allowed. However, preapproval is not needed for nonaudit services representing less than 5% of the annual amount paid to the accountant if (1) the services were not recognized as nonaudit at the time of the engagement, and (2) the audit committee approves prior to completion of the audit.
 - (b) An issuer must disclose in its proxy statement or annual filing fees paid to the accountant segregated into four categories: (1) audit, (2) audit-related, (3) tax, and (4) all other. The disclosure is for the two most recent years and must describe the services in (2)-(4).
 - (c) The lead and concurring (reviewing) audit partners must rotate every 5 years, with a 5-year time-out period. Other audit partners must rotate every 7 years, with a 2-year time-out.
 - (d) An accountant is not independent if, during the audit and the period of the professional engagement, any audit partner (excluding specialty partners such as tax partners) earns or receives compensation for selling services (excluding audit, review, or attest services) to the audit client.
 - (e) Conflicts of interest. An accounting firm is not independent with respect to an audit client if a former partner, principal, shareholder, or professional employee accepts employment with a client if (s)he has a continuing financial interest in the firm or is in a position to influence the firm's operations or financial policies. Moreover, an accounting firm is not independent if a CEO, CFO, controller, or person in an equivalent position for an issuer was employed by that firm and participated in any capacity in the audit of that issuer during the year before the

beginning of the audit.

- (f) Communications with the audit committee by the accounting firm must include (1) all critical accounting policies and practices; (2) all material alternative accounting policies and practices within GAAP that were discussed with management; and (3) other material written communications with management, such as management representations and schedules of unadjusted audit differences. These communications must be prior to filing the audit report with the SEC.

Rule 102 — *Integrity and Objectivity.* A member shall maintain objectivity and integrity, be free of conflicts of interest, not knowingly misrepresent facts, and not subordinate his/her judgment to others when performing professional services.

Rule 201 — *General Standards.* A member shall comply with the following:

- (1) Undertake only those services that the member can reasonably expect to complete with professional competence.
- (2) Exercise due professional care when performing professional services.
- (3) Adequately plan and supervise performance of professional services.
- (4) Obtain sufficient relevant data to provide a reasonable basis for conclusions in relation to any professional service.
 - (a) Proficiency. Auditors must have adequate technical training and proficiency. According to SAS 1, both education and experience, as well as proper supervision, are necessary. Objectivity and independent judgment are necessary in the preparation of the audit opinion. An auditor must have experience and seasoned judgment to accept final responsibility for an audit opinion.
 - (b) Due professional care must be exercised in the planning and performance of the audit and the preparation of the report. According to SAS 1, an auditor should have the degree of skill commonly possessed by other auditors and must exercise it with reasonable care and diligence. An auditor should also exercise professional skepticism. The exercise of due professional care allows the auditor to obtain reasonable assurance. Absolute assurance is impracticable due to characteristics of fraud such as concealment by collusion, withheld or falsified documentation, or management override of controls.

Rule 202 — *Compliance with Standards.* A member who performs professional services must comply with promulgated standards.

Rule 203 — *Accounting Principles.* A member shall not express an opinion or make an affirmative statement about conformity with GAAP or state that (s)he is not aware of any material modifications that should be made to achieve conformity with GAAP, given any departure from an accounting principle promulgated by bodies designated by the AICPA Council to establish such principles that has a material effect on the financial statements or data taken as a whole. However, if the member can demonstrate that, due to unusual circumstances, the financial statements or data would have been misleading without a departure from GAAP, the member can comply with the rule by describing the departure, its approximate effects, if practicable, and the reasons compliance with the principle would be misleading.

Rule 301 — *Confidential Client Information.* A member in public practice cannot disclose confidential client information without the client's consent. However, this Rule does not affect a CPA's obligations

- (1) To comply with a validly issued and enforceable subpoena or summons or with applicable laws and regulations
- (2) To discharge his/her professional obligations properly under Conduct Rules 202 and 203
- (3) To cooperate in a review of the CPA's professional practice under AICPA or state CPA society or board of accountancy authorization
- (4) To initiate a complaint with or respond to any inquiry made by the professional ethics division, trial board of the AICPA, or an investigative or disciplinary body of a state society or board of accountancy

Rule 302 — *Contingent Fees.* A contingent fee is established as part of an agreement under which the amount of the fee is dependent upon the finding or result.

- (1) The receipt of contingent fees by a member is prohibited when the member performs an audit, a review, a compilation when the report will be used by third parties and the report does not disclose the CPA's lack of independence, or an examination of prospective financial information.
- (2) A contingent fee is not permitted for preparing an original or amended tax return or claim.
- (3) Fees are not deemed to be contingent if fixed by courts or other public authorities, or in tax matters, if they are based on the results of judicial proceedings or the findings of governmental agencies.

Rule 501 — *Acts Discreditable.* A member shall not commit an act that is discreditable to the

profession. Withholding as a result of nonpayment of fees for a completed engagement certain information contained in the client's books would not be considered such an act. The member's duty to return client records is absolute. However, the duty to return other information not related to the client's books and records is not absolute. Although the client's financial information may be incomplete as a result, if fees for a completed engagement have not been paid, such other information may be withheld. Thus, the duty to return is conditional upon payment of fees with respect to information such as adjusting, closing, combining, or consolidating entries and information normally found in books of original entry and general or subsidiary ledgers.

Rule 502 — *Advertising and Other Forms of Solicitation.* A member in public practice shall not seek to obtain clients by advertising or other forms of solicitation done in a false, misleading, or deceptive manner. Solicitation through coercion, overreaching, or harassing conduct is prohibited.

Rule 503 — *Commissions and Referral Fees.* A member in public practice shall not accept a commission for recommending or referring to a client any product or service, or for recommending or referring any product or service to be supplied by a client, if the member performs for that client an audit, a review, a compilation when a third party will use the financial statement and the report does not disclose the CPA's lack of independence, or an examination of prospective financial information.

- (1) Permitted commissions must be disclosed to any person or entity to whom the member recommends a product or service.
- (2) A member who accepts a referral fee for recommending services of a CPA or who pays a referral fee to obtain a client must disclose the arrangement to the client. A referral fee is compensation for recommending or referring any service of a CPA to any person. Referral fees are not considered commissions.

Rule 505 — *Form of Organization and Name.* A member may practice public accounting only in a form of organization allowed by law or regulation that conforms with resolutions of the AICPA Council.

- 1) The firm name must not be misleading.
- 2) Names of past owners may be included in the name of the successor organization.
- 3) A firm cannot designate itself as "members of the AICPA" unless all CPA owners are members.

INTERPRETATIONS AND RULINGS

Interpretations and rulings are presented for each of the eleven Rules. The Interpretations are in outline format followed by brief summaries of the Rulings.

Rule 101 — *Independence.*

A. Interpretation 101-1 (Interpretation of Rule 101)

1. Independence is impaired if, during the period of the professional engagement, a covered member

- 1) Had a direct financial interest or a material indirect financial interest in the client.
- 2) Was a trustee of any trust or executor of any estate that had a direct or material indirect financial interest in the client AND (1) the covered member's position conferred investment authority, (2) the trust/estate owned more than 10% of the client, or (3) the interest of the trust/estate was more than 10% of its total assets.
- 3) Had any joint, closely held investment that was material to the covered member.
- 4) Had a loan to or from a client, any of its officers or directors, or an individual owning at least 10% of the client. Exceptions are grandfathered loans and certain other permitted loans.

2. Independence is impaired if, during the period of the professional engagement, a firm partner or professional employee, such individual's immediate family, or a group of these individuals acting together owned more than 5% of the client.

3. Independence is impaired if, during the period covered by the financial statements or during the period of the professional engagement, a firm, or partner or professional employee of the firm, was

- 1) Also associated with the client as an officer, director, employee, promoter, underwriter, or voting trustee, or in a management capacity.
- 2) A trustee for any pension or profit-sharing trust of the client.

4. An individual may have been employed by the client or associated with the client in a capacity listed in Interpretation 101-3. Independence is impaired if (1) the employment or association overlapped the engagement, and (2) the individual participated in the engagement or was able to influence it. Independence is also impaired if the individual was otherwise a covered member relative to the client unless the individual dissociates from the client by

- 1) Ending any relationship described in Interpretation 101-3.
- 2) Disposing of any direct or material indirect financial interest in the client,

- 3) Collecting or repaying any loans to or from the client (except as permitted under the rules for grandfathered loans),
- 4) Ceasing participation in any client-sponsored employee benefit plan (unless the client is legally required to allow participation and the individual pays the full cost), and
- 5) Liquidating or transferring any vested benefits in a client plan as soon as legally permitted. This is not required if a large penalty would result.

5. A covered member's immediate family is subject to Rule 101. However, independence is not impaired solely because

- 1) An immediate family member was employed by the client in a non-key position.
- 2) As part of his or her employment, an immediate family member of one of the following participated in a benefit plan that is a client, is sponsored by a client, or invests in a client if the plan is offered to all similarly situated employees:
 - a) A partner or manager who provided at least 10 hours of nonattest services to the client
 - b) Any partner in the office where the lead engagement partner primarily practiced in relation to the engagement

6. Independence is impaired if an individual who is participating on the engagement team, who can influence the engagement, or who is a partner in the office where the lead engagement partner primarily practices, has a close relative who

- 1) Occupied a key position with the client,
- 2) Held a material financial interest in the client that was known to the individual, or
- 3) Held a financial interest that permitted significant influence over the client.

7. Because listing all situations in which an appearance of a lack of independence might arise is not feasible, members also should consider whether a relationship between the member and the client or an associate of the client might lead to a reasonable conclusion that independence is lacking.

8. Under Rule 101, materiality is determined by aggregating the interests of the covered member and his/her immediate family.

B. Interpretation 101-2 (Employment or association with attest clients)

A former partner or professional employee (POPE) of the firm who is employed by or associated with an attest client in a key position impairs the firm's independence unless

- (1) Amounts due to the former POPE are not material to the firm, and the payment

formula is fixed during the payout period. Retirement benefits may also be adjusted for inflation, and interest may be paid.

