

TECHNICAL ANALYSIS PAPER

Subject: ED 01/12 APES GN 30 Outsourced Services – Summary and Analysis of Key Issues Raised by Respondents

Introduction

The trend of Outsourcing Professional Services has grown rapidly over the last decade with benefits such as staff utilisation on core activities, lower costs and access to specialised skills, all resulting in greater efficiencies in the performance of Professional Services. However, with these benefits risks also arise such as confidentiality of Client information, integrity of information transferred between the Member in Public Practice and the Outsourced Service Provider and management, and control and supervision of the work performed.

Given the increasing use of Outsourced Services in the delivery of Professional Services it is important that the risks associated with conducting business in this manner are managed to minimise risks to the Member and the Member's Firm.

Purpose

The purpose of this paper is to provide the APES GN 30 Taskforce and the APES Board with:

- a summary of key issues raised by respondents in response to APESB's ED 01/12 APES GN 30 *Outsourced Services*; and
- Technical staff comments, views and recommendations.

A summary of the major issues raised by respondents and Technical staff comments, views and recommendations on the issues raised in the Exposure Draft is given below.

1. Review of Respondents' Comments

(i) Consistency with international developments in Outsourcing

[GC2, GC3, GC6, GC10 - GC13, GC18, GC35]

Respondents' Comments

A number of respondents noted their preference for the development of internationally consistent standards and guidance and noted the absence of an international equivalent. One respondent stated that proposed Guidance Note imposes additional layers of obligation on Members that do not apply to other service providers. Other respondents questioned the need for guidance in Australia when Outsourcing is not unique to the local environment. It was also suggested that the Guidance Note as currently drafted does not consider the extent to which the proposed guidance is consistent with, or more onerous than, guidance issued by other countries.

Technical Staff Response

APESB is a National Standards Setter and has a mandate to issue professional and ethical standards for the three major accounting bodies in Australia. For the majority of APESB's pronouncements (over 85%) there are no international equivalents. One of the reasons for this is that IESBA's work primarily focuses on the Code of Ethics and to date IESBA has issued no other pronouncements. However, the situation is quite different when considering Accounting Standards or Auditing and Assurance Standards where the equivalent International Boards (IASB and IAASB) have issued a suite of standards for their respective areas that are adopted internationally.

In the short term it is unlikely that IESBA will be issuing professional and ethical standards other than the Code. Accordingly, when there are matters that need to be specifically addressed in a national jurisdiction then the National Standards Setter of that jurisdiction can consider this and issue national standards as appropriate. For example, APESB has issued standards for Valuation Services, Forensic Accounting Services and Insolvency Services for which there are no international equivalents.

Conclusion

The APES Board and the APES GN30 Taskforce considered this issue and agreed that a lack of an international equivalent should not deter APESB from developing and issuing its own standards or guidance notes that are applicable to Members.

(ii) Structure and drafting style of the proposed Guidance Note

[GC19, GC24 – GC 29, SC49, SC53, SC55, SC56]

Respondents' Comments

All respondents raised concerns with the current structure and drafting style of the proposed Guidance Note. Some respondents noted that the degree of detail and prescriptive tone of the document results in the proposed Guidance Note reading more like a standard than guidance.

Technical Staff Response

The objective of APES GN 30 is to provide Members with guidance when utilising or providing Outsourced Services. It was not intended that APES GN 30 would be read in a manner to imply that it contains mandatory requirements but rather it was intended to serve as identifying best practice guidance and suggestions for Members. The proposed Guidance Note has now been redrafted to incorporate sufficient flexibility.

Conclusion

Technical staff reviewed the drafting style to incorporate additional flexibility and have amended where necessary to reflect the original intention of the Guidance Note.

(iii) **Interaction of APES GN30 with ASA600 group audits and Network Firms**
[GC8, GC14, SC6, SC8, SC17, SC29, SC32]

Respondents' Comments

Some of the respondents highlighted the requirements and application material for the conduct of group audits contained in ASA 600 *Special Considerations – Audits of a Group Financial Report (Including the Work of Component Auditors)* as well as using other experts in audit engagements which is addressed by ASA 620 *Using the Work of an Auditor's Expert*. These are based on the international equivalent standards ISA 600 and ISA 620 and establish the auditor's obligations in a group audit situation and in respect of the use of other experts for the purpose of audit engagements. The majority of the respondents suggested that the Guidance Note should specifically exclude these situations as they are addressed by Auditing Standards. Some respondents have also raised the issue of cross border teams in the larger firms and the application of the proposed Guidance Note to Network Firms who have common quality control procedures.

