

# A BASIC ETHICS GUIDEBOOK FOR CONNECTICUT CPAS

A Continuing Professional  
Education Ethics Course

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# Part I: Framework of Ethical Thought



# What are ethics?

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1. A general pattern or “way of life.”
2. A set of rules of conduct or “moral code.”
3. An inquiry about ways of life and rules of conduct.

# Primary Branches of Ethical Thought

- *Normative Ethics*, which is the study of how define right and wrong action – covered in Part I and II of these materials.
- *Applied Ethics*, which discusses how to put ethics into action – covered in Part III.

# Types of Normative Ethical Theory

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- Consequentialism
- Deontological Theory
- Virtue Ethics

# Consequentialism

- The right action is based on the consequences of the action.
- Encompasses the axiom “ends justifies the means.”
- Individuals often evaluate only the short-term instead of long-term consequences, and foreseeable vs. possible consequences.

# Case Study

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# Mortgage Crisis of 2007-2010

# Deontology

- Focuses on “doing your duty for duty’s sake.”
- A person must tell the absolute truth even though the fall-out could be significant.
- The right thing is determined by universal ethical values such as honesty, promise-keeping, fairness, loyalty, justice, responsibility, compassion, and respect for human beings/property.



# Case Study

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# Toronto Dominion Bank



# Virtue Ethics

- States that having the right character, or virtues, is the most important aspect of morality.
- What makes an action right is that it is one that a virtuous person would take.
- Aristotle is the most famous proponent of virtue ethics.

# Aristotle's Virtue

1. *Courage*
2. *Temperance* - moderation
3. *Liberality* – spending money well
4. *Magnificence* – living “well”
5. *Pride* – taking pleasure in accomplishments
6. *High handedness* - concern with the noble, not with the petty
7. *Diligence* – between reckless ambition and total lack of effort

# Aristotle's Virtues (cont'd)

8. *Gentleness* - concern for others
9. *Truthfulness*
10. *Wit* - pleasure in group discussions
11. *Friendliness* - pleasure in group associations
12. *Modesty* - pleasure in personal conduct
13. *Righteous indignation*
14. *Justice*

# Whistleblowing Provisions

- Dodd-Frank Wall Street Reform and Consumer Protection Act
- Provides whistleblower awards if certain criteria are met.
- Provides protection within CPA firms for whistleblowers serving public companies.

# Other Whistleblowing Provisions/

- Seems to indicate that CPAs who are aware of material misstatements in a public company client are obligated to whistle blow.
- SEC Office of the Whistleblower - <https://www.sec.gov/whistleblower>

## **Part II: Codes of Conduct for CPAs**





*“[These] Principles call for an unswerving commitment to honorable behavior, even at the sacrifice of personal advantage.”*

*--ET § 0.300.020.2*

# Codes of Conduct for CPAs

- CPAs are subject to specific codes from state boards of public accountancy, the SEC, the GAO, the Treasury Department, the Internal Revenue Code, common law and other national or international rule-setting bodies.

# Codes of Conduct for CPAs (cont'd)

- The Connecticut legislature passed **Connecticut General Statutes, Chapter 389 Public Accountancy (“Code”)**.
- Governs the licensing and the practice standards expected from licensee.
- The Code also establishes the Board and its powers and the Code of Professional Conduct.

# AICPA Code of Professional Conduct

- “ET” or “Code”
- Governs a CPA’s ethical and professional conduct.
- Should apply the most restrictive provision.

# Integrity

*“Integrity requires a member to be, among other things, honest and candid within the constraints of client confidentiality. Service and public trust should not be subordinated to personal gain and advantage. Integrity can accommodate the inadvertent error and honest difference of opinion; it cannot accommodate deceit or subordination of principle.”*

-- ET § 0.300.40.3

# Independence - ET § 0.400.21

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Consists of two elements:

*1. Independence of mind*

*2. Independence in appearance*

# Responsibility to the Public

“A distinguishing mark of a profession is acceptance of its responsibility to the public. The accounting profession’s public consists of clients, credit grantors, governments, employers, investors, the business and financial community, and others who rely on the objectivity and integrity of members to maintain the orderly functioning of commerce. This reliance imposes a public interest responsibility on members.”