- (2) The former POPE cannot influence the firm's operations or financial policies.
- (3) Once employed or associated with the client, the former POPE does not participate or appear to participate in, and is not associated with, the firm, regardless of compensation, for example, by consulting, use of an office, or inclusion in membership lists.
- (4) The engagement team considers the risk that the POPE's knowledge of the audit plan will reduce audit effectiveness.
- (5) The firm assesses when team members can effectively deal with the POPE.
- (6) The engagement is reviewed to determine whether team members maintained professional skepticism in dealings with the POPE.

A team member's consideration of employment or association with the client impairs independence absent prompt reporting to the firm and removal from the team.

C. Interpretation 101-3 (Performance of nonattest services)

- 1) Before a member and his or her firm performs nonattest services (such as tax or consulting services) for an attest client, (s)he must comply with Interpretation 101-3 to avoid impairment of independence. If the applicable independence rules of an authoritative body (e.g., the SEC or a state board of accountancy) are more restrictive, the member must comply with them.
- 2) General Requirements. Performing management functions or making management decisions impairs independence, but providing advice, research, and recommendations does not.
 - a) The member should be satisfied that the client will make an informed judgment about the results of nonattest services and be able to designate a competent employee (preferably a senior manager) to oversee the services; evaluate their adequacy and results; make management decisions and perform management functions; accept responsibility for results; and establish and maintain internal controls.
 - b) The member and client should agree about the objectives and limitations of the engagement, the services to be performed, and mutual responsibilities. The understanding should be documented in writing. This requirement does

not apply to routine services, those provided before the client became an attest client, and those performed before 2005.

- 3) General activities that impair independence include
 - a) Exercise or possession of authority over transactions on a client's behalf
 - b) Preparing source documents evidencing transactions
 - c) Custody of client assets
 - d) Supervision of client employees in normal activities
 - e) Determining member recommendations to be implemented
 - f) Reporting to the board on behalf of management
 - g) Service as a stock transfer or escrow agent, registrar, or general counsel
- 4) Examples of nonattest services that may not impair independence if the general requirements are met include bookkeeping, disbursement, benefit plan administration (e.g., preparing participant account valuations and statements), investment advisory, finance, executive search, business risk consulting, and IT (but designing a system or operating a network impairs independence).
- 5) An appraisal, valuation, or actuarial service impairs independence if the results are material to the financial statements and significant subjectivity is involved. For example, a valuation for a business combination, but not an actuarial valuation for a pension liability, usually involves significant subjectivity. Furthermore, appraisal, valuation, and actuarial services not performed for financial statement purposes do not impair independence if the other requirements of Interpretation 101-3 are satisfied.
- 6) Internal audit assistance services impair independence unless the member ensures that the client understands its responsibility for internal control and managing the internal audit function. Accordingly, the member must ensure that the client designates a competent individual to oversee internal audit; determines the scope, risk, and frequency of its activities; evaluates its findings; and evaluates the adequacy of its procedures.
 - a) The member should be satisfied that the client's governing body is informed about his/her role so that it can develop proper guidelines.
 - b) The member may assist in preliminary risk assessment, preparation of the audit plan, and recommendation of priorities.
 - c) Independence is impaired if the member, among other things, performs an ongoing monitoring or control function, determines which control recommendations are adopted, reports to the board on behalf of management, approves or is responsible for the overall audit work plan, or is a client employee or manager (or the equivalent).

- d) Services that are normal extensions of the external audit scope (e.g., confirming receivables or analyzing balances) and engagements under the attestation standards do not impair independence.
- 7) SEC regulations promulgated under the Sarbanes-Oxley Act of 2002 prohibit auditors of public companies from performing certain nonaudit services:
- a) Appraisal and other valuation services.
 - b) Designing and implementing financial information systems.
 - c) Internal auditing or actuarial functions unless the firm reasonably concludes it will not examine such work during the financial statement audit.
 - d) Management services.
 - e) Human resource services.
 - f) Bookkeeping if the firm also conducts an audit.
 - g) Expert services not pertaining to the audit.
 - h) Investment banking or advisory services.
 - i) Broker-dealer services.

D. Interpretation 101-4 (Honorary directorships and trusteeships of non-for-profit organizations)

A member in an honorary position will not impair independence if (s)he is associated with the financial statements of a not-for-profit organization that (s)he allows to use his/her name on letterheads and circulated materials to lend prestige to the organization. However, the member should not be able to vote or participate in board or management decisions and should be identified as an honorary director or trustee.

E Interpretation 101-5 (Loans from financial institution clients)

- 1) Grandfathered loans. Independence is not impaired by (a) unsecured loans that are not material to the covered member's net worth or (b) secured loans (including home mortgages) provided that the loans were obtained from a financial institution under its normal lending procedures, terms, and requirements. However, loans are grandfathered only if
 - a) They were kept fully current at all times after the borrower became a covered member, and the terms did not change in a way not allowed in the original agreement.
 - b) They were obtained
 - i) From a financial institution before it became a client requiring independence;

- ii) From a client not requiring independence and were sold to one requiring independence;
 - iii) Prior to February 5, 2001 and satisfied the requirements of the Interpretation then effective;
 - iv) During the period from February 5, 2001 through May 31, 2002, and the covered member complied with SEC regulations then effective; or
 - v) After May 31, 2002 from a client requiring independence before the borrower became a covered member relative to the client.
- 2) The date a grandfathered loan is obtained is the date a loan commitment or line of credit was granted.
- 3) The collateral for a secured grandfathered loan must equal or exceed the remaining balance of the loan during its term. If the loan exceeds the value of collateral, this excess must not be material to the covered member's net worth.
- 4) In the case of a limited partnership in which covered members have a combined interest exceeding 50% or a general partnership in which covered members control the partnership, the loan is ascribed to each covered member based on his/her legal liability as a limited or general partner. Even if this amount is zero, renegotiating the loan or entering into a new loan that is not an "other permitted loan" is deemed to impair independence.
- 5) Other permitted loans. The following loans are permitted even if the client is one for which independence is required, provided that they are obtained under normal lending procedures, terms, and requirements and are always kept current:
 - a) Automobile loans and leases collateralized by the automobile
 - b) Loans fully collateralized by the cash surrender value of insurance
 - c) Loans fully collateralized by cash deposits
 - d) Credit cards and overdraft reserve accounts with an aggregate outstanding balance of \$10,000 or less on a current basis by the payment due date

F. Interpretation 101-6 (Effect of actual or threatened litigation)

- 1) Litigation between client and member
 - a) Independence is impaired when litigation is begun by
 - i) The present management alleging deficiencies in audit work
 - ii) The member alleging management fraud or deceit
 - b) An expressed intention by the management to litigate against the member for alleged deficiencies in audit work will impair independence if it is probable that the claim will be filed.
 - c) Independence is not impaired when the threatened or actual litigation is

not related to the audit and the amount is not material. Examples include disputes over billings for services and results of tax advice.

2) Litigation by security holders (primary litigation)

- a) Shareholders may bring a class action against the client company or its management without impairing independence. Often the member and the client are both defendants, but if cross-claims are filed, adverse interests may arise and independence may be impaired.
- b) Cross-claims filed by the client to protect a right to legal redress in the event of a future adverse decision do not impair independence in the absence of a significant risk of a material settlement.
- c) Cross-claims against the member by an underwriter do not impair independence if no similar claims are made by the client.
- d) Cross-claims filed against the member by persons who are also officers or directors of other clients do not usually impair independence with respect to the other clients.

3) Other third-party litigation

- a) Litigation may be commenced against the member by a creditor or insurer that alleges reliance on financial statements of the client. This litigation does not affect independence if the client is not the plaintiff or is a nominal plaintiff. Independence may be impaired if the third party (e.g., an insurance company) is also a client of the member and there is a significant risk of a material settlement.
- 4) If a reasonable person would conclude that litigation poses an unacceptable risk of impairment of independence, the member should disengage or disclaim an opinion for lack of independence.

G. Interpretation 101-8 (Financial interests in nonclients having investor or investee relationships with the client)

1) Independence is impaired when

- a) A member has a direct or material indirect financial interest in the nonclient if the investee is material to the investor.
- b) A member has a material interest in a nonclient who is an immaterial investee of the client investor.
- c) A member can exercise significant influence over a nonclient investor who has an immaterial interest in the client investee.

- 2) Independence is not impaired if a member did not know about the financial interests described above.

H. Interpretation 101-10 (Effect on independence of relationships with entities included in governmental financial statements)

- 1) A financial reporting entity's basic financial statements (BFS) issued in accordance with U.S. GAAP include the government-wide statements (reporting governmental activities, business-type activities, and discretely presented component units), fund financial statements (reporting major funds, nonmajor governmental and enterprise funds, internal service funds, blended component units, and fiduciary funds), and other entities disclosed in the notes of the BFS. Disclosures should be made in the notes to the BFS about related organizations, joint ventures, jointly governed organizations, etc.
- 2) An auditor of the BFS of the entity must be independent of it. Nevertheless, a primary auditor need not be independent with respect to any fund, component unit, or disclosed entity if (s)he explicitly relies on reports by other auditors on such fund, etc. Moreover, (s)he need not be independent of a disclosed entity if the reporting entity is not financially accountable for it and the required disclosure does not include financial information.
 - a) Neither the covered member nor a member of his/her immediate family should occupy a key position with a fund, component unit, or disclosed entity.
- 3) An auditor of the statements of a fund, component unit, or disclosed entity who is not auditing the primary government must be independent only of the statements reported on. Nevertheless, the covered member or a member of his/her immediate family may not occupy a key position with the primary government.

I. Interpretation 101-11 (Independence and attest engagements)

- 1) This interpretation applies only to engagements, other than examinations and reviews, covered by SSAEs when the use of the report is restricted.
- 2) The following covered members and their immediate families must be independent in relation to the responsible party:
 - a) An individual on the attest engagement team.

- b) An individual who directly supervises or manages the attest engagement partner.
 - c) Individuals who consult with the attest engagement team about technical or industry-related matters specific to the engagement.
- 3) Independence is impaired if the firm had a material relationship with the responsible party prohibited under Rule 101.
- 4) A firm may provide nonattest services to the responsible party that are prohibited due to an association as an employer, director, officer, promoter, voting trustee, or pension trustee. However, if they do not relate directly to the subject matter of the attest engagement, independence is not impaired.
- 5) When the party that engages the firm is not the responsible party or associated therewith, individuals on the attest engagement need not be independent of the party that engaged the firm. However, they should consider their responsibilities regarding conflicts of interest.

