2015-2016

NEW YORK STATE

QUALITY REVIEW OVERSIGHT COMMITTEE

ANNUAL REPORT

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I. Message from the Committee

The QROC is pleased to present its 2015-2016 annual report to the State Board for Public Accountancy. The QROC continues to actively monitor the AICPA's evolution of the Peer Review Program, the PCAOB's oversight of independent audit reports, the New York State Society of CPA's administration of the quality review program and the CPA firms that are enrolled in the peer review program.

The past year the QROC reviewed proposed changes for the administration of the peer review program that will enhance and refine various peer review standards. In February 2016, the AICPA issued the discussion paper: Proposed Evolution of Peer Review Administration – A discussion paper seeking input from state CPA society leaders. The discussion paper proposes having fewer administrating entities with the goal of increasing quality and consistency throughout the program. In March 2016, the AICPA's Exposure Draft Proposed Changes to the AICPA Standards for Performing and Reporting on Peer Reviews was issued. The proposal would allow firms with no AICPA members to enroll in the AICPA Peer Review Program, expand the availability of administration by the National Peer Review Committee, and includes other minor changes. Other changes to the peer review program continue to refine the program as necessitated by changes in financial statement reporting standards, and the need to improve the overall quality of financial statement reporting. These proposed changes may affect the Committee's ability to conduct its oversight responsibilities, and will most likely require regulatory changes.

The QROC continues to be an active partner in the quality review program at the state and national level. Our relationship with our partners at the New York State Society of CPAs and the AICPA continue to enhance the QROC's effectiveness of monitoring the program. During the changing peer review environment and the continued refinement of the program, the Committee is committed to its continued oversight of the program on behalf of the Education Department.

II. Background

In 2009, the NYS Legislature passed significant changes to laws that regulate Public Accounting in New York. In addition to many other changes, the legislature required the implementation of the Mandatory Quality Review Program (MQRP). The program became effective for firms registering on or after January 1, 2012. Firms with three or more CPAs, providing attest services, are required to participate in the MQRP. In addition, any firm performing attest services under Education Law, Section 7410.4 is also required to participate. Firms in the MQRP are required to undergo a peer review once every three years as a condition of their firm registration renewal. The purpose of the MQRP is to promote quality in the attest services provided by CPAs.

III. QROC Responsibilities

The QROC derives its regulatory authority from Section 70.10 of the Regulations of the Commissioner. The purpose of the QROC includes approving and monitoring the Sponsoring Organization, informing and reporting matters concerning peer review to the Department, assessing and reporting on the effectiveness of the program, and reviewing individual peer reports for compliance.

The Committee has the responsibility to:

- receive and approve administration plans from entities applying to be sponsoring organizations;
- monitor sponsoring organizations to provide reasonable assurance that the sponsoring organization is conducting the peer review program in accordance with the quality review standards;
- inform the Department of any issues and/or problems relating to the quality review program which may require the Department's intervention;
- annually report to the Department as to whether each sponsoring organization meets the standards necessary to continue as an approved sponsoring organization;
- annually assess the effectiveness of the quality review program;
- annually report to the Department on any recommended modifications to the quality review program;
- review each quality review report submitted by a firm, as part of its registration or renewal of its registration, to determine whether the firm is complying with applicable professional standards.
- where applicable, the QROC may refer firms that are not in compliance with applicable standards to the Office of Professional Discipline pursuant to Education Law section 6510; and
- ensure that any documents received from a firm or reviewer remain confidential and not constitute a public record, unless such document is admitted into evidence in a hearing held by the Department.

IV. QROC Recognized Peer Review Program Providers

The American Institute of Certified Public Accountants is currently the only Peer Review Program Provider that is acceptable to the Committee. The Committee accepts all AICPA-approved organizations authorized to administer the AICPA Peer Review Program. The AICPA's Peer Review Board (PRB) is responsible for maintaining, furthering and governing the activities of the AICPA's Peer Review Program, including the issuance of peer review standards, and peer review guidance. The Peer Review Program provides for a triennial review of a firm's accounting and auditing services performed by a peer reviewer who is unaffiliated with the firm being reviewed to ensure work performed conforms to professional standards.

There are two types of peer reviews. System reviews are designed for firms that perform audits or other attest engagements. Engagement reviews are for firms that do not perform audits but perform other engagements such as compilations and/or reviews. Firms can receive a rating of pass, pass with deficiency, or fail. Firms that receive ratings of pass with deficiency or fail must perform corrective actions.

