

2/7/94

## STATEMENT OF NEED AND REASONABLENESS

### (Proposed Permanent Rules Relating to the Code of Professional Conduct)

#### 1100.0100 Definitions

Subp. 1a. Using the term "AICPA" is necessary to identify the American Institute of Certified Public Accountants and is reasonable in that this is the abbreviation for the Institute commonly used in the profession. Thus, users of the rule will recognize it easily when using these rules.

Subp. 1b. Using the term "applicant" to describe someone who takes the CPA examination is necessary since it is the best description possible of that person and is reasonable in that it accurately describes someone who is sitting for the exam.

Subp. 3a. Using the term "certificate holder" is necessary to describe the class of people who have passed the exam, received a certificate, but are not yet licensed. It is reasonable in that it accurately describes the class, distinguishing them from applicants and licensees.

Subp. 3b. This definition has been moved from section .3800 and combined with the definitions in section .0100. This is necessary in order to get all the definitions into one section and is reasonable because it allows the user to know where to find them for quick and easy reference.

Subp. 4a. (See explanation in Subp. 3b.)

Subp. 4b. (See explanation in Subp. 3b.) Also, it is necessary to add the words "limited liability company" and "limited liability partnership" since these forms of practice were created by the 1992 and 1993 Legislatures. These definitions are reasonable to include since CPAs and LPAs may now choose to organize as this type of firm and the Board's rules should reflect that.

Subp. 4c. (See explanation in Subp. 3b.)

Subp. 5. This definition is necessary to clear up confusion that exists about what acts constitute the practice of public accounting. This definition makes clear that the rules are in complete harmony with the statute (326.20, Subd. 3). It is reasonable to use the same definition for this important concept in both the statute and the rules to avoid confusion the part of the public and persons under the Board's jurisdiction.

Subp. 7a. (See explanation in Subp. 3b.)

Subp. 10. This definition is necessary in order to clarify the definition of "practice of public accounting" in Minnesota Statutes Section 326.165 Subd. 2, which refers to "holding one's self out to the public as skilled in the knowledge and practice of accounting." It is necessary to define exactly what the knowledge and practice of accounting are and this rule does that. It is reasonable in that it gives further clarification to the

statute and lists exactly what is considered to be the practice of public accounting. It is consistent with the standard commonly accepted in the profession. The wording of the proposed rule is the exact wording from the Uniform Accountancy Act which has been developed and circulated by the AICPA and the National Association of State Boards of Accountancy (NASBA), of which the Board is a member, as a "Model Act" that the AICPA and NASBA hope each state will adopt for uniformity purposes. Since this is the preferred definition being used in the profession, it is reasonable to adopt it.

Subd. 11. It was necessary to add the word "accounting" to the term "professional services" in order to notify the user that these rules refer only to professional accounting services and not other types of services. This was reasonable to do in order to clear up any confusion that might exist regarding the scope of the rules.

1100.0600 Communications The first part of this rule is old rule 1100.6200 (communications) which has been combined with 1100.0600 (communications with Board). The only new language is "and provide copies of all pertinent records, including handwriting samples, to assist the board in its deliberations." This new language is necessary so that the Board's complaint committee can get vital information during the consideration

of complaints against licensees. It is reasonable in that the committee has been unable to obtain certain information in the past and, thus, unable to resolve complaints because of its inability to obtain records and handwriting samples. It is consistent with the authority given to many other licensing boards. The combination of old rules 1100.6200 and 1100.0600 is necessary to avoid duplication and confusion and is reasonable in that it makes it easier for a user to find the entire language on communication so that the user does not have to go to two different spots in the rules.

1100.0650 Agreement to Observe the Code The first part of this rule is the old rule 1100.0650 (agreement to observe code) which has now been combined with 1100.3900 (compliance with code of professional conduct). There is no new language.

The combination of old rules 1100.0650 and 1100.3900 is necessary to avoid duplication and confusion and is reasonable in that it makes it easier for a user to find the entire language on the requirements to observe the code so that the user does not have to go to two different spots in the rules.