J. Interpretation 101-12 (Independence and cooperative arrangements with clients)

- 1) Independence is impaired if, during the engagement or at the time of expressing an opinion, a member's firm had any material cooperative arrangement with the client.
 - a) A cooperative arrangement means joint participation in a business activity.

K. Interpretation 101-14 (Effect of APSs on independence rules)

- 1) The independence rules for an alternative practice structure (APS) apply to all structures in which "the 'traditional firm' engaged in attest services is closely aligned with another organization, public or private, that performs other professional services." For example, a CPA firm may be sold to another entity having subsidiaries or divisions such as a bank, an insurance company, a broker-dealer, and entities providing nonattest services (tax, management consulting, etc.). The owners and employees of the CPA firm become employees of one of the parent's subsidiaries or divisions and may offer nonattest services. Moreover, the original owners of the acquired CPA firm create a new CPA firm to offer attest services. The majority ownership of the new firm must be held by CPAs, but it leases employees, offices, and equipment from the parent, which

may also provide advertising and perform back office functions. The owners of the new CPA firm pay a negotiated amount for such services.

- 2) In the example above, the term “member or a member’s firm” includes the new CPA firm (the firm) and any leased or employed person or entity.
- 3) When two or more new CPA firms are “closely aligned” with another organization, issues arise as to whether owners of one perform services or have significant economic interests in another. Thus, if an owner of one performs services for another, (s)he is deemed to be an owner of both. Similar issues arise regarding managers (leased or otherwise).
- 4) In an APS, persons and entities included in “member or a member’s firm” are closely aligned with other persons and entities. The latter include direct superiors who can directly control the activities of an owner or manager. A direct superior is an immediate superior who can direct the activities of an owner or manager so as to be able to directly or indirectly derive a benefit. Direct superiors are subject to the same independence rules as persons included in “member or a member’s firm.”
- 5) An indirect superior (defined to include a spouse, cohabitant, or dependents of an indirect superior) is one or more levels above a direct superior and does not have a direct reporting relationship with the new CPA firm’s owners and managers. Less restrictive standards apply to indirect superiors and to other entities in the consolidated group.
 - a) These parties may not have a relationship involving a direct financial interest or an indirect material financial interest with an attest client of the new CPA firm that is material.
 - b) These parties also should not exercise significant influence over the attest client.
 - c) Other entities in the consolidated group and their employees may not be promoters, underwriters, directors, officers, or voting trustees of an attest client. However, with the foregoing exceptions, indirect superiors and other consolidated entities may provide services to an attest client that a member could not without impairing independence.
- 6) The new CPA firm may not perform a service requiring independence for any entity in the consolidated group.

- 7) Independence is impaired with regard to an attest client who exercises significant influence over, or has a material investment in, the parent.
- 8) Referrals within the consolidated group are subject to the provisions regarding conflicts of interest.

Rule 102— *Integrity and Objectivity.*

- a. Interpretation 102-1. Knowing misrepresentations of facts include knowingly making materially false and misleading entries in financial statements or records, failing to make corrections in materially false or misleading statements or records when the member has such authority, or signing a document with materially false and misleading information.
- b. Interpretation 102-2. If a conflict of interest arises that could impair objectivity When a member performs a professional service, Rule 102 will not prohibit the service if disclosure is made to and permission is obtained from the appropriate parties. However, an independence objection cannot be overcome by disclosure and consent. The following are examples of situations in which objectivity may be impaired:
 - 1) Performing litigation services for the plaintiff when the defendant is a client
 - 2) Providing tax or personal financial planning (PFP) services to both parties to a divorce
 - 3) Suggesting that a PFP client invest in a business in which the member has an interest
 - 4) Providing tax or PFP services to family members with conflicting interests
 - 5) Performing consulting services for a client that is a major competitor of a company in which the member has a significant financial interest, occupies a management position, or exercises influence
 - 6) Serving on a board of tax appeals that hears matters involving clients
 - 7) Providing services in connection with a real estate purchase from a client
 - 8) Referring a tax or PFP client to a service provider that refers clients to the member under an exclusive arrangement

- 9) Referring a client to a service bureau in which the member or a partner in the member's firm has a material interest
- c. Interpretation 102-3. In dealings with an employer's external accountant, a member must be candid and not knowingly misrepresent facts or fail to disclose material facts.
- d. Interpretation 102-4. If a member and his/her supervisor have a dispute about statement preparation or recording of transactions, the member should do nothing if the supervisor's position is an acceptable alternative and does not materially misrepresent the facts.
 - 1) If the member concludes that a material misstatement would result, (s)he should consult the appropriate higher level(s) of management and should consider documenting relevant matters.
 - 2) If, after such discussions, the member concludes that action was not taken, (s)he should consider the continuing relationship with the employer, the obligation to communicate with third parties, and the desirability of consulting legal counsel.
- e. Interpretation 102-5. Educational services, e.g., teaching and research, are professional services subject to Rule 102.
- f. Interpretation 102-6. Professional services involving client advocacy are governed by the Code, e.g., Rules 201, 202, 203, and 102. If independence is required for a service, Rule 101 also applies.
 - 1) If the service stretches the bounds of performance standards, exceeds sound and reasonable professional practice, or compromises credibility, and therefore poses an unacceptable risk of injury to the member's or the firm's reputation, the propriety of accepting the engagement should be considered.

Rule 201 — *General Standards.*

- a. Interpretation 201-1. A member should have the competence to complete professional services according to professional standards and with reasonable care and diligence.
 - 1) Competence involves technical qualifications and the ability to supervise and evaluate the work. It relates to knowledge of standards, techniques, and technical subject matter and to the ability to exercise sound

judgment.

- 2) In some cases, additional research and consultation is a normal part of performing services. However, if a member cannot gain sufficient competence, (s)he should suggest the engagement of someone competent.

Rule 202 — *Compliance with Standards. No interpretations.*

Rule 203 — *Accounting Principles.*

- a. Interpretation 203-1. Professional judgment should be used in determining what constitutes unusual circumstances requiring a departure from established principles to prevent the financial statements or data from being misleading. Events that may justify such departures are new legislation or evolution of a new form of business transaction. An unusual degree of materiality or conflicting industry practices ordinarily do not justify departures.
- b. Interpretation 203-2. The body designated to establish accounting principles for nongovernmental entities is the FASB. Unsuperseded SFASs, ARB5, and APB Opinions are accounting principles within the meaning of Rule 203. The GASB, with respect to Statements of Governmental Accounting Standards, is the designated body for state and local governments. The Federal Accounting Standards Advisory Board (FASAB), with respect to its Statements of Federal Accounting Standards adopted and issued beginning in March 1993, is the designated body for federal governmental entities.
- c. Interpretation 203-4. Rule 203 applies to all members regarding any affirmative statement about GAAP conformity.
 - 1) Thus, Rule 203 applies to members who sign client reports to regulatory agencies, creditors, or auditors that contain such representations.

Rule 301 — *Confidential Client Information*

- a. Interpretation 301-3. The rule against disclosure of confidential information does not prohibit the review of a member's professional practice pursuant to a purchase, sale, or merger of the practice. However, appropriate precautions (e.g., a written confidentiality agreement) should be taken so that the prospective buyer does not disclose any confidential client information.

Rule 302 — *Contingent Fees.*

- a. Interpretation 302-1. An example of circumstances in which a contingent fee is not allowed is the preparation of an amended income tax return for a client claiming a refund of taxes because of an inadvertent omission of a proper deduction.
 - 1) Examples of circumstances in which a contingent fee is allowed include
 - a) Representation of a client in an examination by a revenue agent
 - b) Representation of a client who is obtaining a private letter ruling
 - c) Filing an amended tax return claiming a refund based on a tax issue that is the subject of a test case involving a different taxpayer

Rule 501 — *Acts Discreditable*

- a. Interpretation 501-1. Client records must be returned after a client demands them even if fees have not been paid. This ethical standard applies even if the state in which the member practices grants a lien on certain records in his/her possession.
 - 1) Client records are defined as “any accounting or other records belonging to the client that were provided to the member by or on behalf of the client.”
 - 2) However, “a member’s workpapers — including, but not limited to, analyses and schedules prepared by the client at the request of the member — are the member’s property, not client records, and need not be made available.”
 - 3) Moreover, the duty to return is not absolute regarding certain other information. Examples include adjusting, closing, combining, and consolidating entries; information usually found in the journals and ledgers; and tax and depreciation carryforward information. When the engagement is complete, this information should be made available upon request in the medium in which it is requested if it exists in that medium. But information need not be converted from a nonelectronic format to an electronic one. Furthermore, the information need not be provided if all fees due the member have not been paid.
- b. Interpretation 501-2. When a court or administrative agency has made a final determination that a member has violated an antidiscrimination law, (s)he is deemed to have committed an act discreditable.
- c. Interpretation 501-3. In a governmental audit, failure to adhere to applicable

audit standards, guides, procedures, statutes, rules, and regulations is an act discreditable to the profession unless the report discloses the failure and the reasons therefore.

- d. Interpretation 501-4. Negligently making, or permitting or directing another to make, materially false and misleading entries in the financial statements or records; negligently failing to correct materially false and misleading statements when the member has such authority; or negligently signing, or permitting or directing another to sign, a document with materially false and misleading information is an act discreditable.
- e. Interpretation 501-5. A member must follow GAAP and the requirements of governing bodies, commissions, or regulatory agencies when preparing financial statements or related information or in performing attest services for entities subject to their jurisdiction. A material departure from the requirements is an act discreditable unless the member discloses the reasons.
- f. Interpretation 501-6. Solicitation or knowing disclosure of May 1996 or later CPA examination questions or answers is an act discreditable.
- g. Interpretation 501-7. Failing to comply with laws regarding timely filing of personal or firm tax returns or timely remittance of taxes collected for others is an act discreditable.

Rule 502 — *Advertising and Other Forms of Solicitation.*

- a. Interpretation 502-2. False, misleading, or deceptive acts are prohibited because they are against public interest. These prohibited activities include
 - 1) Creating false expectations of favorable results
 - 2) Implying the ability to influence any court, regulatory agency, or similar body
 - 3) Representing that specific services will be performed for a stated fee when it is likely at the time of the representation that the fees will be substantially increased and the client is not advised of the possibility
 - 4) Other representations that would cause a reasonable person to misunderstand or be deceived
- b. Interpretation 502-5. Members are permitted to render services to clients of third parties. If the third party obtained its clients through advertising, the members must ascertain that all promotional efforts were within the Rules of Conduct. Members must not do through others what they are prohibited from doing themselves.