Entities that are acceptable to administer the peer review program in New York State are:

- New York State Society of CPAs (NYSSCPA) - NYSSCPA administers the AICPA Peer Review Program in New York. As the administering entity, NYSSCPA is responsible for ensuring that peer reviews are performed in accordance with the AICPA's Standards. The NYSSCPA Peer Review Committee (PRC) monitors the administration, acceptance, and completion of peer reviews. The PRC assigns the system review report acceptance function to Report Acceptance Bodies (RABs); pass engagement review report acceptance is delegated to the Technical Reviewers with the Peer Review Committee oversight.

- National Peer Review Committee (NPRC) -The AICPA also administers a peer review program through the National Peer Review Committee for firms required to be registered with and/or inspected by the Public Company Accounting Oversight Board (PCAOB) or performs audits of non-Securities and Exchange Commission (SEC) issuers pursuant to the standards of the PCAOB.

- Other State Societies - New York registered accountancy firms with their main office located in another state are allowed to have their peer review administered by AICPA's administering entity for that state. In most cases, the administering entity is the state society of CPAs in that state.

V. Committee Members

The QROC consists of six members: five licensed members and one public member who are appointed by the NYS Board of Regents. Licensed members must be licensed certified public accountants in New York State, hold current registrations with the Department, and may not be members of the State Board for Public Accountancy or one of its committees. The public member must have received or used the services provided by CPAs.

Members are appointed to five-year terms and may serve up to two terms. There was one vacancy, which was filled by Mr. David Iles, CPA.

Member Name:	Member Term:
Diane Christensen, CIA, CRMA	Feb 1, 2013 – Jan 31, 2018 (First term)
David Iles, CPA	Oct 1, 2015 – Sep 30, 2020 (First term)
Mary MacKrell, CPA Vice Chair	Mar 1, 2013 – Feb 28, 2018 (First term)
John C. Olsen, CPA	Apr 1, 2016 – May 31, 2021 (Second term)
James Rockwitz, CPA	Sep 1, 2014 – Aug 31, 2019 (First term)
Frank S. Venezia, CPA Chair	Apr 1, 2015 – May 31, 2020 (Second term)

VI. Statistics: The following statistics were obtained from the NYSSCPA's annual report to the QROC on the administration of the Peer Review Program (PRP) for the calendar years 2013-2015. The NYSSCPA PRP program is administered by the NYSSCPA for firms that are not members of the AICPA or the NYSSCPA. The AICPA PRP is the program administered by the NYSSCPA for firms that have at least one partner that is a member of the AICPA.

	2013				2014				2015			
	NYSSCPA PRP		AICPA PRP		NYSSCPA PRP		AICPA PRP		NYSSCPA PRP		AICPA PRP	
System Reviews:												
Pass	15	(58%)	182	(80%)	21	(70%)	211	(73%)	20	(67%)	208	(77%)
Pass with deficiencies	9	(35%)	31	(14%)	3	(10%)	52	(18%)	4	(13%)	34	(13%)
Fail	2	(7%)	14	(6%)	6	(20%)	25	(9%)	6	(20%)	24	(10%)
Subtotal – System	***26***		***227***		***30***		***288***		***30***		***269***	
Engagement Reviews:												
Pass	8	(57%)	106	(76%)	6	(86%)	124	(93%)	11	(92%)	133	(89%)
Pass with deficiencies	5	(36%)	24	(17%)	0	(0%)	8	(6%)	1	(8%)	10	(7%)
Fail	1	(7%)	9	(6%)	1	(14%)	1	(.75%)	0	(0%)	6	(4%)
Subtotal – Engagement	***14***		***139***		***7***		***133***		***12***		***149***	
Total System & Engagement	**40**		**366**		**37**		**421**		**42**		**418**	

*Percentages are of the subtotal

VII. Meetings and Accomplishments

Following are the meetings and accomplishments in 2015 - 2016.

a. Committee Meetings - The QROC holds meetings in order to conduct business and report to the Department regarding the effectiveness of mandatory quality review program. Minutes from each public meeting are available upon request.