Technical Staff Response

When drafting APES GN 30, the Guidance Note did not contemplate the issue of group audits and the use of Network Firms. The ASA 620 definition of Expert specifically excludes accounting and related skills. As there is a Member in Public Practice involved in providing services and what is contemplated in ASA 620 is an activity the Member could not carry out as they do not have the relevant skills. Accordingly, the work addressed by ASA 620 does not satisfy the definitions of Outsourcing in the proposed APES GN 30.

In accordance with the requirements of ASA 600 paragraph 19, where a group audit is performed, the group auditor is required to obtain an understanding of the component auditor's understanding of and compliance with ethical standards, professional competence and the level of interaction required to obtain sufficient appropriate audit evidence. The group auditor also needs to ascertain whether independence requirements have been met by the component auditor. ASA 600 paragraphs 46-49 further requires the group auditor to communicate with management and those charged with governance of the group.

In a group audit situation the component auditors would also be engaged by the Client or one of its related entities. Thus it will not meet the definition of Outsourcing. Accordingly, these engagements should be excluded (refer new paragraph 1.6).

The AICPA ethical ruling 112 applies in the following circumstances:

"A member in public practice uses an entity that the member, individually or collectively with his or her firm or with members of his or her firm, does not control (as defined by accounting principles generally accepted in the United States) or an individual not employed by the member (a third-party service provider) to assist the member in providing professional services...."

Generally a Network Firm will not be subject to "control" in accordance with the accounting principles of the relevant jurisdiction. However, it is acknowledged that a Network Firm will be subject to common quality control and risk management procedures of that Network. These procedures would be similar to or possibly more stringent than the best practice guidance in this Guidance Note. The key issue is whether the Client is aware of the use of Network Firms in performing the relevant Engagement. A new example 8 has been developed to address this circumstance.

Conclusion

If a Member is performing a group audit Engagement subject to ASA 600 then the Member should be excluded from the scope of this Guidance Note. This is in recognition of the Member's obligations to comply with ASA 600 as well as APES 320 *Quality Control for Firms*.

The scope of APES GN30 has been amended to address Engagements that have been performed in accordance with ASA 600 (refer paragraph 1.6). In addition, new examples have been developed to illustrate the use of Network Firms (example 8) and group audits under ASA 600 (example 10).

(iv) Interaction with other standards and regulations

[GC23, SC8]

Respondent's Comments

A respondent noted the operation of other guidance and standards for Outsourced Services. The standards noted include CPS 231 issued by the Australian Prudential Regulatory Authority (APRA), which contains requirements and guidance for entities regulated by APRA.

Technical Staff Comments

During the development phase of APES GN 30 the APRA standards were considered by the taskforce. Some of the definitions and guidance developed are based on these standards. APRA standards will generally be applicable to Members in Business and paragraph 1.10 allows sufficient flexibility in this regard.

Conclusion

Paragraphs 1.3, 1.4, 1.5 and 1.10 allow flexibility required in relation to other standards. Note also that key definitions of Outsourcing and Material Business Activity are broadly consistent with APRA standards.

(v) Treatment of existing contracts

[GC21, SC7, SC71]

Respondent's Comments

Some respondents noted the need for the Guidance Note to address existing Outsourced Service arrangements and the method by which such arrangements should be transitioned to best practice arrangements. It was noted that many Members in Public Practice already participate in Outsourcing arrangements and have contracts that are currently in place. Legally binding obligations will arise from such existing contracts leading a respondent to suggest that the Guidance Note needs to provide clear principles based guidance addressing transition from existing contractual obligations.

Technical Staff Response

We have considered the implications of existing contracts and the need for clarity around the prospective application of the proposed APES GN 30. Technical staff researched the approach of other standard setting bodies such as AUASB and noted that there are occasions where start dates have been applied to Guidance Notes.

The taskforce discussed the issues associated with the effective date for the Guidance Note and identified two potential approaches:

- Immediate application from the date of issue of the Guidance Note; or
- An application date such as 1 April 2013 to allow Members time to consider the implications of the guidance.

