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Los Angeles – LAX
Los Angeles – Orange County
Sacramento
San Diego
San Francisco – Downtown
San Francisco – Marin County
San Francisco – Walnut Creek

Colorado

Denver

Connecticut

Hartford

Delaware

Wilmington

Florida

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Miami
Orlando
Tampa

Georgia

Atlanta
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Savannah

Illinois

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Indiana

Indianapolis

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Lexington

Massachusetts

Boston

Nevada

Las Vegas

New Jersey

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Newark

New Mexico

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New York

New York City

Ohio

Cincinnati
Cleveland
Columbus

Pennsylvania

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Tennessee

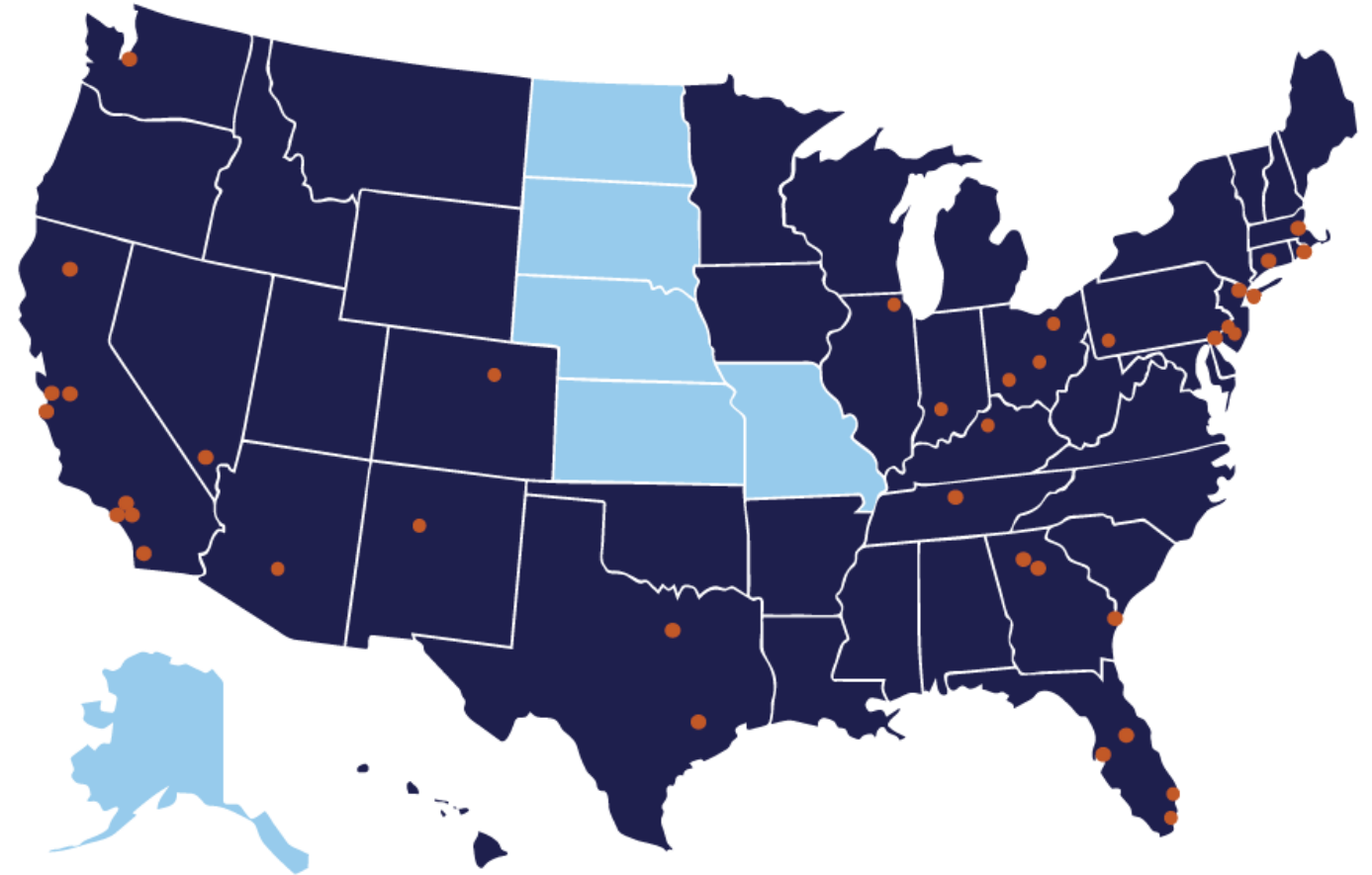
Nashville

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Protect and Collect – The Effective Use of Engagement Letters

