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# AICPA Professional Standards: Statements of management advisory services as of July 1, 1976

American Institute of Certified Public Accountants. Management Advisory Services Executive Committee

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**AICPA** PROFESSIONAL  
STANDARDS

VOLUME 1

**AUDITING**  
**MANAGEMENT ADVISORY**  
**SERVICES**  
**TAX PRACTICE**

AS OF JULY 1, 1976



**COMMERCE CLEARING HOUSE, INC.**

PUBLISHERS of TOPICAL LAW REPORTS

4025 W. PETERSON AVE., CHICAGO, ILLINOIS 60646



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## MS Section 101

# Management Advisory Services Practice Standards

Issue date, unless  
otherwise indicated:  
January, 1975

### Introduction

.01 CPAs have historically been business consultants to their clients. The Council of the American Institute of Certified Public Accountants specifically encourages all CPAs to perform “the entire range of management services consistent with their professional competence, ethical standards and responsibility.”<sup>1</sup>

.02 The Institute recognizes a need for a separate set of standards specifically applicable to the practice of management advisory services. Management advisory services are described as follows:

The function of providing professional advisory (consulting) services, the primary purpose of which is to improve the client’s use of its capabilities and resources to achieve the objectives of the organization. . . . In providing this advisory service, the independent accounting firm applies an analytical approach and process which typically involve—

- Ascertaining the pertinent facts and circumstances,
- Seeking and identifying objectives,
- Defining the problem or opportunity for improvement,
- Evaluating and determining possible solutions, and
- Presenting findings and recommendations,

and, following the client’s decision to proceed . . .

- Planning and scheduling actions to achieve the desired results, and
- Advising and providing technical assistance in implementing . . . to produce solutions. . . .<sup>2</sup>

.03 These Standards apply only to management advisory services engagements as described above. They are not intended to apply to “informal advice,” which has been described as follows:

During the course of providing any type of service, independent accounting firms are called upon to give informal advice on

<sup>1</sup> Proceedings, Council Meeting, April 17-20, 1961, pp. 157-165. [See MS section 410.03.]

<sup>2</sup> MS section 410.04.

many diverse questions. . . . This type of service differs from the structured approach to management advisory services . . . in that the nature of such services is informal and therefore no presumption should exist that an extensive study has been performed to identify and consider pertinent facts and alternatives. Further, no responsibility is assumed for seeking to achieve client action or for seeking to assure that any ensuing action will be effective. Here, the appropriate role is simply to respond as practicable at the moment and to express the basis for the response so that such informal advice is offered and accepted for what it is.<sup>3</sup>

.04 The Code of Professional Ethics (Rule 101) [ET section 101.] precludes a member or his firm from expressing an opinion on the financial statements of an enterprise which he or his firm serves in any capacity equivalent to that of a member of management or of an employee. In rendering management advisory services to audit clients, members must take this into account.

.05 The definitions set forth in the March 1, 1973, Code of Professional Ethics<sup>4</sup> are applicable throughout these standards. The term "practitioner" as used herein pertains to all those, whether CPAs or not, who perform management advisory services in CPA firms.

#### **List of Management Advisory Services Practice Standards**

- .06
1. *Personal Characteristics.* In performing management advisory services, a practitioner must act with integrity and objectivity and be independent in mental attitude.
  2. *Competence.* Engagements are to be performed by practitioners having competence in the analytical approach and process, and in the technical subject matter under consideration.
  3. *Due Care.* Due professional care is to be exercised in the performance of a management advisory services engagement.
  4. *Client Benefit.* Before accepting an engagement, a practitioner is to notify the client of any reservations he has regarding anticipated benefits.
  5. *Understanding with Client.* Before undertaking an engagement, a practitioner is to inform his client of all significant matters related to the engagement.
  6. *Planning, Supervision, and Control.* Engagements are to be adequately planned, supervised, and controlled.

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<sup>3</sup> MS section 430.24.

<sup>4</sup> See ET section 91, Volume 2, *AICPA Professional Standards*.

7. *Sufficient Relevant Data.* Sufficient relevant data is to be obtained, documented, and evaluated in developing conclusions and recommendations.
  8. *Communication of Results.* All significant matters relating to the results of the engagement are to be communicated to the client.
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**MS Section 110*****Personal Characteristics***

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 1—In performing management advisory services, a practitioner must act with integrity and objectivity and be independent in mental attitude.**

.01 The CPA, while performing management advisory services, practices in a unique professional environment, evolving from his traditional role in the attestation to the fairness of financial statements. His professional stature, and the reliance of his clients upon that stature, depend to a large extent upon his integrity and objectivity, and on his ability to be independent in mental attitude on all matters relating to client service.

.02 Integrity is a highly personal characteristic which ensures that the practitioner's statements of findings and recommendations are free of intentional distortions or misstatements. Objectivity is the ability to avoid bias and to maintain an impartial attitude on all matters under review.

.03 A practitioner may undertake only those engagements in which he can maintain an independent mental attitude. This requirement is based on the practitioner's obligation to the client and on the need to avoid impairment of public confidence in the profession.

.04 The role which a practitioner assumes in a management advisory services engagement is fundamental to his maintaining integrity, objectivity, and an independent mental attitude. In all aspects of the practitioner's performance of management advisory services, he must avoid assuming the role of management, limiting his services to those of an objective researcher, analyst, or advisor, rather than a decision maker.

.05 In developing recommendations for a client, the practitioner should study the problem involved, gather the information needed, consider alternative solutions to achieving the client's objective, and present his professional judgment. Any management decision made as a result of such activities must be made by the client.

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➤→ *The next page is 2231.* ←➤



**MS Section 120****Competence**

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 2—Engagements are to be performed by practitioners having competence in the analytical approach and process, and in the technical subject matter under consideration.**

.01 In each technical area in which a practitioner performs management advisory services, the services performed are to be of a professional quality. Competence in professional work involves (a) the technical qualifications of the practitioners and (b) the ability to supervise the personnel assigned, to evaluate the quality of work performed, and to accept responsibility to the client for successful completion of the engagement.