The taskforce discussed the issue and agreed that the Guidance Note can be effective from the date of issue similar to APES GN 40. It will only be applicable prospectively and should not impact on existing contractual arrangement. As it is only best practice guidance and due to the changes made to address respondents comments (such as moving the Service Level Agreement to an appendix) the taskforce was of the view that an additional period was not required.

Conclusion

Similar to APES GN 40, adopt the date of issue as the effective date.

(vi) Scope of guidance in relation to the provision of Outsourced Services

[SC1- SC4, SC6]

Respondent's Comments

Many of the respondents disagreed with the application of the guidance to the provision of Outsourced Services suggesting that only utilisation of such services should be within the scope of the guidance. The general opinion of respondents can be summarised by one comment received which states that Outsourcing should not be viewed as a stand-alone service offering rather a method by which an underlying Professional Service is delivered. Such services are addressed by existing standards and guidance and therefore should not fall within the scope of APES GN 30.

Technical Staff Response

Whilst we acknowledge that there are a number of standards that address services which may be offered by a Member in Public Practice, there is benefit in giving guidance to Members when providing Professional Services as part of an Outsourcing arrangement.

Existing standards assume that the Member in Public Practice is primarily providing the services, not a third party service provider. Outsourcing a Professional Service carries its own inherent risks which are directly addressed by this Guidance Note. For example, a Member may be providing an Outsourced Service to a non-member that may not have considered threats to the principles of the Code such as threats to confidentiality. On this basis, Technical Staff are of the view that the provision of Outsourced Services should remain within the scope of APES GN 30.

Conclusion

At the July 2012 Board meeting, the APES Board agreed with the taskforce's recommendation that Outsourced Services should remain within the scope of the proposed Guidance Note.

(vii) Definitions

[SC13- SC31]

Respondent's Comments

All respondents raised concern with the definitions of key terms such as "Outsourcing", "Material Business Activity", "Outsourced Service Provider", "Outsourcing Agreement" and "Outsourced Service". Some respondents noted that there was a lack of clarity with regard to key definitions and one respondent stated that the ED does not adequately define the term "Outsourcing" due to the circular nature of key definitions.

A respondent commented that the ED does not adequately define the term "Outsourcing" with the argument as follows:

The ED defines Outsourcing to mean the transfer of responsibility for conducting processes to an Outsourced Service Provider. An Outsourced Service Provider is defined to mean an entity that is providing services in accordance with an Outsourcing Agreement. An Outsourcing Agreement is defined to mean the document in which the terms and conditions of an Outsourced Service are set out. An Outsourced Service is defined to mean a service involved in Outsourcing a Material Business Activity to an Outsourced Service Provider.

Technical Staff Response

Technical staff considered the definitions included in the Guidance Note and agree that the terms are circular leaving the reader without a succinct definition of the subject matter of the Guidance Note, Outsourcing. Technical staff also considered the definitions and their consistency with Prudential Standard CPS 231 *Outsourcing* (CPS 231) as follows:

| CPS 231 Definition | Revised APES GN30 Definition | Comments |
|--|--|--|
| <p>9. Outsourcing involves a regulated institution entering into an arrangement with another party (including a related body corporate) to perform, on a continuing basis, a business activity that currently is, or could be, undertaken by the regulated institution itself.</p> <p>10. For the purposes of this Prudential Standard, offshoring means the outsourcing by a regulated institution of a material business activity associated with its Australian business to a service provider (including a related body corporate) where the outsourced activity is to be conducted outside Australia. Offshoring includes arrangements where the service provider is incorporated in Australia, but the physical location of the outsourced activity is outside Australia. Offshoring does not include arrangements where the physical location of an outsourced activity is within Australia but the service provider is not incorporated in Australia.</p> | <p>Outsourcing means the transfer of the conduct of processes to another service provider other than the Member in Public Practice engaged by the Client. It generally occurs when an entity engages a party on a continuing basis to perform on the entity's behalf, a business activity that is, has been, or could be performed by that entity. Processes may include the remote hosting of business systems by the service provider Outsourcing can be from a Client to a Member in Public Practice or from a Member to another service provider.</p> | <p>CPI 230 refers to a business activity that is provided on a <u>continuing basis</u> in the definition of Outsourcing. It also highlights that the activity <u>could be performed by the entity itself</u>. Discussion of Offshoring then refers to the provision of a <u>material business activity</u>.</p> <p>The revised APES GN 30 definition is broadly consistent with that of CPS 231.</p> |
| <p>A material business activity is one that has the potential, if disrupted, to have a significant impact on the regulated institution's business operations or its ability to manage risks effectively, having regard to such factors as:</p> <p>(a) the financial and operational impact and impact on reputation of a failure of the service provider to perform over a given period of time;</p> <p>(b) the cost of the outsourcing arrangement as a share of total costs;</p> <p>(c) the degree of difficulty, including the time taken, in finding an alternative service provider or bringing the business activity in-house;</p> <p>(d) the ability of the regulated institution to meet regulatory requirements if</p> | <p>Material Business Activity means an activity of an entity that has the potential, if disrupted, to significantly impact upon the quality, timeliness or scale of Professional Services offered by a Member in Public Practice or received by a Client. Whether an activity is a Material Business Activity should be based on an assessment of the risk associated with the nature and size of the activity conducted. Material Business Activities exclude the internal activities of the Firm such as record storage or software application hosting that do not involve an active role in the Professional Service delivered to the Client.</p> | <p>CPS 231 refers to the impact that disruption of material business activities could have on the ability to <u>manage risks</u> effectively and lists a number of factors to consider. CPS 231 then specifically includes the <u>internal audit function</u> within the definition of material business activity.</p> <p>In addition to risk, the revised APES GN 30 definition highlights the need to consider the impact on quality, timeliness and scale of services offered. The definition then <u>specifically excludes activities such as software application and hosting</u>. The revised definition is broadly consistent with CPS 231.</p> |

| CPS 231 Definition | Revised APES GN30 Definition | Comments |
|---|------------------------------|----------|
| <p>there are problems with the service provider; (e) potential losses to the regulated institution's customers and other affected parties in the event of a service provider failure; and (f) affiliation or other relationship between the regulated institution and the service provider.</p> <p>For the purposes of this Prudential Standard, the internal audit function is a material business activity.</p> | | |

Conclusion

The key defined terms have been amended to enhance clarity and remove the circular nature of the definitions. Definitions are broadly consistent with those in Prudential Standard CPS 231 *Outsourcing*.

(viii) Disclosure requirement for written consent

[SC40, SC41, SC43, SC44, SC46]

Respondents' Comments

Some respondents do not see the benefit of disclosing Outsourcing arrangements to Clients and do not understand the necessity to obtain written consent for such arrangements. It was stated that standard engagement terms which state that part of the services for a client may be Outsourced or provided outside of Australia is sufficient disclosure to clients. Most of the respondents did not think it necessary to disclose the nature and extent of the Professional Service being Outsourced.

Another respondent noted that since the Member in Public Practice retains the primary responsibility to deliver the Professional Service, the extent to which Outsourced Services are used is no more relevant for disclosure to a Client than any other valid business practices employed by the Member in Public Practice. Furthermore it would be unwieldy and burdensome for large firms to obtain consent from each Client.

These arguments are not unique to Australia. **The Journal of Business Ethics** recently published the article: ***Deficiencies in the Code of Conduct: The AICPA Rhetoric Surrounding the Tax Return Preparation Outsourcing Disclosure Rules*** ('the article'). APESB Technical Staff have prepared an abstract of the article which is in appendix 2. The authors of this article consulted a number of resources in their investigation of the AICPA disclosure requirements for outsourced tax returns, and noted the AICPA's and large accounting firms' resistance to disclosure of offshoring of tax return preparation to clients. They concluded that required disclosures from the AICPA are inadequate and argued that it in effect leads to concealment of offshoring of tax return preparation.

The article found that, similar to local respondents to ED 01/12, the US has seen much resistance to disclosure of offshoring arrangements. Accordingly, as a result of this pressure the language adopted by AICPA Ethics Ruling No. 112 under Rule 102 provides the member with significant flexibility in relation to disclosing the use of third party service provided who may be located offshore. The disclosure states:

Before disclosing confidential client information to a third-party service provider, a member should inform the client, preferably in writing, that the member may use a third-party service provider. AICPA 2004a)

The article suggests that the two main features that the disclosure should be comprised of are opaque. That is, the member's intent to outsource and the identity and location of the Third Party Service Provider. Further, there is no requirement for specific disclosure of off-shoring.