-- ET § 0.300.30.2

# Case Study

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Olympus



# Case Study: Integrity and Objectivity

James, CPA, is a manager in a company's financial reporting department. He was asked by his supervisor to offset period expenses with "cookie jar reserves" – such as a warranty liability account – instead of properly charging such items through the P & L (profit and loss statement). James has determined that his bosses' request would run afoul of the IFRS and FASB rules, although it would result in analysts' expectations being met for this quarter's earnings release.

# Case Study: Integrity and Objectivity

He is also aware that year-end bonuses could be affected and that the stock price could plunge if expectations are not met. It was also rumored that a former co-worker who had refused to comply with a similar request had been mysteriously “laid-off.” James has a stay-at-home spouse and three young school-aged children.

# Case Study: Integrity and Objectivity (cont'd)

While James knows that the correct treatment of the expenditure in question is to currently expense it through the P & L, James may feel conflicted since he knows that potentially, his career (and by extension his family) could be adversely affected should his boss decide to retaliate. The Code requires James to show integrity and objectivity by using the correct accounting treatment despite the possible consequences. James must act independently of his management and cannot subordinate his own judgment to his supervisor's.

# Threats to Independence - ET § 1.210.010

“Many different relationships or circumstances . . . can create threats to compliance with the ‘Independence Rule’ [1.200.001]. . . Many threats fall into one or more of the following seven broad categories: adverse interest, advocacy, familiarity, management participation, self-interest, self-review, and undue influence.”

# Conflicts of Interest - ET §§ 1.110.010/2.110.010

“When a conflict of interest exists, the member should disclose the nature of the conflict to the relevant parties, including to the appropriate levels within the employing organization and obtain their consent to undertake the professional service. The member should disclose the conflict of interest and obtain consent even if the member concludes that threats are at an acceptable level.”

# Knowing Misrepresentations - ET § 1.130.010

## Examples:

- CPA makes or directs another to make, materially false and misleading entries in an entity's financial statements or records.
- CPA fails to correct an entity's financial statements or records that are materially false and misleading when he/she has the authority to record the entries.
- CPA signs, or directs another to sign, a document containing materially false and misleading information.

# Threats - ET § 1.000.10/2.000.10

CPAs are obligated to:

1. *Identify* threats.
2. *Evaluate* the significance of a threat.
3. Identify and *apply safeguards*.

# Responsibilities to Clients or Employers

“The quest for excellence is the essence of due care. Due care requires a member to discharge professional responsibilities with competence and diligence. It imposes the obligation to perform professional services to the best of the member’s ability, with concern for the best interest of those whom the services are performed, and consistent with the profession’s responsibility to the public.”

-- ET § 0.300.060.2



# Unpaid Fees - ET § 1.230.010

“Threats to [Independence] would not be at an acceptable level . . . if a covered member has unpaid fees from an attest client for . . . service provided more than one year prior to the date of the current-year report. Accordingly, independence would be impaired. Unpaid fees include fees that are unbilled or a note receivable arising from such fees.”

# Discreditable Acts – ET § 1.400.001

- A CPA may be subject to license suspension or revocation for committing an acts discreditable to the profession.
- Examples of discreditable acts include:
  - Fraud in obtaining a CPA license
  - Dishonesty, fraud or gross negligence in the practice of public accountancy.
  - Violation of the independence status.

# Examples of Discreditable Acts (cont'd)

- Fiscal dishonesty or breach of fiduciary responsibility.
- Final conviction of a felony, deferred adjudication in connection with a criminal prosecution of a felony, including crimes associated with alcohol abuse, controlled substances or physical harm.
- Knowingly participating in the preparation of a false or misleading financial statement or tax return.

# Examples of Discreditable Acts (cont'd)

- Failure to comply with a final order of any court
- Repeated failure to respond to a client's inquiry within a reasonable time without good cause.
- Threats of bodily harm or retribution to a client.

