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## Testimony by William C. Bruschi, AIPA Staff Vice President - Regulation

William C. Bruschi

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**PUBLIC HEARING CONDUCTED BY  
TEXAS STATE BOARD OF ACCOUNTANCY  
AUSTIN - JANUARY 4, 1985**

**TESTIMONY BY WILLIAM C. BRUSCHI  
AICPA STAFF VICE PRESIDENT - REGULATION**

My name is William C. Bruschi and I am a salaried member of the staff of the American Institute of CPAs. My title is Vice President - Regulation and the AICPA Professional Ethics Division is in my area of responsibility.

I am pleased to appear at this public hearing in response to the invitation of the Texas State Board of Accountancy to present the AICPA's position on three rules in the AICPA Code of Professional Ethics and to report on the status of the study of the AICPA Committee on Ethical Responsibilities of CPAs.

At the outset, I should point out that all three rules on which I am commenting apply only to AICPA members in public practice.

The first rule I was asked to comment on is Rule 302 which prohibits AICPA members from offering or rendering professional services on a contingent fee basis. This rule provides an exception for fees fixed by courts or other public authorities or, in tax matters, if the fee is determined by the results of judicial proceedings or the findings of governmental agencies.

Council, the governing body of the AICPA, was asked at its May 1984 meeting by the AICPA Board of Directors to authorize a ballot of the AICPA membership to amend this rule. The amendment would have continued the prohibition against contingent fees

for engagements requiring independence, that is, audit, review and compilation report engagements, but permitted contingent fees for other professional engagements.

The chief reason for the Board's proposal was the advice from legal counsel that there was a serious likelihood that the board prohibition against contingent fees would be found in violation of anti-trust law if challenged in a court proceeding but that there was a good likelihood that a prohibition limited to engagements requiring independence would not be found in violation of anti-trust law.

The Board also believed that permitting contingent fees for other types of engagements would be responsive to changed practice conditions.

After extensive floor debate at its May meeting, Council voted to decline to ballot the AICPA membership for this rule amendment. Council reconsidered this matter at its October 1984 meeting and again declined to authorize a ballot of the AICPA membership.

It was my impression that Council was largely persuaded by the argument that relaxing the prohibition would seriously undermine AICPA members' professional reputation for integrity and objectivity in the eyes of the general public. Council also seemed to be not unduly concerned by legal counsel's recital of the legal implications of retaining the broad prohibition.

The AICPA's current position with regard to rule 302 is to enforce it in its literal entirety.

The second AICPA rule I have been asked to comment on is Rule 503 - Commission, in particular that aspect of the rule that prohibits AICPA members from accepting a commission for referral to a client of products or services of others.

The Professional Ethics Executive Committee had advice from legal counsel that the prohibition against commissions could be held in violation of anti-trust law and that the application of the prohibition to all types of transactions that an AICPA member could be involved in may exceed the intent of the rule as adopted by the AICPA membership.

Accordingly, the Ethics Committee issued exposure drafts of two interpretations which, without amending the rule, would have permitted acceptance of commissions under certain conditions. The committee believed these interpretations carried out the original intent of the rule.

The first interpretation defined the term "client." Since the rule prohibited commissions on sales to clients, the interpretation would have permitted commissions on sales of products or services of others to those who were not clients.

The second interpretation defined the term "products or services

of others" as those items or matters which members were expected to have special expertise to evaluate by their training and experience. Commissions on the sale of those items would continue to be prohibited, but commissions on sale of other items or services, where the purchaser would not be expected to rely on the expertise of the member as a CPA, would be permitted.

A third interpretation was prepared by the Ethics Committee which would have permitted the flow through to clients of commissions on the sales of tax shelters.

These interpretations had been exposed to members of Council and at its May meeting, Council voted to direct the Ethics Committee to not issue those interpretations. At its October meeting, Council reconsidered the interpretation on the flow-through of commissions to clients and reaffirmed its original decision to direct the Ethics Committee to not issue it.

