



STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

A PERFORMANCE AUDIT
of

THE ARIZONA STATE BOARD OF ACCOUNTANCY

AUGUST 1979

UNLIKE 40 OTHER STATES, ARIZONA DOES NOT
LICENSE ACCOUNTANTS. AS A RESULT, THE
POTENTIAL FOR FINANCIAL HARM EXISTS FOR THE
GENERAL PUBLIC IN ARIZONA.

A REPORT TO THE
ARIZONA STATE LEGISLATURE

REPORT 79-5



DOUGLAS R. NORTON, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

DEBRA K. DAVENPORT, CPA
DEPUTY AUDITOR GENERAL

August 7, 1979

The Honorable Bruce Babbitt, Governor
Members of the State Legislature
Members of the State Board of Accountancy

Transmitted herewith is a report of the Auditor General, A Performance Audit of the Arizona State Board of Accountancy. This report is in response to a September 19, 1978, resolution of the Joint Legislative Budget Committee and a January 18, 1979, resolution of the Joint Legislative Oversight Committee.

A summary of this report is found on the blue pages at the front of the report. A response to this report from members of the State Board of Accountancy is found on the yellow pages preceding the appendices of the report.

My staff and I will be happy to meet with the appropriate legislative committees, individual legislators or other state officials to discuss or clarify any items in this report or to facilitate the implementation of the recommendations.

Respectfully submitted,

A handwritten signature in cursive script that reads "Douglas R. Norton".

Douglas R. Norton
Auditor General

Staff: Gerald A. Silva
Coni R. Good
James A. Sexton
Steven A. Wallace

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SUMMARY

The Arizona State Board of Accountancy was created in 1919 together with the first accountancy laws. The Board is responsible for administration and enforcement of Arizona laws concerning the practice of accounting. These duties include examination of applicants, issuance of certificates to individuals that have fulfilled examination, experience and other requirements; registration of firms and individuals to practice accounting and investigation of complaints and violations of accountancy law.

Arizona accountancy law provides for two types of certificates to be issued, the Certified Public Accountant and the Public Accountant. Individuals meeting requirements can be certified and are then allowed to use the reserved titles of "Certified Public Accountant" and "Public Accountant."

The State Board of Accountancy consists of five members, four of whom are required to be Certified Public Accountants and one member to represent the public at large. The Board also has an advisory committee of four Public Accountants whose responsibilities include providing advice and aid to the Board on matters affecting Public Accountants.

The activities of the Board and its administrative office are funded through fees charged for examination, certification and registration, ten percent of which are deposited in the state general fund.

Our review of the State Board of Accountancy revealed that unlike 40 other states, Arizona does not license accountants but instead uses a less extreme form of regulation called "Reserve of Title." As a result, potential for financial harm exists for the general public in Arizona. (page 23)

Our review revealed that the Public Accountant classification is unnecessary. (page 45)

In addition, our review disclosed the performance of the State Board of Accountancy in investigating and resolving complaints and reviewing the competency of certificate holders has been superior when contrasted with other Arizona state regulating bodies and other state boards of accountancy. The Board not only investigates and resolves complaints it receives, but actively pursues a limited quality review program. However, it appears that this program can be expanded to include areas not currently subject to review. (page 55)

Our review also disclosed that the State Board of Accountancy has been substandard in its encouragement and use of public input in its operations. Information regarding proposed rules, regulations and legislative changes has primarily been provided to registrants and not the consumer. (page 75)

Our review revealed the State Board of Accountancy can reduce operating costs by approximately \$28,000 over a four-year period by adopting a biennial registration cycle and by automating the registration process and maintenance of investigative files. In addition, State general fund interest earnings can be increased by as much as approximately \$27,000 in four years. (page 81)

Finally, an analysis of entrance requirements revealed that five areas including education, examination, age, residency and moral character are assessed before persons are certified by the State Board of Accountancy. (page 89)

It is recommended that:

1. The performance of the attest function be limited to individuals approved by the State Board of Accountancy and, therefore, required to adhere to the American Institute of Certified Public Accountants standards for auditing and accounting principles. (page 49)
2. The Public Accountant classification be eliminated through designation of the classification as a "dying class" that will allow current certificate holders to retain their certificates until they no longer wish to do so. (page 54)

3. The State Board of Accountancy request an Attorney General's opinion regarding the Board's legal authority to expand its quality review program to include audit reports and financial statements performed for commercial and nonprofit organizations and corporations by certified accountants. Within 90 days after receiving the Attorney General opinion, the Board should formulate a policy regarding the expansion of its quality review program and communicate this policy to appropriate Senate and House of Representatives committees. (page 73)
4. The Board adopt methods to encourage public input and participation in the promulgation of rules and regulations and the development of legislative proposals. (page 80)
5. ARS 32-730 requiring annual registration be amended to allow less frequent registration. Legislature and the Governor approve the State Board of Accountancy budget to include costs for automating the processing of data. The Board review methods for automation and implement the method with maximum cost savings and flexibility for future needs. (page 88)

INTRODUCTION AND BACKGROUND

In response to a September 19, 1978, resolution of the Joint Legislative Budget Committee and a January 18, 1979, resolution of the Joint Legislative Oversight Committee, the Office of the Auditor General has conducted a performance audit as part of the sunset review of the State Board of Accountancy in accordance with ARS 41-2351 through 41-2374.

The State Board of Accountancy is composed of five members, four of whom are required by Arizona statute* to be Certified Public Accountants and one member to represent the public at large.

The Board is responsible for the administration and enforcement of Arizona laws concerning the practice of accounting. Board duties include:

1. Administration of initial examination to be a certified accountant.
2. Issuance of certificates to individuals meeting education, testing and experience requirements.
3. Annual registration of certified individuals, partnerships and professional corporations.
4. Resolution of complaints and violations of Arizona accountancy laws.

The Board and its office are funded through fees charged for examination, certification and registration. Ten percent of the fees received are deposited in the state general fund while the remaining ninety percent are used for Board operations within the limits of an annual budget approved by the legislature.

Table 1 summarizes the actual fee receipts, expenditures and full-time equivalent employees of the State Board of Accountancy for fiscal years 1975-76 through 1977-78 and projections for fiscal years 1978-79 and 1979-80.

* Appendix I contains selected Arizona Statutes regarding the accountancy profession.

TABLE 1

ACTUAL AND PROJECTED FEE RECEIPTS,
EXPENDITURES AND FULL-TIME EQUIVA-
LENT EMPLOYEES (FTE) FOR THE STATE
BOARD OF ACCOUNTANCY DURING FISCAL
YEAR 1975-76 THROUGH 1979-80

Fiscal Year	<u>Actual</u>			<u>Projected</u>	
	<u>1975-76</u>	<u>1976-77</u>	<u>1977-78</u>	<u>1978-79</u>	<u>1979-80</u>
Net Receipts (fees)*	\$80,180	\$127,530	\$152,540	\$145,420	\$205,860
Expenditures	<u>83,420</u>	<u>108,620</u>	<u>136,880</u>	<u>160,600</u>	<u>222,200</u>
Change in Fund Balance	(3,240)	18,910	15,660	(15,180)	(16,340)
Beginning Fund Balance	<u>36,200</u>	<u>32,960</u>	<u>51,870</u>	<u>67,530</u>	<u>52,350</u>
Ending Fund Balance	<u>\$32,960</u>	<u>\$ 51,870</u>	<u>\$ 67,530</u>	<u>\$ 52,350</u>	<u>\$ 36,010</u>
Full-Time Equivalent Employees	<u>3</u>	<u>3</u>	<u>5</u>	<u>7</u>	<u>7</u>

Accounting Profession Defined

Accounting is defined in Arizona law** as:

"any accounting service, including recording and summarizing financial transactions, analyzing and verifying financial information, reporting of financial results to an employer, clients or other parties and rendering of tax and management services to an employer, clients or other parties."

According to the American Institute of Certified Public Accountants:

"Accounting is a service activity. Its function is to provide quantitative information, primarily financial in nature, about economic entities that is intended to be useful in making economic decisions...Through the financial accounting process, the myriad and complex effects of the economic activities of an enterprise are accumulated, analyzed, quantified, classified, recorded, summarized and reported..."

Accountants are employed in government, private industry, education and in public accounting (the offering of accounting services to the general public). Public accounting can include a wide range of services including tax and management services, recording and analyzing financial data and the audit or attest function.

* Amount is net after depositing ten percent of the amount received in the state general fund.

** State law as amended in 1979.

The recording and analyzing of financial data includes establishing, modifying or maintaining accounting systems. Tax services include tax consulting, tax planning and tax return preparation while management services may be analyzing markets, product and market feasibility, consumer attitudes, actuarial and general management consulting. The attest function is the performance of an audit and expression of an opinion on the financial statements of an organization.

Regulation of the Accounting Profession

The first legislation regulating accountancy in the United States was established by the State of New York in 1896. In 1919 Arizona legislators passed the first Arizona accountancy law and created the Board of Accountancy, the forerunner of the present Arizona State Board of Accountancy. By 1925 all states, including Arizona, had some form of accountancy legislation.

As of March 1979, 40 of the 50 states (80 percent) have enacted legislation that restricts the performance of the attest function to license holders. This type of legislation is called a "licensing" law. Ten other states (20 percent), including Arizona, restrict the use of the titles Certified Public Accountant, their abbreviations and similar titles to the certificate holder through a "reserve of title" law.*

Arizona law provides for two types of certificates to be issued. One, the Certified Public Accountant, requires passage of a national examination, appropriate education and two years of acceptable experience. The other, Public Accountant, requires passage of certain subjects of the national examination plus specified educational and experience requirements. Individuals meeting these requirements can be certified and are then allowed to use the title "Certified Public Accountant" or "Public Accountant."

* Appendix II contains a comparison of state accountancy laws.

Both the examination for proficiency and the standards for performance in accountancy that the State Board of Accountancy has adopted are developed and updated nationally through the American Institute of Certified Public Accountants (AICPA). The role of the Board includes the administration of the national examination in Arizona and interpretation of the AICPA standards in cases of complaint or violation of Arizona accountancy law.

The Board has an advisory committee of four members not less than three of whom must be Public Accountants active in public practice in this state. Committee responsibilities are to advise and aid the Board in matters affecting Public Accountants and to vote as a body with the Board on matters pertaining to Public Accountants.

