

DECEMBER 14, 2004 OPEN MEETING

**PROPOSED ETHICS AND INDEPENDENCE RULES CONCERNING
INDEPENDENCE, TAX SERVICES, AND CONTINGENT FEES**

Statement of Daniel L. Goelzer

I am very pleased that the Board is today considering a proposal to address the relationship between auditor independence and the performance of tax services for audit clients. When an auditor invents a novel, too-good-to-be true, tax strategy and recommends it to an audit client, there is a high potential to undermine both the fact and appearance of independence. Revelations of auditor marketing of dubious tax-avoidance schemes to audit clients have been extremely corrosive of the public's confidence in audited financial reporting. While the major firms have voluntarily adopted limits on this kind of activity, I believe that the Board's responsibilities require that we also act.

The proposal the Board's staff has formulated would draw some clear boundaries between the kinds of tax services that impair independence and those that do not. In my view, the lines the staff has proposed would not have untoward effects on either accounting firm economics or on the ability of firms to retain top-flight tax expertise. In particular --

- Banning contingent fee arrangements is not new. The SEC has already barred them.
- Prohibiting auditor involvement in tax strategies that the IRS has identified as problematic, that must be kept secret, or that don't meet the standard of having at least a 51 percent chance of being allowable, should not put much of a crimp in the tax practices of reputable firms.

The need to prohibit auditors from providing tax services to senior officers of audit clients is more open to debate. However, I have become convinced that that aspect of the proposal is also justified. Auditing a public company and simultaneously assisting its officers with their personal taxes carries too great a potential that the auditor will eventually find itself caught in the middle when the interests of its audit client and the interests of the officers in minimizing their taxes diverge.

I also believe that the proposal before us today is significant for what it does not prohibit. The release would make clear that routine tax compliance assistance and tax

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planning advice are not incompatible with independence. Auditors have traditionally performed these kinds of services for their audit clients, and this kind of assistance is particularly important to small and medium-sized businesses that lack the resources to maintain extensive in-house tax expertise.

The proposal would also help audit committees do their job. I believe that informed, case-by-case, audit committee decision-making is preferable to the Board's attempting to address by rule every conceivable situation that might raise independence concerns. By arming the audit committee with the relevant information and requiring the auditor to discuss the independence implications of proposed tax services with the committee, the proposal would promote that goal.

Finally, these proposals would have ramifications that extend beyond tax services. Proposed Rule 3520 would add to the Board's rules a general requirement, parallel to existing SEC requirements, that the auditor must be independent of its audit client. This will give the Board a predicate for further rulemaking, and for issuing interpretive guidance, regarding independence matters. In light of the critical importance of auditor independence to the Board's statutory mission of strengthening and maintaining investor confidence in audited financial reporting, proposed Rule 3520 may, in the long run, prove to be more significant than the specific rules related to tax services.