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**SFA**



**BILL ANALYSIS**

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House Bill 4238 (as reported without amendment)

Sponsor: Representative Barbara J. Dobb

House Committee: Regulatory Affairs

Senate Committee: Economic Development, International Trade and Regulatory Affairs

Date Completed: 3-24-97

### RATIONALE

According to the Department of Consumer and Industry Services (DCIS), a number of changes in the practice and corporate structure of public accountancy have occurred in recent years, and the profession has sought amendments to a number of State regulations to reflect these changes. Among other things, there apparently is a nationwide move toward diversification of the financial services offered by certified public accountant (CPA) firms, as well as a related move toward dropping the current ban against contingency fees and commissions for CPAs. A concern of licensing agencies, according to the DCIS, is the need for consistent standards for recognizing credentials from other jurisdictions, due to the increased numbers of interstate and international applicants for CPA licensure. It has been suggested that the Occupational Code be amended to address these issues, and to bring provisions governing CPAs into line with the rest of the Code.

### CONTENT

**The bill would repeal and replace provisions in the Occupational Code regulating certified public accountants. Among other things, the bill would include a definition of "certified public accountant"; permit a licensed CPA to receive contingent fees and commissions under certain circumstances; require that persons intending only to use a CPA title be registered with the Department of Consumer and Industry Services, rather than licensed; provide that at least two-thirds (rather than all) of the individuals holding equity and voting rights of a firm would have to be CPAs; and extend current penalty provisions to a violation of professional standards. The bill would delete, among other things, the current**

**residency requirement to sit for the CPA exam, the requirement that qualifying experience be completed within the six-year period preceding examination for certification as a CPA, and a requirement that the DCIS publish biennially a register containing a list of registered CPAs and firms of CPAs in the State.**

Many of the provisions of the bill are substantially the same as existing law. The differences are summarized below.

#### Definitions

"Certified public accountant" would mean an individual who was qualified by education, examination, and experience as evidenced by a certificate as a certified public accountant under provisions of the bill to engage or offer to engage in the practice of public accounting.

"Firm" would mean a corporation, partnership, limited liability company, unincorporated association, sole proprietorship operating under an assumed name, or other legal entity.

"Practice of public accounting" would mean rendering or offering to render an opinion on or offering to attest to the reliability of a representation or estimate, including giving an opinion that financial information as set forth fairly presented the condition of the entity reviewed or audited. Additionally, the bill specifies that the practice of public accounting would include one or more of the following activities when performed or offered to be performed by a person holding himself or herself out as a CPA:

- The issuance of reports on financial statements.

- One or more kinds of management advisory, financial advisory, or consulting services.
- The preparation of tax returns.
- The furnishing of advice on tax matters.

- accounting records.
- The participation in the preparation and analysis of financial statements together with explanations and notes.

### CPA Certification

The bill generally would retain current certification criteria, but would revise the qualifying experience requirement. In addition, although individuals still would have to pass an examination in order to become certified, the examination no longer would have to be "written".

Presently, an individual must have two years of qualifying experience that was obtained within the six-year period immediately preceding the date of initial application for a CPA certificate. The experience must be obtained in the practice of accounting under the direction and supervision of a CPA of this or another state; and/or in a position with a governmental agency involving auditing the books and accounts or financial activities of three or more distinct lines of commercial or industrial business, auditing the books and accounts of financial activities of three or more distinct governmental agencies or independent organizational units, or reviewing a financial statement and supporting material covering the financial condition and operations of entities engaged in three or more distinct lines of commercial or industrial business.

The bill would omit the requirement that the qualifying experience be gained during the six-year period preceding application. Work experience in an accounting practice could be performed while the applicant was meeting the educational requirements, and would have to be obtained in one financial audit and in all of the following areas:

- The application of a variety of auditing procedures and techniques to the usual and customary financial transactions recorded in accounting records.
- The preparation of working papers that covered examination of accounts found in accounting records for audit, review, and compilation.
- The participation in planning a program of work, including the selection of the procedures to be followed, for audit, review, and compilation.
- The participation in the preparation of reports, including written explanations and comments on the findings of the examinations and the content of the

Concerning experience with a governmental agency, the bill would delete the provision pertaining to reviewing a financial statement and supporting material covering the financial condition and operations of entities engaged in three or more distinct lines of commercial or industrial business.

The bill also would revise provisions for the certification of CPAs from another state or country. Currently, the DCIS must issue a certificate to an applicant who holds a valid CPA certificate issued by another state, or holds a valid certificate as a chartered accountant or its equivalent issued by a foreign country, if the applicant has complied with the requirements of the Code and rules promulgated under it, and either the original certificate was secured as a result of an examination equivalent to this State's examination, or the certificate holder has maintained an office for the practice of public accounting for at least 10 years.

The bill, instead, would require the DCIS to issue a CPA certificate to an individual who both held a valid CPA certificate issued by another state or United States jurisdiction, and provided proof that his or her original certificate was secured on the basis of requirements that the Board of State Accountancy determined were equivalent to the standards required for qualification in this State at the time the applicant was issued his or her original certificate. In addition, the DCIS would have to issue a CPA certificate to an individual who both held a valid certificate as a CPA or an equivalent title issued by a jurisdiction outside the United States that the board determined to be equivalent to this State's requirements, and had passed an examination on topics specific to the practice of public accounting in the United States and approved by the board.