The article subsequently noted that members of small firms that do not outsource tax returns and non-practising AICPA members were critical of the AICPA approach to this disclosure requirement. In contrast, the large firms were supportive of this style of disclosure and were opposed to providing specific disclosures to Clients.

Technical Staff Response

Technical staff considered the issues raised in light of the fundamental principles of the Code, in particular, confidentiality. Clients are entitled to know whether their confidential information is being transferred to another entity, whether local or overseas, and should be given the opportunity to consider the manner in which their information will be managed.

This is particularly relevant to offshored Outsourced Service Providers that may not be subject to the same legal and confidentiality requirements as they are no longer under the same jurisdiction as the Client or the Member in Public Practice (whether it is a Network Firm or not). This view is supported by the AICPA's *Ethics Ruling on Independence, Integrity and Objectivity* provided in appendix 1)

Conclusion

Given the above discussion and the potential threat against the fundamental principle of confidentiality, the suggested disclosure of Outsourced Service arrangements to the Client is considered best practice for a Member in Public Practice.

2. Technical Staff Recommendations/Way forward

Technical Staff recommend that the APES Board consider the contents of this Technical Analysis paper and amendments made to the proposed Guidance Note, and subject to the Board's review comments approve the issue of the Guidance Note.

3. Appendices

Appendix 1: Extracts from AICPA's Professional Standards – *Ethics Ruling on Independence, Integrity and Objectivity*

Appendix 2: Summary of AICPA's Outsourcing article - Deficiencies in the Code of Conduct: The AICPA Rhetoric Surrounding the Tax Return Preparation Outsourcing Disclosure Rules

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Date: 7 November 2012

Appendix 1

Extracts from AICPA's Professional Standards – *Ethics Ruling on Independence, Integrity and Objectivity*:

112. Use of a Third-Party Service Provider to Assist a Member in Providing Professional Services

.224 Question – A member in public practice uses an entity that the member, individually or collectively with his or her firm or with members of his or her firm, does not control (as defined by accounting principles generally accepted in the United States) or an individual not employed by the member (a third-party service provider) to assist the member in providing professional services (for example, bookkeeping, tax return preparation, consulting, or attest services, including related clerical and data entry functions) to clients. Does rule 102, *Integrity and Objectivity* [ET section 102.01], require the member to disclose the use of third-party service provider to the client?

.225 Answer – Yes. The concept of integrity set forth in Rule 102 *Integrity and Objectivity* [ET section 102.01] and Article III, *Integrity* [ET section 54] requires a member to be honest and candid. Clients might not have an expectation that a member would use a third-party service provider to assist the member in providing the professional services. Accordingly, before disclosing confidential client information to a third-party service provider, a member should inform the client, preferably in writing, that the member may use a third-party service provider. This disclosure does not relieve the member of his or her obligations under ethics ruling No. 1 [ET section 391.001-.002] under Rule 301, *Confidential Client Information* [ET section 301.01]. If the client objects to the member's use of a third-party service provider, the member should provide the professional services without using the third-party service provider or the member should decline the engagement.

A member is not required to inform the client when he or she uses a third-party service provider to provide administrative support-services (for example, record storage, software application hosting, or authorised e-file transmittal services) to the member.

See ethics ruling No. 12 [ET section 291.023 – .024] under Rule 201, *General Standards* [ET section 201.01], and Rule 202, *Compliance with Standards* [ET section 202.01]; and ethics ruling No. 1 [ET section 391.001 – .002] under Rule 301, *Confidential Client Information* [ET section 301.01], for additional responsibilities of the member when using a third-party service provider.

Appendix 2

Deficiencies in the Code of Conduct: The AICPA Rhetoric Surrounding the Tax Return Preparation Outsourcing Disclosure Rules

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This paper examines the American Institute of Certified Public Accountants' (AICPA) efforts to **conceal** the **offshoring of tax return preparation services** by US Certified Public Accountants (CPAs) through justification and recommendation of **an inadequate disclosure format** for this type of work.

Several theories have been drawn upon to analyse the underlying agenda behind the two new and one revised AICPA Ethics Rulings (AICPA Ethics Ruling No. 112 under Rule 102, No. 12 under Rule 201, and No. 1 under Rule 301) in relation to a CPA's responsibilities when outsourcing services to domestic or overseas Third Party Service Providers (TPSPs). Theories include *Giddens' theory of trust and expert systems*, *the public accounting professionalism literature* and *Flyvbjerg's concept of power*.