The Board's responsibilities for regulating the accountancy profession in Arizona have steadily expanded as the number of certificate holders has increased. Table 2 summarizes this growth for fiscal years 1975-76 through 1977-78 and its projected continuation through fiscal year 1979-80.

TABLE 2
ACTUAL AND PROJECTED EXAMINATION,
CERTIFICATION AND CERTIFICATE RENEWAL
ACTIVITY OF ARIZONA STATE BOARD
OF ACCOUNTANCY FISCAL YEARS 1975-76
THROUGH 1979-80

<u>Fiscal Year</u>	<u>Candidates Examined</u>		<u>Certificates Granted</u>		<u>Registrations Renewed</u>	
	<u>Number</u>	<u>Percentage Increase Over 1975-76</u>	<u>Number</u>	<u>Percentage Increase Over 1975-76</u>	<u>Number</u>	<u>Percentage Increase Over 1975-76</u>
1975-76	735		252		1927	
1976-77	894	22%	227	(10)%	2048	6%
1977-78	981	33	284	13	2273	18
1978-79	1150	56	219	27	2240	27
1979-80	1250	70	356	41	2600	35

In addition, the initiation by the Board of an active quality monitoring and review program has also increased the level of the Board's activity. Using the services of a contracted investigator, the Board has reviewed publicly filed audit reports for compliance with accountancy standards. If serious violations are detected, the Board enters motions in the public's behalf and institutes disciplinary proceedings.

The Office of the Auditor General expresses its gratitude to present and former members of the State Board of Accountancy and its staff for their cooperation, assistance and consideration during the course of our audit.

SUNSET FACTORS

In accordance with ARS 41-2351 through 41-2374, nine factors were considered to determine, in part, whether the State Board of Accountancy should be continued or terminated.

These factors are:

1. Objective and purpose in establishing the Board,
2. The degree to which the Board has been able to respond to the needs of the public and the efficiency with which it has operated,
3. The extent to which the Board has operated within the public interest,
4. The extent to which rules and regulations promulgated by the Board are consistent with the legislative mandate,
5. The extent to which the Board has encouraged input from the public before promulgating its rules and regulations and the extent to which it has informed the public as to its actions and their expected impact on the public,
6. The extent to which the Board has been able to investigate and resolve complaints that are within its jurisdiction,
7. The extent to which the attorney general or any other applicable agency of state government has the authority to prosecute actions under enabling legislation,
8. The extent to which the Board has addressed deficiencies in their enabling statutes which prevent them from fulfilling their statutory mandate, and
9. The extent to which changes are necessary in the laws of the Board to adequately comply with the factors listed in this subsection.

SUNSET FACTOR: OBJECTIVE AND PURPOSE
IN ESTABLISHING THE BOARD

The purpose for the State Board of Accountancy has been defined by Arizona Revised Statutes. The duties of the Board follow:

- 1) The Board shall issue a certificate of certified public accountant or public accountant to any person meeting specified requirements. (ARS 32-721-22)
- 2) Examination of persons applying for certificates shall be held within the state, as the Board decides, at least once a year. (ARS 32-723)
- 3) The Board may waive examination of and may issue a certificate of certified public accountant or public accountant to anyone who is a holder of a valid and unrevoked certificate, from the state or foreign country of original issue. (ARS 32-727)
- 4) The Board shall each year require every certified public accountant, every public accountant, every partnership and every professional corporation to register with the Board and pay a registration fee. (ARS 32-730)
- 5) After notice and hearing, the Board may revoke or suspend any certificate or may censure the holder for any one or any combination of causes including:
 - a. Conviction of a felony where civil rights have not been restored.
 - b. Conviction of any crime which has a reasonable relationship to the practice of accounting.
 - c. Fraud or deceit in obtaining a certificate.
 - d. Dishonesty, fraud or continuing negligence in the practice of accounting.
 - e. Cancellation, revocation or suspension of certificate or other authority to practice or refusal to renew the certificate or other authority to practice as a certified public accountant by any other state or foreign country.

- f. Violation of accountancy law or knowing violation of rules and regulations promulgated by the Board.
 - g. Suspension or revocation for cause of the right to practice before any governmental body or agency. (ARS 32-741)
 - h. Final action in a civil or administrative proceeding where a court or agency makes findings of accounting violations, dishonesty, fraud, misrepresentation or breach of fiduciary duty or fraud.
- 6) The Board may initiate proceedings under accountancy law, for cause, either upon its own motion or a verified complaint. (ARS 32-743)
 - 7) Upon application in writing and after hearing, the Board may issue a new certificate to a certified public accountant or public accountant whose certificate shall have been revoked or may permit registration of anyone whose certificate has been suspended or may reissue certificates or modify suspension of a certificate. (ARS 32-748)
 - 8) The Board shall establish and collect a uniform fee from each applicant for an examination and from each applicant for a certificate. (ARS 32-729)
 - 9) The Board may adopt and amend regulations for the conduct of its affairs and administration of accountancy law. The Board may also prescribe and amend rules of conduct appropriate to establish and maintain a high standard of competence, independence and integrity in public accounting. (ARS 32-703)

According to Board members, the overall objective of accountancy law and the Board is to identify to the public those accountants that have attained and continue to possess a minimal level of skill in the practice of accounting.

Specific operational objectives established by the Board in 1977 were:

- Obtain adequate long-range financing.
- Determine type and number of personnel needed for enforcement.
- Continue quality control program.
- Review areas required for continued competence and recommend to the Legislature any needed changes.
- Review and initiate an office organization capable of handling the Board's future needs.
- Review rules that need revising and hold hearings to amend those rules on a timely basis.

SUNSET FACTOR: THE DEGREE TO WHICH THE
BOARD HAS BEEN ABLE TO RESPOND TO THE
NEEDS OF THE PUBLIC AND THE EFFICIENCY
WITH WHICH IT HAS OPERATED

The State Board of Accountancy has actively responded to the public's need for competent, accurate accounting services through the use of a nationally recognized examination for potential certificate holders, scrutiny of applicants' experience and educational background and an active program to enforce accountancy laws and Board adopted standards of performance. The efficiency of Board operations can, however, be improved through use of automated equipment and re-distribution of the workload. (page 81)

Of particular note is the Board's initiative in monitoring publicly filed accounting reports for compliance with accountancy laws, rules and regulations. If a certified accountant's work is substandard, the Board imposes sanctions that can include suspension or revocation of certificate, restriction of practice, peer review of work performed or continuing education.

In cases of complaints or publicly known wrongdoing, the Board institutes proceedings to investigate and if valid, discipline the certificate holder. The Board has reviewed a steadily increasing number of investigations resulting from public and board initiated complaints. Table 3 summarizes investigations, revocations, suspensions and consent order sanctions from fiscal year 1975-76 through 1977-78.

TABLE 3

INVESTIGATIONS OF ACCOUNTANCY LAW, RULE
OR REGULATION VIOLATIONS AND RESULTING
REVOCATIONS, SUSPENSIONS AND CONSENT
ORDER SANCTIONS AND CEASE AND DESIST
ORDERS BY THE STATE BOARD OF
ACCOUNTANCY FOR CALENDAR YEARS 1976,
1977 AND 1978 AND THE FIRST QUARTER
OF 1979

INVENTORY OF INVESTIGATIONS

	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>1979*</u>
Beginning Investigations in Process	14	32	51	64
New Investigations	<u>58</u>	<u>61</u>	<u>91</u>	<u>19</u>
Total Investigations	72	93	142	83
Investigations Completed	<u>40</u>	<u>42</u>	<u>78</u>	<u>40</u>
Ending Investigations in Process	<u>32</u>	<u>51</u>	<u>64</u>	<u>43</u>

SANCTIONS AND ORDERS IMPOSED

	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>1979*</u>
Revocations	1	1	3	2
Suspensions	1	-	4	2
Other Disciplinary Sanctions	2	12	8	2
Cease and Desist Orders	<u>13</u>	<u>12</u>	<u>4</u>	<u>2</u>
Totals	<u>17</u>	<u>25</u>	<u>19</u>	<u>8</u>

* 1st Quarter of 1979

(For a discussion of the Board's enforcement of accountancy laws and standards of performance, see page 55.)

The administrative efficiency of the registration, complaint and reciprocity certification processes can be improved. Cost savings of up to \$28,000 over a four-year period could result from automated processing of data and redistribution of the workload generated by the annual registration process. In addition, State general fund interest earnings can be increased by as much as approximately \$27,000 in four years. (For a discussion of this issue, see page 81.)

SUNSET FACTOR: THE EXTENT TO WHICH THE BOARD
HAS OPERATED WITHIN THE PUBLIC INTEREST

The Board's actions appear to be consistently within the public interest. The Board has received both national and local recognition for its efforts to enforce accountancy law and adopted standards of performance. In addition, the Board has initiated interagency meetings to discuss accountancy issues and problems, and has used volunteer committees to supplement its resources.

The U.S. Securities and Exchange Commission, in a 1978 report to Congress on the regulation of the accounting profession,* praised the Arizona State Board of Accountancy and stated, in part:

"A few states, notably Arizona, Colorado and Florida, have begun relatively ambitious monitoring, review and enforcement programs." (Emphasis added)

Mr. James C. Sell, Director of Regulations for the Arizona Corporation Commission, in a letter to the Office of the Auditor General dated March 1, 1979** stated, in part:

"The aggressive actions taken by the State Board of Accountancy over the past two and one-half years has greatly helped this Agency in upgrading the quality of the accounting work found in public registrations...The Division believes the continued existence of the State Board of Accountancy is vital to the protection of Arizona investors." (Emphasis added)

* Appendix III contains the relevant text of the Congressional report by the Securities and Exchange Commission.

** Appendix IV contains the letter from the Arizona Corporation Commission.

In 1978, the Board initiated quarterly meetings with other state agencies, such as the Corporation Commission, interested in maintaining quality accounting services. These meetings are held informally to discuss mutual concerns and to exchange information.

Also notable is the Board's use of two volunteer committees which provide additional resources in regulating accounting services. A five-member Complaint Committee, consisting of three certified accountants, a lawyer and a banker, conducts a preliminary review of complaints investigated and provides the Board with a recommendation on any action needed. A three-member Administrative Committee conducts a preliminary review of certificate applicants' education and work experience and provides recommendations to the Board.

