4-23 **(OBJECTIVE 4-5)** Marie Janes encounters the following situations in doing the audit of a large auto dealership. Janes is not a partner.

1. The sales manager tells her that there is a sale (at a substantial discount) on new cars that is limited to long-established customers of the dealership. Because her firm has been doing the audit for several years, the sales manager has decided that Janes should also be eligible for the discount.
2. The auto dealership has an executive lunchroom that is available free to employees above a certain level. The controller informs Janes that she can also eat there any time.
3. Janes is invited to and attends the company's annual holiday party. When presents are handed out, she is surprised to find her name included. The present has a value of approximately $200.

Required Use the three-step process in the AICPA conceptual framework to assess whether Janes' independence has been impaired.

a. Describe how each of the situations might threaten Janes' independence from the auto dealership.
b. Identify a safeguard that Janes' firm could impose that would eliminate or mitigate the threat of each situation to Janes' independence.
c. Assuming no safeguards are in place and Janes accepts the offer or gift in each situation, discuss whether she has violated the rules of conduct.
d. Discuss what Janes should do in each situation.

4-23 The *Code of Professional Conduct* and interpretations are not clear as to what constitutes a violation in these three situations. A central point is that Marie Janes must maintain independence of mind and in appearance because she is not an employee of the company and must not give the impression that she is one. The table on the following page applies the three-step process to evaluate whether independence is impaired.

4-23 (continued)

(a) POTENTIAL THREATS TO INDEPENDENCE	(b) POSSIBLE SAFEGUARDS?	(c) RULES OF CONDUCT VIOLATED?	(d) APPROPRIATE ACTION?
1. The ability to purchase a car at a substantial discount due to Marie's long-standing audit service may cause Marie to be favorably disposed to the client when evaluating the client's financial statements. Also, if users of the financial statements heard of this arrangement, some might perceive that there is a lack of independence.	1. Marie Janes' firm could establish policies regarding services provided by attest clients that require the managing partner's approval prior to engaging in any transactions with the client. Some transactions could be explicitly prohibited by the policy, while others may require the managing partner's approval.	1. Marie Janes has likely not violated the rules; the discount is available to customers on a widespread basis. Presumably many of the employees of the CPA firm buy automobiles from the dealership.	1. Marie Janes should discuss the discount with the firm's managing partner if she intends or wants to buy the automobile. She should certainly not feel compelled to buy the automobile, but she should not automatically turn it down. The situation would be entirely different if the sale were limited to employees. In such a case it would likely be a violation.
2. The ability to eat meals on an ongoing basis may cause Marie to be favorably disposed to the client when evaluating the client's financial statements. Also, if users of the financial statements heard of this arrangement, some might perceive that there is a lack of independence.	2. Marie Janes' firm could establish a policy regarding free services or gifts provided by clients. Perhaps the firm policy could establish a minimal dollar threshold of allowable free services or gifts. Those exceeding the threshold may either be prohibited by the policy or may require approvals by a more senior member of management of the audit firm.	2. If Marie Janes were to eat there on an ongoing basis, that would likely be a violation of the rules of conduct. It would not likely be a violation if she occasionally eats with employees who she is dealing with at the audit.	2. Marie Janes should eat elsewhere if it is practical to do so, but if the only practical place for her to eat is the lunchroom, she should make arrangements with her firm to make certain that the company is reimbursed for the expenses.
3. Gifts from clients might be perceived as a subtle form of bribe, and thus may create a lack of appearance of independence. Gifts may also cause Marie to be favorably disposed to the client when evaluating the client's financial statements. Also, if users of the financial statements heard of this arrangement, some might perceive that there is a lack of independence.	3. Marie Janes' firm could establish a policy regarding free services or gifts provided by clients. Perhaps the firm policy could establish a minimal dollar threshold of allowable free services or gifts. Those exceeding the threshold may either be prohibited by the policy or may require approvals by a more senior member of management of the audit firm.	3. Accepting such a gift is likely to be a violation of the rules of conduct. That gift is reasonably large, and would be considered by many employees as equivalent to a bonus.	3. Ideally Janes should not accept the gift and state that since she is not an employee, she would prefer not to take it. If she believes that it would be embarrassing to the company, she should graciously accept it and return it with an explanation of her reasons as soon as practical.