.02 Competence in performing management advisory services is the ability to identify and define client needs, to utilize the analytical approach and process, to apply knowledge of the technical subject matter under consideration, to communicate recommendations effectively, and to assist in implementing the recommendations.

.03 The evaluation of competence in management advisory services is sometimes subjective. With respect to a specific engagement, this evaluation can require careful assessment of background and ability to determine whether a particular engagement should be undertaken.

.04 Competence is acquired and maintained through a combination of education and experience. Education, beyond that which is initially required for admission to the profession, includes formal and informal instruction and self-study. Experience relates to the knowledge and judgment acquired by personal participation in management advisory services engagements and other business affairs. Competence may be augmented by research and by consultation with others.

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➤ ➤ ➤ *The next page is 2241.* ← ← ←

**MS Section 130*****Due Care***

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 3—Due professional care is to be exercised in the performance of a management advisory services engagement.**

.01 The concept of due care is concerned with what the practitioner does and how well he does it. It involves diligence and appropriate attention in carrying out the assignment. It does not imply infallibility. It does require systematic critical review by the practitioner, throughout the engagement, of work accomplished and judgments exercised.

.02 Due professional care requires that all work be done within the provisions of the Code of Professional Ethics and other professional standards of the AICPA.

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**MS Section 140*****Client Benefit***

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 4—Before accepting an engagement, a practitioner is to notify the client of any reservations he has regarding anticipated benefits.**

.01 Problem definition, identification of objectives, and benefits to be derived should be considered in structuring the engagement. While in some cases the potential benefits are obvious both to the client and to the practitioner, an assessment of anticipated benefits often requires sufficient exploratory work to establish their reasonableness, and also requires the exercise of judgment. Some benefits can be quantified in financial or statistical terms, but many others are less tangible.

.02 The client's willingness to accept recommendations, and his ability to implement them, should be considered by the practitioner. Unwillingness to accept or inability to implement appropriate recommendations could impair realization of potential benefits.

.03 If during the course of the engagement the relationship between anticipated benefits and costs changes significantly, the client should be informed.

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➤ *The next page is 2261.* ←

**MS Section 150*****Understanding with Client***

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 5—Before undertaking an engagement, a practitioner is to inform his client of all significant matters related to the engagement.**

.01 The significant matters related to an engagement generally include (a) the engagement's objectives, (b) its scope, (c) the approach, (d) the role of all personnel, (e) the manner in which results are to be communicated, (f) the timetable, and (g) the fee.

.02 A preliminary discussion or investigation is generally necessary to develop sufficient information for formulating engagement objectives and identifying scope. The engagement objectives reflect the results expected to be derived. There should be a clear expression by the practitioner as to both the engagement objectives and the extent and nature of the practitioner's involvement.

.03 Engagement scope should be broad enough to encompass matters likely to be significant in developing appropriate recommendations and producing desired results. Particular attention should be given to informing the client of possible consequences of significant constraints.

.04 The respective roles and responsibilities of the practitioner and the client should be defined. Where a third party is involved, it is especially important to establish which party—the practitioner or the client—assumes responsibility for third-party performance.

.05 Definition of major tasks to be performed, the methods to be used in reporting engagement status and achievements, and the timing of such reporting should be established. There should be a clear statement as to what will constitute completion of the engagement and as to the content of the end product.

.06 There should be an expression of when work will commence, the estimated completion date, and the fee and expense arrangements.

.07 These matters should be recorded in writing, particularly for engagements of significant duration or complexity. This can be done in a formal contract, in a letter of understanding, or in a file memorandum summarizing the terms of an oral agreement with the client. Should a significant aspect of the engagement change as work progresses, there should be a new arrangement with the client and a written record thereof.

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➤→ *The next page is 2271.* ←➤

**MS Section 160*****Planning, Supervision, and Control***

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 6—Engagements are to be adequately planned,  
supervised, and controlled.**

.01 Planning, supervision, and control are based directly on the practitioner's understanding with the client as to the engagement and as to the role of all personnel concerned.

***Planning***

.02 Planning is the translation of engagement objectives into a structured set of activities and events within a targeted time schedule. The resultant engagement plan is to be used in supervising and controlling the engagement.

.03 The practitioner is usually responsible for engagement planning. The greater the problem complexity and the larger the number of persons involved, the more formal and detailed the engagement plan should normally be. Both the practitioner and the client should recognize the provisional nature of any plan and the need for monitoring and possible revision throughout the engagement.

***Supervision***

.04 Engagements must be performed and supervised by competent personnel. The practitioner in charge must exercise judgment as to the appropriate amount of supervision, based on the experience of the persons involved and the complexity of the assignment.

***Control***

.05 Effective control requires measurement of progress in meeting the engagement plan and objectives. Adequate documentation should be maintained to permit measurement and assessment of progress at significant engagement points. Evaluation of progress should be made in terms of accomplishments, time schedule, and quality of work.

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**MS Section 170*****Sufficient Relevant Data***

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 7—Sufficient relevant data is to be obtained, documented, and evaluated in developing conclusions and recommendations.**

.01 A practitioner must exercise his professional judgment in determining the type and amount of data required. Such determinations take into consideration the nature and scope of the engagement and related circumstances. The source and reliability of the data, and any limitations with respect thereto, must be considered in formulating conclusions.

.02 The amount and formality of documentation will vary according to the nature and scope of the engagement. The documentation should demonstrate that due care has been exercised. It should record, as appropriate, (a) the evidential matter obtained and its source, (b) the alternatives considered, and (c) the analytical process leading to specific recommendations.