SUNSET FACTOR: THE EXTENT TO WHICH RULES
AND REGULATIONS PROMULGATED BY THE BOARD
ARE CONSISTENT WITH THE LEGISLATIVE MANDATE

Based upon a review of legislation (ARS Chapter 6), it appears that the Board, with one exception, has promulgated rules and regulations consistent with legislative mandate.

The one exception is rule R4-1-42 which has requirements for reciprocity beyond those stated in the law.

ARS 32-727 states, in part:

"The board may waive the examination of and may issue a certificate of certified public accountant or public accountant to any person who is the holder of a valid and unrevoked certificate, from the state or foreign country of original issue...provided the applicant meets the requirements set forth in Section 32-721, paragraphs 1, 2 and 5."

An additional phrase was added to rule R4-1-42 which states:

"...meets the requirements set forth in Section 32-721.A. 1, 2 and 5, and the educational requirements existing in Arizona at the time the applicant was issued the certificate upon which reciprocity is requested..."
(Emphasis added)

The Board had recently held this rule in abeyance and supported legislation to incorporate the additional reciprocity requirement in Arizona law during 1976, 1977 and 1978. During the 1979 legislative session, ARS 32-727 was amended to agree with rule R4-1-42, thus eliminating the inconsistency.

SUNSET FACTOR: THE EXTENT TO WHICH THE AGENCY HAS ENCOURAGED INPUT FROM THE PUBLIC BEFORE PROMULGATING ITS RULES AND REGULATIONS AND THE EXTENT TO WHICH IT HAS INFORMED THE PUBLIC AS TO ITS ACTIONS AND THEIR EXPECTED IMPACT ON THE PUBLIC

The State Board of Accountancy, in the promulgation of its rules and regulations has limited its request for public input to compliance with accountancy law and the Administrative Procedures Act. This has resulted in the encouragement of public input being primarily limited to certified accountants, rather than the public using the services of accountants.

Accountancy law ARS 32-703 states:

"At least thirty days prior to the promulgation of any such rule or amendment, the board shall mail copies of the proposed rule or amendment to each holder of a certificate..." (Emphasis added)

The Board has complied with this law as well as submitting the proposed rule or rule amendment to the Secretary of State as statutorily required. These proposals and the prospective adoption dates are published in the monthly Administrative Digest which is distributed to parties requesting it.

However, as stated by noted law professor and former Dean of the College of Law at Arizona State University; Ernest Gellhorn:

"That existing procedures conform to constitutional minima is not a reason for agencies to fail to explore appropriate procedures for providing effective notice to the affected public and their representatives."

The Board also limits encouragement of public input to the certificate holders and the accountancy profession when developing proposed changes to the accountancy law. (For a full discussion of the issue of public input, see page 75.)

The Board has provided public notice of its meetings, publicly advertised the semiannual accountancy examination and provided information to the press regarding disciplinary actions it has taken. Despite these efforts, 62.4 percent of users of accountant services, who were aware of the Board, as revealed in a survey of 625 users conducted in 1978, did not know or had misconceptions of the State Board of Accountancy's role and powers. (page 78)

A notable accomplishment of the Board in communicating its actions to registrants is the quarterly newsletter, ASBA UPDATE, which details disciplinary actions, certificates granted and other board related affairs.

SUNSET FACTOR: THE EXTENT TO WHICH THE
BOARD HAS BEEN ABLE TO INVESTIGATE AND
RESOLVE COMPLAINTS THAT ARE WITHIN ITS
JURISDICTION

The State Board of Accountancy has actively investigated and resolved complaints brought to its attention and any violations of accountancy law discovered through its own initiative.

The Board reviews each complaint received. Complaints range from fee disputes to corporate fraud. Complaint sources include consumers, certificate holders, and Federal and State agencies. If the Board determines that a complaint is within its jurisdiction, it initiates an investigation.

The Board, through its quality monitoring and review program, initiates investigations to determine if certificate holders are complying with adopted standards of performance. If violations are detected, an investigation is begun. It should be noted that this quality monitoring and review is restricted to publicly filed audits, such as those performed for municipalities and educational institutions. Therefore, the Board's quality monitoring and review does not extend to certified accountants who perform private audits. (For a discussion of investigation procedures and constraints on quality review monitoring, see page 55.)

It should be noted that the ability of the Board to actively pursue both complaint and quality monitoring investigations can potentially be limited by a lack of sufficient funds. Our review revealed that a complex investigation of a large accounting firm involving a public hearing would leave the Board with insufficient monies for other complaint and/or quality review investigations. Table 4 illustrates this situation.

TABLE 4

PROJECTED BUDGET
DEFICIT IF THE STATE BOARD OF
ACCOUNTANCY PERFORMS A COMPLEX
INVESTIGATION OF A LARGE ACCOUNTING
FIRM INVOLVING A PUBLIC HEARING*

Budget Allocation for Investigations (FY 1977-78)	\$22,500
Estimated Potential Cost of A Complex Investigation of a Large Accounting Firm Involving A Public Hearing	<u>(11,600)</u>
Remaining Budget Allocation Available for Complaints and Quality Review	10,900
Estimated Annual Cost for Complaint and Quality Review Investigations During 1977-78	<u>(22,528)</u>
Projected Budget Deficit Resulting From A Complex Investigation	<u>\$(11,628)</u>

As shown above, a complex investigation by the Board would necessitate either a curtailment of complaint and/or quality review investigations or a supplemental budget appropriation.

* Based on historical information from Fiscal Year 1977-78.

SUNSET FACTOR: THE EXTENT TO WHICH THE ATTORNEY GENERAL
OR ANY OTHER APPLICABLE AGENCY OF STATE GOVERNMENT HAS
THE AUTHORITY TO PROSECUTE ACTIONS UNDER ENABLING
LEGISLATION

Based upon a review of legislation (ARS 32-741 through 743, 32-746, 32-747, and 32-750), the Attorney General and the State Board of Accountancy have sufficient authority to prosecute actions under the enabling legislation.

The Attorney General is empowered to institute criminal proceedings for violation of accountancy law through ARS 32-746.B which states:

"Fraudulent audit practice is a class 5 felony, fraudulent audit practices in connection with any securities offering or involving the filing of financial statements with securities agencies of this state is a class 4 felony."

The Board has the necessary authority to prosecute violators of state accountancy laws through several sections of these laws. These sections are:

- ARS 32-741 - Authority to revoke or suspend a certificate granted by the Board or censure the holder of such certificate for various actions, primarily related to fraud or deceit, committed by the certificate holder.
- ARS 32-742 - Authority to revoke the registration to practice public accounting, of a partnership or professional corporation for violations similar to those of individual certificate holders.
- ARS 32-743 - Authority to initiate proceedings under the accountancy law, for cause, either upon its own motion or a verified complaint. Includes the authority to conduct investigations and hold hearings.

- ARS 32-747 - Authority to prosecute persons who are guilty of a class 2 misdemeanor for using titles which suggest certification when, in fact, the person is not certified.
- ARS 32-750 - Authority to make an application to the applicable court to issue an injunction, restraining order or other order to a person who has engaged or is about to engage in a violation of ARS 32-747.

SUNSET FACTORS: THE EXTENT TO WHICH THE BOARD
HAS ADDRESSED DEFICIENCIES IN THEIR ENABLING
STATUTES WHICH PREVENT THEM FROM FULFILLING
THEIR STATUTORY MANDATE

The State Board of Accountancy has proposed legislative changes in the accountancy laws, in the years 1973 through 1979, to address deficiencies the Board perceived in their enabling statutes.

As a result, in 1973, several changes in the accountancy statutes were enacted including the addition of a public member to the Board and adjustments in the examination requirements. During the 1975 through 1978 sessions, the State Board of Accountancy proposed unsuccessful legislative changes that included the following major issues:

- 1975 - Restriction of attest function to certified accountants; continuing educational requirements; deletion of reciprocity for public accountants. (HB 2321)
- 1976 - Restriction of attest function to certified accountants; continuing educational requirements; education requirements for reciprocity; additional certification requirements relating to fraud. (HB 2140)
- 1977 - Similar to 1976 plus suspension for certain actions relating to fraud. (SB 1295)
- 1978 - Similar to 1976 plus definition of accounting and other related terms; rule making power for establishing and maintaining high standards of competence, independence and integrity as required by generally accepted accounting principles, auditing standards and securities law; power to authorize Attorney General to bring action to recover civil penalties. (SB 1220)

During the 1979 legislative session, the Board proposed successful legislation concerning mandatory continuing education, education requirements for reciprocity, reinstatement of revoked certificates, various accounting definitions and other changes. (HB 2131)

SUNSET FACTOR: THE EXTENT TO WHICH CHANGES ARE NECESSARY
IN THE LAWS OF THE BOARD AGENCY TO ADEQUATELY COMPLY WITH
THE FACTORS LISTED IN THIS SUBSECTION

For a discussion of these issues, see pages 44, 54, 73 and 88.

FINDING I

UNLIKE 40 OTHER STATES, ARIZONA DOES NOT LICENSE ACCOUNTANTS. AS A RESULT, THE POTENTIAL FOR FINANCIAL HARM EXISTS FOR THE GENERAL PUBLIC IN ARIZONA.

Under the Arizona accountancy law any individual may provide the public with the same accounting services provided by Certified Public Accountants and Public Accountants. Arizona law only restricts the usage of the titles "Certified Public Accountant" and "Public Accountant" and abbreviations of these titles to persons who have demonstrated a minimum level of skill and competency. This form of state regulation does not constitute licensing but rather a less extreme degree of state regulation called "Reserve of Title." However, in 40 states one accounting service, the attest function, has been recognized to be of such importance to the financial and economic welfare of the general public that its practice is restricted to Certified Public Accountants and Public Accountants. The general public in Arizona does not have this protection from financial harm.

Alternative Methods of State Regulation of Occupations

Licensing is the most extreme form of state occupational regulation. In March 1978, the Council of State Governments* published Occupational Licensing: Questions A Legislator Should Ask. In this publication licensing is defined as:

- * The Council of State Governments is a joint agency of all the state governments - created, supported and directed by them. It conducts research on state programs and problems; maintains an information service available to state agencies, officials, and legislators; issues a variety of publications; assists in state-federal liaison; promotes regional and state-local cooperation; and provides staff for affiliated organizations.

"Licensing is a process by which an agency or government grants permission to an individual to engage in a given occupation upon finding that the applicant has attained the minimal degree of competency required to ensure that the public health, safety, and welfare will be reasonably well protected.