# Responsibilities to the Board/Profession

## *Discrimination and Harassment in Employment Practices - ET § 1.400.010/2.400.010*

“A member would be presumed to have committed an act discreditable to the profession. . . . if a final determination, no longer subject to appeal, is made by a court or an administrative agency. . . . that a member has violated any antidiscrimination laws . . . including those related to sexual and other forms of harassment.”

# Responsibilities to the Board/Profession (cont'd)

## *Failure to File a Tax Return or Pay a Tax Liability - ET § 1.400.030/2.400.030*

“A member who fails to . . . (a) the timely filing of the member’s personal tax returns or tax returns of the member’s firm that the member has the authority to timely file or (b) the timely remittance of all payroll and other taxes collected on behalf of others may be considered to have committed an act discreditable to the profession”

# Responsibilities to the Board/Profession (cont'd)

## *Negligence in the Preparation of Financial Statements or Records - ET § 1.400.040/2.400.040*

“A member shall be considered in violation of the ‘Acts Discreditable Rule’ [1.400.001] if the member, by virtue of his or her negligence, does any of the following:

- Makes, or permits or directs another to make, materially false and misleading entries in the financial statements or records. . .
- Fails to correct an entity’s financial statements that are materially false and misleading when the member has the authority to record an entry.
- Signs, or permits or directs another to sign, a document containing materially false and misleading information. “

**PART III: BEHAVING  
ETHICALLY: PUTTING THE  
RULES INTO ACTION**





# Ethics Alarms: Unethical Rationalizations and Misconceptions

1. The Golden Rationalization, or “Everybody does it.”
2. Ethics Surrender, or “We can’t stop it.”
3. A Sicilian Ethics, or “They had it coming”
4. Marion Barry’s Misdirection, or “If it isn’t illegal, it’s ethical.”
5. The “Tit for Tat” Excuse
6. The Trivial Trap (“No harm no foul”)
7. The Unethical Tree in the Forest, or “What they don’t know won’t hurt them.”

# Ethics Alarms: Unethical Rationalizations and Misconceptions (cont'd)

8. The King's Pass, The Star Syndrome, or "What Will We Do Without Him?"
9. The Saint's Excuse, "It's for a good cause"
10. The Futility Illusion: "If I don't do it, somebody else will."
11. The Perfect Diversion: "Nobody's Perfect?" or "Everybody makes mistakes?"
12. The Victim's Distortion "I'm being punished for doing the right thing."

# Ethics Alarms: Unethical Rationalizations and Misconceptions (cont'd)

13. The Prospective Repeal: “It’s a bad law / stupid rule”
14. The Troublesome Luxury: “Ethics is a luxury we can’t afford right now”
15. “We’ve never had a problem with it!”
16. The Apathy Defense, or “Nobody Cares.”
17. Tessio’s Excuse, or “It’s just business”
18. “I’m all right with it!” organizational abuse

# Seven Signs of Organizational Collapse

1. Pressure to maintain numbers
2. Fear and silence
3. Young 'uns and a larger-than-life CEO
4. A weak board
5. Conflicts of interest and nepotism
6. Innovation like no other
7. Belief that goodness in some areas atones for wrong doing in others

# Situations Leading to Moral Failure

- The individual fails to recognize the existence of a moral problem.
- The person may recognize a moral dilemma but does not know how to resolve it.
- The employee knows the right thing to do but fails to do it because he/she puts a higher priority on other values
- The involved party does right thing occasionally but not all the time.

# Ethical Conflicts - ET §§ 01.000.020 / 02.000.020

An ethical conflict arises when a member encounters one or both of the following:

- a. Obstacles to following an appropriate course of action due to internal or external pressures
- b. Conflicts in applying relevant professional standards or legal standards

# Keeping Yourself on the Straight and Narrow

1. Know what you believe is right and wrong. Write down the values you will live by and what you will do if your values collide.
2. Guard against being lulled into thinking you're not capable of making bad decisions. . . Keep in mind that what is legal and what is ethical are sometimes different. . .
3. Ask yourself: Would I be comfortable with my decisions landing on the front page of a newspaper? . .
4. Practice ethical decision making every day. . .

