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November 20, 2006

Ms. Lisa A. Snyder
Director
Professional Ethics Division
AICPA
Harborside Financial Center
201 Plaza Three
Jersey City, NJ 07311-3881

By email: lsnyder@aicpa.org

In re: Exposure Draft - Omnibus Proposal of Professional Ethics Division Interpretations and Rulings: Proposed Interpretation No. 101-16 on Indemnification, Limitation of Liability and ADR Clauses in Engagement Letters under Rule 101, dated September 8, 2006

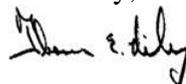
Dear Ms. Snyder:

The New York State Society of Certified Public Accountants, representing 30,000 CPAs in public practice, industry, government and education, is pleased to submit the attached comments on the above-referenced Exposure Draft issued by the AICPA Professional Ethics Executive Committee.

This letter only addresses Proposed Interpretation 101-16: *Indemnification/Limitation of Liability Provisions and ADR Clauses in Engagement Letters under Rule 101*. Under separate cover dated November 14, 2006, the Society submitted comments on proposed deletion of Ethics Rulings Nos. 94 and 95 and the proposed revisions to Interpretation 101-3 under Rule 101: *Performance of Nonattest Services*.

The NYSSCPA Professional Ethics Committee deliberated the exposure draft and prepared the attached comments. If you would like additional discussion with us, please contact Francis T. Nusspickel, chair of the Professional Ethics Committee, at (201) 891-2754, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,



Thomas E. Riley
President

Attachment



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**NEW YORK STATE SOCIETY OF
CERTIFIED PUBLIC ACCOUNTANTS**

COMMENTS ON AICPA EXPOSURE DRAFT

**OMNIBUS PROPOSAL OF
PROFESSIONAL ETHICS DIVISION
INTERPRETATIONS AND RULINGS
(September 8, 2006)**

Omnibus Proposal:

**Proposed Interpretation 101-16, *Indemnification, Limitation of Liability, and ADR Clauses
in Engagement Letters*, Under Rule 101, Independence**

November 20, 2006

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**The New York State Society of Certified Public Accountants
Professional Ethics Committee**

**Comments on AICPA Exposure Draft - Proposed Interpretation 101-16,
Indemnification, Limitation of Liability, and ADR Clauses in Engagement Letters, Under
Rule 101, dated September 8, 2006**

Comments

The Professional Ethics Committee (the "Committee") of the New York State Society of Certified Public Accountants has reviewed the above-referenced AICPA Exposure Draft (ED) and offers the following comments for consideration by the Professional Ethics Executive Committee (PEEC) of the American Institute of Certified Public Accountants (AICPA).

The Committee acknowledges that the AICPA's *Code of Professional Conduct* (the "Code") is silent with respect to the appropriate terms for an auditor's contractual relationship with his or her attest client. Therefore, we appreciate the efforts of PEEC to develop guidance on the impact of certain provisions in engagement letters or other contractual agreements on auditor's independence.

The AICPA historically has been the principal source of authoritative guidance on a CPA's conduct. The fundamental guidance in the Code and related interpretations on independence is as follows:

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

The Committee believes the guidance provided in this new proposed interpretation is useful and, accordingly, supports its adoption. We also believe the proposed interpretation is an improvement over the proposal that was issued last year.

PEEC has recognized that the United States Securities and Exchange Commission has viewed that the inclusion of "indemnification agreements remove[s] one of the major stimuli to objective and unbiased consideration of problems encountered in an [attest] engagement." In fact, PEEC concluded that certain types of indemnification and limitation of liability provisions do pose an unacceptable threat to a member's independence. However, PEEC concluded that this threat could be sufficiently mitigated as long as the attest services are performed in accordance with professional standards.

We agree and support the adoption of the proposed interpretation. Under the proposed standard, an auditor retains sufficient liability for failure to adhere to professional standards, thus providing an adequate incentive to the auditor to conduct the attest services fully in conformance with professional standards. Further, the rights of third parties who are not party to the contractual relationship are unaffected.