Rule 503 — *Commissions and Referral Fees. No interpretations.*

Rule 505 — *Form of Organization and Name.*

- a. According to the relevant AICPA Council Resolution, a member may practice public accounting only in a firm or organization with certain characteristics.
 - 1) If such an entity performs any audit under the SASs, a review under the SSARs, or an examination of prospective information under the SSAEs or holds itself out as a firm of CPAs, an entity must have the following attributes:
 - a) CPAs must own a majority of the firm in terms of financial interests and voting rights.
 - b) A non-CPA owner, including an investor or commercial enterprise, must be actively engaged in providing services to clients as his/her/its principal occupation.
 - c) A CPA must have ultimate responsibility for all services provided.
 - d) A non-CPA owner must have a baccalaureate degree.
 - e) Non-CPA owners cannot hold themselves out to be CPAs, must abide by the Code, must complete the work-related CPE requirements, and are ineligible for AICPA membership.
 - f) Owners must own their equity in their own right.
 - g) Ownership must be transferred to the firm or to other qualified owners within a reasonable time if the owner ceases to be actively engaged in the firm.
 - 2) The characteristics of all other entities are considered to be whatever is legally permissible except as indicated in 3) below.
 - 3) If a firm or organization not meeting the foregoing requirements performs compilations under SSARs, a CPA must have ultimate responsibility for any such services and for each business unit performing such services. Moreover, any compilation report must be signed individually by a CPA.
- b. Interpretation 505-2. A member in the practice of public accounting may own an

interest in a separate business that performs the services for which standards are established. If the member, individually or with his/her firm or members of the firm, controls the separate business (as defined by U.S. GAAP), the entity and all its owners and employees must comply with the Code. Absent such control, the member, but not the separate business, its other owners, and its employees, would be subject to the Code.

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- c. Interpretation 505-3. The overriding focus of the Council Resolution, the Code, and other AICPA requirements is that CPAs remain responsible, financially and otherwise, for the attest work performed to protect the public interest. However, in the context of alternative practice structures (APSs), CPAs may own the majority of financial interests in the attest firm, but substantially all revenues may be paid to another entity in return for services and the lease of employees, equipment, etc. Nevertheless, given the previously mentioned safeguards, if the CPA-owners of the attest firm remain financially responsible under state law, they are deemed to be in compliance with the financial-interests requirement of the Resolution.

CONSULTING SERVICES PROHIBITED BY SARBANES-OXLEY ACT OF 2002

Title II of the Sarbanes-Oxley Act of 2002 prohibits most “consulting” services outside the scope of practice of auditors.

(a) These services are prohibited even if pre-approved by the issuer’s audit committee.

(b) Prohibited services include:

- Bookkeeping and related services,
- Design and implementation of financial information systems,
- Appraisal or valuation services (including fairness opinions and contribution-in-kind reports), (*Note:* The valuations relate to financial statement items and not valuations per se.)
- Actuarial services,
- Internal audit outsourcing, *Note:* “Operational” internal audits are allowed.
- Services that provide any management or human resources,
- Investment or broker/dealer services, and
- Legal and “expert services unrelated to the audit.”
- Any other service that the board determines, by regulation, is impermissible.

(c) Services Not Prohibited. Firms, however, may provide tax services (including tax planning and tax compliance) or others that are not listed, provided the firm receives pre-approval from the board. However, certain tax planning products, like tax avoidance services, may be considered prohibited nonaudit services.

STANDARDS FOR TAX SERVICES

The AICPA has issued eight Statements on Standards for Tax Services. The statements are enforceable under the AICPA's *Code of Professional Conduct*.

SSTS No. 1 — *Tax Return Positions*

- a. An AICPA member should not recommend a position unless (s)he has a good faith belief that the position has a realistic possibility of being sustained if challenged. A member may reach such a position on the basis of well-reasoned articles or treatises or pronouncements of the taxing authority.
- b. A member should not prepare or sign a return if (s)he knows it takes a position that cannot be recommended as stated in a. above.
- c. Despite a. and b., a member may recommend a position that is not frivolous (knowingly advanced in bad faith and improper) if (s)he advises disclosures. The member may prepare or sign a return containing such a position if the position is properly disclosed.
- d. A member should advise the taxpayer of possible penalties associated with the recommended tax return position.
- e. A member should not recommend a position that
 - 1) Exploits the taxing authority's audit selection process, or
 - 2) Is advanced solely to obtain leverage in the bargaining process.
- f. A member has the right and responsibility to be an advocate for the taxpayer. A taxpayer has no obligation to pay more taxes than legally owed.

SSTS No.2— *Answers to Questions on Returns*

- a. A member should make a reasonable effort to obtain appropriate answers to all questions on a tax return before signing as preparer.
- b. Examples of reasonable grounds for omitting an answer
 - 1) Information is not readily available, and the answer is insignificant with respect to taxable income or loss or the tax liability.
 - 2) Genuine uncertainty exists as to the meaning of the question in relation to the particular return.
 - 3) The answer to the question is voluminous, and the return states that the data will be supplied upon examination.

- c. A taxpayer is not required to explain on the return the omission of an answer when reasonable grounds exist for the omission. The member should consider whether the omission causes the return to be incomplete.

SSTS No. 3— *Certain Procedural Aspects of Preparing Returns*

- a. A member may rely without verification on information provided by the taxpayer or third parties. Reasonable inquiries should be made if information appears to be incorrect, incomplete, or inconsistent on its face or on the basis of other facts known. Prior returns should be consulted if feasible.
- b. Inquiries should be made to determine whether the taxpayer has met requirements to maintain books, records, or documentation to support deductions.
- c. A member who prepares a return should consider information known from another taxpayer's return if it is relevant, its consideration is necessary, and its use does not violate any law or rule of confidentiality.

SSTS No.4— *Use of Estimates*

- a. A member may use the taxpayer's estimates if it is impracticable to obtain exact data, and the estimates are reasonable under the facts.
- b. Estimates should be presented so as not to imply greater accuracy than exists.
- c. The taxpayer is responsible for providing the estimated data.
- d. Appraisals and valuations are not considered estimates.

SSTS No.5— *Departure from a Position Previously Conducted in an Administrative Proceeding or Court Decision*

- a. The treatment of an item as determined in an administrative proceeding or a court decision does not restrict the recommendation of a different tax treatment in later years, unless the taxpayer is bound to a specified treatment in the later year.

SSTS No.6— *Knowledge of Error: Return Preparation*

- a. The member should inform the taxpayer upon becoming aware of an error in a previously filed return or that the taxpayer did not file a required form.
- b. The member should recommend measures to take.

- c. The member is not obligated to inform the taxing authority and may not do so without the taxpayer's permission, unless required by law.
- d. If the member is requested to prepare a return when the taxpayer has not corrected a previous year's error, the member should consider whether to continue a professional relationship with the taxpayer or withdraw.
- e. If the member prepares the current return, the member should take reasonable steps to ensure that the error is not repeated.

SSTS No.7— *Knowledge of Error: Administrative Proceedings*

- a. The responsibilities are the same as stated in SSTS No. 6 except that they relate to representation of a taxpayer in an administrative proceeding.
- b. The taxpayer's agreement must be obtained to disclose the error to the taxing authority.
- c. Errors include a position on a return that no longer meets these standards (SSTS No. 1) because of retroactive legislation, judicial decisions, or administrative pronouncements. An error does not include an item with an insignificant effect.

SSTS No. 8— *Form and Content of Advice to Clients*

- a. When providing tax advice to a taxpayer, a member should use judgment to ensure that the advice reflects professional competence and meets the taxpayer's needs.
- b. When advising or consulting on tax matters, the member should follow SSTS No. 1.
- c. A member is not obligated to communicate with the taxpayer when subsequent developments affect previous advice. However, (s)he is obligated to do so when helping to implement the plans associated with the advice or when undertaking the obligation by specific agreement.
- d. Tax advice can be in any form. However, important, unusual, or complicated transactions should be in writing.

Note: Members may use a trade name as long as it is not deceptive or misleading. "Pay Less" may be construed as misleading for a tax service.

DISCIPLINARY SYSTEMS WITHIN THE PROFESSION

1. The AICPA's disciplinary mechanisms include the Professional Ethics Division and a joint trial board.

- a. The Professional Ethics Division investigates ethics violations. It imposes sanctions in less serious cases. For example, it may require an AICPA member to take additional CPE courses as a remedial measure.
- b. More serious infractions come before a joint trial board panel, which can acquit, admonish (censure), suspend, or expel a member. It may also take such other disciplinary, remedial, or corrective action as it deems to be appropriate. The *CPA Letter* publishes information about suspensions and expulsions.
 - 1) A decision of a trial board panel may be appealed to the full trial board. The determination of this body is conclusive.
 - 2) Upon the member's exhaustion of legal appeals, automatic expulsion without a hearing results when a member has been convicted of, or has received an adverse judgment for,
 - a) Committing a felony
 - b) Willfully failing to file a tax return
 - c) Filing a fraudulent tax return on the member's or a client's behalf
 - d) Aiding in preparing a fraudulent tax return for a client
 - 3) Automatic expulsion also occurs when a member's CPA certificate is revoked by action of any governmental agency, e.g., a state board of accountancy.
 - 4) Expulsion from the AICPA or a state society does not bar the individual from the practice of public accounting.
 - a) A valid state-issued license is required to practice.
 - b) Thus, violation of a state code of conduct promulgated by a board of accountancy is more serious than expulsion from the AICPA because it may result in revocation of the CPA certificate.
- c. Joint Ethics Enforcement Program (JEEP)
 - 1) The AICPA and most state societies have agreements that permit referral of an ethics complaint either to the AICPA or to a state society.