1100.4200 Scope of Code of Professional Conduct

Subp 1B. This rule makes clear that individuals with inactive licenses and retirees do not have to comply with rules regarding the practice of public accounting since, by definition, they are not practicing public accounting.

This is reasonable because unlicensed persons not practicing should not be subject to rules not meant to be applicable to them.

1100.4300 Acts Discreditable

Subp. 1 This new rule combines old rule 1100.5600 (acts discreditable) with 1100.4300 (nonexclusiveness of rules). The language in old .5600 is the first sentence of the new rule. The language in old .4300 is the rest of the first paragraph.

The combination of old rules 1100.5600 and 1100.4300 is necessary to avoid duplication and confusion and is reasonable in that it makes it easier for a user to find the entire language on what acts are discreditable so that the user does not have to go to two different spots in the rules.

Subp. 2 This is new language based upon the language of Rule 501.2 of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993). The only departure from the AICPA language is that, rather than listing the types of discrimination as the AICPA code does, the proposed rule references the Minnesota Statutes section on discrimination. This is an addition to current rules and is necessary in that it makes clear that discrimination in violation of the statute is an act discreditable to the profession. It is reasonable in that it is already the national professional standard in this profession, we are just adopting it, and it

ensures that the level of service to the public is uniformly high.

Subp. 3 This is new language based upon the language of Rule 501.4 of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

This is an addition to our current rules and is necessary in that it makes clear that negligence is an act discreditable to the profession. It is reasonable in that it is already the national professional standard in this profession, we are just adopting it, and the Board's professional conclusion is that this rule will enhance the public's protection by permitting the Board to take appropriate disciplinary action against licensees who have been found to be negligent.

Subp. 4 This is new language based upon the language in the second paragraph of Rule 501.5 of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

This is an addition to our current rules and is necessary in that it makes clear that failure to follow the requirements of governmental bodies, commissions, or regulatory agencies is an act discreditable to the profession. It is reasonable in that it is already the national professional standard in the profession, we are just adopting it, and the Board's professional

conclusion is that this rule will enhance public protection by requiring licensees to be familiar with and abide by the requirements of agencies with whom they work, providing for discipline when they do not.

1100.4400 Independence This is new language based upon the language in Rule 101 and 101-1, Interpretation of Rule 101, of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

While this is new language, there are no material differences between our current rule and the proposed new rule. It is necessary to adopt the new rule so that there are not two differently phrased rules in effect, one by the AICPA (a national organization) and another by the Board, possibly leading to confusion. This has led to confusion by Minnesota licensees in the past - do they follow the AICPA rule or the Board rule? It is reasonable in that it is already the national professional standard in the profession, we are just adopting it, and it protects the public by ensuring a uniform, clean standard for all practitioners without the possibility of confusion.

1100.4500 Integrity and Objectivity, Conflicts of Interest

This is new language based upon the language in Rule 102, and 102-1 and 102-2, Interpretations of Rule 102, of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

While the language from 102 and 102-1 is new language, there are no material differences between our current rule and the proposed new rule. It is necessary to adopt the new rule so that there are not two different rules in effect, one by the AICPA (a national organization) and another by the Minnesota State Board. This has led to confusion by Minnesota licensees in the past - do they follow the AICPA rule or the Board rule? It is reasonable in that it is already the national professional standard in the industry, we are just adopting it, and it protects the public by ensuring a uniform, clean standard for all practitioners without the possibility of confusion.

The new language from 102-2 introduces the new concept of "conflict of interest" into our rules. This is necessary in order to replace our current rule 1100.5900 on incompatible occupations. This change is necessary in order to keep up to date with modern forms of

practice where a CPA or LPA may also be an attorney, real estate broker, licensed securities dealer, etc. This new rule recognizes that a person may have more than one occupation without compromising their independence as a CPA or LPA. The rule further gives a definition of conflict of interest and a method for resolving conflicts.

It is necessary to adopt this new rule to reflect the change in many CPA's and LPA's practices and it is reasonable to move to the national professional standard in the industry. While the rule

now permits more diverse activity by licensees, the protections offered protect the public from licensees engaged in potentially conflicting activities through clarification of when conflicts occur and full disclosure to the client.