Licensing makes it illegal for anyone who does not hold a license to engage in the occupation, profession, trade, etc. covered by the statute..."

According to the Montana Office of the Legislative Auditor in its 1978 publication entitled, Alternative Methods of Regulating Professions, Occupations, and Industries, there are seven alternative methods of state occupational regulations.

These methods of occupational regulation range from the most extreme, licensing, to the least extreme, no regulation. The appropriate method of regulation for a particular occupation is dependent upon the severity of potential physical or financial harm incompetent or unscrupulous practitioners may inflict upon the general public. The more severe the potential for harm is to the public, the more extreme the appropriate method of state regulation. Conversely, the less severe the potential for harm is to the public, the less extreme the appropriate method of state regulation.

The seven alternative methods of state occupational regulations are listed below in order from the most extreme to the least extreme:

Licensing

- The granting by some government authority of a right or permission to carry on a business or do an act which would otherwise be illegal. The essential elements of licensing are the stipulation of circumstances and individual prerequisites under which permission to perform an otherwise prohibited activity may be granted and the actual determination of permission in specific instances. The latter function is generally an administrative responsibility and includes rule-making authority by some entity. Licensing may also create a mechanism for monitoring an occupation or profession on an ongoing basis. This may entail enforcement decisions made during complaint adjudication, periodic inspections or investigations. Licensing also provides a "police effect" over the regulated profession, trade or industry.

- Practice Restriction - Differs from licensing in that there is no need for an interim body with the general authority to promulgate rules and regulations, and no specific mechanism for monitoring the profession, trade or industry on an ongoing basis.
- Reserve of Title - Any member of the public, who desires, could participate in the regulated occupation. However, the titles of "certified," "licensed," or "registered" would be reserved by law for only those who have met certain statutory requirements. The stipulation of individual prerequisites would be set by the legislature. Requirements such as examination or education may be imposed. An administrative body attached to a state agency or department may also be necessary.
- Limited Statutory Regulation - State regulation of an occupation via statutes which specify certain requirements. Under this alternative, the state would statutorily require an individual to comply with certain measures to protect the public. These measures include requirements such as bonding, errors and omissions insurance, or a recovery fund which would monetarily protect the public in the case of harm or loss through erroneous actions.
- Registration - Allows persons practicing in a profession, trade or industry to register with the state, private or professional association. This alternative provides the public with a list of registered individuals but provides no assurance of the competency of the individuals. Non-registered individuals may participate in the regulated profession, trade or industry.
- Certification* - Requires no state involvement. The profession, trade or industry is responsible for certification requirements and procedures. Certification acts as an identification measure only, indicating that the individual has complied with certain requirements.
- No Regulation - No regulation by the state or direct regulation by the profession, trade or industry.

* The Council of State Governments defines "Certification" as a form of regulation which grants recognition to individuals who have met predetermined qualifications set by a state agency. Only those who meet the qualifications may legally use the designated title. However, noncertified individuals may offer similar services to the public as long as they do not describe themselves as being "certified."

For our purposes we have classified this method of occupational regulation as "Reserve of Title."

Professional and Occupational

Regulation in Arizona

In Arizona 85 professional and occupational areas are regulated. Practitioners in 72 (85 percent) of the professions and occupations are licensed; 12 (14 percent) have reserved titles; and one (1 percent) is registered. Table 5 lists the type of regulation for these 85 professions and occupations.

TABLE 5

PROFESSIONAL* AND OCCUPATIONAL REGULATION IN ARIZONA

<u>Regulated Professions</u>	<u>Type of Regulation</u>
CERTIFIED PUBLIC ACCOUNTANT	Reserved Title
PUBLIC ACCOUNTANT	Reserved Title
Architect	Licensure
Assayer	Reserved Title
Attorney at Law	Licensure
Barber	Licensure
Chiropractor	Licensure
Cosmetologist	Licensure
Cosmetologist**	Licensure
Dental Hygienist	Reserved Title
Dental Laboratory Technician	Licensure
Dentist	Licensure
Denturist	Licensure
Doctor of Medicine	Licensure
Embalmer	Licensure
Engineer	Licensure
Finger Weaver	Licensure
Funeral Director	Licensure
Geologist	Licensure
Hair Stylist	Licensure
Manicurist	Licensure
Naturopath	Licensure
Optometrist	Licensure
Osteopath Physician and Surgeon	Licensure
Pharmacist	Licensure
Pharmacist Intern	Licensure
Physical Therapist	Licensure
Physician's Assistant	Licensure
Podiatrist	Reserved Title
Practical Nurse	Licensure
Psychologist	Reserved Title
Registered Nurse	Reserved Title
Student Intern or Resident	Licensure
Surveyor	Registration***
Teacher, Administrative Officer	Reserved Title
Veterinarian	Reserved Title
	Licensure
<u>Regulated Occupations</u>	
Ambulance Driver and Attendant	Reserved Title
Agriculture Pest Control Advisor	Licensure
Boxing and Wrestling Personnel	Licensure
Cemetery Broker	Licensure
Cemetery Salesman	Licensure
Citrus Broker	Licensure
Citrus Commission Merchant	Licensure
Citrus Dealer	Licensure
Citrus Packer	Licensure
Citrus Shipper	Licensure
Collection Agencies	Licensure
Contractor	Licensure
Court Reporter	Reserved Title
Dispensing Optician	Licensure
Egg Dealer	Licensure
Egg Manufacturer	Licensure
Egg Producer	Licensure
Emergency Medical Technician	Reserved Title
Escrow Agent	Licensure
Hay and Feed Grain Broker	Licensure
Hearing Aid Dispenser	Licensure
Insurance Agent	Licensure
Insurance Adjustor	Licensure
Insurance Broker	Licensure
Insurance Solicitor	Licensure
Meat Processor, Wholesaler or Jobber	Licensure
Midwife	Licensure
Mobile and Manufactured Housing	
Standards: Dealer	Licensure
Installer	Licensure
Manufacturer	Licensure
Mortgage Broker	Licensure
Motor Carrier Transportation Agent	Licensure
Motor Vehicle Dealer and Wrecker	Licensure
Motor Vehicle Operator and Chauffeur	Licensure
Polygraph Examiner	Licensure
Private Investigator	Licensure
Private Security Guard Service	Licensure
Private Security Guard	Licensure
Professional Driver Training School	Licensure****
Instructor	Licensure****
Public Weighmaster	Licensure
Racing Officials and Personnel	Licensure
Radiologic Technologists	Licensure
Real Estate Broker	Licensure
Real Estate Salesman	Licensure
Securities Dealer and Salesman	Licensure
Structural Pest Control	Licensure
Structural Commercial Application	Licensure
Taxidermist	Licensure
Trapper and Guide	Licensure
Weight and Measure Serviceman	Licensure

* Webster's Seventh New Collegiate Dictionary defines a profession as:

"A calling requiring specialized knowledge and often long and intensive academic preparation." Accordingly, the professional regulatory agencies were determined by a post-high school educational requirement to enter the profession.

** Cosmetologists practicing without compensation have a reserved title.

*** Student interns or residents must meet minimum requirements in addition to registering.

**** Must be licensed only if compensation is received for the service.

It should be noted, as shown in Table 5, that the Certified Public Accountant and Public Accountant constitute two (17 percent) of the 12 reserved titles in Arizona.

Justification for Selecting the
Licensing Method of Regulating
the Attest Function

The attest function is the one accounting service that should be restricted to Certified Public Accountants and Public Accountants.* This conclusion is based upon the following:

- Forty states and several federal agencies currently restrict the attest function to Certified Public Accountants and Public Accountants.
- A number of legal and practical limitations exist in Arizona which have the effect of restricting the attest function to Certified Public Accountants and Public Accountants.
- The severity of potential financial harm incompetent or unscrupulous practitioners may inflict upon the general public.
- Potential users cannot be expected to possess the knowledge needed to properly evaluate the qualifications of those offering service.
- Benefits to the public outweigh any potential harmful effects such as decrease in the availability of practitioners, higher costs of service and restrictions on optimum use of personnel.

* In Occupational Licensing: Questions A Legislator Should Ask, the Council of State Governments identified those questions a state must answer when evaluating the need for licensing an occupation. The questions are:

- (1) whether the unlicensed practice of an occupation poses a serious risk to the consumers' life, health, and safety or economic well-being;
- (2) whether potential users of the occupational service can be expected to possess the knowledge needed to properly evaluate the qualifications of those offering services; and
- (3) whether benefits to the public clearly outweigh any potential harmful effects such as a decrease in the availability of practitioners, higher costs of goods and services, and restrictions on optimum utilization of personnel.

Attest Function Defined

The attest function is the most critical public accounting service affecting the general public. A memorandum* from the Legislative Council, dated May 31, 1979, includes a definition of the attest function and states in part:

"The attest function of an independent auditor is the performance of an audit in accordance with generally accepted auditing standards and expressing an opinion on the financial statements as to the fairness of those statements in representing the financial condition of the audited entity." Arizona State Board of Accountancy v. Keebler, (1977 ct. App.) 115 Ariz. 239.

"The Generally Accepted Auditing Standards and Generally Accepted Accounting Principles of the American Institute of Certified Public Accountants have been adopted by the Arizona Board of Accountancy...The difference between the standards and principles...is that the generally accepted auditing standards involve how an auditor goes about obtaining information, while the generally accepted accounting principles involve the format in which to present the information." (Emphasis added)

National Restrictions on the Practice of

The Attest Function

Although Arizona accountancy law does not restrict the practice of the attest function to Certified Public Accountants and/or Public Accountants, agencies of the federal government and a substantial number of other states have imposed such restrictions. For example, the Securities and Exchange Commission (SEC), which is the primary regulator of publicly held corporations, requires that all publicly held corporations be audited and their financial statements attested to by a licensed accountant, either a Certified Public Accountant or Public Accountant.

* Appendix V contains a full text of the Legislative Council memorandum.

In addition, the General Accounting Office (GAO) in setting standards for governmental audits, has stated:

"When outside auditors are engaged for assignments requiring the expression of an opinion on financial reports of governmental organizations, only fully qualified public accountants should be employed."

The Comptroller General of the United States, has further confirmed the GAO position on the need for qualified accountants:

"Governmental entities provide some of the most diverse and challenging work in the accounting and auditing field. Accordingly, government departments and agencies need the best audit skills obtainable. Authorizing auditors who have not demonstrated that they possess such skills to render opinions on financial statements will not provide the public with the protection it needs."