- 2) The AICPA handles matters of national concern, those involving two or more states, and those in litigation.
 - a) JEEP also promotes formal cooperation between the ethics committees of the AICPA and of the state societies.
2. The SEC, IRS, and PCAOB may also discipline accountants.
- a. The SEC may seek an injunction from a court to prohibit future violations of the securities laws. Moreover, under its Rule of Practice 2(e), the SEC may conduct administrative proceedings that are quasi-judicial.
 - 1) Pursuant to such proceedings, it may suspend or permanently revoke the right to practice before the SEC, including the right to sign any document filed by an SEC registrant, if the accountant
 - a) Does not have the qualifications to represent others
 - b) Lacks character or integrity
 - c) Has engaged in unethical or unprofessional conduct
 - d) Has willfully violated, or willfully aided and abetted the violation of, the federal securities laws or their rules and regulations
 - 2) Suspension by the SEC may also result from
 - a) Conviction of a felony, or a misdemeanor involving moral turpitude
 - b) Revocation or suspension of a license to practice
 - c) Being permanently enjoined from violation of the federal securities acts
 - 3) Some Rule 2(e) proceedings have prohibited not only individuals but also accounting firms from accepting SEC clients.
 - 4) Under the Securities Law Enforcement Act of 1990, the SEC may impose civil penalties in administrative proceedings of up to \$100,000 for a natural person and \$500,000 for any other person. Furthermore, the SEC may order a violator to account for and surrender any profits from wrongdoing and may issue cease-and-desist orders for violations.
 - b. The IRS may prohibit an accountant from practicing before the IRS if the person is incompetent or disreputable or does not comply with tax rules and regulations.

- 1) The IRS may also impose fines.
- c. The PCAOB was established by the Sarbanes-Oxley Act of 2002.
 - 1) A firm's registration application must contain information about a firm's quality control and a description of all actions pending against it. This information may have a great effect on enforcement actions and potential punishments. Moreover, the firm must give consent to cooperate with PCAOB investigations.
 - 2) The PCAOB has rule-making authority regarding quality control, ethics and auditing standards. These rules, especially those governing quality control, will have great relevance to enforcement actions.
 - 3) The PCAOB will inspect large firms annually and report violations to the SEC and state authorities. All attestation engagements, notably those in litigation, may be reviewed. The inspection also involves a quality control assessment. Furthermore, the inspection report must include the firm's response. The firm then has twelve months to correct the reported weaknesses.
 - 4) The PCAOB has substantially the same investigatory scope with respect to accountants as the SEC. The PCAOB may request that the SEC issue subpoenas to third parties, and it may deregister any uncooperative firm.
 - 5) The PCAOB has no injunctive power, but it may institute administrative proceedings. It may seek disassociation of a person from a registered firm, suspension (temporary or permanent) of the firm's registration, or a penalty of up to \$15 million. The extreme cases in which the harshest penalties may be imposed include repeated instances of negligent misconduct. By contrast, the SEC may impose the severest punishments when the firm has engaged in just one instance of highly unreasonable conduct.
3. State boards of accountancy and state CPA societies also have codes of ethics and/or rules of conduct.
 - a. State boards are governmental agencies that license CPAs to use the designation "Certified Public Accountant" and prohibit non-CPAs from performing the attest function. They can suspend or revoke licensure through administrative process.
 - 1) Like the AICPA, state boards have trial boards to conduct administrative hearings.
 - b. State societies are voluntary, private organizations that can admonish, suspend, or

expel members.

Note: A CPA may not claim to be endorsed by the Institute. A member may, however, state that (s)he is a member.

CHAPTER 3 MARYLAND ETHICS

LEARNING OBJECTIVES:

After studying this chapter you will be able to:

1. Outline the professional ethics and conduct for Maryland CPAs.
2. Summarize the ethical concepts promulgated in the Code of Professional Conduct.

.06 CODE OF PROFESSIONAL CONDUCT

A. Independence.

(1) A licensee who is performing an engagement in which the licensee is to issue a written certificate or opinion, other than one in which a lack of independence is disclosed, shall be independent with respect to the client in fact and appearance.

(2) Independence is considered to be impaired if, for example, during the period of a licensee's professional engagement, or at the time of issuing the written certificate or opinion, the licensee:

(a) Had or was committed to acquire any direct or material indirect financial interest in the client;

(b) Was a trustee of any trust, or personal representative of any estate, if this trust or estate had or was committed to acquire any direct or material indirect financial interest in the client;

(c) Had any joint, closely held business investment with the client or any officer, director, or principal stockholder of the client which was material in relation to the net worth of either the licensee or the client; or

(d) Had any loan to or from the client or any officer, director, or principal stockholder of the client other than loans of the following kinds made by a financial institution under normal lending procedures, terms, and requirements:

(i) Loans obtained by the licensee which are not material in relation to the net worth of the licensee,

(ii) Home mortgages, and

(iii) Other secured loans, except those secured solely by a guarantee of the licensee.

(3) Independence is also considered to be impaired if, during the period covered by the financial statements, during the period of the professional engagement, or at the time of issuing the written certificate or opinion, the licensee:

- (a) Was connected with the client as a promoter, underwriter, or voting trustee, a director, or officer or in any capacity equivalent to that of a member of management or of an employee;
 - (b) Was a trustee for any pension or profit-sharing trust of the client; or
 - (c) Received other compensation from a third party, or had a commitment to receive other compensation from the client or a third party, with respect to services or products procured or to be procured by the client.
- (4) The examples in §A(2) of this regulation are not intended to be all-inclusive.

B. A licensee may not in the performance of professional services knowingly misrepresent facts, or subordinate judgment to others. In tax practice, however, a licensee may resolve doubt in favor of the client as long as there is reasonable support for the licensee's position.

C. A licensee may not, during the period in which the licensee is engaged to perform any of the following services, and during the period covered by any historical financial statements involved in the listed services:

(1) Perform for a contingent fee any professional services for, or receive a contingent fee from a client for whom the licensee or the licensee's firm performs:

- (a) An audit or review of a financial statement;
- (b) A compilation of a financial statement, unless the licensee's compilation report discloses a lack of independence; or
- (c) An examination of prospective financial information; or

(2) Prepare an original or amended tax return or claim for a tax refund for a contingent fee for any client.

D. A licensee may not concurrently engage in the practice of certified public accountancy and in any other business or occupation which impairs independence or objectivity in rendering professional services.

E. With respect to other compensation:

(1) A licensee who receives or agrees to receive other compensation with respect to services or products recommended, referred, or sold by the licensee to another person shall make, not later than the making of the recommendation, referral, or sale, the following disclosures to the other person in writing:

- (a) If the other person is a client, the nature, source, and amount of the other compensation, or
- (b) If the other person is not a client, the nature and source only of any other compensation received from a third party;

(2) The disclosure required by this regulation shall be made regardless of the amount, as defined by Regulation .01A(4) of this chapter, of the other compensation involved;

(3) This regulation does not apply to payments received from the sale of all or a material part of an accounting practice, or to retirement payments to persons formerly engaged in the practice of public accountancy;

(4) Compliance with the requirements of this section does not constitute a defense to a charge of impaired independence under §A(3)(c) of this regulation.

F. A licensee may not pay a commission to a third party to obtain a client unless, before being engaged by the client, the licensee discloses to the client in writing the fact and the amount of the commission. This regulation does not apply to payments made by a licensee for the purchase of all or a material part of an accounting practice, or to retirement payments to persons formerly engaged in the practice of public accountancy.

G. Competence and Technical Standards.

(1) A licensee may not undertake any engagement for the performance of professional services which the licensee cannot reasonably expect to complete with due professional competence, including compliance, where applicable, with §G(2)—(4) of this regulation.

(2) A licensee may not permit the licensee's name to be associated with financial statements in such a manner as to imply that the licensee is acting as an independent certified public accountant with respect to these financial statements unless the licensee has complied with applicable generally accepted auditing standards, as such standards may be amended, modified, issued, or reissued. Statements on auditing standards issued, reissued, amended, or modified, from time to time, by the American Institute of Certified Public Accountants, and other pronouncements having similar generally recognized authority, are considered to be interpretations of generally accepted auditing standards, and departures therefrom shall be justified by those who do not follow them.

(3) A licensee may not issue a report asserting that financial statements are presented in conformity with generally accepted at that time accounting principles if these financial statements contain any departure from those accounting principles which have a material effect on the financial statements taken as a whole, unless the licensee can demonstrate that by reason of unusual circumstances the financial statements would otherwise have been misleading. In this case, the licensee's report shall describe the departure, the approximate effects thereof, if practicable, and the reasons why compliance with the principle would result in a misleading statement. For purposes of this regulation, generally accepted accounting principles are considered to be defined by pronouncements issued, reissued, amended, or modified, from time to time, by the Financial Accounting Standards Board and its predecessor and successor entities and similar pronouncements issued by other entities having similar generally recognized authority.

(4) A licensee in the performance of accounting and review services or management advisory services, consulting, financial planning, or tax services shall conform to the professional standards applicable to these services at the time the services are performed.

H. Responsibilities to Clients.

(1) Except by permission of the client or the heirs, successors, or personal representatives of the client, a licensee or any partner, officer, shareholder, or employee of a licensee may not voluntarily disclose information communicated by the client relating to and in connection with professional services rendered to the client by the licensee. This regulation does not:

- (a) Relieve a licensee of any obligations under §G of this regulation;
- (b) Affect in any way a licensee's obligation to comply with a validly issued subpoena or summons in a criminal or bankruptcy case;
- (c) Prohibit disclosures in the course of a quality review of a licensee's professional services; or
- (d) Preclude a licensee from responding to any inquiry made by the Board or any investigative or disciplinary body established by law or formally recognized by the Board.

(2) Members and agents of the Board and professional practice reviewers may not disclose any client information which comes to their attention from licensees in disciplinary proceedings or otherwise in carrying out their responsibilities, except that they may furnish this information to an investigative or disciplinary body of the kind referred to above.

(3) A licensee shall furnish to the licensee's client or former client, upon request and reasonable notice made within a reasonable time after original issuance of the document in question:

- (a) A copy of a tax return of the client;
- (b) A copy of any report, or other document, issued by the licensee to or for this client;
- (c) Any accounting or other records 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 account, but the licensee may make and retain copies of these documents when they form the basis for work done by the licensee; and
- (d) A copy of the licensee's working papers, to the extent that these working papers include records which would ordinarily constitute part of the client's records and are not otherwise available to the client.

I. Other Responsibilities and Practices.

(1) A licensee may not commit any act that reflects adversely on the licensee's fitness to engage in the practice of public accountancy.