Three pertinent issues that depict AICPA's on-going promotion of **their private interests** were analysed in this paper namely:

- i. AICPA leadership's stated professional justifications for outsourcing and its recommended client disclosures;
- ii. risks associated with outsourcing tax return preparation work overseas and the trust issues that result; and
- iii. the resistance within the rank and file of the CPA profession.

Introduction

The wave of **accounting scandals** has damaged the **AICPA's public image** and has created the need to restore their commitment to the **public interest**. Despite AICPA's effort to do so, the revision of AICPA's Ethics Rulings in relation to the disclosure rule of TPSPs appears to promote the **US public accounting profession's private interests** over the **interest of its clients and the public**.

The revised ethics rulings suffer from **several inadequacies** from a **public interest standpoint**. One major issue identified is that **no distinction** has been drawn between **domestic TPSPs** and **overseas TPSPs**. The AICPA's disclosure format suggests that there are no significant differences between outsourcing domestically and offshoring, thus equal weight should be given when developing ethical disclosure requirements. However, the public was of the view that clients have the right to know if their confidential information is being sent overseas outside the US jurisdiction where privacy and security laws is not the same as the US jurisdiction. It was concluded on this basis that the revised disclosure rules reflect AICPA's continuing efforts to further **the profession's private interests** by magnifying the **benefits of offshoring** whilst playing down the associated risks.

Outsourcing Professional Tax Services

The trend of outsourcing preparation of income tax returns overseas, particularly to India, began in the early 2000s. Benefits of offshoring include staff utilisation of core activities, lower costs, access to specialised best

practice skills, lower level of layoffs after busy season and reduced recruitment and training; that resulted in extensive cost savings for firms.

While offshoring opens avenues for increased revenues and speedy delivery of returns, there may be unintended consequences to modifying business processes which expose firms offshoring tax returns to additional business risks. One of the greatest concerns about offshoring is the privacy and security risk of posting confidential client information such as social security numbers to a facilitator's website. The offshoring of tax preparation services also raises several legal concerns such as the potential liability US tax preparer incur when hiring foreign subcontractors to process tax returns for US tax payers; and ethical issues associated with US tax preparers' duty to disclose to clients the use of offshore tax preparers.

The AICPA's stance on the practice of offshoring is that it is an economic activity necessary for the continuing economic development of the CPA profession. AICPA describes offshoring of tax returns as an improvement of work processes and a step towards the adoption of global business practices.

Analysis of Three Critical Issues Related to Tax Return Preparation Outsourcing

In order to examine the AICPA's development of ethical rulings regarding disclosure of offshoring a client's tax return preparation work, evidence was gathered through a latent content analysis of archival material supplemented with interviews. As **client confidentiality and information security** were key considerations in the debates over disclosure rules, interviews with a sample of three leading TPSPs in India were conducted to obtain an understanding of the **risks involved with offshore outsourcing** and the measures adopted by the TPSPs to ensure confidentiality of information.

Based on the interviews and review of archival materials, three recurring critical issues were identified:

i. AICPA leadership's stated professional justifications for outsourcing and its recommended client disclosures

Opaque disclosure requirements

Past scandals and loss of reputation dictate the importance of reminding the public about integrity, objectivity, competence and professionalism of CPAs. The AICPA's Professional Ethics Executive Committee (PEEC) concluded that there is a need to revise their Code of Professional Conduct in connection with the use of TPSPs. **The final language recommended in the revised rulings suggested that the member 'should' and not 'must' disclose that a TPSP may be used thereby shifting the onerous concern of disclosing to the member's discretion.** Further, the disclosure format requires that the member state that the return 'may' be outsourced to a TPSP. AICPA Ethics Ruling No. 112 under Rule 102 states:

Before disclosing confidential client information to a third-party service provider, a member **should** inform the client, preferably in writing, that the member **may** use a third-party service provider.

Such disclosure merely stating a possibility to outsource is misleading if the CPA firm is aware of their definite intention to outsource. The final rulings do not require specific disclosure of offshoring since the PEEC noted that they believed it was appropriate to focus on the ethical issues when a member uses the services of a TPSP and not to address the specific risks associated with overseas outsourcing.

The AICPA's justifications for **opaque disclosure rules** were revealed most clearly as the leadership of the AICPA debated the disclosure issue with the United States Internal Revenue Service (IRS) and the United States Congress.