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First Step in Client Relationship

- Client Acceptance/Retention
 - Do you want to be associated?
 - Client integrity
 - Assess client (management, directors, owners) integrity
 - Consider background checks
 - Engagement Acceptance
 - Assess firm capabilities and competence (“due care”)
 - Conventional Wisdom
 - Risks of association (believed to be more audit related)
 - vs. risks of execution (more tax and consulting related)

Engagement Letters

- Goal is very simple – Managing Expectations
 - Defined, understood and agreed
 - Expectations “gap” single biggest contributor to non-audit failures
- Defines scope of engagement
- Tailored to reflect objectives; scope and limitations; responsibilities; fees and other terms and conditions
- Controlling factors in determining the responsibilities of client and CPA

Engagement Letter Tips



Annual for all
engagements



Scope



All changes in
scope in writing



Responsibilities:
Client and Firm



Dispute
Resolution



Fees

Engagement Letter Required Contents

- Engagement letter is a contract
 - Goal is to manage expectations
- Identify parties to engagement
- Scope of the engagement
- Fees
- What are the deliverables
- Exclusions
- Use Restrictions
- Risk allocations
 - Limitation of liability
 - Indemnity
 - Controlling law
- Professional Standards that govern

Content Engagement Letters

Client's Responsibilities

- Maintain Business Records
- Maintain documents to support data in return, i.e. Business expenses
- Ownership changes
- Designate a Partnership representative
- Verify accuracy of return
- Terms can be negotiated

Essential Terms of the Engagement Letter

- Fee Structure
 - Match services to the fees
 - Review documents = \$_____
 - Prepare annual filings = \$_____
 - How much and how often the client will be billed
 - Triggers if client requests services outside the scope of engagement
 - Clause for late payment
 - Period of engagement
- Confirmation of terms
 - Signed by both parties before work begins

Business Risk Allocation

- Limitation of Liability
 - Critical if a lawsuit is filed
 - Law varies from state to state
 - Addresses contractual liability to clients
 - Direct damages (e.g. cost to complete or warranty work)
 - Special or consequential damages (might include lost profits or business opportunities – potentially much greater)
 - Punitive damages
- Drafting issues
 - Try to capture any basis upon which a claim could be made including breach of contract or negligence
 - Do not make it broader than the law will allow

Business Risk Allocation cont'd

- Limitation of Liability cont'd
 - Drafting issues cont'd
 - Try to capture any basis upon which a claim could be made including breach of contract or negligence
 - Do not make it broader than the law will allow
 - Make it prominent and bring it to the client's attention
 - Might need the clause in several sections

Business Risk Allocation cont'd

- Indemnification
 - What is it?
 - Shifts cost of liability from one contractual party to the other
 - Pay client's costs to defend a claim made by third parties against the client that resulted from the CPA firm's negligence
 - Fund a settlement, judgment
 - To a Third Party
 - Client's bank

Business Risk Allocation cont'd

- Indemnification
 - Protect yourself against unreasonable clients
 - Clients want to insulate themselves from exposure and shift liability to the CPA firm
 - Absent a contractual duty, a CPA firm is not liable to reimburse a client for its legal costs or amounts paid by the client to settle claims made by a third party
 - Some states have anti-indemnification statutes

Business Risk Allocation cont'd

- Indemnification cont'd
 - Need to protect your firm against client management's misrepresentation or intentional withholding of information
 - Review rules related to independence
 - Does not necessarily impair it
- PCAOB Auditing Standard No. 16 – certain matters should not be in an engagement letter
 - Indemnification provisions are not permissible for audits of issuers

Business Risk Allocation cont'd

- Dispute Resolution
 - Speak to a lawyer in your jurisdiction first
 - Often helpful to compel arbitration or mediation and avoid lengthy litigation expenses
 - Could have insurance coverage implications.
- Non-engagement letter
 - For those non-clients you do not take, it is critical to get a timely letter to the non-client informing them that you do not represent them

Confidentiality and Privacy

- Legal and regulatory requirements
- State Privacy Regulations
- Contractual Requirements
- AICPA Code of Professional Conduct



CONFIDENTIAL

Modifying Boilerplate Engagement Letters

- Confidentiality/Protection of Client Data
 - Cyber Risks and Liability are at the forefront for everyone
 - Use of Technology
 - Transfer to Third Parties
 - Protection of Privilege