(2) A licensee may not permit others to carry out on the licensee's behalf, either with or without compensation, acts which, if carried out by the licensee, would place the licensee in violation of the Code of Professional Conduct.

(3) A licensee may practice public accountancy only in a proprietorship, a partnership, or a professional corporation, organized in accordance with Business Occupations and Professions Article, Title 2, Annotated Code of Maryland.

(4) A licensee may not engage in the practice of public accountancy using a professional or firm name or designation which is misleading in any way, about the legal form of the firm, or about those who are partners, members, directors, or shareholders of the firm, or about any other matter. However, names of one or more former partners, members, directors, or shareholders may be included in the name of a firm or its successor, with the written consent of the former partner, member, director, or shareholder. A partner, member, director, or shareholder surviving the death of all other partners, members, directors, or shareholders may continue to practice under a firm name for 1 year after becoming a sole practitioner. An accounting firm may not use in its name terms such as "Group", "and Company", "and Associates", or similar terms which imply the presence in the firm of more licensees than those identified by name in the firm name unless the number of licensees associated with the firm, whether as partners, shareholders, members, directors, or full-time employees, exceeds the number of licensees named in the firm name.

(5) A licensee shall respond in writing to any communications from the Board requesting a response, within 30 days of the mailing of these communications, by registered or certified mail, to the last address furnished to the Board by the licensee.

(6) Advertising and Solicitation.

(a) A licensee may not use or participate in the use of any form of communication, written or oral, having reference to the licensee's professional services, which contains a false, fraudulent, misleading, deceptive, or unfair statement or claim.

(b) A licensee may not solicit clients by the use of coercion, duress, compulsion, intimidation, threats, overreaching, or vexatious or harassing conduct.

(c) A false, fraudulent, misleading, deceptive, or unfair statement or claim includes but is not limited to a statement or claim which:

(i) Contains a misrepresentation of fact;

(ii) Is likely to mislead or deceive because it fails to make full disclosure of relevant facts;

(iii) Is intended or likely to create false or unjustified expectations of favorable results;

(iv) Implies educational or professional attainments or licensing recognition not supported in fact;

- (v) Represents that professional services can or will be competently performed for a stated fee when this is not the case, or makes representations with respect to fees for professional services that do not disclose all variables that reasonably may be expected to affect the fees that will in fact be charged; or
- (vi) Contains other representations or implications that in reasonable probability will cause those of ordinary prudence to misunderstand or be deceived.
- (d) A licensee or CPA firm offering or performing public accounting services on an Internet webpage or website shall include the following information on the webpage or website:
 - (i) Name of the licensee or firm;
 - (ii) Principal place of business of the licensee or firm;
 - (iii) Business phone of the licensee or firm; and
 - (iv) The Maryland license or permit number issued by the Board accompanied by the language "Maryland license number" or "Maryland permit number", as appropriate.
- (e) A CPA firm webpage or website need not include the individual registration number of each CPA firm member.

ACTIVE CPA – INITIAL LICENSE

Applicants for a license must:

1. Satisfactorily complete a Board approved-accounting curriculum while earning a minimum of 150 semester hours or their equivalent.
2. Pass the Uniform CPA Examination. Examination candidates must pass each of the following sections of the Uniform CPA Examination with a grade of 75%: Business Law and Professional Responsibilities (LPR); Auditing (AUD); Accounting and Reporting (ARE); and Financial Accounting and Reporting (FARE).
3. After passing the Uniform CPA Examination, a candidate must complete a Home Study Course in Professional Ethics that is offered by the American Institute of Certified Public Accountants. The candidate must send a copy of the ethics course completion certificate with the Report of Practical Experience in order to complete the license application process.
4. Following passage of the Uniform CPA Examination, an applicant must file a Report of Practical Experience that documents that the applicant has a minimum of 2,000 hours of experience in accounting-related activities verified and endorsed by a licensed CPA.

Board Approved Accounting Curriculum

Applicants must have satisfactorily completed 150 semester hours, or their equivalent, (57 semester hours must be in accounting and related subjects) including the attainment of a baccalaureate or higher degree that meets the following requirement: A major in accounting on the baccalaureate level, or its substantial equivalent from an institution that is a member of the American Assembly of Collegiate Schools of Business; the Association of Collegiate Business Schools and Programs; is accredited by or is a constituent of an institution accredited by the Middle States Association of Colleges and Schools; or the equivalent regional accrediting association for other regional areas; or is recognized and approved by the Board.

Colleges and Universities Offering Accounting Degree Programs

Candidates with Accounting Degrees from Other Countries

The academic credentials of applicants who have earned their degrees from foreign colleges or universities must be evaluated to determine whether their educational preparation fulfills Maryland's education requirements to sit for the Uniform CPA Examination. There are many foreign credential service organizations that review the foreign credentials to determine whether they meet Maryland's examination requirements.

Accounting/Business Education - Curriculum

Candidates must document through official college or university transcripts that a minimum of 57 semester hours in accounting and related subjects were successfully completed. Applicants must document the following core courses (minimum credit hours required are in parenthesis):

Group 1 At least 27 semester hours of accounting education which include:

Auditing (3 hours)	Financial accounting (9 hours)
Cost accounting, (3 hours)	U.S. federal income tax (3 hours)

Group 2 A minimum of 30 undergraduate semester hours in:

Business ethics (3 hours)	Corporation or business finance (3 hours)
Economics (6 hours)	Management (3 hours)
Marketing (3 hours)	Oral communication (3 hours)
Statistics (3 hours)	U.S. business law (3 hours)
Written communication (3 hours)	

Applicants with a master's degree or higher from an accredited institution, need not complete 3 undergraduate semester hours of written communication to meet the requirement of a major in accounting on the baccalaureate level. Therefore, candidates with a Masters degree need only list 30 semester hours in Group 2 courses and do not have to have a course in written communication. Your transcript(s) must reflect 150 credit hours.

NOTE: (1) A higher than baccalaureate degree is not required to fulfill the 150 hour requirement. The Board will not accept substitution for the courses listed above nor accept less

than 3 credits in fulfillment of a requirement. When qualification is sought on the basis of a combination of undergraduate and graduate level courses, a candidate will receive credit of 3 semester hours for every 2 graduate hours successfully completed.

COURSE DESCRIPTIONS

The following course descriptions are given to assist you in completing the checklist, as these are the subjects that generate the most questions regarding eligibility. If you are uncertain of the eligibility of your course(s) as related to these descriptions, refer to SUPPLEMENTAL COURSE DESCRIPTIONS in the directions.

MANAGEMENT means a course in general business management, which includes such topics as planning, organizing, controlling, decision-making and leadership. Courses listed as Management, Principles of Management, or Organization and Management clearly meet this requirement. Courses in specialized areas i.e. "Personnel", "Production" do not qualify even if they have the word "management" in the course title.

U.S. BUSINESS LAW includes the analysis and study of the law of contracts, agency, employment, negotiable instruments, real property, personal property, sales and insurance.

WRITTEN COMMUNICATION courses should emphasize effective writing principles, problem analysis and the writing process. The course should include developing the reasoning processes needed to conceive, clarify and limit a thought and the discipline of gathering and organizing the details necessary for the clear development of thought in writing. Various stages of the process of composition, revision and editorial functions should be required. Courses, which may qualify, are those beyond the basic English composition classes. (Ex. Effective Writing, Written Communication for Business, Technical Writing, Business Writing.)

NOTE: The Maryland Board has determined that conferral of a Masters degree is indication that the candidate is proficient in the area of written communication. Therefore, candidates with a Masters degree need only list 30 semester hours in Group 2 courses and do not have to have a course in written communication. Your transcript(s) must reflect 150 credit hours.

ORAL COMMUNICATION courses should focus on the practical application and basic principles and techniques of public speaking. Included should be practice in the presentation of written information/reports, participation in group discussions and interview situations. Planning, organizing, delivering and critiquing both informative and persuasive speeches should be required. (Ex. The Art of Public Speaking, Business and Professional Speaking, Communication in Business, communication skills for Professionals)

BUSINESS ETHICS courses should examine the major ethical issues in business. The profit motive and the public good, social responsibility in corporations, environmental concerns, consumer and employee relations, confidentiality, whistle blowing, advertising and hiring practices should be discussed. (Ex. Business Ethics, Ethics and Professionalism in Accounting/Business) Note: other specialty fields' ethics courses do not qualify.

CORPORATION, PARTNERSHIP, LIMITED LIABILITY PARTNERSHIP, LIMITED LIABILITY COMPANY PERMIT APPLICATION

Initial Application fee - \$25.00. Permit Fee after approval - \$25.00

On-Line application

A Corporate applicant for a permit:

- a. Must meet the applicable requirements of the **Maryland Professional Service Corporation Act**.
- b. Must have a permanent office in Maryland or, at the time of application, submit proof of the corporation's intent to immediately establish a permanent office in Maryland; and
- c. Be organized such that a simple majority of the ownership of the corporation, in terms of financial interests and voting rights, is held by individuals licensed to practice certified public accountancy in this or another state. All non-CPA owners must be active participants in the corporation.

Note: At least one officer, partner or member must reside in Maryland and must be licensed to practice in Maryland.

A Limited Liability Company (LLC)

- a. Must have a permanent office in Maryland or, at the time of application, submit proof of the limited liability company's intent to immediately establish a permanent office in Maryland from which an individual is to practice certified public accountancy;
- b. Each permanent office shall be under the immediate direction of a member of the limited liability company who resides in Maryland.
- c) Be organized such that a simple majority of the ownership of the corporation, in terms of financial interests and voting rights, is held by individuals licensed to practice certified public accountancy in this or another state. All non-CPA owners must be active participants in the limited liability corporation.

A Partnership

- a. Must have a permanent office in Maryland or, at the time of application, submit proof of the limited liability company's intent to immediately establish a permanent office in Maryland from which an individual is to practice certified public accountancy;
- b. Each permanent office shall be under the immediate direction of a partner of the partnership who resides in this Maryland.

- c. Be organized such that a simple majority of the ownership of the partnership, in terms of financial interests and voting rights, is held by individuals licensed to practice certified public accountancy in this or another state. All non-CPA owners must be active participants in the partnership.