1100.5100 Confidential Client Information The new language at the end of this rule is based upon the language in Rule 301-3, Interpretations of Rule 301, of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

The language from 301-3 is new language, but covers situations that have occurred in the past where there has been no Minnesota rule on the subject. It is necessary to adopt the new rule so that there are not two different rules in effect, one by the AICPA (a national organization) and another by the Board. It is reasonable in that it is already the national professional standard in the profession and we are just adopting it based on careful review by the Board that the new rule protects the public as well as the old Board rule.

1100.5300 Furnishing Information to Clients This is new language based upon the language in 501-1, Interpretation of Rule 501, of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

While this is new language, there are no material differences between our current rule and the proposed new rule. It is necessary to adopt the new rule so that there are not two different rules in effect, one by the AICPA (a national organization) and another by the Minnesota State Board. This has led to confusion by Minnesota licensees in the past - do they follow the AICPA rule or the Board rule? It is reasonable in that it is already the national professional standard in the profession, we are just adopting it, and it protects the public by ensuring a uniform high standard for all practitioners.

1100.5800 Commissions This is new language based upon the language in Rule 503 of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

This is completely new language and represents a major departure from our previous rule. It is necessary in order to keep up to date with modern forms of practice. It is also necessary so that CPAs and LPAs are not put at a competitive disadvantage in the marketplace when competing against other providers of these services since the public is better served by a licensed professional in many cases. It is necessary to adopt this new rule to reflect the change in many CPA's and LPA's practices and it is reasonable to move to the national professional standard in the because it offers great advantages to the public in terms of

expanded services by licensees and has not caused the problems the old prohibitive rule sought to prevent.

1100.5850 Contingent Fees This is new language based upon the language in Rule 302 of the AICPA Code of Professional Conduct, as published in the AICPA Professional Standards, Volume 2 (1993).

This is completely new language and represents a major departure from our previous rule. It is necessary in order to keep up to date with modern forms of practice. It is also necessary so that CPAs and LPAs are not put at a competitive disadvantage in the marketplace when competing against other providers of these services since the public is better served by a licensed professional in many cases. It is necessary to adopt this new rule to reflect the change in many CPA's and LPA's practices and it is reasonable to move to the national professional standard in the profession because it offers great advantages to the public in terms of expanded services by licensees and has not caused the problems the old prohibitive rule sought to prevent.

(repealed sections)

1100.3800 Definitions

All the material in this section was moved to 1100.0100 so that all definitions could be in the same section. It is therefore both reasonable and necessary to repeal this section.

1100.3900 Compliance with Code of Professional Conduct

All the material in this section was moved to 1100.0650 so that all material relating to compliance with the code would be in one spot. It is therefore both reasonable and necessary to repeal this section.

1100.5200 Contingent Fees

This section has been renumbered 1100.5850 and it is therefore necessary and reasonable to repeal the old section number.

1100.5400 Services to Clients of Other Accountants

This is archaic language which should have been repealed two years ago when the Board's rules on advertising and soliciting clients were changed, it was somehow overlooked. Since it was not changed at that time, it is therefore necessary to repeal it now for internal consistency and to effectuate the other changes that were made. It is reasonable to repeal it now since this is the first chance the Board has had to correct its oversight.

#### 1100.5500 Offers of Employment

This is archaic language which should have been repealed two years ago when the Board's rules on advertising and soliciting clients were changed, it was somehow overlooked. Since it was not changed at that time, it is therefore necessary to repeal it now for internal consistency and to effectuate the other changes that were made. It is reasonable to repeal it now since this is the first chance the Board has had to correct its oversight.

#### 1100.5600 Acts Discreditable

All the material in this section was moved to 1100.4300 so that all material relating to acts discreditable would be in one spot. It is therefore both reasonable and necessary to repeal this section.

#### 1100.5900 Incompatible occupations

The Board decided repealing this section in favor of new section .4500 on conflicts of interest was necessary in order to keep up to date with modern forms of practice where a CPA or LPA may also be an attorney, real estate broker, licensed securities dealer, etc. The new rule on conflicts of interest recognizes that a person may have more than one occupation and the rule further gives a definition of a conflict of interest and a method for resolving conflicts. It is necessary to adopt that new rule to reflect the

change in many CPA's and LPA's practices and it is reasonable to move to the national professional standard in the industry. It is therefore both reasonable and necessary to repeal this section.