A number of federal agencies have responded to the GAO declaration and now require independent auditors who express opinions on financial reports of federal funds be licensed accountants. These federal agencies include the United States Treasury Department, which requires revenue sharing recipients to have licensed accountants perform independent audits of their financial statements, the Department of Health, Education and Welfare and Department of Labor, which stipulates that licensed accountants must perform any required audits.

In addition to federal restrictions of the attest function, as of March 22, 1979, 40 of the 50 states have enacted laws restricting the performance of the attest function to Certified Public Accountants and Public Accountants. Table 6 lists the 40 states that have enacted accountancy laws restricting the attest functions to certified accountants, and the states, including Arizona, that have not.

TABLE 6

STATES RESTRICTING AND NOT
RESTRICTING THE ATTEST FUNCTION
TO CERTIFIED ACCOUNTANTS AS OF MARCH 22, 1979*

STATES RESTRICTING THE ATTEST FUNCTION

Alabama	Connecticut	Indiana	Maryland
Alaska	Florida	Iowa	Massachusetts
Arkansas	Georgia	Kentucky	Michigan
California	Hawaii	Louisiana	Mississippi
Colorado	Idaho	Maine	Missouri
Montana	New York	Pennsylvania	Texas
Nebraska	North Dakota	Rhode Island	Utah
Nevada	Ohio	South Carolina	Virginia
New Hampshire	Oklahoma	South Dakota	Washington
New Jersey	Oregon	Tennessee	Wisconsin

STATES NOT RESTRICTING THE ATTEST FUNCTION

ARIZONA	New Mexico
Delaware	North Carolina
Illinois	Vermont
Kansas	West Virginia
Minnesota	Wyoming

* SOURCE: Survey of 50 state boards of accountancy by the Arizona Office of the Auditor General as of March 22, 1979.

Arizona Limitations on the
Practice of the Attest Function

Although Arizona accountancy law does not limit the attest function to licensed accountants, a number of legal and practical limitations exist which have the effect of restricting the attest function.

The Securities Division of the Arizona Corporation Commission performs a similar regulatory function for publicly owned Arizona corporations as does the Federal Securities Exchange Commission. ARS 44-1872 requires an issuer of securities to file financial statements prepared by a Certified Public Accountant or Public Accountant. In addition, 26 other Arizona statutes specify Certified Public Accountants (CPA) or Public Accountants (PA) shall provide certain accounting services, primarily related to the attest function or may provide these accounting services in lieu of others. These 26 statutes include audits of cities and towns, escrow agents, hospitals, public transit authorities, state compensation, police pension and other public funds.*

In addition to these legal restrictions, many financial institutions in Arizona impose de facto restrictions upon the practice of the attest function. For example, Mr. Bud Clark, Assistant Vice-president, of Valley National Bank stated in a February 7, 1979, letter to the Office of the Auditor General that:

"Basically our policy states that all credit facilities to business entities of \$250,000.00 or more, the borrower and guarantors (if any) must submit a minimum of three years annual financial statements with unqualified opinions by a recognized competent certified public accountant."**
(Emphasis added)

Ms. Tina A. Zeller, Assistant Vice-president of First National Bank of Arizona, in a letter to the Office of the Auditor General dated February 8, 1979, stated:

"When a certified financial statement is received the loan officer relies heavily on the figures in making the loan decision. He also trusts that the presentation adheres to the AICPA standard (generally accepted accounting principles) and is in fair and consistent form unless otherwise noted."** (Emphasis added)

* Appendix VI is a memorandum from Legislative Council dated March 14, 1979, that details these statutes.

** Appendix VII contains the full text of these letters and similar ones from other Arizona financial institutions.

As a result of these legal and practical restrictions, the actual amount of the attest function being performed in Arizona by non-Certified Public Accountants and Public Accountants is relatively insignificant. (page 40)

The Severity of Potential Financial
Harm Incompetent or Unscrupulous
Practitioners May Inflict Upon
The General Public

According to Legislative Council in a memorandum dated April 13, 1979:

"It is evident that the only accounting function which is sufficiently endowed with public interest to justify legal restriction is the auditing and expression of opinion on financial statements on which third parties rely."*

The critical nature of the financial audit stems from the reliance others place on its accuracy and completeness and the independence of the auditor. Audited financial statements are a primary means of communicating financial information to those outside an entity. The financial statements most frequently prepared are (a) balance sheet or statement of financial position, (b) income or earnings statement, (c) statement of retained earnings, (d) statement of other changes in owners' or stockholders' equity, and (e) statement of changes in financial position (source and application of funds). Persons outside the organization rely on audited financial statements to be accurate, complete and factual.

Audited financial statements are intended to provide information that is useful in making business and economic decisions. Individuals, enterprises, markets and governments in making decisions use audited financial statement information to evaluate various alternatives and assess the expected returns, costs and risks.

* Appendix VIII is full text of this memorandum.

The users of financial statement information include business owners, lenders, suppliers, potential investors and creditors, employees, management, directors, customers, financial analysts, brokers, underwriters, stock exchanges, lawyers, economists, taxing authorities, regulatory authorities, legislators, news media, labor unions, trade associations, business researchers and the general public. Users most directly concerned with the operation of any entity include owners, creditors and employees in that they invest cash, goods or services in an entity with the expectation of obtaining sufficient cash in return to make the investment worthwhile. According to AICPA Professional Standards, "Objectives of Financial Accounting and Financial Statements and General Financial Accounting," financial reports and statements provide these users with the evenhanded and unbiased information necessary to form judgments about the ability of the enterprise to service, adapt, grow and prosper amid changing economic conditions.

As noted in the AICPA Professional Standards, "Objectives of Financial Reporting by Business Enterprises," when financial statements are audited, users will believe they are factual and dependable for decision-making:

"Independent auditors commonly examine or review financial statements and perhaps other information, and both those who provide and those who use that information often view an independent auditor's opinion as enhancing the reliability or credibility of the information."

If generally accepted auditing standards and generally accepted accounting principles, as specified by the AICPA, are not followed, an accountant can substantially misrepresent an entity's financial position. The general public, relying upon this financial information, would then reach inaccurate conclusions, invest or extend credit to the entity and increase the likelihood that financial harm would occur. Two notable national examples, McKesson Robbins, Incorporated and Equity Funding Corporation of America, demonstrate the financial harm that can occur when inadequate audits are performed.

In 1939 a serious fraud was disclosed in the accounts of McKesson Robbins, Incorporated, which had for years been audited by a firm of independent auditors. Approximately \$19 million in fictitious inventories and accounts receivable were listed in the balance sheet total of \$87 million in assets, a 21.8 percent misrepresentation. The fictitious assets were supported by invoices, advices, shipping and other documents using fictitious names; records of fictitious transactions; forged contracts; guarantees and supposedly independent credit rating reports. After an SEC inquiry into this fraud, confirmation of receivables and physical observation of inventory were incorporated into mandatory auditing standards.

In 1972 Equity Funding Corporation of America was discovered to have created \$120 million in nonexistent assets and to have sold, to reinsurers, up to \$2 billion in fraudulent life insurance policies. Auditors apparently failed to sufficiently confirm assets and data processing reports on loans and were misled by Equity Funding officials.

In Arizona in 1975, Lincoln Thrift Association, the related U. S. Thrift Association and 53 subsidiaries were discovered to be involved in fraud of the public. In a prospectus for the Arizona Corporation Commission, the accountant for Lincoln Thrift significantly departed from generally accepted accounting principles, committed reporting deficiencies and failed to comply with generally accepted auditing standards by inappropriately issuing an unqualified opinion on the financial statements for calendar years 1971, 1972, 1973 and six months of 1974. The two firms had more than 20,000 investors and liabilities exceeded assets by \$32.5 million. In December 1975 the firms were placed in federal receivership.

Certified Public Accountants and Public Accountants in Arizona are legally required to comply with the AICPA standards adopted by the State Board of Accountancy. Other practicing accountants are not required by law to comply with the AICPA standards. If a certified accountant fails to comply with the AICPA standards the Board can revoke or suspend the accountant's use of the "Reserved Titles" under Arizona law. However, this authority does not extend to non-titled accountants. As a result, the state of Arizona cannot currently restrict the most critical accounting service - the attest function - to persons with demonstrated competence. Further, persons whose titles have been revoked by the Board for failure to comply with AICPA standards, as in the instance of the accountant for Lincoln Thrift Association, can still legally perform an audit and express an opinion on financial statements.

Potential Users Cannot Be
Expected to Possess the
Knowledge Needed to Properly
Evaluate the Qualifications
of Those Offering Service

The objective of an auditor in performing the attest function is, according to AICPA Professional Standards for Field Work:

"...to form an opinion on whether the financial statements present fairly (the) financial position, results of operations and changes in financial position in conformity with generally accepted accounting principles consistently applied. Consequently, under generally accepted auditing standards the independent auditor has the responsibility to plan his examination, to search for errors or irregularities that would have a material effect on the financial statements, and to exercise due skill and care in the conduct of that examination."

The audit procedures and standards which must be followed in order to accomplish the above objective of the attest function appears to be sufficiently technical and complex to preclude members of the general public who are not financially sophisticated from evaluating the qualifications of those offering the service. The attest function requires the auditor to apply a series of analytical reviews of financial information. These reviews include the following:

- Comparison of the financial information with information for comparable prior period(s).
- Comparison of the financial information with anticipated results (for example, budgets and forecasts).
- Study of the relationships of financial data that would be expected to conform to a predictable pattern based on the entity's experience.
- Comparison of the financial information with similar information regarding the area in which the entity operates.
- Study of relationships of the financial information with relevant nonfinancial information.
- Investigation and documentation of any material irregularities.

Most of the auditor's work consists of obtaining and examining accounting data and corroborating information. Such information includes:

- source documents of original entry
- general and subsidiary ledgers
- accounting manuals
- worksheets explaining allocations of costs, computations and reconciliations
- documentary material such as checks, invoices, contracts and minutes of meetings
- confirmations and other written representations by knowledgeable people
- information obtained by inquiry, observation, inspection and physical examination.

In summary, to reach a conclusion on the financial statements, the auditor:

- tests underlying accounting data by analytical review
- retraces the procedures and steps followed in the accounting process and in developing work sheets and allocations
- recalculates and
- reconciles related types and applications of financial information.