Since the last annual report was issued, the QROC has held the following meetings:
November 19, 2015 – Albany, NY
January 27, 2016 – Albany, NY
May 3, 2016 – New York City, NY
August 3, 2016 – Albany, NY
October 12, 2016 – Albany, NY

On September 16, 2015, members of the QROC attended the State Board for Public Accountancy's meeting to present its 2014-2015 Annual Report. A QROC meeting was scheduled for that afternoon; however, it was cancelled due to an extended fire alarm at the State Education Building.

b. Approval of the Sponsoring Organization - At the May 3, 2016 meeting, the QROC unanimously agreed to continue with the NYSSCPAs as a Sponsoring Organization through December 31, 2017.

c. NYSSCPA Peer Review Committee Oversight - The QROC attended the Society's Peer Review Committee Meeting on May 4, 2016 at the Society's main office in New York City. QROC members in attendance unanimously agreed the program is run by dedicated professionals in accordance with the AICPA standards. The QROC members agreed that the PRC was well informed and engaged in the process. Throughout the year, QROC members and board office staff attended other Peer Review Committee meetings via telephone conference. The conclusion regarding the PRC oversight by QROC was that the peer review program was administered in accordance with the AICPA standards.

d. QROC Review of Peer Reviewers – In November 2015, the Committee reviewed 170 Peer Reviewers who were listed on the AICPA's website as providing peer review services in NYS. Of the 170 listed, one was not a CPA and three CPAs had expired registrations. The AICPA agreed to remove the non-CPA from the list. The three CPAs with expired registrations were contacted and are now properly registered.

e. NYSSCPA's Annual Report on Oversight, August 29, 2016 – The Society issues this report annually and it describes the various oversight activities undertaken in the normal course of the peer review committee. Included are oversights of Individual Reviews and Reviewers, the NYSSCPA Peer Review Committee Oversight of AE Administration of AICPA Peer Review Program, and the Annual Verification of Reviewers' Resumes. The report also provides numerical information pertaining to number of enrolled firms, type of peer reports issued, and other related information.

f. NASBA's Compliance Assurance Committee (CAC): The CAC's role is to promote effective oversight of compliance with professional standards by CPAs and their firms. The CAC fulfills their role by having two representatives on the National Peer Review Committee (NPRC), issuing comment letters on standards and proposals, and providing an annual oversight of the NPRC. The objective of the oversight is to evaluate and report on whether the NPRC is operating according to the peer review standards. On February 29, 2016, the CAC released its fourth monitoring report, concluding that the NPRC had operated within the standards for the period of November 1, 2014 – October 31, 2015. The QROC continues to review the CAC's oversight role and supports their continued work.

The CAC has discussed the AICPA's *Exposure Draft – Improving Transparency and Effectiveness of Peer Review* dated November 10, 2015. The CAC has focused on the regulatory changes to identify poor peer review performance and taking appropriate action of the peer reviewer. The CAC generally approves of the draft and the need to identify specific performance deficiencies and when required to prevent certain peer reviewers from performing peer reviews. The QROC has also reviewed the draft and is supportive of the changes.

The CAC has expressed interest in assisting state Peer Review Oversight Committees (PROC), such as NY's QROC and other States' PROCs. To that end, the CAC is involved with a project for the Accountancy License Database (ALD) that will provide a listing of CPA firms and their peer review information. The QROC is also supportive of these changes.

g. Peer Review Standards: The QROC monitors the AICPA's Peer Review Exposure Drafts and their effects on future peer review administration. The QROC reviewed the following: AICPA's *Exposure Draft Proposed Changes to the AICPA Standards for Performing and Reporting on Peer Reviews* dated May 23, 2016. The proposal would allow firms with no AICPA members to enroll in the AICPA Peer Review Program, expand the availability of administration by the National Peer Review Committee, and includes other minor changes. The Committee is supportive of the changes and is hopeful that the expanded access will improve the program and resolve issues related to firms without AICPA membership. The QROC continues to monitor the evolution of the peer review program and suggests any regulatory changes, as required.

h. AICPA's Proposed Changes to Sponsoring Organizations: In February 2016, the AICPA issued the discussion paper: *Proposed Evolution of Peer Review Administration – A discussion paper seeking input from state CPA society leaders*. The discussion paper sought the input from state CPA society leaders. Additionally, a supplemental paper: *Proposed Evolution of Peer Review Administration – A supplemental discussion paper seeking input from State Boards of Accountancy* was issued on July 18, 2016. The papers discuss a proposed plan to increase the quality, consistency, efficiency and effectiveness in the administration of peer reviews, while providing for appropriate cost recovery. The proposal calls for fewer Administering Entities (AEs). Currently there are 41 AEs, including the National Peer Review Committee (NPRC) and the proposal is to have 8 to 10 AEs. The Committee has

several concerns, including the possibility that the future AE for NYS could be located outside of NYS. In which case, changes to the Commissioner's Regulations would be required. The Committee and the State Board for Public Accountancy have agreed to issue a joint comment letter stating its concerns.