After listening to Council's debate over the issuance of these interpretations, my impression is that a majority of the Council members believed that the AICPA members' professional reputation for integrity and objectivity would be undermined if the prohibition on commissions were relaxed.

The AICPA's current position is to enforce the prohibition against the acceptance of commissions for the referral or sales of the products or services of others.

The third rule I have been asked to comment on is Rule 504 - Incompatible Occupations.

When this rule was adopted by the AICPA membership in 1973, it stated that a member who is engaged in the practice of public accounting shall not concurrently engage in any business or occupation that would serve as a feeder to his practice.

In 1978 when the Code was examined for rules in possible violation of anti-trust law under recent U.S. Supreme Court decisions, the "feeder" aspect of rule 504 was judged to fall into that category along with other rules which at that time prohibited advertising solicitation and encroachment. Accordingly, rule 504 was amended to replace "feeder" with "conflict of interests," an application that was believed to not violate anti-trust law.

Since the rule was amended 7 years ago, the Ethics Committee has had no complaints to investigate that would fall under the Rule. Nevertheless, the Committee has discussed the rule from time to time.

My impression of those committee discussions is that it has not been possible to identify an activity or function that CPAs may legally undertake that would be in conflict with the practice of public accountancy as defined by the Code of Professional Ethics.

It is recognized, of course, that certain activities are denied to CPAs because state laws reserve them to other licensed professionals. Examples are the practice of law and medicine.

This broad definition of the practice of public accounting is in conformity with long standing AICPA policy that there should be no artificial restraints on what CPAs can do in their public practice.

The Ethics Committee has also discussed the conflict of interest issue as it might be applied to relations with a client and identified certain relationships that were questionable. Those relationships, however, dealt with specific situations in which the facts had to be weighed for their significance.

One of the results of those discussions was the issuance of ruling #175 on holding a bank directorship. The ruling does not preclude AICPA members from holding bank directorships but alerts them to possible conflicts of interest.

In summary, the Ethics Committee stands ready to enforce the rule prohibiting conflicts of interest but has had no complaints to investigate.

I have also been asked to report on the progress of the AICPA Special Committee on Standards of Professional Conduct for CPAs which is chaired by George Anderson. I do not provide staff

services to that committee, therefore, my remarks are based on recent talks of George Anderson and Tom McRae, AICPA Vice President - Technical, who does provide staff service.

The committee was appointed in late 1983 to study the changing economic, social, legal, and regulatory climate under which CPAs are licensed and practice and, in light of those considerations:

- To evaluate the relevancy of present ethical standards to professionalism, integrity, and commitment to both quality service and the public interest
- To consider the role of the AICPA in the process of establishing standards of professional conduct
- To recommend a course of action based on our conclusions.

It should be noted that the Committee is not being asked to develop a new Code of Professional Ethics, but rather to propose a philosophical basis for a Code and a structure for its implementation. The committee has been asked to have its report ready for the 1985 fall meeting of Council.

While the committee reserves the right to temper or change its



conclusions, it is my understanding that at the present time the committee believes that the Institute should take a major leadership role in establishing and coordinating all elements of standards of professional conduct. The committee has concluded that in that role, the Institute should:

1. Strive to become an organization in which membership is seen as a professional designation that means more than the mere possession of a CPA certificate.
2. Lead in coordinating and gaining acceptance of all the diverse groups involved in the process of establishing and maintaining standards in all areas.
3. Establish procedures to monitor performance in all areas, to assure that educational and remedial or corrective action is taken when poor performance is found, and to impose appropriate sanctions against those who do not take the required corrective action or who commit egregious acts demaging to the profession.
4. Establish a functional code of professional conduct comprehensive enough to serve as a

performance guide to all members in all of their areas of activity and against which the quality of performance can be judged.

5. Communicate to all interested audiences the meaning of its standards, the results of its monitoring of the activities of its members, the scope of professional activity, and the meaning and significance of membership.