Finally, the auditor prepares a report which must include the following to be in compliance with AICPA professional standards:

- 1) Whether the financial statements are presented fairly in accordance with generally accepted accounting principles,*
- 2) that the accounting principles have been used consistently in the time period reflected in the financial statements and that the information is comparable to previous time periods,
- 3) whether the financial statements adequately disclose all matters needed to make them sufficiently informative to the readers, and
- 4) either an opinion regarding the financial statements "as a whole" or a statement that an opinion cannot be expressed.

* According to the AICPA, the phrase "generally accepted accounting principles" can be defined as "a technical accounting term which encompasses the conventions, rules, and procedures necessary to define accepted accounting practice at a particular time. It includes broad guidelines of general application, and detailed practices and procedures..."

General accounting principles define which economic resources and obligations should be recorded as assets and liabilities, which changes in them should be recorded, when these changes should be recorded, how the recorded assets and liabilities and changes in them should be measured, what information should be disclosed, how it should be disclosed, and which financial statements should be prepared...

The auditor's judgment is applied in determining 'fairness' within this framework of 'generally accepted accounting principles' that represent a uniform standard for judging the financial statements."

Therefore, although not surveyed due to the complexity of identifying the users of the attest function, it appears that the procedures, standards and reporting aspects of the attest function are sufficiently complex and technical to preclude assessment of the practitioners professed qualifications by anyone other than the most financially sophisticated users.

Benefits to the Public Outweigh
Any Potential Harmful Effects
Such as Decrease in the Availability
of Practitioners, Higher Costs of
Service and Restrictions On Optimum
Use of Personnel

It does not appear that restricting the attest function to Certified Public Accountants and Public Accountants would decrease the availability of practitioners, result in higher costs of service or cause any additional restrictions on the optimum use of personnel.

In a survey conducted by the Office of the Auditor General* of Arizona, titled and non-titled accountants identified the type and amount of accounting services offered to the general public. Table 7 summarizes the services provided by Arizona titled and non-titled accountants and the percentage each service represents of the accountants' total practice.

* Appendix IX contains the complete results of this survey.

TABLE 7

PERCENTAGE OF TOTAL ACCOUNTING PRACTICE
ATTRIBUTABLE TO VARIOUS ACCOUNTING
SERVICES FOR TITLED AND NON-TITLED ARIZONA
ACCOUNTANTS BY ACCOUNTING FIRM SIZE

Titled and Non-Titled Accountants By Firm Size	Percentage of Total Accounting Practice By Type of Accounting Service*								Number of Responses
	Attest Auditing	Other Auditing	Income, Estate and Gift Tax	Other Tax	Accounting Bookkeeping	Management Services	Other Services	TOTAL	
Certified Public Accountants									
Sole Practitioners	13.7%	2.4%	46.7%	5.1%	21.7%	7.1%	3.3%	100.0%	75
2-5 Employees	8.3	2.6	35.0	7.8	38.2	6.9	1.2	100.0	138
6-12 Employees	21.3	3.9	30.1	7.0	29.0	6.9	1.8	100.0	122
13-25 Employees	25.1	3.8	32.1	6.6	22.1	8.2	2.1	100.0	63
Over 25 Employees	49.5	4.5	22.5	2.4	11.3	8.9	.9	100.0	77
Average Total Percentage	21.1%	3.4%	33.2%	6.1%	26.7%	7.4%	1.8%	100.0%	475
Public Accountants									
Sole Practitioners	.5%	1.2%	31.3%	7.5%	59.5%	-	-	100.0%	7
2-5 Employees	1.8	3.2	29.5	9.5	52.3	3.7	-	100.0	11
6-12 Employees	-	-	-	-	-	-	-	-	-
Over 25 Employees	-	-	-	-	-	-	-	-	-
Average Total Percentage	1.3%	2.4%	30.2%	8.7%	55.1%	2.3%	-	100.0%	18
Non-Titled Accountants									
Sole Practitioners	.7%	-	40.6%	8.2%	46.6%	3.1%	.8%	100.0%	40
2-5 Employees	.2	1.4	31.3	9.1	50.5	5.7	1.8	100.0	86
6-12 Employees	-	.2	27.6	9.2	53.5	9.0	.5	100.0	12
13-25 Employees	3.0	57.0	5.0	20.0	15.0	-	-	100.0	1
Over 25 Employees	-	-	-	-	-	-	-	-	-
Average Total Percentage	.3%	1.3%	33.5%	8.9%	49.4%	5.2%	1.4%	100.0%	139

* Percent of total practice is based on amount of client fees received for performance of each service compared to total fees.

SOURCE: Survey of the Arizona accounting profession by the Office of the Auditor General, March 1979.

As Table 7 illustrates, both titled and non-titled accountants offer all accounting services to the public. However, attest auditing represents a relatively insignificant proportion of non-titled accountants' practices (.3%). Thus, restricting the attest function to titled accountants would not have a significant impact on the availability of practitioners to perform the service.

In addition, since titled accountants generally perform the attest function while non-titled accountants do not, restriction of the attest function to titled accountants would not cause any significant change in the utilization of accounting personnel.

Our survey also revealed that the cost of accounting services appears to be more a function of firm size and not the accountant's title. For example, the average sole practitioner Certified Public Accountant charges less per hour to perform the attest function than does the average Public Accountant and only slightly more than the non-titled accountant. However, the average hourly rate for Certified Public Accountants and non-titled accountants who responded to the survey by the Office of the Auditor General to perform the attest function increases in direct proportion to the size of firm providing the service.* Table 8 summarizes the hourly rates for accounting services charged by Certified Public Accountants, Public Accountants and non-titled accountants by firm size.

* Responses from Public Accountants were limited to two sizes of firm - sole practitioner and firms with 2-5 employees - and for these the average hourly rate was the same.

TABLE 8

SUMMARY OF HOURLY RATES FOR
ACCOUNTING SERVICES CHARGED
BY CERTIFIED PUBLIC ACCOUNTANTS,
PUBLIC ACCOUNTANTS AND NON-TITLED
ACCOUNTANTS BY FIRM SIZE

Titled and Non-Titled Accountants By Firm Size	Average Hourly Rate Charged			Number Responding
	Attest Function	Income, Estate and Gift Taxes	Accounting Bookkeeping	
Certified Public Accountants				
Sole Practitioners	\$28.10	\$34.80	\$22.20	75
2-5 Employees	36.20	36.20	24.60	138
6-12 Employees	38.20	38.50	26.30	122
13-25 Employees	39.40	44.20	29.30	63
Over 25 Employees	44.40	47.30	30.60	77
				<u>475</u>
Public Accountants				
Sole Practitioners	\$35.00	\$29.40	\$26.40	7
2-5 Employees	35.00	33.30	18.60	11
6-12 Employees	-	-	15.00	1
13-25 Employees	-	-	-	-
Over 25 Employees	-	-	-	-
				<u>19</u>
Non-Titled Accountants				
Sole Practitioners	\$26.70	\$23.90	\$19.80	40
2-5 Employees	27.00	28.00	20.80	86
6-12 Employees	-	35.00	30.00	12
13-25 Employees	35.00	40.00	20.00	1
Over 25 Employees	-	-	-	-
				<u>139</u>

SOURCE: Survey of the Arizona accountancy profession, Office of the Auditor General, March 1979. Appendix IX Table 11, contains a complete listing of hourly rates by type of service.

It does not appear that restricting the attest function to titled accountants will result in higher costs of service based upon the similarity of hourly rates charged by titled and non-titled accountants as shown in Table 8 coupled with the relatively insignificant amount of attest auditing now being performed by non-titled accountants in Arizona.

CONCLUSION

Arizona accountancy law now restricts the usage of the titles Certified Public Accountant and Public Accountant to persons approved by the State Board of Accountancy. Lawmakers in 40 other states have determined that this was insufficient protection for the public and have further restricted the attest function to titled accountants. In Arizona anyone can legally perform the attest function without being approved by the State Board of Accountancy. Substantial financial harm can and has occurred when generally accepted standards of accounting and auditing were not followed in the performance of the attest function.

It appears appropriate to restrict the performance of the attest function to titled accountants who have demonstrated a minimum level of competence since the attest function meets the three criteria for licensing outlined by the Council of State Governments, in that:

1. The unlicensed practice of the attest function can result in severe financial harm to the general public.
2. The performance of audit is sufficiently technical and complex to preclude proper evaluation of the audit or the persons offering the service by the general public.
3. Benefits to the public outweigh potential harmful effects such as a decrease in available practitioners, higher costs of the service and further restriction on the usage of available personnel.

Practical restrictions imposed by business and federal and state law restrict the attest function to titled accountants, and result in minimal practice of the attest function by non-titled accountants in Arizona. Therefore, public protection from financial harm would be increased with minimal adverse effect if the attest function were limited to titled accountants.

RECOMMENDATION

Consideration should be given to limiting the performance of the attest function to individuals approved by the State Board of Accountancy. These individuals will, therefore, be required to adhere to AICPA standards for auditing and accounting principles.

Legislation will be needed to implement this recommendation.*

* Appendix V is a memorandum from Legislative Council dated March 14, 1979, stating legislative change is needed to limit the attest function.

FINDING II

THE PUBLIC ACCOUNTANT CLASSIFICATION IS UNNECESSARY

The Arizona State Board of Accountancy grants certificates and has authority over two classes of accountants - Certified Public Accountant (CPA) and Public Accountant (PA).

Our review of the PA classification reveals that there does not appear to be a demonstrated need for the PA designation in Arizona in that -

- Since 1955 only 246 persons have been classified as PAs
- From 1961 to 1978 the number of PAs has declined 39 percent while the number of CPAs has increased 281 percent
- 58 percent of the 91 PAs as of December 31, 1978, had been granted certificates as PAs between 1955 and 1960 without examination through a "grandfather" clause in accountancy law
- Of the 119 persons classified as PAs during the 22 year period from 1957 to 1979, approximately 53 percent subsequently became CPAs
- Arizona is one of only 15 states that currently grants PA certificates
- The accounting services generally provided by PAs do not justify regulation.

