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June 23, 2005

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: **Proposal of Professional Ethics Divisions Interpretations and Rulings, April 18, 2005**

Dear Ms. Snyder:

The New York State Society of Certified Public Accountants, the oldest state accounting association, representing approximately 30,000 CPAs, is pleased to submit the attached comments on *Proposal of Professional Ethics Division Interpretations and Rulings*

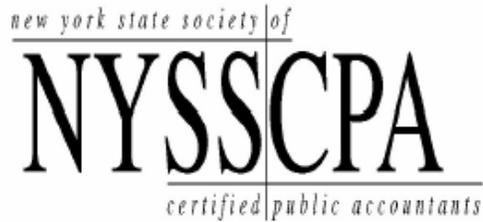
The NYSSCPA Professional Ethics Committee drafted the attached comments, which have been reviewed and approved by the Quality Enhancement Policy Committee. If you would like additional discussion with us, please contact the Quality Enhancement Policy Committee chair, Thomas E. Riley, at (315) 471-2777 x 122, or Robert Colson, NYSSCPA staff, at (212) 719-8350.

Sincerely,

A handwritten signature in cursive script that reads "Stephen F. Langowski".

Stephen F. Langowski,  
President

Attachment



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

**COMMENTS ON AICPA EXPOSURE DRAFT**

**Proposal of Professional Ethics Division Interpretations and Rulings April 18, 2005**

**June 23, 2005**

**Principal Drafters**

**Francis T. Nusspickel**

**Richard D. Isserman**

**Kevin Bandoian**

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**The New York State Society of Certified Public Accountants**  
**Professional Ethics Committee**  
**Comments on Exposure Draft - *Proposal of Professional Ethics Division***  
***Interpretations and Rulings April 18, 2005***

**June 23, 2005**

**General Comment**

Most of the proposed Interpretations and Rulings address guidance to members in determining the effect on member independence of direct or indirect financial interests. The primary issues in the proposal relate to the discussion of financial interest and to the guidelines for determining whether direct or indirect financial interests should be considered when evaluating independence in specific situations.

**Specific Comments**

- 1) Explanation 4 on Page 5 states that the new Interpretation would:

“Provide a limited exception for financial interests received through an unsolicited gift or inheritance, which in certain respects is more restrictive than a similar exception promulgated by the Securities and Exchange Commission (SEC).”

  - a. It would be preferable for the code of professional conduct to conform to the SEC rules on independence. The proposal is more restrictive than the current SEC requirement. Because the additional restrictions in the proposal have merit, however, the appropriate course of action would be first to initiate discussions with the SEC to change its rules and then conform the AICPA code to those changes.
  
- 2) Under “Retirement, Savings, Compensation or Similar Plans” on page 6, the fourth line of the first paragraph contains the following text:

“The committee believes that investments held by defined benefit plans would not normally be considered financial interests of a plan participant, because in a defined benefit plan the amount of the benefit is not dependent upon the performance of any investments that make up the funding.”

  - a. The term "defined benefit plans" should be changed to "multi-participant defined benefit plans" to exclude any individual plans from this exception.
  
- 3) The last sentence in the last paragraph on page 7, under “IRC Section 529 Plans” reads:

“However, the covered member must transfer the account as soon as the transfer can be made without a penalty or tax significant to the account.”

- a. A reasonable time limit after the restrictions have been lifted, such as 30 days, should be set for the transfer to be made. Also, the transfer should not be made to any person included in the definition of a "covered member" in order to exclude those over whom influence could be exercised
- 4) Page 8, Section .17 101-15, "Financial relationships," has the following definition of a direct financial interest:

"A direct financial interest is a financial interest:

- 1. Owned directly by an individual or entity (including those managed on a discretionary basis by others); or
- 2. Under the control<sup>1</sup> of an individual or entity (including those managed on a discretionary basis by others); or
- 3. Beneficially owned through a collective investment vehicle, estate, trust, or other intermediary when the beneficiary:
  - a. Controls the intermediary; or
  - b. Has the authority to supervise or participate in the intermediary's investment decisions."

