

*American Accounting Association ♦ Auditing Section
Auditing Standards Committee*

February 10, 2005

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

Via email to comments@pcaobus.org

RE: Invitation to Comment on PCAOB Rulemaking Docket Matter No. 017

Dear Board Members:

The Auditing Standards Committee of the Auditing Section of the American Accounting Association welcomes the opportunity to comment on *Proposed Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees*. We offer the comments below to enhance the clarity of the proposed standard and to address a few more substantive questions. We find the proposed rules and discussion to be very well constructed and firmly grounded in existing tax rules and SEC requirements.

The views expressed in this letter are those of the Auditing Standards Committee members and do not reflect an official position of the American Accounting Association. In addition, the comments reflect the overall consensus view of the Committee, not necessarily the views of every individual member.

1. Rule 3522 and related discussion of general tax planning and advice.

We acknowledge the discussion and support for the proposed rule regarding allowable tax planning subject to specific approval of the audit committee, yet offer several observations suggesting that auditors' provision of general tax planning services should be prohibited.

First, the goal of tax planning services is to facilitate management decision-making to reduce taxes. As a result, the audit firm is acting in a consulting role and working with management toward a common decision-making objective – structuring business transactions in a manner that is advantageous from a tax perspective. In our opinion, the very nature of this service results in the audit firm and the client having a shared interest of reducing future taxes. This role for the audit firm appears to us to be quite different than an attest role or a compliance role.

Second, from a public perception standpoint, we question whether investors view the auditor as truly independent when the auditor provides significant tax planning services to the client. In such a case, the perception may be that the auditor and client are “too close” due to their working together to reduce taxes.

Third, we wonder exactly where the line is drawn between tax planning services that are appropriate versus those that are inappropriate. For example, how would one assess whether management truly “makes all decisions relating to, and takes responsibility for, . . . the tax work . . .”? A trusted tax advisor involved in tax planning work could reasonably be expected to have a significant impact on the decisions of management. As a result, it is unclear how close the audit firm can get to driving management’s decisions without impairing its own independence. As a public policy matter, we wonder about the impact on the market if some audit firms cross this “fuzzy” line and must resign from audits due to independence violations.

We believe the proposed rule provides an improvement from the current environment and should be approved, with the recommendation that the Board remain sensitive to the independence risks posed by allowing tax planning for audit clients. In the best of circumstances the professional judgment of the audit committee can be relied upon to monitor the first and third issues raised above. Unfortunately, the public perception of independence is not within the control of audit committees or management. In the final analysis, there are many available providers of tax planning services, and in today’s environment, the risks of allowing auditors to provide tax planning services may outweigh the advantages.

2. Rule 3522 and clarification of opining on tax treatment.

The Board should clearly define when opining on a tax transaction is separate from the audit process. Clearly, an auditor has to opine on transactions as part of the audit process. If a client asks whether their accounting for a tax transaction is appropriate, is that opining? If the client asks about proposed accounting for a proposed tax transaction (whether or not the auditor subsequently determines the transaction is restricted under Rule 3522) is the auditor’s independence impaired by virtue of having provided that opinion? This issue was raised during the Board’s December 14, 2004 meeting to approve release of these proposed changes, and we agree that clarification would be beneficial.

3. Rule 3523 and related discussion of provision of tax services for senior officers.

We believe that auditor independence is impaired if the audit firm provides personal tax services to any person in a financial reporting oversight role. The restriction should not be limited to officers in financial reporting oversight roles as proposed. All employees in a financial reporting oversight role are in critical positions, and the auditor should be independent of these parties.

Finally, while the role of audit committees and the approval required for the provision of tax services by the auditor is present in the proposed rules, we note the lack of discussion of audit firms' quality control procedures regarding tax services and the related threats to independence. We encourage the Board to consider quality control procedures in the future to provide guidance on the appropriate level of review and safeguards within audit firms related to threats to independence.

We hope that our suggestions are helpful and will assist in finalizing the auditing standard. Please feel free to contact our committee Chair for elaboration on or clarification of any comment.

Respectfully Submitted,

Auditing Standards Committee
Auditing Section, American Accounting Association

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