Limited License -
Corporation, Partnership, Limited Liability Partnership, Limited Liability Company

Application Fee -\$25

Limited Permit - Corporation

Limited Permit Requirements for a Partnership. A limited permit authorizes a corporation that does not have a permanent office in this state to practice of certified public accountancy on a specific job for a period not more than one year. The term of the limited Corporation permit may not exceed the limited license held by the shareholders of the Corporation. Each new job requires a new permit.

The requirements are:

1. each shareholder is licensed to practice certified public accountancy in Maryland or another state or in a foreign country; or
2. each shareholder who practices or intends to practice accountancy in this State has a limited license issued by the Board.

Limited Permit for Limited Liability Companies (LLC)

Limited Permit Requirements for a Limited Liability Company (LLC). A limited permit authorizes LLC that does not have a permanent office in this state to practice of certified public accountancy on a specific job for a specific period of time. The term of the limited liability company permit may not exceed the limited license held by the members of the LLC. Each additional job requires a new permit.

The requirements are:

1. each member is licensed to practice certified public accountancy in Maryland or another state or in a foreign country; or
2. each member who practices or intends to practice accountancy in this State has a limited license issued by the Board.

Limited Permit - Partnership

Limited Permit Requirements for a Partnership. A limited permit authorizes a partnership that does not have a permanent office in this state to practice of certified public accountancy on a

specific job for a specific period of time. The term of the limited partnership may not exceed the limited license held by each partner. Each additional job requires a new permit.

The requirements are:

1. each partner is licensed to practice certified public accountancy in this or another state or in a foreign country; and at least 1 general partner and any other partner who practices or intends to practice accountancy in the State is licensed by the Board.

FEES FOR LICENSES

New Examination Fees
(Effective August 14, 2006)

Application Review (1st time applicants) \$ 40 (no change)
Auditing and Attestation \$ 207
Business Environment and Concepts \$ 158
Financial Accounting and Reporting \$ 195
Regulation \$ 170

Individual CPA License - Active
Original First Time - \$15
Renewal - \$40
Reinstatement Fee - \$60

Reciprocal License
Reciprocal Support Documentation
Initial Application - \$50
Fee for License after approval - \$15
Individual CPA License - Inactive
First Time - \$20
Renewal - \$20
Late Fee - \$20.00
Transfer of Grades
Initial Application -\$25
License Fee after approval -\$15
Limited License- Individual
Application Fee -\$25

Permit
Initial Application
Corporation - \$25
Limited Liability Company- \$25

Limited Liability Partnership- \$25
Partnership - \$25
Permit Fee After Approval
Corporation - \$25
Limited Liability Company- \$25
Limited Liability Partnership- \$25
Partnership - \$25

Limited Permit
Application Fee
Corporation - \$25
Limited Liability Company- \$25
Limited Liability Partnership- \$25
Partnership - \$25

License Certification for submission to other States/Organizations
Fee - \$10
Wall Certificates
Original - No Cost
Duplicate Fee - \$25

DISCIPLINARY ACTIONS

REVOCATIONS

CPAS 0500043, CPAS050045, CPAS050046, CPAS050047, CPAS050048 - Terry Ricord Klapko (Lic. No. 01-31278), REVOKED and FINED \$5,000 for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-315(a)(1)(ix), and a number of regulations for failure to perform work for which she was engaged; failure to return original documents upon request of her clients; and failure to respond to official requests to respond to the issues raised in these complaints from the Board of Public Accountancy. Additionally, Ms. Klapko was ORDERED to immediately cease and desist any representation to public in any manner that she is licensed as a certified public accountancy. (March 10, 2006)

CPAS030012 - Katrina J. Krug (Lic. No. 01-21312) REVOKED for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-315(a)(8). Ms. Krug was sanctioned by the U.S. Securities and Exchange Commission which resulted in the revocation of her right to practice before the Commission. (April 4, 2003)

CPAS000025 - Charles G. Fagan (Lic. No. 01-3516) REVOKED for violation of Business Occupations and Professions Article, Section 2-315(a)(3)(i). Mr. Fagan was convicted of a felony theft in the amount of \$15,909 in the Circuit Court for Anne Arundel County. (November 1,

2001)

SUSPENSIONS

CPAS030028 - John W. Brill, (Lic. No. 01-6392). SUSPENDED for two months, from September 23, 2005 through November 22, 2005; FINED \$2,500; ordered to complete 16 hours of continuing professional education in the principles of auditing; and ordered to undergo PEER REVIEW encompassing all audits that he performed or will perform during the period January 1, 2004 and August 26, 2006. In a consent order, Mr. Brill agreed to accept the Board's sanctions and admitted that he violated Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-315 (a)(1); COMAR 09.24.01.06(G) Competence and Technical Standards (1) and (2) for preparing a deficient financial statements and issuing improper auditor's reports that he performed for the Board of Trustees of the Pressman's Local #72 401(k) Retirement Fund during 1999 and 2000. (September 23, 2005).

CPAS020019 - James L. Yates (Lic. No. 01-9031) SUSPENDED INDEFINITELY for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-315(a)(1)(iii). On June 4, 2002, in the United States District Court for the District of Maryland, Mr. Yates was convicted of felony offenses for making false claims against the United States and conspiracy to defraud the United States Government. If Mr. Yates' conviction is affirmed, the Board will REVOKE his license without further hearing. Further, if Mr. Yates' appeal of the conviction is overturned on appeal, the Board will lift the suspension and permit Mr. Yates to renew his license. (February 17, 2004)

FINES

CPAS06002 and CPAS060008 - Michael D. Scheve (01-9434), Fined \$2,000 for holding himself as a licensed practitioner despite the fact that his license expired on December 23, 2001. In a consent order, Mr. Scheve agreed to cease practicing public accountancy services in Maryland and representing himself as licensed to practice certified public accountancy in Maryland until he is issued a license by the Board (March 22, 2006).

CPAS030010 - Gregory B. Dyer (01 -8787) - Fined \$500 for violating 2-315(a)(1)(ix) and COMAR 09.24.06 (I)(5) for failure to respond to an official communication from the Board. In a consent agreement dated January 3, 2006, Mr. Dyer agreed to pay the fine and accept a written reprimand of his license (January 3, 2006).

CPAS050036 - Stephen M. Samuels (01-3910) Fined \$2,000 for holding himself out as a licensed practitioner despite the fact that his license expired on December 31, 1984. (August 2, 2005)

CPAS050006 - Charles Dubin (Not Licensed) Fined \$100 for holding himself out as a licensed practitioner. (April 1, 2005)

CPAS040005 - Norman Lovick (Not licensed) - Fined \$5,000 for holding himself out to the public as a licensed practitioner. Mr. Lovick was ordered to cease and desist from representing himself a licensed CPA. (April 1, 2005)

CPAS040002 - Jerry D. Johnston (Not Licensed) FINED \$2,500 for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-603(a) by holding himself out as a certified public licensed in Maryland through the firm of Johnston & Associates, P.A. In a consent order, Mr. Johnston agreed to cease practicing public accountancy services in Maryland and representing himself and his firm as licensed to practice certified public accountancy in Maryland until he is issued a license by the Board. (September 2, 2004)

CPAS040009--Susan M. Ballman (Lic. No.01-6706) FINED \$1,000 for holding herself out a licensed CPA and practicing as a CPA in violation of for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-603(a). Ms. Ballman's license to practice as a CPA expired on December 31, 1996. Despite the fact that her license expired, Ms. Ballman continued to practice as a CPA. (August 3, 2004)

CPAS020046 - Patrick J. Curran (Lic. No. 01-7525) - FINED \$1,500 for holding himself out as a licensed CPA in violation of for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-603(a). Mr. Curran's license to practice as a CPA expired December 31, 1992. In a consent agreement, Mr. Curran agreed to pay the fine and refrain from engaging in the public accountancy or holding himself out as a CPA until properly licensed by the Board (September 17, 2003).

CPAS030007 - Stephen R. Emme (Lic. No. 01 - 4575) - Fined \$1,000 for holding himself out as a licensed CPA in violation of for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Section 2-603(a). Mr. Emme's license to practice as a CPA expired December 31, 1996. In a consent agreement dated July 10, 2003, Mr. Emme agreed to pay the fine and refrain from engaging in the public accountancy or holding himself out as a CPA until properly licensed by the Board. (August 1, 2003)

CPAS030017 - Maurice S. Hamilton (01 -12496) - Fined \$1,000 for violating ?-315(a)(1)(vii). In a consent agreement dated January 6, 2004, Mr. Hamilton agreed to pay the fine and accept a written reprimand of his license.

CPAS 010025 - Craig L. Rickard - (Expired License 01-2911) Fined \$1,500 for violation of Business Occupations and Professions Article, Annotated Code of Maryland, Sections 2-603 and ?-604, by holding himself out as a licensed practitioner and his firm as possessing a permit to provide certified public accountancy services in Maryland. He was also ordered to cease and desist from representing himself licensed to practice and his firm as having a permit to provide

CPA services in this State. (October 3, 2002).

CONTINUING EDUCATION: WHAT PROGRAMS QUALIFY?

Licensees who renew their licenses (with the exception of individuals who are renewing for the first time) must certify that they have completed at least 80 hours of continuing education, within the two years before application for renewal, in accounting related subjects. Continuing education may take the form of:

1. **Professional development programs** of recognized national and state accounting organizations and their chapters.
2. Programs by educational institutions accredited by the **AACSB** or appropriate accrediting associations.
3. Technical sessions at **meetings of recognized national and state accounting** organizations and their chapters.
4. Non-credit short courses at universities and colleges.
5. Formal, organized in-firm education programs.
6. Programs offered by other recognized professional or industrial organizations.
7. **Formal correspondence and individual study programs**, including programs designed to use interactive learning methodologies.
8. Credit as an instructor, discussion leader, or speaker. The Board allows up to 3 hours of credit for any meeting or engagement provided that the session is one which would meet the continuing education requirements for those attending.

NOTE: All Certified Public Accountants licensed to practice by the State of Maryland are subject to the provisions of the continuing education statutes and the regulations and policies relating to those statutes as adopted by the Maryland State Board of Public Accountancy.

Part 1 - Policies Concerning Renewals of Licenses

Regulations provide that all active licensees are required to have 80 continuing education hours (CPE) with the exception of those licensees renewing for the first time. For inactive status, no CPE is required.