### Licensure/Registration

Currently, each individual certified as a CPA, or firm or corporation organized for the practice of public accounting, must be registered with the DCIS. A person is prohibited from holding himself or herself out as a CPA or practicing public accounting unless licensed by the Department. Under the bill, an individual seeking to use a title authorized under the Occupational Code and engaging in the

practice of public accounting would have to be licensed. A person seeking only to use the title would have to apply for registration with the DCIS. As currently provided, in order to renew an individual license, a licensee would have to complete at least 40 hours of continuing education for each year since the issuance of the original license or the last renewal. The bill also provides that the board would have to require that up to eight of the 40 credit hours be in the areas of auditing and accounting.

The bill would continue to require licensure of a firm organized to practice public accounting. In addition, at least two-thirds of the equity and voting rights of the firm would have to be held by individuals who were licensed in good standing as CPAs of this or another state or licensing jurisdiction acceptable to the board, and the principal officer and each officer or director having authority for the practice of public accounting by the firm would have to be licensed in good standing as a CPA in this or another state or an approved licensing jurisdiction. (Currently, each partner or member must be a CPA in good standing in this or another state.) A firm would have to provide a change in address to the DCIS within 30 days of the change.

#### Contingent Fees

The bill would define "contingent fee" as a fee established for the performance of a service pursuant to an arrangement in which no fee would be charged unless a specified finding or result was attained or in an arrangement in which the amount of the fee was dependent upon a finding or result of the service. A contingent fee would not include a fee fixed by a court or other public authority and, in tax matters, a fee determined based upon the results of judicial proceedings or the findings of a governmental agency.

The bill would permit a CPA to charge or receive a contingent fee. A licensee could not charge or receive a contingent fee, however, for the preparation of an original or amended tax return or claim for a tax refund, or during the period in which the licensee or the licensee's firm was engaged to perform one or more of the following services or during the period of time covered by any historical financial statements involved in those services:

- An audit or review of a financial statement.
- A compilation of a financial statement when the licensee expected, or could reasonably expect, that a third party would use the

financial statement and that the compilation report did not disclose a lack of independence.

- An examination of prospective financial information.

#### Commissions

The bill would permit CPAs to perform services for a commission, or receive a commission for services performed. A CPA would have to disclose the arrangement to the person to whom the CPA recommended or referred a product or service to which the commission related. A licensee would not be prohibited from paying or receiving a referral fee for recommending or referring a service involving the practice of public accounting if the payment or receipt of the referral fee were disclosed to the client. A licensee would be prohibited from receiving a commission for recommending or referring to a client a product or service or for causing to be recommended, referred, or supplied to a client a product or service during the period in which the licensee or the licensee's firm was engaged by the client to perform one or more of the following services or during the period of time covered by any historical financial statements involved in those services:

- An audit or review of a financial statement.
- A compilation of a financial statement when the licensee expected, or could reasonably expect, that a third party would use the financial statement and that the compilation report did not disclose a lack of independence.
- An examination of prospective financial information.

#### Penalties

Currently, the Code describes activities that are subject to penalties, such as fraud or deceit in obtaining a CPA certificate, or conviction of a felony related to dishonesty, fraud, or negligence. The bill would add to those activities a violation of professional standards regarding the issuance of reports on financial statements; one or more kinds of management advisory, financial advisory, or consulting services; the preparation of tax returns; or the furnishing of advice on tax matters. The bill would retain the current provision that a person or firm who engages in the practice of public accounting without a license or who uses the title of CPA is guilty of a misdemeanor punishable by a fine of up to \$5,000 or imprisonment for up to one year, or both.

## **ARGUMENTS**

*(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)*

### **Supporting Argument**

The bill would make a number of substantive changes concerning the regulation of CPAs, particularly in regard to fees and corporate structure. According to the DCIS, the American Association of Certified Public Accountants dropped its ban on contingency fees and commissions in response to a suit by the Federal Trade Commission, which had charged that the ban constituted a restraint of trade. While the bill would permit CPAs to accept fees and commissions, it would conform to recommendations of the National Association of State Boards of Accountancy (NASBA) and the Michigan Board of Accountancy. Under the bill, a CPA could not receive a contingent fee or commission while engaged in an attest function (i.e., an audit, review, or compilation that determines whether the information contained in a financial statement is presented fairly and accurately), and client disclosure would be required whenever a CPA received a commission.

Another significant change would allow non-CPA ownership in a CPA firm, as long as two-thirds of the owners, principal officers, and officers with authority for public attest functions of the firm were licensees. This would accommodate the recent national trend for CPA firms to offer diversified financial services, such as estate planning. According to the DCIS, this provision would conform to NASBA and State board recommendations.

In addition, the bill would clarify procedures for the recognition of interstate and international applicants; remove outdated language that restricts the use of computerized examination instruments; and eliminate separate nonconforming disciplinary provisions.

### **Opposing Argument**

The bill would eliminate the required list of all registered CPAs and CPA firms in this State. Without this register, the citizens would have no document to verify a CPA's authenticity.

**Response:** Under the bill, registration would apply only to CPAs and firms that did not engage in the practice of public accounting (while

practitioners would have to be licensed). A citizen could still verify a CPA's registration or licensure with the DCIS.

Legislative Analyst: S. Margules

## **FISCAL IMPACT**

The bill would have no fiscal impact on State or local government.

Fiscal Analyst: M. Tyszkiewicz

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an

official statement of legislative intent.