Confidentiality (Broadly)

- General – absolute obligations for client confidentiality
 - Cal. Prof. Bus. Code § 5063.3
 - “No confidential information obtained by a licensee, in his or her professional capacity, concerning a client or a prospective client shall be disclosed by the licensee without the written permission of the client or prospective client, except the following”
 - Exceptions:
 - Court order to respond to subpoena or summons
 - Necessary to maintain/defend in legal proceeding initiated by client
 - Official inquiry from federal or state regulatory agency
 - Made to another licensee in connection with proposed sale or merger of licensee’s professional practice (with written nondisclosure)
 - Made to another licensee (1) professional consultation, (2) professional standards review
 - Specifically required by law
 - Specified by the board of accountancy in regulation
- AICPA Rule 301
 - “A member in public practice shall not disclose any confidential client information without specific consent of the client.”

Essential Terms of the Engagement Letter

- Work Papers/Client records
 - Common sources of complaints/problems
 - Lost client issues
 - Return of client records (varying standards by state)
 - Access by successor to accountant's workpapers
 - Ownership of Accountant's workpapers
 - Written permission
 - Release
 - Contingent upon payment of fees



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Contractual and other Legal Obligations for Confidentiality

- Engagement Letters
- Nondisclosure Agreements

Element of a Confidentiality Agreement

- Definitions
- Exclusions
 - “Need to know” language
 - Obligations for contractors and employees
- Protection obligations
- Return obligations
 - Often problematic because of electronic storage, professional obligations to support work product
- Legal proceedings

Standards and Compliance

- Keep Current
 - Circular 230
 - SAS 99
- Training
- Data Privacy Regulations
- AICPA Code of Conduct

Standards and Compliance

- Common standards that apply to audit engagement
 - ET – Ethics
 - QT – Quality Control
 - AU – Auditing
 - SAS – Statements on Auditing Standards
- Cal. Code Regs. Tit. 2 § 1131.2 – Minimum Audit Requirements
 - Generally accepted auditing standards
 - GAAS, AICPA
 - Professional judgment

Common Challenges

- Fee pressures
- Client push back
- Lack of knowledge and education
- Fear
- Complacency

Due Diligence Situations

- Permissions
- Reliance and level of responsibilities
- To whom is a duty owed?
 - California
- Publicly Held = INDEPENDENCE

Time to Disengage?

- Difficult, manipulative or uncooperative client behavior
- Unresolved client complaints about the service provided
- Client complaints about fees being too high
- Consistently delinquent payment
- Clients suffering business or personal hardship

Reasons to Disengage (cont.)

- Personality conflicts between the client and the firm
- Unseemly, unethical or fraudulent activity
- Changes in client's business
- Changes in your firm's partners, staff or goals
- Conflicts of interest

Document Retention/Destruction Policy

- Goal = Create record retention policies that are cost effective and not unduly burdensome to establish, maintain and simplify the purging and disposal of records no longer needed
- Why?
 - In recent years, corporate and accounting frauds and allegations of wrongful document destruction have prompted legislators, regulators and others to establish new laws and regulations that impose civil and criminal penalties and other sanctions for mishandling certain types of records

Document Retention/Destruction Policy

- Maintaining a documented policy which is consistently followed and monitored to prevent improper destruction of paper or electronic documents is an effective means of avoiding allegations or presumptions of improper document destruction when faced with a lawsuit or government inquiry.
- A written policy provides clear direction to professional staff about which records should be maintained by the firm at the conclusion of an engagement, which should be returned to the clients and which should be destroyed.

Document Retention/Destruction Policy

- It also provides internal communications about records management by providing instructions on how long records should be maintained, how and where they should be maintained, and how they should be destroyed.
- Providing clients with the firm's written records retention policy helps eliminate misunderstandings about responsibility for maintaining records and notified clients of the time frames for destruction of the firm's records. It also demonstrates the firm's commitment to client confidentiality and adherence to applicable record retention laws and regulations.
- The timely destruction of records no longer needed reduces the risk that these records become subject to discovery.

Document Retention/Destruction Policy

- Why retain workpapers and records?
 - Facilitating future engagements
 - Responding to client requests
 - Responding to inquiries by taxing authorities
 - Participating in peer or quality review and inspections.
 - Comply with legal, regulatory and contract requirements
 - Defending malpractice claim or litigation



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