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**MS Section 180*****Communication of Results***

Issue date, unless  
otherwise indicated:  
January, 1975

**Standard No. 8—All significant matters relating to the results of the engagement are to be communicated to the client.**

.01 The principal findings, recommendations, and accomplishments, and the major assumptions relied upon, should be conveyed to the client, together with any limitations, reservations, or other qualifications.

.02 Reports to a client may be written or oral. When a practitioner does not issue a written report to the client, he should prepare a file memorandum documenting the significant recommendations and other pertinent information discussed with the client.

***Interim Communications***

.03 Interim communications are desirable. Interim communication encourages the involvement of management, helps preserve management's role as decision-maker, and keeps management informed of progress towards the final conclusions, recommendations, and accomplishments.

.04 Interim communications should normally summarize (a) findings to date, (b) work accomplished in relation to plan, and (c) when appropriate, tentative recommendations. They are also used to review problems encountered, to obtain management decisions, and to reassess priorities.

***Final Report***

.05 A final report should be made to the client upon completion of an engagement to ensure that results and recommendations are communicated. Reports should be responsive to the objectives and scope of the engagement. The nature of work performed and the extent of interim communications will influence the degree of detail of the final report.

.06 Reports should describe the significant alternatives considered by the practitioner and the rationale supporting any recommendations. Related significant facts and assumptions, and their source and bases, should be disclosed.

➤➤➤→ *The next page is 2451.* ←➤➤➤

**MS Section 410*****Tentative Description of the Nature  
of Management Advisory Services  
by Independent Accounting Firms<sup>1</sup>***

Issue date, unless  
otherwise indicated:  
February, 1969

**Introduction**

.01 An independent accounting firm's purpose in engaging in management advisory services is to utilize the essential qualifications it has available to provide advice and technical assistance which will enable client management to conduct its affairs more effectively. These essential qualifications are based in part on attributes acquired in conducting other aspects of practice and include technical competence; familiarity with the client's finance and control systems and his business problems; analytical ability and experience in problem solution; professional independence, objectivity and integrity. Although not always identified as "management advisory services," independent accounting firms have rendered advice and assistance to clients outside the accounting, auditing and tax areas for as long as the accounting profession has existed.

The role of an independent accounting firm in performing management advisory services is to provide advice and technical assistance, and should provide for client participation in the analytical approach and process. Specifying this as the proper role recognizes both the appropriate place of management advisory services and the realities of practice. This is the only basis on which the work should be done and it is the only basis on which responsible management should permit it to be done.

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<sup>1</sup> Originally issued by the Committee on Management Services as *Statement on Management Advisory Services No. 1*.



When the services to a client also include expression of an opinion on the fairness of financial statements, the matter of role has special significance, since it also relates to the independence of the accounting firm. The accounting firm's role is to provide advice and technical assistance and to avoid making management decisions or taking positions that might impair the firm's objectivity.

.02 In recent years, management advisory services have been in an accelerating process of evolution, with the profession's participation growing in response to requests from clients for assistance. In many instances, management needs and problems are more complex and the techniques involved in their solution more sophisticated than ever before. The profession's response to the demand for advice has been to develop a broader range of services.

.03 The American Institute of Certified Public Accountants set forth the Institute's basic policy regarding management advisory services in the following resolution adopted by Council in April, 1961:

It is an objective of the Institute recognizing that management services activities are a proper function of CPAs, to encourage all CPAs to perform the entire range of management services consistent with their professional competence, ethical standards, and responsibility.

The Committee on Management Services believes that an interpretation of the phrase "the entire range of management services consistent with their professional competence, ethical standards, and responsibility," will contribute to the orderly implementation of this policy throughout the profession.

Subsequently, Council, in October 1966, adopted "A Description of the Professional Practice of Certified Public Accountants." Within the framework of this description, the committee believes that a further description of that portion of the practice generally referred to as management advisory service is desirable. Such an interpretation and further description will, among other things, serve to—

- a. Guide independent accounting firms in selecting and practicing in areas of service in which they can and wish to

- render advice and technical assistance to clients beyond those relating to auditing, financial accounting, and taxes;
- b. Assist those responsible for developing and conducting educational programs for CPAs; and
  - c. Provide a basis for the general business community to become better informed regarding the nature of management advisory services as performed by independent accounting firms.

### **Description of Management Advisory Services**

.04 Management advisory services by independent accounting firms can be described as the function of providing professional advisory (consulting) services, the primary purpose of which is to improve the client's use of its capabilities and resources to achieve the objectives of the organization. This can relate to areas such as—

- The management functions of analysis, planning, organizing, and controlling,
- The introduction of new ideas, concepts, and methods to management,
- The improvement of policies, procedures, systems, methods, and organizational relationships,
- The application and use of managerial accounting, control systems, data processing, and mathematical techniques and methods, and
- The conduct of special studies, preparation of recommendations, development of plans and programs, and provision of advice and technical assistance in their implementation.

In providing this advisory service, the independent accounting firm applies an analytical approach and process which typically involve—

- Ascertaining the pertinent facts and circumstances,
- Seeking and identifying objectives,
- Defining the problem or opportunity for improvement,
- Evaluating and determining possible solutions, and
- Presenting findings and recommendations,

and, following the client's decision to proceed, the independent accounting firm may also be involved in—

- Planning and scheduling actions to achieve the desired results, and
- Advising and providing technical assistance in implementing,

in combination with knowledge and experience in such areas as—

- Organization and management methods,
- Office and management functions,
- Systems and procedures,
- Data processing methods,
- Quantitative methods (mathematics, statistics, etc.), and
- Financial management,

to produce solutions such as—

- A management information system,
- A sales reporting system,
- A cost accounting system,
- A work measurement program,
- Improved production control,
- An organization plan with statements of duties and responsibilities, or
- An electronic data processing system.

