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INDEPENDENT REGULATORY REVIEW COMMISSION
333 MARKET STREET, 14TH FLOOR, HARRISBURG, PA 17101

May 4, 2000

Thomas J. Baumgartner, Chairman
State Board of Accountancy
116 Pine Street
Harrisburg, PA 17105

Re: IRRC Regulation #16A-557 (#2101)
State Board of Accountancy
Commissions and Referral Fees

Dear Chairman Baumgartner:

Enclosed are our Comments on the subject regulation. They are also available on our website at <http://www.irrc.state.pa.us>.

Our Comments list objections and suggestions for consideration when you prepare the final version of this regulation. We have also specified the regulatory criteria which have not been met. These Comments are not a formal approval or disapproval of the proposed version of this regulation.

If you would like to discuss these Comments, please contact Kimberly Trammell de Bien at 783-6834.

Sincerely,

A handwritten signature in black ink that reads "Robert E. Nyce".

Robert E. Nyce
Executive Director

wbg
Enclosure

cc: Steven Wennberg
Joyce McKeever
Honorable Kim Pizzingrilli
Dorothy Childress
Office of General Counsel
Office of Attorney General
Lee Ann Labecki

Comments of the Independent Regulatory Review Commission

on

State Board of Accountancy Regulation No. 16A-557

Commissions and Referral Fees

May 4, 2000

We submit for your consideration the following objections and recommendations regarding this regulation. Subsections 5.1(h) and 5.1(i) of the Regulatory Review Act (71 P.S. § 745.5a(h) and (i)) list the criteria the Commission must use to determine if the regulation is in the public interest. The State Board of Accountancy (Board) must respond to these Comments when it submits the final-form regulation. If the final-form regulation is not delivered by April 3, 2002, the regulation will be deemed withdrawn.

1. Section 11.24(b) Notification to Board. -- Need; Clarity.

This subsection requires a licensee "who receives or intends to receive commissions" to report that fact on the biennial renewal form filed with the Board. The Preamble indicates that the Board will monitor licensees for compliance. The Board should explain the need for this monitoring and how it will be implemented. Additionally, the Board should clarify what is meant by the phrase "intends to receive commissions."

2. Subsection (c) Cooperation with peer reviewer. -- Reasonableness; Clarity.

This subsection states that a licensee, who receives commissions and is subject to peer review, will "furnish peer reviewers with the necessary documentation." What is included in the phrase "necessary documentation"? If it is "workpapers" under Subsection (f), then this subsection should cross-reference Subsection (f). If not, the Board should detail what is meant by "necessary documentation" in the final-form regulation.

3. Subsection (d) Related licensure/registration. -- Reasonableness; Clarity.

This subsection provides that a licensee should acquire and maintain "any license or registration required by another governmental or regulatory body for the purpose of receiving commissions." In discussing this subsection, the Preamble refers to registering with the National Association of Securities Dealers (NASD). The NASD is not a "governmental or regulatory body." The Board should explain the intent of this subsection, include examples of the appropriate licensure or registration required by a regulatory body. The Board should also make revisions to match its intent concerning registration with private standard-setting bodies such as NASD.

4. Subsection (f) Workpapers. -- Reasonableness; Clarity.

This subsection requires a licensee to maintain workpapers that document discussions with clients on investment strategies. We have two concerns with this provision. First, there is no indication of how long these records should be retained. Since failure to comply could lead to disciplinary action, a specific time period is necessary. Second, justification for the expense of retention and storage of documents is required. The Board should review and explain the need for retaining these documents. If retention is necessary, then the Board should consider setting a retention period that is consistent with other workpaper retention requirements with which licensees must comply.

5. Subsection (g) Attest clients. -- Legislative intent; Policy issue that requires legislative review; Fiscal impact; Consistency with statute; Reasonableness; Need; Clarity.

This subsection extends the statutory prohibition to “an individual or entity that can exercise significant influence over the operating, financial or accounting policies of the client.” However, the statutory prohibition in Subsection 12(p)(1) of the CPA Law (63 P.S. § 9.12(p)(1)) states:

(1) A licensee in public practice shall not for a commission recommend or refer to a **client** any product or service, or for a commission recommend or refer any product or service to be supplied by a **client**, or receive a commission when the licensee or the licensee’s firm also performs for that **client** any of the following:

(i) An audit or review of a financial statement.

* * *

(iii) An examination of prospective financial information....
[Emphasis added]

“Client” in this subsection of the CPA Law is also referred to as “attest client” in the regulation. We have five objections to Subsection (g) of the proposed regulation.

First, extending the statutory prohibition on commissions beyond a “client” to “an individual or entity that can exercise significant influence” over a client, is inconsistent with the intent of the General Assembly. In its comments, the House Professional Licensure Committee questioned whether there is statutory authority to expand the scope of this section to parties other than clients, regardless of whether these parties are in a position to exercise significant influence over clients. The House Committee’s comments clearly indicate that the legislative intent was to limit this prohibition to transactions involving attest clients.

Second, given the legislative intent, any expansion of the prohibition is a policy matter requiring legislative review. Section 3(a)(11) of the Act (63 P.S. § 9.3(a)(11)) allows the Board to establish rules of professional conduct. This provision may justify the Board’s position. However, before the Board exercises its discretion in this manner, it should seek clarification from the General Assembly.

Third, this provision is likely to have a negative fiscal impact that will adversely affect competition in this Commonwealth. Numerous commentators, including the Pennsylvania Institute of Certified Public Accountants, have expressed concerns over the negative fiscal impact on current business practices that will occur.

Specifically, this provision could:

- Curtail or limit the current practice and ability of licensees to serve various clients; and
- Place Pennsylvania licensees at a competitive disadvantage with accountants licensed in other states that do not have the same restrictions as this proposed regulation.

Currently, Maryland, New Jersey and Ohio, allow licensed accountants to receive commissions and place no restrictions on situations involving parties with significant influence over attest clients. If the Board does not delete this provision, it should respond to these concerns.

Fourth, the Board's intent is unclear by including Subsection 12(p)(1)(ii) of the CPA Law as an exception to the commission prohibition for situations involving parties with "significant influence." This subsection of the CPA Law already establishes an exception. Why is it included in the regulation? Subsection 12(p)(1)(ii) of the CPA Law reads:

A compilation of a financial statement when the licensee expects, or reasonably might expect, that a third party will use the financial statement and the licensee's compilation report does not disclose a lack of independence.

The statutory exception applies if there is a disclosure of a lack of independence. Rather than mirror the statutory exception, the regulation expands the exception to include situations when there is no disclosure. It is our understanding that this was not the Board's intent. If so, the exception clause in the regulation should be deleted.

Fifth, Subsection (g) is ambiguous in that it appears to have unlimited application. It states that the term significant influence "includes" three situations. The use of the word "includes" indicates that the definition of "significant influence" is not limited to just the three situations. Hence, the three situations do not provide a complete list or definition for the term "significant influence." The term could refer to a number of different parties that may be connected to a client. If the term "significant influence" is retained in the final-form regulation, a definition must be added.