Regulations allow a maximum of 80 hours of CPE (earned in excess of the 80 hours used to meet the CPE requirement) to be carried over to the next succeeding licensing period. CPE hours earned through individual study programs and teaching in excess of the 40 hour maximum may not be carried over to the next licensing period. To qualify for CPE, college credit or self-study

courses must include an examination and must be final (examination corrected and a passing grade obtained) before claims for CPE credit can be made.

It is the primary responsibility of each licensee to fulfill the requirements of the law and to be able to document, to the Board's satisfaction, such fulfillment. All active licensees must maintain, for 4 years, records substantiating (proof of attendance, course outline & expertise of instructor) the continuing education credits claimed by them as a prerequisite for renewal of their license.

A wide range of educational programs are "recognized" by the Board as being of value in fulfilling the continuing professional education requirement. The overriding consideration in determining whether a specific program qualifies is that it contributes directly to the professional competence of an individual after the individual has been licensed to practice certified public accounting. Educational programs which qualify are those which are formal programs of learning as defined below. CPE credits must be earned in the two year period prior to renewing the license.

Part 2 - Policies Concerning Continuing Educational Programs

SUBJECT MATTER:

a) For a program to qualify for CPE credit, it must meet the following criteria:

1. principally not repeat material to the licensee; and
2. the knowledge gained from the course(s) must reasonably be directly usable by the participant to produce, as a practicing CPA, a service or product for a client. This generally eliminates areas of general administration, the marketing of a CPA's services and areas of self-improvement that have only an indirect connection to a CPA's service or product.

b) Courses in accounting, auditing, taxation, financial planning, and management advisory services are acceptable if they directly contribute to the professional competence of an individual after the individual is licensed to practice as a certified public accountant.

(CAUTION: Courses given by companies which sell or promote tax services, books, periodicals and other library materials will qualify for credit only if they meet the professional competence standard. Seminars which provide instruction in the use of computer tax preparation even if they include an ancillary discussion of tax do not qualify for credit.

c) It is possible that courses in general business related subjects may be acceptable, but only if they meet the professional competence standard.

(CAUTION: The Board does not accept courses which are: 1) designed for the general public, not for CPAs, 2) sales-oriented presentations of any kind, 3) programs restricted to policies and

procedures of a particular company, or, 4) programs presenting scientific and technical knowledge of a sophistication beyond the scope required for the practice of a CPA.

WHERE CONTINUING EDUCATION PROGRAMS MAY BE TAKEN

a) formal group programs sponsored by professional organizations and other organizations:

1. recognized certified public accounting professional organizations, and, related educational foundations.
2. in-house programs presented by certified public accounting firms licensed by the Board.
3. programs put on by a group of certified public accounting firms, which includes at least one accounting firm licensed by the Board.
4. programs presented by other organizations which meet the subject matter and format requirements stated in these policies.

NOTE: Group Study Programs (using tape or video) will not be considered formal group programs unless a qualified instructor is present or access thereto by the participants for questions raised concerning the program subject matter, etc.

b) programs by educational institutions accredited by the American Assembly of Collegiate Schools of business (AACSB) or appropriate regional accrediting associations.

1. non credit short courses
2. degree programs and courses for credit within degree programs.

A graduate program in business administration, accounting, taxation, or anything directly related to the field of business or accounting is not only acceptable, but encouraged. Any course in such a program on the Master's or higher level is acceptable if the CPA is a degree candidate for that program. In the matter of law school or degree program in such things as administrative science, public administration, data processing, etc., which do not address the subject matter of public accountancy directly, the courses should be examined on a case-by case basis by the licensee to determine if the subject matter contributes to professional competency as a CPA. Credit towards the continuing education requirement will be calculated at 15 hours for each semester hour credit and 10 hours for each quarter hour credit.

Caution: Undergraduate college and university courses in general, do not fulfill the concept of continuing education for CPAs, both as to the teaching and taking thereof, unless the course subject matter is not repetition for the licensee and is appropriate for CPE as defined above.

c) formal correspondence and individual study programs: The amount of credit to be allowed for formal correspondence and individual study programs (including taped study programs) will be 50% of the average completion time as determined by the course producer.

EVIDENCE OF FULFILLMENT OF CONTINUING EDUCATION REQUIREMENTS

Satisfaction of the requirements may be accomplished as follows:

a) programs sponsored by professional organizations, firms and other organizations:

Active licensees must maintain, for four years, evidence of attendance, course outline, and expertise of instructor.

b) programs by educational institutions accredited by the AACSB or appropriate accrediting associations:

In the event of courses taken for scholastic credit, evidence of satisfactory completion of the course will be sufficient. In the case of noncredit short courses taken in educational institutions, a signed statement of the hours of attendance must be obtained from the institution. If a for-credit course is audited, attendance records must be maintained by the school registrar (not the instructor) in order to obtain credit. In all instances, the documentation must be retained by the licensee.

c) formal correspondence and individual study programs.

There are two types of self-study programs: regular self study and interactive self study.

Regular self study. - Materials are received from the program sponsor in the form of a hard copy document, computer disc, tape, and or video for study. An examination is taken when the course is completed. *The amount of CPE credit awarded by the Board is 50% of the average completion time of regular self study program as determined by the course sponsor.*

Interactive self-study - This form of self-study takes the form of computerized course issued by a program sponsor for study. As a student progress through the course, the computer program prompts the student with questions. If a student answers questions incorrectly, the programs returns the student to the area of study that the student does not understand. The program continues to return the student to material until the student demonstrates proficiency in the subject matter. The student takes the examination at the end of the course. The course sponsor evaluates the examination and issues credit upon a passing grade. *The amount of CPE credit awarded by the Board is 100% of the average completion time of interactive self study program as determined by the course sponsor.*

Licensees claiming credit for such courses are required to obtain evidence of satisfactory completion of the courses from the program sponsor. Credit will be allowed in the year in which

the course is completed. Self-study programs are to be pre-tested to determine average completion time. One-half of the average completion time is the credit to be allowed.

NOTE: For each course taken for CPE, it remains the responsibility of the licensee to demonstrate that the program contributes directly to the licensee's professional competence as an active Certified Public Accountant.

Part 3 - Other Policies for CPE

- a) Credit as an instructor, discussion leader, or speaker will be allowed for any meeting or engagement provided that the session is one which would meet the continuing education requirements for those attending. The credit allowed an instructor, discussion leader, or a speaker will be based on contact hours of teaching. The Board allows 3 hours for each class hour which includes 2 hours prep time.
- b) Credit may be allowed for published articles and books provided they contribute to the professional competence of the licensee. Credit for preparation of each publication may be given on a self-declaration basis up to 10 hours of the renewal period requirement. In exceptional circumstances, a licensee may request additional credit by submitting the articles(s) or book(s) to the Board with an explanation of the circumstances which justify a greater credit.
- c) Continuing education credit may be given for whole hours only, with a minimum of 50 minutes constitution one class hours. As an example, 100 minutes of continuous instruction would count for two class hours, however, more than 50 minutes but less than 100 minutes of continuous instruction would only count for one hour.
- d) The AICPA's Ethics course completed as a requirement for original licensure in Maryland does not qualify for CPE.

Satisfaction of the requirements may be accomplished as follows:

Active licensees must maintain, for four years, evidence of attendance, course outline, and expertise of instructor.

In the event of courses taken for scholastic credit, evidence of satisfactory completion of the course will be sufficient. In the case of noncredit short courses taken in educational institutions, a signed statement of the hours of attendance must be obtained from the institution. If a for-credit course is audited, attendance records must be maintained by the school registrar (not the instructor) in order to obtain credit. In all instances, the documentation must be retained by the licensee.

Licensees claiming credit for such courses are required to obtain evidence of satisfactory completion of the courses from the program sponsor. Credit will be allowed in the year in which

the course is completed. Self-study programs are to be pre-tested to determine average completion time. One-half of the average completion time is the credit to be allowed.

NOTE: For each course taken for CPE, it remains the responsibility of the licensee to demonstrate that the program contributes directly to the licensee's professional competence as an active Certified Public Accountant.

GLOSSARY

ATTEST ENGAGEMENT TEAM participants in the engagement, including partners who perform concurring or second reviews and all employees and contractors retained by the firm, but excluding specialists.

DEONTOLOGY (KANTIAN ETHICS) the concept of duty and the rightness of acts. It emphasizes maxims, duties, rules, and principles that are so important that they should be followed whatever the consequences.

ETHICS 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.

IMMEDIATE FAMILY a covered member's spouse, equivalent of a spouse, or dependents.

INTERNAL CONTROL REPORT a report on the company's internal control over financial reporting required under Section 404 of the Sarbanes-Oxley Act. For example, the report must include a statement of management's responsibility for internal control.

JOINT CLOSELY HELD INVESTMENT an investment in any entity or property by the member and (1) the client, (2) the client's officers or directors, or (3) an owner who can exercise significant influence if the investment permits such parties to control the entity or property.

LAWS bodies of rules governing members of a community, state, organization, professional, etc ... and enforced by authority or compelling legislation.

MORAL an accepted rule or standard of human behavior.

OBJECTIVITY a state of mind, a quality that lends itself to a member's services. The principle of objectivity imposes the obligation to be impartial, intellectually honest, and free of conflicts of interest.

PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD (PCAOB)

(www.pcaobus.com) established in 2002 as a result of the Sarbanes-Oxley Act, a private sector, non-profit corporation set up to oversee the audits of public companies and ensure that accountancy firms should no longer derive non-audit revenue streams, such as consultancy, from their audit clients.

SARBANES-OXLEY (SOX) ACT wide-ranging U.S. corporate reform legislation, coauthored by the Democrat in charge of the Senate Banking Committee, Paul Sarbanes, and Republican Congressman Michael Oxley. The Act, which became law in July 2002, lays down stringent

procedures regarding the accuracy and reliability of corporate disclosures, places restrictions on auditors providing non-audit services and obliges top executives to verify their accounts personally. Section 409 is especially tough and requires that companies must disclose information on material changes in the financial condition or operations of the issuer on a rapid and current basis.

UTILITARIANISM (TELEOLOGICAL ETHICS) the promotion that the best long-term interest of everyone concerned should be the moral standard. One should take those actions that lead to the greatest balance of good versus bad consequences