.05 The above represents a conceptual description of management advisory services rather than a definition in terms of area of application of the services. The committee believes that the adoption of an itemized "list of acceptable areas of service" would be useful; however, no generally accepted classification of subject matter currently exists for this purpose. Also, the validity and acceptability of such a list would have to be dependent on there being clearly discernible criteria for differentiating among the range of possible subject matter, and no such precise bases have yet been found.

There are several further reasons why the development of such a list appears to be unattainable. In the first place, many of the subject areas themselves do not have definitions which are precise and exclusive enough to be usable or acceptable in preparing the list. Second, the decisions regarding many of the subject areas, as being an "acceptable area of service," could depend on

considerations of the underlying subareas with which the independent accounting firm is concerned (e.g., research per se vs. a system for the planning and control of manpower participating in research). Third, the circumstances under which services are to be rendered in a particular subject area (a large vs. small client; a simple vs. complex problem) and the role of the independent accounting firm (as a fact-gatherer vs. a recommender vs. a technical implementor) would also be pertinent in the determination of the list.

### **Determining A Scope of Service**

.06 The committee believes that an independent accounting firm in reaching a decision as to the scope of its management advisory services should be guided by certain significant criteria established by the profession, such as competence and independence. Certain criteria will apply primarily to the profession as a whole, while others will be more relevant to the particular independent accounting firm or engagement.

.07 The CPA's ability to learn and successfully apply the basic analytical approach and process is well recognized. The more difficult questions which must be answered by an independent accounting firm in determining a scope of management advisory services, however, relate to the depth of knowledge and experience required in the various subject areas and kinds of problems and solutions with which the firm might become involved. Since it is not possible to specify all the subject areas and types of problems with which independent accounting firms may be called upon to deal, the committee suggests the following guidelines which should be useful in selecting a scope of services.

### **General Guidelines**

.08 *Responsibility to Establish Scope of Services*—Each independent accounting firm has the responsibility to determine the scope of services it is competent to offer to the public, subject to the pronouncements of the profession. Each independent accounting firm should make its own decisions in accordance with the type of practice which it desires to conduct. It is anticipated that many firms will not choose to render management advisory services in all subject areas.

**.09 Independence**—When providing management advisory services, the independent accounting firm must, as in all areas of practice, give particular consideration to independence as set forth in the Code of Professional Ethics particularly in Rule 101. This rule states in part:

A member or a firm of which he is a partner or shareholder shall not express an opinion on financial statements of an enterprise unless he and his firm are independent with respect to such enterprise.

A commentary entitled *Concepts of Professional Ethics*, which was promulgated by the Division of Professional Ethics, elaborates:

Independence has traditionally been defined by the profession as the ability to act with integrity and objectivity. . . .

When a CPA expresses an opinion on financial statements, not only the fact but also the appearance of integrity and objectivity is of particular importance. For this reason, the profession has adopted rules to prohibit the expression of such an opinion when relationships exist which might pose such a threat to integrity and objectivity as to exceed the strength of countervailing forces and restraints. These relationships fall into two general categories: (1) certain financial relationships with clients and (2) relationships in which a CPA is virtually part of management or an employee under management's control.

Although the appearance of independence is not required in the case of management advisory services and tax practice, a CPA is encouraged to avoid the proscribed relationships with clients regardless of the type of services being rendered. In any event, the CPA, in all types of engagements, should refuse to subordinate his professional judgment to others and should express his conclusions honestly and objectively.

[As amended, effective March 1, 1973 by adoption of the revised Code of Professional Ethics. (See Volume 2, AICPA PROFESSIONAL STANDARDS.)]

**.10 Competence**—The scope of management advisory services of an independent accounting firm also depends on another fundamental and obvious matter—competence. Independent accounting firms have the responsibility to evaluate their ability to render management advisory services of a professional quality in each specific area. They also have the responsibility to refrain from representing themselves as qualified and willing to accept work in areas where they do

not possess the required competence. Competence in professional work involves both the technical qualifications of staff personnel and the firm's ability to supervise and evaluate the quality of the work performed. Competence embraces both the analytical approach and process and the subject matter of the area involved.

The degree of competence required will naturally vary according to the degree of difficulty of the engagement and the importance of the recommendations for which the independent accounting firm will assume responsibility. It will also vary according to the role assumed by the firm—i.e., as an advisor, fact-gatherer or technical implementor.

The independent accounting firm will not always begin an engagement with a full and detailed knowledge of the characteristics of the business or of all of the techniques available for the solution of the problem, for no two situations faced by a firm are ever exactly the same, nor are the technical procedures required to achieve the desired result identical. The firm is expected to adapt its procedures and knowledge to the circumstances of the particular case and to research unfamiliar subject matter involved in the solution of the problem. In those instances in which the acquisition of the necessary knowledge is not a natural part of the conduct of the engagement as a result of the fact-gathering procedure or of the normal research process, the independent accounting firm should question its competence to carry out the engagement.

This matter is considered more fully in MS Section 420, *Competence in Management Advisory Services*.

**.11 Other Considerations**—The scope of management advisory services is such that no one person can be expected to develop sufficient specialized knowledge and skill in all areas in which clients might require assistance. A wide range of management advisory services can normally be performed only by a firm which includes both generalists and individuals who have acquired specialized qualifications in the subject matters or techniques involved. Accordingly, the requirements for specialization in certain areas may limit the scope of management advisory services offered by any given independent accounting firm. As a result, many independent

accounting firms will decide on a scope of practice which does not include areas of service offered by others in the profession.

The scope of services offered by the independent accounting firm also should be adequate to identify and resolve the clients' basic problems and not just problem symptoms. If the scope is excessively narrow, there is a danger that the problem may be defined and solutions developed from too narrow a point of view to be really useful to the client.