- a. It would be helpful to provide an example to clarify the type of entities and characteristics of control addressed in sub-paragraph 3 of this definition.
- b. In addition, it would also be helpful if an example of control could be given for footnote 1, which states:

"When used herein, the term control includes situations where the covered member, individually or acting together with his or her firm or with other partners or professional employees of his or her firm, has the ability to exercise such control."

- c. Because there are different concepts of "control," the proposal should specifically refer to a recognized definition of control in order to promote consistent application.

- 5) Page 9, Section .17 101-15, "Unsolicited Financial Interests" reads:

"Independence would not be considered to be impaired if an unsolicited financial interest is received, such as through gift or inheritance, and the financial interest is disposed of as soon as practicable, but no later than 30 days after the covered member has knowledge of and the right to dispose of the financial interest. However, when the covered member becomes aware that he or she will receive or has received a material direct or indirect financial interest in a client requiring independence but does not have the right to dispose of the financial interest, independence will not be impaired provided the covered member does not participate on the attest engagement team and disposes of the financial interest as soon as the right to dispose exists."

- a. Consideration should be given to applying this interpretation to all individuals within the term "covered member." Should only those on the attest engagement team be required to dispose of the financial interest as soon as the right to dispose exists? Why exclude other persons within the definition of "covered member?"
  - b. A time limit, such as 30 days after a covered member has the right to dispose, should be required to dispose of such interest.
- 6) Under ".17 101-15 - Financial relationships," under "Mutual Funds," page 9, the second paragraph reads:

“If the mutual fund is diversified (as defined in section 5(b)(1) of the Investment Company Act of 1940), a covered member’s ownership of 5 percent or less of the outstanding shares of the mutual fund would not be considered to constitute a material indirect financial interest in the underlying investments.”

  - a. It would be helpful to include the definition of a diversified mutual fund from Section 5(b) (1) of the Investment Company Act of 1940 within the text of the proposal or in a footnote.
- 7) Under ".17 101-15 - Financial relationships," under "Retirement, Savings, Compensation or Similar Plans," page 10, the second example illustrating the concepts reads:

“If investments in a defined contribution plan are participant-directed, whereby a covered member selects his or her underlying plan investments or selects from investment alternatives offered by the plan, the covered member would be considered to have a direct financial interest in those investments. However, if the investments offered by the plan consist solely of investments requiring independence, the investments would be considered indirect financial interests provided that the covered member is not on the attest engagement team or in a position to influence the attest engagement.”

  - a. What is meant by "investments requiring independence?" Would the phrase "investments in an attest client" clarify the intent?
- 8) Under 17 101-15 "Financial relationships, Section 529 Plans," page 11,
  - a. Please see comments in number 3 above.
  - b. In addition, the third paragraph reads:

“A covered member who is the account owner of a Section 529 savings plan is considered to have a direct financial interest in both the plan and the investments of the plan because he or she decides in which sponsor’s Section 529 savings plan to invest and prior to

making the investment has access to information about the plan's investments. If a covered member invests in a Section 529 savings plan that does not hold financial interests in an attest client at the time of the investment, but the plan subsequently invests in an attest client, the covered member should (1) transfer the account to another sponsor's Section 529 savings plan, or (2) transfer the account to another account owner who is not a covered member. However, when the transfer of the account will result in a penalty or tax that is significant to the account, the covered member may continue to own the account until the account can be transferred without significant penalty or tax, provided the covered member does not participate on the attest engagement team and is not in a position to influence the attest engagement."

- The interpretation should be expanded to prohibit the transfer from being made to a family member or other close relative over whom the covered member could have influence. In addition, a time limit should be established for transfer once the possibility of significant penalty or tax is eliminated.