# Keeping Yourself on the Straight and Narrow

5. Discuss tough ethical dilemmas with others you respect.
6. Find your courage. [ “Courage is fear that has said its prayers.” ] . . .
7. Apply the same code of ethics whether at home, work, school or a house of worship. . .
8. Pay attention to your instincts. . . .
9. Above being loyal to your superiors, be loyal to your principles. ..

From: Cooper, Cynthia, *Extraordinary Circumstances* (NJ: Wiley & Sons, 2008), pgs. 365-366.



# Steps for Rebuilding Moral Character

Recognize what is wrong



Feel remorse - be sorry for the action, not because you got caught



Resolve to change



Plan new behavioral intentions



Demonstrate improved moral behavior

# Connecticut Rules

# The Connecticut State Board of Accountancy

Organization and Powers

# Connecticut State Board of Accountancy (“Board”)

- Board areas of responsibility:
  - Licensing
  - Continuing education
  - Quality review
  - Examination
  - Regulation and discipline.
- The Board renews yearly currently held licenses, registrations and permits.

# Connecticut State Board of Accountancy (cont'd)

- Permit holders must undergo a peer review to determine compliance with technical standards. Results are reported to the Board for review and action.
- All licensees must report 40 hours of continuing education each year.
- Investigations of allegations of violations are investigated and may result in suspension, revocation, reprimand, probation or censure.
- Board can impose civil penalties of up to \$50,000.

# Connecticut Statutes

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- Connecticut General Statutes, Chapter 389 Public Accountancy (“Code”) which governs the licensing and the practice standards expected from licensee.
- The Code also establishes the Board and its powers and the Code of Professional Conduct.

# Code Sec. 20-280 - Board of Accountancy

- Consist of nine members, to be appointed by the Governor.
  - Must be Connecticut residents
  - Five must be CT CPAs who practice public accountancy
  - Four must be public members.
  - Terms shall be coterminous with that of the Governor.
- The Board may adopt regulations governing its administration, the conduct of licensees and registrants as well as their professional conduct.
- Additional areas over which the Board has jurisdiction includes quality reviews, the use of the CPA designation, and disclosures of commissions.

# Code Sec. 20-280c - Investigation of complaints

- The Board has the power to review or investigate any possible violations of statutes or regulations, disciplinary matters or policy.



# Use of CPA Designation & Practice Privileges



# Code Sec. 20-281e - Permit Renewal and Exemptions

- The Board has the power to grant or renew permits to practice public accountancy.
- The following firms shall be required to hold a permit:
  - Any firm with an office in this state performing attest services;
  - Any firm with an office in this state that uses the title “Certified Public Accountant”, “CPA”, “CPA firm” or other similar title; or
  - Any firm that does not have an office in this state but performs attest services described for a client having its home office in this state.

## Code Sec. 20-281e - Permit Renewal & Exemptions (cont'd)

A firm that does not have an office in this state may perform services and may use the title “Certified Public Accountant”, “CPA”, “CPA firm” or other similar title without a permit issued under this section if:

- It has passed all peer reviews; and
- Services are performed through an individual who has practice privileges and has their principal place of business.

# Code Sec. 20-281g - Prohibition Against Issuing Report Without Valid License or Permit

- A person or a firm which does not hold a valid license is not permitted to issue a report on financial statements or render any attest or compilation services.
- A person or firm who does not hold a Connecticut license or registration or who does not qualify for reciprocal practice privileges is not permitted to use the CPA designation or the terms “accountant”, “auditor” or “accounting.”
- A registered firm may not use a professional or firm name or designation that is misleading.

# Code Sec. 20-281n – Reciprocal Practice Privilege

- An individual whose principal place of business is not in this state may qualify for a practice privilege.
- Must hold a valid CPA license from any state where the qualifications are substantially equivalent.
- No notice, fee or other submission shall be required of any such individual.
- However, any individual or firm who performs assurance, audit, attest or compilation work must obtain a Connecticut permit.
- Any individual or firm that violates these provisions will be subject to disciplinary action by the Board.

# Due Care



# Code Sec. 20-281d - Continuing Education Requirements

- Licensees are required to report a minimum of 40 hours of continuing professional education during the one-year renewal period.