.12 *Referrals*—Referral of management advisory services work to other independent accounting firms is an alternative course of action to that of developing individual or firm capability. Recognizing the depth and breadth of skills required to deal effectively with the clients' basic problems and the economic limits of practice, the independent accounting firm's sense of responsibility to its clients may in some or all instances lead it to refer the management advisory services requirements of its clients to others. The referral arrangement may provide for a joint effort or provide for the services to be performed solely by the referee brought in for that purpose. In any event, to the extent that the independent accounting firm finds an effective way to cooperate with others, it may thereby expand its own knowledge and extend its own scope of service toward providing the full range of management advisory services.

.13 *The Code of Professional Ethics*—The applicability of the Code of Professional Ethics to management advisory services is clearly stated in the introductory section of the Rules of Conduct as follows: "The Rules of Conduct . . . apply to all services performed in the practice of public accounting including tax and management advisory services except (a) where the wording of the rule indicates otherwise and (b) that a member who is practicing outside the United States will not be subject to discipline [except under certain specified conditions]." It is, therefore, the responsibility of the independent accounting firm to assure itself that the nature and scope of the management advisory services it elects to offer are in conformity with this requirement. [As amended, effective March 1, 1973 by adoption of the revised Code of Professional Ethics. (See Volume 2, AICPA PROFESSIONAL STANDARDS.)]

**Conclusion**

.14 The American Institute of Certified Public Accountants, recognizing the needs of the business public and the long record of substantial and varied accomplishments by independent accounting firms in rendering management advisory services, has encouraged and continues to encourage firms to develop capabilities in this field.

The appropriate range of services for the profession and the accounting firm should depend on considerations of—

- Responsibility of the independent accounting firm to establish its scope of services,
- Independence,
- Competence,
- Requirements for specialization,
- Attention to the client's basic problems,
- Referral arrangements, and
- The Code of Professional Ethics.

This statement has described the nature of management advisory services by independent accounting firms and is intended to provide guidelines for determining a scope of service and to serve as a basis for future statements in this area of practice.

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➤ *The next page is 2501.* ←



**MS Section 420****Competence in Management  
Advisory Services<sup>1</sup>**

Issue date, unless  
otherwise indicated:  
February, 1969

.01 MS Section 410.10 states in part:

... Independent accounting firms have the responsibility to evaluate their ability to render management advisory services of a professional quality in each specific area. They also have the responsibility to refrain from representing themselves [to clients] as qualified and willing to accept work in areas where they do not possess the required competence. Competence in professional work involves both the firm's technical qualifications of staff personnel and the ability to supervise and evaluate the quality of the work performed. . . .

The committee considers it desirable to amplify the application of this statement and to provide guidance to the CPA whereby, in the exercise of his judgment, he may consider whether he is competent.

**The Nature of Competence**

.02 MS Section 410 tentatively describes the nature of management advisory services as involving the application of an analytical approach and process, in conjunction with knowledge and experience in specific subject areas, to the solution of management problems. Competence in management advisory services refers to knowledge, experience, skill, and research capability in applying judgment and finding and implementing solutions via this analytical approach and process.

.03 In performing management advisory services, it is expected that the independent accounting firm will bring to a client situation a professional-level ability to find facts and

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<sup>1</sup> Originally issued by the Committee on Management Services as *Statement on Management Advisory Services No. 2*.

define problems, to structure problems so attention is focused on fundamentals rather than symptoms and fringe issues, to communicate and persuade people to accept the definitions and be disposed to take action, to find and sift alternative solutions, to know sources of technical information, to consider what others have tried and what worked and did not work and why, to adapt general or theoretical solutions to fit particular situations in a practical way, and to be objective.

While some attributes involved in performing management advisory services relate to factual matters and are subject to objective evaluation, other essential elements relate to judgmental, psychological, and personality factors susceptible only to subjective evaluation.

### **Acquisition of Competence**

.04 Considerable variety is found in the educational and experience backgrounds of both CPAs and others recognized as proficient in management advisory services. There are those with academic degrees in accounting, general management, marketing, engineering, and other fields. Some have industry experience while others may have worked for consulting firms, and still others may have had all their prior experience with independent accounting firms. The common characteristic is that, generally, all have met the fundamental intellectual standards in some academic field and have built their proficiency from that base. This proficiency has been built by actual performance under more experienced supervision or by undertaking simple problems before those that are more complex; by reading and self-study; by attending courses offered by colleges and universities or by trade and professional associations; and by researching for solutions to actual problems during the course of an engagement.

A range of capability can thus be built upon a base of academic achievement. The academic training and examination requirement for the CPA certificate provides such a base. In fact, the pervading nature of financial accounting provides as broad and adequate a base as any other area in which initial qualifications could be attained.

.05 In establishing a range of capability in management advisory services, an independent accounting firm is likely to

commence with a base of accounting-related matters. This then, may lead a member into cost controls, budgeting, inventory controls, and other areas of management concern. However, as a member approaches such areas, more special training and experience become necessary.

.06 Competence in management advisory services relates to both proficiency in applying the analytical approach and process, and to knowledge of the subject matter and techniques concerned. These are acquired by education and audit or other experience, and by the actual performance of management advisory services.

In addition, consulting attributes of problem definition, motivation, communication, and the like, which relate to psychological and personality factors are also important. A specific approach that works well for one may not work equally well for another. Management advisory services involve a large element of personal relations, and in time, the practitioner develops a pattern of approach that works best for him.

The specifics of a particular industry or functional area of an organization, as well as applicable operating techniques, are often found in professional or other literature. The practitioner is, therefore, often in a position to generally prepare for a specific assignment in advance and to research for possible solutions as the nature of a problem unfolds. In those instances in which the acquisition of the necessary knowledge is not a natural part of the conduct of the engagement as a result of the fact-gathering procedure or of the normal research process, the CPA should question his competence to carry out the engagement.

### **Areas and Extent of Participation**

.07 The CPA's decision regarding his competence in a given instance will depend upon his knowledge of the subject matter, as developed through experience, training, and as related to the purposes of the engagement; the degree of knowledge about the subject possessed by the client; and the role to be assumed.