(See 1100.4500)

#### 1100.6200 Communications

All the material in this section was moved to 1100.0600 so that all material relating to communications would be in one spot. It is therefore both reasonable and necessary to repeal this section.

#### **RULE CHANGES - IMPACT ON SMALL BUSINESS**

The Board notes below how the five suggested methods listed in section 14.115, subdivision 2, for reducing the impact of the rules on small businesses should be applied to the proposed rules. The five suggested methods enumerated in subdivision 2 are as follows:

- (a) The establishment of less stringent compliance or reporting requirements for small businesses;
- (b) The establishment of less stringent schedules or deadlines for compliance or reporting requirements for small businesses;
- (c) The consolidation or simplification of compliance or reporting requirements for small businesses;

- (d) The establishment of performance standards for small businesses to replace design or operational standards required in the rule; and
- (e) The exemption of small businesses from any or all requirements of the rule.

The feasibility of implementing each of the five suggested methods and whether implementing any of the five methods would be consistent with the statutory objectives that are the basis for this rulemaking are considered below.

1. It would not be feasible to incorporate any of the five suggested methods into these proposed rules.

Methods (a) to (c) relate to lessening compliance or reporting requirements for small businesses either by establishing less stringent requirements, establishing less stringent schedules or deadlines for compliance with the requirements, or consolidating or simplifying the requirements. The Board finds that it would be unworkable to lessen the requirements for those licensees who practice in a solo, or practice consisting of fewer than 50 employees, since that would include, at a minimum, the vast majority of all licensees. Method (d) suggests replacing design or operational standards with performance standards for small businesses. The Board's rules do not propose design or operational standards for businesses and therefore there is no

reason to implement performance standards for small businesses as a replacement for design or operational standards that do not exist. Finally method (e) suggests exempting small businesses from any or all requirements of the rules. The application of this provision would exempt a large percentage of licensees from the purview of the rules, which would not make sense.

2. Reducing the impact of the proposed amendments on small businesses would undermine the objectives of the Minnesota licensing law.

Pursuant to Minn. Stat. Section 326.165, et seq., the Board was created for the purpose of establishing requirements for licensure and adopting standards for disciplinary action to govern the practices or behavior of all licensees. Pursuant to Minn. Stat. Section 326.18 the Board is specifically mandated to promulgate rules as may be necessary in order to carry out the Board's purpose. Given these statutory mandates, it is the Board's duty to establish licensure qualifications and disciplinary standards which apply to and govern all applicants and licensees regardless of the nature of their practice. As stated above, it is the Board's position that the proposed rules will not affect small businesses and certainly do not have the potential for imposing a greater impact on licensees in a solo, or small practice, than on those practices large enough to remove them from the definition of small business. It has also been explained above that the Board considers it unfeasible to implement any of

the five suggested methods enumerated in subdivision 2 of the small business statute. Nonetheless, to the extent it may be feasible to implement any of the suggested methods for lessening the impact on small businesses, the Board believes it would be unwise and contrary to the purposes to be served by these rules for the Board to exempt one group of licensees - indeed, the vast majority of licensees - from the requirements of these rules. Similarly, the Board believes it would be unwise and contrary to its statutory mandate for the Board to adopt one set of standards for those licensees who work in a large business setting and adopt another, less stringent, set of standards to be applied to those licenses who practice in a solo or small practice. It is the Board's view that these rules must apply equally to all licensees if the public whom they serve is to be adequately protected.

EXPENDITURE OF PUBLIC MONEY BY LOCAL PUBLIC BODIES AND IMPACT ON AGRICULTURAL LAND. Promulgation of these rules will not result in the expenditure of public monies by local public bodies nor have any impact on agricultural land; therefore, no further information need be provided under Minn. Stat. Section 14.11 (1992).

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January 24, 1994

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David J. O'Connell  
Executive Secretary  
Minnesota State Board of Accountancy