History of the PA Classification

The PA classification was established in Arizona in 1933 when the accountancy law was amended to provide that the Board of Accountancy would

"...issue to all accountants of good moral character who were maintaining an office and engaged exclusively in public practice on their own account on January 1, 1933, and who do not qualify under the provisions...of this section, a certificate of authority to practice as a public accountant. This certificate of authority shall not confer any added title and the holder shall be known and styled only as a 'Public Accountant'. Application must be made for this certificate of authority before January 1, 1934." (ARS 67-604, Laws 1933)

The above amendment provided for a one-time granting of PA certificates to persons not qualified to be CPAs and an estimated 56 practicing accountants applied for and were granted PA certificates. No new PA certificates were granted after 1933 until the accountancy law was amended in 1955 to provide for a continuing PA classification. With the enactment of the 1955 law, 137 persons were "grandfathered" (granted PA certificates without having to pass an examination) if a major portion of their income for the previous three years was earned in the practice of accounting.

The 1955 amendment defined the present requirements for CPAs and PAs. The primary difference between the two classifications being that a CPA must pass all four subjects of the AICPA examination (accounting practice, theory of accounts, auditing and commercial law) while a PA must pass either the accounting practice subject of the AICPA examination or the other three subjects. The requirements for CPAs and PAs are contrasted below.

Requirements For
A Certified Public Accountant (ARS 32-721)

A person shall:

- 1) be eighteen years of age, a resident of the state and of good moral character
- 2) has not engaged in conduct that would constitute grounds for certificate revocation or suspension
- 3) obtain score of 75 or better on each subject of the AICPA examination*
- 4) have two years experience as a staff member in the office of a CPA or PA that includes the practice of accounting including examination and reporting of financial statements or a master's degree in accounting or business administration and one year's experience

Requirements For
A Public Accountant (ARS 32-722)

A person shall:

- 1) be eighteen years of age, a resident of the state and of good moral character
- 2) obtain a score of 75 or better on the accounting practice or each of the other subjects given in the AICPA examination
- 3) have the same experience as required for a Certified Public Accountant

It should be noted that since Arizona accountancy law does not restrict the performance of any accounting service, the CPA and PA can perform the same functions.

* To qualify to take the examination, individuals must 1) have, or will within 90 days, have a bachelor's degree with 24 semester hours in accounting, 12 of which must be in intermediate theory or advanced accounting or cost accounting or auditing theory and practice or income taxes and, shall also have 18 additional hours in economics and business administration classes or 2) have, or within 90 days will have, a bachelor's degree and passes an examination by the State Board of Accountancy in accounting, economics, business law, English composition and business mathematics.

Number of Public Accountants Declines

Since the 1955 enactment of the Public Accountant classification, 246 individuals have been granted PA certificates by the Board of Accountancy.

Table 9 summarizes the number of PA certificates granted from 1955 to December 1978, the method of certification, the number of PA certificate holders who subsequently became CPAs and the number of lapsed PA certificates.

TABLE 9

SUMMARY OF THE NUMBER OF PUBLIC ACCOUNTANTS
CERTIFIED AND BY WHAT METHOD, THE NUMBER
OF PA CERTIFICATE HOLDERS WHO SUBSEQUENTLY
BECAME CPA'S AND THE NUMBER OF LAPSED
PA CERTIFICATES FROM 1955 TO DECEMBER 1978

Method of Certification	Number of PA Certificates Granted	Number of PA Certificate Holders Who Subsequently Became Certified Public Accountants	Number of Lapsed PA Certificates	Number of PAs As Of December 1978
Waiver	137	1	83	53*
Examination	107	57	14**	36***
Reciprocity	<u>2</u>	<u>-0-</u>	<u>-0-</u>	<u>2</u>
Total	<u><u>246</u></u>	<u><u>58</u></u>	<u><u>97</u></u>	<u><u>91</u></u>

* Includes 14 individuals over 65 years of age.

** Includes one individual whose PA license was revoked.

*** Includes two individuals over 65 years.

The number of PAs in Arizona reached its peak in 1961 when there were 150 PAs. Since 1961 the number of PAs in Arizona has steadily declined while the number of CPAs has increased dramatically as is illustrated in Table 10.

TABLE 10

COMPARISON OF THE NUMBER
OF PAs AND CPAs IN ARIZONA
FROM 1961 TO 1978

<u>Year</u>	<u>PAs Number</u>	<u>CPAs Number</u>
1961	150	519
1962	144	571
1963	144	640
1964	141	668
1965	143	739
1966	141	777
1967	133	790
1968	128	844
1969	120	891
1970	113	963
1971	108	1,039
1972	104	1,142
1973	98	1,271
1974	95	1,369
1975	91	1,500
1976	95	1,676
1977	90	1,791
1978	92	1,979
Percent of Increase (Decrease)	(39%)	281%

As shown in Table 10 above, since 1961 the number of PAs has decreased from 150 to 92, a decrease of 39 percent, while the number of CPAs has increased from 519 to 1,979, an increase of 281 percent. According to Mr. Gerald Rosen, a member of the Arizona State Board of Accountancy, Public Accountants Advisory Committee, the decline in the number of PAs will continue as the number of "grandfathered" PAs continues to diminish. Mr. Rosen stated:

"...as we (the grandfathered public accountants) continue to die the public accountant class will continue to diminish in size..."

Licensing In Other States

Forty-seven states including Arizona have two classes of accountants. However, in 32 of these states the non-CPA classification is treated as a "dying class" and no new certificates are being granted.

Table 11 summarizes the accounting classifications by state and identifies which states treat the non-CPA as a "dying class".

TABLE 11

SUMMARY OF ACCOUNTING
CLASSIFICATIONS BY STATE*

<u>States With Certified Public Accountants Only</u>	<u>States with Certified Public Accountants and Public Accountants that Treat Public Accountants As A "Dying Class" and The Year The PA Classification Was Established as A "Dying Class"</u>	<u>States with Certified Public Accountants and Public Accountants (Or Other Classification of Accountants)</u>
Delaware	Alabama (1974)	Alaska
Kansas	Arkansas (1980)	ARIZONA
Wyoming	California (1955)	Georgia
	Colorado (1959)	Indiana
	Connecticut (1955)	Iowa
	Florida (1927)	Montana
	Hawaii (1955)	New Hampshire
	Idaho (1976)	New Mexico
	Illinois (1961)	Ohio
	Kentucky (1946)	Oklahoma
	Louisiana (1975)	Oregon
	Maine (1967)	South Carolina
	Maryland (1970)	South Dakota
	Massachusetts (1972)	Tennessee
	Michigan (1926)	Vermont
	Minnesota (1979)**	
	Mississippi (1930)	
	Missouri (1943)	
	Nebraska (1957)	
	Nevada (1960)	
	New Jersey (1977)	
	New York*** (1959)	
	North Carolina (1925)	
	North Dakota (1976)	
	Pennsylvania (1980)	
	Rhode Island (1971)	
	Texas (1947)	
	Utah (1959)	
	Virginia (1928)	
	Washington (1949)	
	West Virginia (1966)	
	Wisconsin (1935)	

* Appendix II is a comparative analysis of state requirements.

** Legislation has passed both houses of Minnesota Legislature and awaiting Governor's signature.

*** Initials "PA" are not permitted in New York. "Public Accountants" must use full title.

It should be noted that North Carolina was the first state to establish the PA Classification as a "dying class" in 1925. Since 1955 there has been a decided trend toward treating the PA as a "dying class" as shown in Table 11.

Services Generally Provided by PAs

Do Not Justify Regulation

A survey of PAs in Arizona conducted by the Office of the Auditor General (page 40) revealed that a preponderance of the work performed by PAs consists of income tax and bookkeeping type services. The Legislative Council, in an April 13, 1979*, opinion stated that income tax and bookkeeping services are not of sufficient public interest to justify regulation. The opinion states in part:

"The attorney general (Arizona, 1970) determined that preparation of income tax returns would not fall under the practice of public accounting. The attorney general concluded that:

1. Freedom to follow any lawful occupation not injurious to others is a fundamental American liberty...
2. The public convenience, prosperity, health, morals or safety was not advanced nor was danger from incompetency decreased by restricting the preparation of income tax returns to certain persons.
3. The preparation of tax returns is not a function of the practice of accounting which is endowed with public interest sufficient to justify regulation..."
(Emphasis added)

* A complete text of this opinion is contained in Appendix VIII.

Bookkeeping, according to the Legislative Council, has generally:

"...been considered separate and different from the practice of public accounting...Bookkeeper...is 'one who keeps accounts: one whose business or vocation is bookkeeping distinguished from accountant.' Bookkeeping is defined as 'a branch of accounting that deals with the systematic classification, recording and summarizing of business transactions in books of account'...One may certainly argue and conclude that legislative regulation of bookkeeping and similar technical services offered by accountants would interfere with the normal right of an individual to deal with anyone he chooses absent a legislative finding that the regulation of bookkeepers is necessary to protect the public welfare." (Emphasis added)

CONCLUSION

Since 1961 the number of Public Accountants (PAs) in Arizona has steadily declined while the number of CPAs has dramatically increased. This trend is expected to continue. The PA classification, in general, is comprised of persons who were certified as PAs prior to 1960 and persons who use the PA classification as an interim step to becoming CPAs. As such, PAs do not presently constitute a viable segment of the accounting practitioners in Arizona. In addition, the vast majority of accounting services provided by PAs do not require state regulation. As a result, it appears that the PA classification is unnecessary and should be established in Arizona as a "dying class" of accountants as it is in 32 other states.

RECOMMENDATION

It is recommended that consideration be given to the following:

- Elimination of the "Public Accountant" classification through the designation of this classification as a "dying class". A "dying class" designation will allow current certificate holders to retain their certificates until they no longer wish to do so.

Legislation will need to be enacted to implement this recommendation.

FINDING III

THE PERFORMANCE OF THE ARIZONA STATE BOARD OF ACCOUNTANCY IN INVESTIGATING AND RESOLVING COMPLAINTS AND REVIEWING THE COMPETENCY OF CERTIFICATE HOLDERS HAS BEEN SUPERIOR WHEN CONTRASTED WITH OTHER ARIZONA STATE REGULATING BODIES AND OTHER STATE BOARDS OF ACCOUNTANCY. THE BOARD NOT ONLY INVESTIGATES AND RESOLVES COMPLAINTS IT RECEIVES AGAINST CERTIFICATE HOLDERS BUT ACTIVELY PURSUES A LIMITED QUALITY REVIEW PROGRAM AS WELL. SUCH A PROGRAM IS EXCEPTIONAL AMONG ARIZONA REGULATORY BODIES AND STATE BOARDS OF ACCOUNTANCY. HOWEVER, OUR REVIEW HAS REVEALED THAT WHILE THE BOARD'S QUALITY REVIEW PROGRAM IS COMMENDABLE, IT APPEARS THAT THIS PROGRAM CAN BE EXPANDED TO INCLUDE AREAS NOT CURRENTLY SUBJECT TO REVIEW.