Some management advisory services relate essentially to accounting systems and financial matters that coincide with the same subject matter which is of concern in the audit process. The purpose, however, is different as the CPA is not only concerned

with the propriety of what the client did in the past (attesting) but also with what should be done to improve matters in the future (management advisory services)—but the subject matter is the same.

Other management advisory services may involve planning, control, and information systems for application throughout an organization that relate to other subject matter. This may require some study in areas such as production, inventory, and other nonfinancial functions. However, in performing such services, the member is concerned with the organization, planning, standards of performance, data processing, measuring and recording, and reporting aspects, and he need not undertake to solve the underlying problems of how to produce or market a product.

Still other management advisory services are directed toward the solution of the management aspects of these underlying problems and are even less related to financial accounting. Such matters as decision rules for inventory control, production scheduling, and the like may have financial accounting aspects but such aspects are largely incidental.

Another form of specialization is in techniques, such as computer technology or operations research. The original purpose of developing such specialization may have been to assist clients in the finance and control function. But computers and operations research can be used to solve problems wholly unrelated to this area, and clients may appropriately seek the help of CPAs in solving other problems where these particular competences are required.

The need for the CPA to have specialized training and experience increases the further he elects to go in the technologies involved.

.08 The CPA is further advised to consider not only the subject matter of his service but how far he is prepared to go in the application of the analytical approach and process. He may elect to assist his client in all the steps of analysis or something less than that. In some subject matter, he may find facts or go on to defining the problem and stop at that point or he may refer the client to other sources of assistance. In other subjects, he may develop a program of action and, in

still others, he may offer to advise and provide technical assistance in implementation.

.09 The scope of management advisory services is such that no one person can be expected to develop sufficient specialized knowledge and skill in all areas in which clients might require assistance. A wide range of management advisory services can normally be performed only by a firm which includes both generalists and individuals who have acquired specialized qualifications in the subject matters or techniques involved.

### **Standards of Competence**

.10 The CPA certificate is the accepted minimum evidence of high-level competence in the public accounting profession. The profession is, and has been for many years, identified as experts in management advisory services as well as accounting, auditing and tax matters. Beyond that, in the field of auditing, the profession has further stated certain general standards for the guidance of practitioners in Statement on Auditing Standards AU section 150.02:

1. The examination is to be performed by a person or persons having adequate technical training and proficiency as an auditor.
2. In all matters relating to the assignment an independence in mental attitude is to be maintained by the auditor or auditors.
3. Due professional care is to be exercised in the performance of the examination and the preparation of the report.

In addition, AU section 110.04 states that, "In the observance of generally accepted auditing standards, the independent auditor must exercise his judgment in determining which auditing procedures are necessary in the circumstances to afford a reasonable basis for his opinion. His judgment is required to be the informed judgment of a qualified professional person."

The explanatory sections related to these auditing standards refer to the acquisition of proficiency through a combination of education and experience. Professional experience requires working under the supervision of a more experienced superior and such superior, exercising authority upon an en-

gement, is expected to exercise his judgment regarding the degree of supervision appropriate.

.11 The Committee on Management Services believes that general standards analogous to those adopted for auditing are applicable to management advisory services.

1. Management advisory services are to be performed by persons having adequate training and experience in both the application of the analytical approach and process, and in the subject matter under consideration.

The committee believes that qualification as a CPA is a proper base on which to develop proficiency in management advisory services. Possession of the certificate evidences the presumption that certain basic prerequisites have been met in certain areas of management advisory services; however, it is the responsibility of each member to build his qualifications on that base and assess and establish his competence in any given instance.

The committee recognizes that competence of an independent accounting firm in an area or areas of management advisory services may be strengthened by employing persons possessing specialized training and experience in non-financial fields. The firm, however, should only undertake those professional engagements for which it has the necessary qualification to supervise and evaluate the work of its staff members.

2. In all matters relating to a management advisory services assignment, an independence in mental attitude is to be maintained by the member and his staff.

The committee recognizes the application of the Code of Professional Ethics to management advisory services including the independence rules when the CPA also serves as independent auditor of the client's financial statements. Aside from the matter of also serving as independent auditor, general standard 2 is directed toward a client's right to have a completely objective, unbiased, and forthright point of view brought to the matter being considered in management advisory services.

3. Due professional care is to be exercised in the performance of management advisory services.

The committee believes that a paragraph in Cooley on Torts quoted in AU Section 230.03 is directly applicable here. This quotation reads as follows:

Every man who offers his service to another and is employed assumes the duty to exercise in the employment such skill as he possesses with reasonable care and diligence. In all these employments where peculiar skill is prerequisite, if one offers his service, he is understood as holding himself out to the public as possessing the degree of skill commonly possessed by others in the same employment, and, if his pretensions are unfounded, he commits a species of fraud upon every man who employs him in reliance on his public profession. But no man, whether skilled or unskilled, undertakes that the task he assumes shall be performed successfully, and without fault or error. He undertakes for good faith and integrity, but not for infallibility, and he is liable to his employer for negligence, bad faith, or dishonesty, but not for losses consequent upon pure errors of judgment.

### **Conclusion**

.12 The Committee on Management Services is of the opinion that the CPA should only undertake those engagements where he or his firm meets the competence requirements discussed above.

This is not an unusual decision for a professional man to make. For example, on the matter of competence, the legal profession leaves the decision of competence to the individual member of the profession. Rule Number 31 of the Canons of Professional Ethics of the American Bar Association says in part, "Every lawyer upon his own responsibility must decide what employment he will accept as counsel. . . ."

The evaluation of the competence of a CPA or an independent accounting firm in the area of management advisory services is primarily a subjective one. The matter of competence to perform an engagement requires that each CPA objectively view his background and ability and determine whether, in fairness to his client and/or the public, he is in a position to undertake an engagement.