Professional tax return preparers in the U.S. must be enrolled to practice before the IRS. Thus, CPAs performing tax preparation services must comply with IRS regulations as well as the AICPA Code of Professional Conduct. The stated purpose of the IRS regulations was to prevent offshore outsourcing of tax return preparation without the taxpayer's knowledge. The AICPA was adamant in expressing its view that the IRS's new rules could potentially erode professional autonomy and diminish their professional authority.

The AICPA was of the view that IRS's **proposed regulations were drafted in a manner that added unnecessary and extremely burdensome** steps to the current tax return processes. AICPA members are already aware of their professional responsibility to the client and are able to remain responsible even when

a TPSP is used. Rule 301, ET 1 states that a member should enter into a contractual agreement with the **TPSP to maintain the confidentiality of the client's information**, and should use reasonable care to determine that the third party has appropriate procedures in place to prevent unauthorised release of confidential client information to others.

ii. Technical Aspects of Outsourcing and Issues of Risk

An important and recurring issue in the debate over tax preparation outsourcing disclosure rules was differing perceptions of client risks associated with outsourcing professional, expert work both domestically or overseas.

The position of the AICPA regarding client's confidential information endorses the view that the TPSPs are competent and have procedures in place to maintain security that are reliable. However, these assertions are debatable as experts can get things wrong, by misinterpreting or being ignorant of expertise they are presumed to possess. When questioned about how the three service providers in India deal with **issues such as risk mitigation, business continuity, privacy and information security**, all were of the view that standards are strictly in place to ensure information security and privacy of data. Means to mitigate risk include periodic certification, email tracking and network sharing drives.

While the results from the sample study corroborate the AICPA's assertions about data security during offshore practices, it is worth noting that the level of exposure to data security risks at the smaller providers has not been explored by any study and hence cannot be quantified with any certainty.

iii. Resistance with the Rank and File of the CPA Profession

Members of **small firms** that do not outsource tax returns and AICPA members who were not in public practice **criticised the AICPA's approach**, arguing that it reduced the **trustworthiness** of the profession. In **contrast** to the position of the small accounting firms, the large accounting firms were supportive of offshoring (and AICPA's proposed disclosure) and opposed to specific disclosure to the Client.

LBMC, the sixth largest firm in the South-eastern U.S. and the 54th largest firm in the United States, strongly opposed a specific disclosure requirement, describing it as **an obstacle** to practicing CPAs who are trying to **be successful and competitive**.

The AICPA, acting in **support of the large firms**, forwarded the argument that the disclosure of **offshoring is counter-productive and impedes economic development**. In addition to their argument against the IRS proposed regulations, the **AICPA argued** that the proposed regulations as currently drafted did not recognise or **adequately reflect the various forms under which large accounting and legal firms** are organised in today's global marketplace; a circumstance that complicates both the domestic disclosure and potentially the offshore disclosures.

The AICPA and the large accountancy firms rationalised their actions by using terms such as 'competitive' and 'improving quality' to persuade their audiences. The AICPA ignored the concerns raised by the small firms and framed the disclosure format to suit the needs of the larger firms.

Conclusion

The article examined an attempt by the AICPA to conceal the offshoring of tax return preparation work by CPAs by recommending a weak disclosure format in their revised ethics rulings – as an instrument to advance the self-interest of the profession.

The **AICPA actively campaigned** on behalf of the larger firms to convince **regulatory agencies** such as the IRS that the disclosure format adopted by the AICPA was comprehensive. However, the study demonstrates that **the format does not reveal the geographical location** of the service provider, does **not mandate explicit disclosure**, leaves the form of disclosure to the **discretion of the member** and does not recommend **any specific format**.

The authors conclude with the following comment:

The trend of commercialisation of the accounting profession witnessed in the last decade is the consequence of the pursuit of self-interest and its aftermath, the loss of trust. The AICPA wanted to continue outsourcing tax return preparation work to a foreign country primarily for commercial reasons. Power, quite simply, often finds ignorance, deception, self deception, rationalisation, and lies more useful for its purposes than truth and rationality, despite all costs (Flyvbjerg 1998).

As stated by Jim Rigos, CPA in his comment letter to the exposure draft: "For once we had the chance to be on the right side and demonstrate that the AICPA serves the public interest by being ahead of the curve. I am disappointed (AICPA 2004c).