We do, however, have the following suggested changes and comments:

- (1) The words "or contracts for services" should be added to the first sentence of the first paragraph in the Interpretation section of the proposed interpretation (page 9). In addition, the word "attest" should be added as a modifier to the word client in the same sentence. As such, the first sentence should be rewritten to read: "This interpretation provides guidance...when included in engagement letters or other agreements or contracts for services entered into with an attest client."
- (2) The word "applicable" should be added as a modifier to the term professional standards in the third paragraph in the Interpretation section (page 10), so that the third paragraph would read either "...the obligation to comply with all applicable professional standards..." or "...the obligation to comply with all professional standards applicable..." Alternatively, the word *all* before the words *professional standards* should be deleted. This change is necessary because not all professional standards apply to all services provided by accountants.
- (3) The first and third paragraphs of the *Indemnification and Limitation of Liability Provisions in Attest Services Engagements* section (page 10) should be combined in order to shorten the section and to clarify the standard. As currently written, the first paragraph in this section indicates that independence would be impaired if indemnification or limitation of liability provisions are obtained. However, the sentence is misleading because it does not reflect the full intent of PEEC. The sentence should clearly state that it is appropriate to obtain such provisions so long as the attest services were performed in accordance with professional standards. We would suggest that the language contained in the Explanation section of the proposed interpretation (first sentence in the last paragraph of page 6) would be a better articulation of the standard than the first paragraph as presently written.

While we support adoption of the proposed interpretation we do have concerns about whether the standard is operable. That is, will members be afforded the protections embedded in indemnification and limitation of liability clauses or will they rarely be able to avail themselves of such protections because clients will allege, rightly or wrongly, that the member did not conduct his or her work in accordance with professional standards in order to avoid compensating the member. A key factor will be who has the burden of proving whether the work was performed in accordance with professional standards. If PEEC has not done so, we encourage it to consult with attorneys who specialize in accountants' malpractice about the application and efficacy of the proposed interpretation.

- (4) The word "attest" should be added as a modifier to the word client in the *Unsuccessful Party to Pay Legal Fees and Expenses* section (page 11), so that the sentence would read: "Independence would not be impaired if a member and the attest client agree...."
- (5) The word "Attest" should be added to the title of the *Limitation on Time Period in Which a Client May File a Claim* section (page 11), so that it would read: *Limitation on Time Period in Which an Attest Client May File a Claim*. In addition, the word

"attest" should be added as a modifier to the word client in the sentence in this section, so that the sentence would read: "A limitation of the time period during which the attest client...."

- (6) The word "Attest" should be added to the title of the *Limitation on a Client's Right to Assign or Transfer a Claim* section (page 11), so that it would read: *Limitation on an Attest Client's Right to Assign or Transfer a Claim*. In addition, the word "attest" should be added as a modifier to the word client in the sentence in this section, so that the sentence would read: "A limitation on the attest client's legal right...."
- (7) The words "an attest" should be added as a modifier to the word client in the paragraph in the *Agreement to Use ADR Technique or Proceeding* section (page 11), so that the first sentence would read: "An agreement between a member and an attest client to use arbitration...."
- (8) The words "an attest" should be added as a modifier to the word client in the paragraph in the *Agreement to Waive a Jury Trial* section (page 11), so that the sentence would read: "An agreement between a member and an attest client to waive a jury trial...."
- (9) The transition period (page 11) provided in the proposed interpretation appears to be too generous. We suggest that each date be rolled back by nine months so that the January 1, 2008 and January 1, 2009 dates set forth in the proposed interpretation are changed to March 31, 2007 and March 31, 2008, respectively.
- (10) The proposed interpretation should include guidance that an indemnification or limitation of liability provision that seeks to limit or eliminate a member's liability with respect to actual damages arising from the attest client's knowing misrepresentation, willful misconduct or fraudulent behavior would not impair independence. That is, the guidance in Ethics Ruling No. 94 should be carried over and included in proposed Interpretation 101-16.