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➤ *The next page is 2551.* ←

**MS Section 430****Role in Management  
Advisory Services<sup>1</sup>**

Issue date, unless  
otherwise indicated:  
September, 1969

**Introduction**

.01 The purpose of this Statement is to consider the role of the member in the practice of management advisory services. Role is significant not only because of its effect on the success of management advisory services engagements, but because of its bearing on all aspects of the member's relationship with his client.

.02 MS Section 410.01 states in part:

The role of an independent accounting firm in performing management advisory services is to provide advice and technical assistance, and should provide for client participation in the analytical approach and process. Specifying this as the proper role recognizes both the appropriate place of management advisory services and the realities of practice. This is the only basis on which the work should be done and it is the only basis on which responsible management should permit it to be done.

The Committee considers it desirable to amplify the application of this Statement in order to provide guidance to the member whereby, in the exercise of his judgment, he may determine his appropriate role in particular management advisory services engagements.

.03 Role implies posture and actions in a given situation or relationship; in this case, that involving the member as a consultant with client management and personnel. In considering this relationship, therefore, both consultant and client roles must be identified. Pervading all aspects of the consultant's role is his posture as an objective advisor.

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<sup>1</sup> Originally issued by the Committee on Management Services as *Statement on Management Advisory Services No. 3*.



.04 Further, the matter of appropriate role in a professional relationship with a client depends on the nature and objectives of the professional service to be provided. The Committee, therefore, considers it important to first describe the nature and objectives of management advisory services as a basis for defining the role that should be assumed in the various types and phases of management advisory services engagements.

### **Background**

.05 MS Section 410.04 generally describes these services as “. . . the function of providing professional advisory (consulting) services, the primary purpose of which is to improve the client’s use of its capabilities and resources to achieve the objectives of the organization. . . .

.06 “In providing this advisory service the independent accounting firm applies an analytical approach and process which typically involve—

- Ascertaining the pertinent facts and circumstances,
- Seeking and identifying objectives,
- Defining the problem or opportunity for improvement,
- Evaluating and determining possible solutions, and
- Presenting findings and recommendations,

and, following the client’s decision to proceed, the accounting firm may also be involved in—

- Planning and scheduling actions to achieve the desired results, and
- Advising and providing technical assistance in implementing. . . .”

.07 These activities usually involve a written statement of the scope and objective of the engagement, a work program related to the statement of scope and objectives, and the preparation of a written report or other form of documentation to be submitted to the client when the engagement is completed.

.08 The execution of an assignment involving some or all of these phases is likely to result in a formal, structured relationship with the client. Structured management consulting can be described as consisting of one or more of three broad stages of

effort—analysis, design, and implementation. The analysis stage consists of ascertaining the pertinent facts and circumstances, seeking and identifying objectives, and defining the problem or opportunity for improvement. The design stage consists of evaluating and determining possible solutions and presenting findings and recommendations. The implementation stage includes planning and scheduling actions to achieve the desired results, as well as advising and providing technical assistance.

.09 The member may be called upon to provide services in some or all of the foregoing stages. While it is impossible to fit all management services engagements into a few clearly identified categories, it is pertinent to identify the various roles assumed by considering the consultant's role in engagements involving all steps in the analytical approach and process along with some discussion of services in which only a portion of the analytical approach and process is involved. These illustrations are offered as a basis for determination of role in the various situations that may be encountered in practice.

.10 This Statement deals only with management advisory services as defined in paragraphs .05 through .08. Services which members might be called upon to render other than those of an advisory nature as defined in paragraphs .05 through .08 are excluded from the scope of this Statement.

## **Statement**

### *Role in Full-Scope Engagements*

.11 In many management advisory services engagements, particularly where implementation of a solution is dependent on a new or revised system, the first five study phases outlined in paragraph .06 that bring a matter to the point of recommendation for management decision are but the preliminary areas of service, and participation by the member is expected to continue through complete implementation. The objective is to supplement management's capability by providing an objective point of view, a consideration of alternate courses of action, a broader perspective from experience in analogous situations, and technical assistance.

.12 Effective participation by the member in this role requires the appropriate composition of management participants.

Client representation should include both working level and decision level participants who are representative of the functions particularly affected by the matter.

.13 This may be accomplished by organizing a team drawn from each of the functions concerned (plus those client staff technicians who can make a contribution), to work directly on the problem, together with a senior client management group whose responsibility is to make decisions and monitor and approve programs and results. The consultant makes his contribution by advising on the overall program and the organization and composition of the participating groups, providing technical assistance at the working level, and monitoring progress and reporting on this and other important matters to the senior management group. To the latter end, the consultant should maintain a degree of participation during the engagement that permits him to be informed as to what is occurring and that will provide a basis for applying his professional judgment to what he observes.

.14 The further the member's participation extends from initial fact finding through implementation, the greater the importance of client involvement. When implementation is concluded, the member's participation is also concluded, and only client personnel remain to carry on the solution. Therefore, the member should adjust his level of participation throughout all phases of the assignment so that he eventually completes his part of the assignment, leaving a complement of client personnel possessing the qualifications to proceed on their own.

.15 The propriety of this role of advisor is clear if one considers that a consultant is not in a position to carry out his recommendations since he has no authority to marshal client resources or to make management decisions. Should he attempt to do so and allow himself to be placed in such a role, he ceases to be a consultant and exercises management prerogatives—with consequent loss of the essential consulting requisites of impartiality and objectivity.

#### *Role in Special Study Engagements*

.16 In some types of engagements, the client seeks only an impartial and objective study of a matter and the resulting rec-

ommendations. This may be to obtain confirmation or denial of a judgment client management has already tentatively reached or to obtain a marshalling of pertinent facts and views on a matter not previously studied. For example, such studies may relate to areas of management concern embracing a review of facts and conclusions on the selection of EDP equipment or the applicability of inventory control decision rules.