i. Regulatory Updates - The QROC continued to work on the Rules of the Board of Regents, Section 29.10, Unprofessional Conduct – Special Provisions for Profession of Public Accountancy as it relates to misconduct regarding the MQRP. The QROC has proposed language and continues to work with the State Board for Public Accountancy to further enhance the rules. The QROC has proposed changes to the Regulations of the Commissioner – Section 70.10 to update and reflect changes since the MQRP's inception in 2012.

j. Employee Benefit Plan (EBP) Audits - In May 2013, it was reported that the U.S. Department of Labor (DOL) had referred firms to the AICPA for remedial peer review action. This matter was reported in last year's annual report. As a result of this referral, firm's peer review reports were recalled. The QROC has continued to monitor the recall process over the past few years. Of the 33 firms that had their peer review recalled, 31 firms have completed the recall process. The remaining 2 firms continue to be monitored by the QROC.

k. In September 2015, a QROC member attended a conference on the PCAOB's *Annual Report on the Interim Inspection Program Related to Audits of Brokers and Dealers*, dated August 18, 2015. The report details the lack of due professional care in the conduct of broker-dealer audits among some firms. Key findings on lack of independence were related to firms that performed the fewest audits. The final recommendation is that the firms that perform these audits should review the Report's findings of independence and audit deficiencies, and take the required action to remedy any deficiencies. The QROC expressed concern that these audits may be conducted by firms that are exempt from the quality review program based on the small firm exemption.

l. AICPA Peer Review Board (PRB) Open Meetings – The QROC monitors the AICPA's PRB's public sessions throughout the year. QROC members and board office staff attend these meetings in person or via teleconference and report back to the Committee. The sessions are informative and allow for an exchange of ideas and practices across state lines.

m. Monitoring of Firms in Peer Review - The QROC monitors firms throughout the remediation phase of their peer review, where applicable. Firms are informed by letter that the QROC is monitoring their remediation progress and are required to acknowledge receipt of the letter. Remediation is considered complete when the peer review is accepted as complete by the Society's Peer Review Committee. The QROC also monitors the firms that have dropped out of the program and those that are terminated by the program.

System and Engagement Reviews that have a rating of fail or pass with deficiencies are monitored by the QROC. Since the last annual report, the QROC has monitored 159 firms, including firms that have been carried over from the prior year. During this time, 107 firms had their peer reviews accepted as complete, while 52 firms are still being actively monitored.

VIII. Recommendations

The QROC continues to oversight the NYSSCPA's administration of the AICPA's Peer Review Program, and the further development of the AICPA's Peer Review Program. The Committee supports the changes that are being implemented currently, but has some reservations regarding the proposed consolidation of Administrating Entities. The QROC will continue to work with our partners at the state and national level. The QROC recommends that the Board continue to support the initiatives already in place and participate in the discussion on future initiatives.

The QROC has made recommendations, in conjunction with the Board, to update the Rules of the Board of Regents and the Commissioner's Regulations as related to the peer review program. These recommendations include clarifying the small firm exemption and when disciplinary action is appropriate for firms failing to meet the peer review standards. The QROC recommends these changes be enacted.

The QROC continues to express concerns that firms with two or fewer accounting professionals are not required to participate in the Mandatory Quality Review Program. In addition to the findings by the US Department of Labor related to EBP audits, the PCAOB's report on Brokers and Dealers also noted deficiencies with smaller firms and issues with independence and audit quality. Other states and the nationally recognized peer review standards do not have an exemption from their peer review program for firms with two or fewer accountants. To ensure the highest level of public protection, the QROC recommends that firms with two or fewer accounting professionals be required to participate in the quality review program. The Committee continues to recommend changing the law and regulations to require firms with two or fewer accounting professionals to enroll in quality review program.

IX. Conclusions

Based on its oversight activities, the QROC concluded that the New York State Society of Certified Public Accountants has been an effective administrator as the MQRP's Sponsoring Organization. Furthermore, the QROC recommends that the Department continue to support the NYSSCPA as the MQRP's Sponsoring Organization. The QROC also believes that the continued oversight of firms enrolled in the peer review program contributes to improving the protection of the public.