# Code Sec. 20-281 - Permit to Practice; Quality Review

- A firm is not permitted to practice public accountancy in Connecticut unless it has obtained a permit to practice, or is exempt from the permit requirement.
- Firms performing audit, assurance, compilations or attest work must undergo a quality review that indicates the degree of compliance with GAAP, GAAS and other similarly recognized authoritative technical standards.
- This review will be required every three years.



# Example: The Renegade External Auditor

Morgan, Connecticut CPA working as a sole practitioner, offered assurance, audit and compilation services to the general public. She failed to register her firm with the Board, and did not indicate on her license renewal that she was performing audits and therefore was not enrolled in the Peer Review process. When the Board found out about the audit work Morgan had performed for a client, she was sent a letter asking her to explain herself. Morgan ignored the notice and instead went on an extended six-week sabbatical to Grand Cayman.

Morgan has violated Code Sec. 20-281e since she performed audits without a registered firm. For failing to enroll or participate in Peer Review, Morgan ran afoul of Code Sec. 20-281.

# Case Study

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# Collin Street Bakery

# Independence, Integrity and Objectivity



# Code Sec. 20-2811 - Contingent fees and referrals

- A licensee is prohibited from paying a fee or commission to obtain a client or accepting a fee or commission for referring a client to the products or services of a third party.
- If a licensee is performing audit, assurance, compilation or attest work, he or she is prohibited from accepting a commission from a client.
- If the licensee is not prohibited from accepting or paying a fee or commission, the licensee must disclose this to the client.
- “Fee” includes, but is not limited to, a commission, rebate, preference, discount or any other consideration.

# Code Sec. 20-281m - Contingent fees

A licensee is not permitted to perform for a contingent fee any of the following professional services:

- An audit or review of a financial statement;
- A compilation of a financial statement; or
- An examination of prospective financial information; or
- Prepare an original or amended tax return or claim for a tax refund.

# Confidentiality & Client Records

# Code Sec. 20-281j - Confidentiality of Client Information

A licensee may not voluntarily disclose information communicated to him or her by the client in connection to an engagement. This information will be treated as confidential. Exceptions to this rule include:

- Reporting on the examination of financial statements;
- Disclosures in court proceedings;
- Disclosures as part of investigations or proceedings
- As part of the peer review process.

# Code Sec. 20-281k - Client Records and Working Papers

- All statements, records, schedules, working papers and memoranda made by a licensee will remain his or her property, or property of the firm unless:
  - The records constitute a report submitted by the licensee to the client; or
  - These items are original client records.



# Code Sec. 20-281k – Transfer of Client Records and Working Papers

- These records may not be sold or transferred without client consent, unless the transfer is to surviving partners or part of the new merged or successor entity.
- Nothing in this section shall be construed as prohibiting any temporary transfer of workpapers or other material necessary in the course of carrying out quality reviews.

# Code Sec. 20-281k - Return of Original Records

- A licensee must return a client's original records upon request and with reasonable notice.
- The licensee may make and retain copies of such documents of the client when such documents form the basis for work done by him.
- A licensee shall provide such other records to a client or former client as the board may provide by regulation.

# Impact of Code Violations

# Code Sec. 20-281a - Revocation or suspension of certificate, license, practice privilege or permit

The Board may revoke or suspend any certificate, license or permit or the practice privilege of an individual or firm for any one or more of the following reasons:

- Fraud or deceit in obtaining a certificate, registration, license, practice privilege or permit;
- Cancellation, revocation, suspension or refusal to renew authority to engage in the practice of public accountancy by any other state for any cause;
- Failure by the licensee to comply with license requirements;
- Revocation or suspension by any state or federal agency or the PCAOB

# Code Sec. 20-281a - Revocation or suspension of certificate, license, practice privilege or permit (cont'd)

- Dishonesty, fraud or negligence in the practice of public accountancy or in the filing or failure to file his own income tax returns;
- Violation of any rule of professional conduct;
- Conviction of a felony, or of any crime an element of which is dishonesty or fraud, under the laws of the United States, of this state, or of any other state;
- Performance of any fraudulent act; and
- Any conduct reflecting adversely upon the licensee's fitness to engage in the practice of public accountancy.

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# Questions?

Thank You!

Contact us!

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