.17 The nature and objectives in such engagements are analogous to audit services in the sense that an impartial, objective judgment is being sought by the client. The role of the member in these engagements is to proceed through the first five steps of the analytical approach and process outlined in paragraph .06, to apply objective judgment to the facts, and to present findings and recommendations to the client for decision and further action. The client's role in this process is primarily to supply pertinent information and subsequently, of course, to make the decision on the matter. In such circumstances, the client does not seek the member's assistance in achieving the desired result but only his professional judgment. The effective action beyond the point of decision is solely the responsibility of the client.

.18 The Committee believes that a sound client-consultant relationship in these situations depends upon the client's disposition to obtain the consultant's impartial and objective point of view and the consultant's disposition to so respond. A relationship based on any other premise serves only for the member to lend his name to a predetermined course of action—hardly an acceptable professional posture for the independent CPA to assume. The member should therefore avoid accepting an engagement in which he is expected merely to carry out the client's dictates.

#### *Implications of Limited Client Participation*

.19 Occasionally, clients seek to engage the independent accounting firm to provide solutions and results on a basis wherein the client expects to be involved only to a limited extent, if at all. The member should carefully consider the implications of such an exclusive role—particularly the degree of responsibility inherent in such an arrangement. Since the member cannot be

responsible for continuing operations, he places himself and his client in a difficult position if he has had the sole responsibility for design and installation of changes with which he subsequently has no further involvement. Only client management is in a position to assume responsibility for all aspects of change (including operations) and, therefore, ultimate success is most likely to be achieved when both consultant and client management recognize this fact and arrange their roles accordingly.

.20 An additional, and often related, problem arises when there is a tendency or disposition to apply a packaged solution indiscriminately. Such approaches can inhibit client participation, underestimate the individuality of each situation, and bypass the analytical process. This increases the likelihood of the development of solutions that do not meet actual needs.

.21 The appropriate response to the above situations is to fully inform the client of the limitations and risks inherent in such an undertaking and to establish a balanced client-consultant relationship that the member believes can lead to a successful result. Failing this, he may find himself acting in a position inconsistent with his objective advisory role and accordingly, may deem it appropriate to withdraw from the engagement.

.22 There are degrees of technical assistance that may be provided depending upon knowledge and experience available in the client organization. The Committee believes, however, that a member should not undertake an engagement that includes implementation unless—

1. The client understands the nature and implications of the recommended course of action.
2. Client management has made a firm decision to proceed with implementation based on this understanding and consideration of alternatives.
3. Client management accepts overall responsibility for implementation of the chosen course of action.
4. Sufficient expertise will be available in the client organization to fully comprehend the significance of the changes being made during implementation.

5. When the changes have been fully implemented, client personnel have the knowledge and ability to adequately maintain and operate such systems as may be involved.

.23 The measure of ultimate contribution by the consultant is the effectiveness with which management acts on a sound recommendation and the degree to which, at the conclusion of the consultant's participation, the client's personnel have acquired the capability to continue at a higher level of effectiveness in the future.

### *Informal Advice*

.24 During the course of providing any type of service, independent accounting firms are called upon to give informal advice on many diverse questions. Clients seek these opinions from the representatives of an independent accounting firm in view of their knowledge of the particular client's affairs and their broad exposure to other situations. This type of service differs from the structured approach to management advisory services, as described in MS Section 410, in that the nature of such services is informal and therefore no presumption should exist that an extensive study has been performed to identify and consider pertinent facts and alternatives. Further, no responsibility is assumed for seeking to achieve client action or for seeking to assure that any ensuing action will be effective. Here, the appropriate role is simply to respond as practicable at the moment and to express the basis for the response so that such informal advice is offered and accepted for what it is.

.25 The Committee believes, however, that while there may not be any presumption on the part of the member that pertinent facts and alternatives have been identified and considered, he should be aware that such qualifications may not be fully appreciated by the client and should govern his discussion accordingly.

### *Consulting Role and Independence*

.26 MS Section 410.01 states:

When the services to a client also include expression of an opinion on the fairness of financial statements, the matter

of role has special significance, since it also relates to the independence of the accounting firm. The accounting firm's role is to provide advice and technical assistance and to avoid making management decisions or taking positions that might impair the firm's objectivity.

.27 The Committee believes that the objective, advisory posture that has been advocated in the previous paragraphs of this Statement on role is the most effective form of consulting and the one most likely to produce lasting benefits to the client. The Committee also believes that when the member as a consultant assumes this objective, advisory role, he places himself in a posture that complies with the admonition to avoid making management decisions or taking positions that might impair the firm's objectivity.

.28 The compelling need for independence in the attest function is such, however, that these principles must be carefully followed in actual practice. For example, in some cases management may indicate a willingness to abdicate its role as decision maker and the member will need to insist on a proper arrangement of roles. Failing in this, he may need to decline the engagement.

.29 This posture seems clear because the member in the role of objective advisor is not in a position to make management decisions. The ultimate choice of any course of action must be made by management because as a consultant, the member cannot command the resources necessary to implement that decision.

.30 The Committee also believes that the objective advisory role that has been described places the member in a position that will not impair his objectivity in his other relationships with his client. He should, however, always be alert to the way his role may be viewed by others and not permit himself to be placed in a posture inconsistent with this Statement that could cause serious question regarding his objectivity and independence.

### Summary

.31 The Committee on Management Services suggests that each member carefully assess the principles set forth in this

Statement to determine the appropriate role to assume in providing these services in any given opportunity for an engagement. In undertaking any management advisory services engagement, the member must understand the nature and objectives of the service he proposes to perform, and the related role and responsibility inherent in that undertaking.

.32 Throughout this Statement, emphasis has been given to the importance of an objective consulting role in providing management advisory services. This role is advocated essentially because such a posture is the most effective, responsible, and professional form of management advisory service. It is also a role that is consistent with a member's obligation to be independent and objective in all aspects of his relationship with his client.



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