The State Board of Accountancy receives complaints against accountants and initiates investigations of complaints when appropriate. In addition, the Board initiated in 1976, a quality review program for audits and financial statements filed with public agencies. This quality review program has proven to be an effective means of identifying substandard accounting work. However, audits and financial statements filed with public agencies represent only a portion of the attest work being performed in Arizona by Certified Public Accountants and Public Accountants. According to Board members, audits and financial statements performed and prepared by Certified Public Accountants and Public Accountants for private organizations, corporations, and in limited instances state agencies, have not been subject to the Board's quality review program because the Board does not have the legal authority to examine supporting documentation and workpapers for these audits and financial statements, unless a complaint has been lodged with the Board against the accountant. As a result, substandard accounting such as has been identified by the Board during the course of its quality review of public filings may go undetected, perhaps with resultant financial losses to the public. However, based upon a Legislative Council opinion, the Board may have access to audits and financial statements performed and prepared by Certified Public Accountants and Public Accountants for private organizations and corporations. In addition, a recent Attorney General opinion includes the suggestion that currently confidential state agency files be made accessible to State Board of Accountancy review. Therefore, it appears that the Board can expand its quality review program to include areas not currently subject to review.

Process of Investigation
and Resolution of Complaints
and Quality Review Findings

The State Board of Accountancy responds to all public complaints that appear to infringe on state accountancy law, rules or regulations and initiates an investigation of the situation.

Since 1976 the Board has also increased investigations through the implementation of a "quality review" for public filings. Audit reports and expressions of opinion regarding financial statements are, in selected instances, public filings when specified by law. Examples of these public filings include audit reports of cities and towns and financial statements filed when a corporation proposes to offer securities for public sale. When conducting a "quality review", the Board investigator compares the filings to a preliminary review checklist containing the basic elements of "generally accepted auditing standards and accounting principles." The investigator reports exceptions from these standards and principles to the Board for its consideration and action.

The Board follows a standard procedure in quality review and complaint investigations. The Board begins by reviewing 1) complaints, 2) referrals, and then determines 3) if sufficient resources exist to direct that a specified number of quality reviews be conducted.

The Board may elect to obtain additional information on complaints and referrals from such sources as the Attorney General or the referral agency before proceeding.

- If, based on this information, no further action is warranted, the Board may close the case. For complaints, the Board will send a letter to the complainant explaining the closure.
- If, however, an in depth investigation appears to be needed, the Board will assign the investigator to perform a "cold review" of the financial statements.

The Board investigator conducts the "cold review" using a checklist developed by the Arizona Society of Certified Public Accountants. This checklist is based on generally accepted auditing standards and accounting principles. The same review is used for complaint investigations and quality reviews performed by the investigator.

The reviewer then prepares a report for Board consideration noting any deficiencies or deviations from standards.

Upon receipt of the investigator's report the Board may: request additional information from the registrant, order a further investigation, refer the matter to the Board's complaint committee, refer to the Attorney General for consent order negotiation, initiate a formal hearing or refer the case to the Attorney General prior to rendering a final decision.

For cases not dismissed, the Board votes upon sanctions to be ordered based on hearing results, consent order negotiations and all obtained information.

The procedure described is used for investigating deviations from standards for auditing and financial statement preparation. Complaints regarding illegal use of the restricted titles "Certified Public Accountant" or "Public Accountant" are usually resolved through direct correspondence with affected parties.

Resolution and Source of
Investigations Conducted

During 1978, the State Board of Accountancy issued 60 resolutions of investigations. Table 12 summarizes these resolutions.

TABLE 12

RESOLUTIONS* OF INVESTIGATIONS BY
THE STATE BOARD OF ACCOUNTANCY
DURING CALENDAR YEAR 1978

<u>Resolution</u>	<u>Number</u>	<u>Percent of Total</u>
Revocation	3	5.0%
Suspension	2	3.3
Corrective Sanctions	8	13.3
Cease and Desist Orders	4	6.7
Advisory Notices	8	13.3
No Action	<u>35</u>	<u>58.4</u>
Total	<u>60</u>	<u>100.0%</u>

As Table 12 details, sanctions were imposed in 41.6 percent of the investigations resolved in 1978. These include revocations, suspensions, corrective sanctions, cease and desist orders and advisory notices.

* Appendix X contains a brief summary of each of the 60 resolutions issued during 1978.

Definitions of these resolutions are:

Revocations - An individual's certificate is rescinded along with privilege of use of title and ability to perform certain functions restricted by law.

Suspension and Corrective Sanctions - An individual's certificate is revoked for a period of time and the individual must complete certain corrective tasks before regaining the certificate.

Corrective Sanctions - Requirements, such as professional education, peer review and restrictions of practice, are imposed to correct the deficient portion of the accountant's practice.

Cease and Desist Orders - Used in enforcement of restrictive title statutes, whereby violators are sent a notice directing the individual to stop the violation. If the individual does not agree and comply, further sanctions may be imposed.

Advisory Notices - If a minor violation of the law or rules has occurred, the violator is notified.

No Action - If an investigation discloses no violations or the Board determines the case is outside of its jurisdiction, no action is taken. If initiated by a complaint, the Board issues a letter of explanation to the complainant.

Quality of Investigation

In a survey of the accounting profession conducted by the Office of the Auditor General in March 1979, accountants who had been subjected to an investigation by the Board were asked to rate the quality and fairness of the Board's investigation process. Table 13 summarizes the accountants' ratings.

TABLE 13

RATING OF THE STATE BOARD OF
ACCOUNTANCY'S INVESTIGATION
PROCESS BY ACCOUNTANTS INVOLVED

BOARD HANDLING OF CASES AND FAIRNESS OF BOARD DECISION

	<u>Excellent</u>	<u>Satis- factory</u>	<u>Neutral or No Opinion</u>	<u>Poor</u>	<u>Unaccep- table</u>	<u>Total Responses</u>
Certified Public Accountant	10	18	7	10	12	57
Public Accountant	-	1	-	-	-	1
Non-licensed Accountant	<u>1</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1</u>
Total	<u>11</u>	<u>19</u>	<u>7</u>	<u>10</u>	<u>12</u>	<u>59</u>
	19%	32%	12%	17%	20%	

As Table 13 reveals, 51 percent of the accountants rated the Board's performance as excellent or satisfactory; 12 percent had no opinion or were neutral; and 37 percent described their case as handled in a poor or unacceptable manner.

Those survey respondents who rated the Board's investigative process and/or fairness of decision as "poor" or "unacceptable" were also asked to comment on their rating. The following comments were made:

- Findings were inaccurate, incomplete or a matter of interpretation*
- Board is "power hungry", prejudiced or unresponsive
- Investigation was not kept confidential

* It should be noted that the Auditor General reviewed five selected cases investigated by the Board. These cases were selected based on whether substantial objections regarding the use and interpretation of appropriate standards were raised by the accountant being investigated. The Auditor General agreed with the appropriateness of the standards used and the interpretation by the investigator.

- Resolution was overly disciplinary rather than corrective
- Board's legal counsel exerted undue pressure
- Process was too slow
- Individual felt they were "guilty until proven innocent"
- Board tends to favor large, "Big-8" accounting firms
- Informal discussions should be held before proceedings
- Sanctions should be based on severity of deficiencies
- Investigation process was fair and prompt, but stern

In addition, 12 practicing accountants who had sanctions imposed on them by the Board for violations of "generally accepted auditing standards and accounting principles" were interviewed. Subjects included in the interview were effectiveness of the sanctions in improving skills, timeliness of the investigation, fairness of disposition and whether undue hardships were incurred. As Table 14 indicates, a majority of interviewees stated the sanctions were fair and effective and the investigation was timely, or had no comment; but half also stated undue hardships had occurred.

TABLE 14

RESPONSES BY SANCTIONED ACCOUNTANTS
REGARDING INVESTIGATION AND CASE
DISPOSITION BY THE STATE BOARD OF ACCOUNTANCY

	<u>Questions Asked</u>				
	<u>Are Sanctions Effective in Improving Skills?</u>	<u>Was Investigation Completed in Timely Manner?</u>	<u>Were Sanctions Fair?</u>	<u>Were Undue Hardships Incurred?</u>	<u>Totals</u>
Yes	9	6	9	6	30
No	3	3	3	6	15
No Comment	<u>-</u>	<u>3</u>	<u>-</u>	<u>-</u>	<u>3</u>
Total	<u>12</u>	<u>12</u>	<u>12</u>	<u>12</u>	<u>48</u>

Table 14 illustrates that accountants practicing under sanctions as of March 30, 1979, had a generally favorable attitude towards the Board's performance. Negative comments included 1) undue influence by the Attorney General, 2) "leaks" on the investigation before formal notification, 3) high expenses for attorney fees, 4) excessive publicity damaging to the accountant's practice, and 5) Board actions being based on service rendered too far (five years) in the past.*

Timeliness of Board Complaint Review Process

A review of the complaints resolved by the Board during 1978 revealed that, on the average, quality reviews of public filings take the least amount of time to resolve; while investigations that are initiated as a result of newspaper articles, take the most time. In addition, those cases that result in the Board revoking the registrant's certificate take longer to complete than any other type of disciplinary action. Table 15 summarizes the timeliness of the Board's complaint and quality review investigations.

* Appendix XI contains a statement by a Certified Public Accountant that describes negative aspects of the investigative process.

TABLE 15

TIMELINESS* OF STATE BOARD
ACCOUNTANCY'S COMPLAINT AND
QUALITY REVIEW INVESTIGATIONS
IN CALENDAR YEAR 1978

<u>Reason The Investigation Was Initiated</u>	<u>Average Time In Calendar Days</u>
Public Filings Reviewed by Board Investigator	119
Board Member or Staff Initiated	445
Other State Agency Referral	313
Public Complaint	189
Newspaper Article	577
 <u>Board Action</u>	
Revocation	910
Suspension	568
Corrective Sanctions	474
Cease and Desist Orders	70
Advisory Notices	325
No Action	87
Overall Average Time for all Investigations	226

* Timeliness is calculated as the number of days elapsing from the date of initial Board review to the date of disposition by the Board.

It should be noted that when a criminal offense is involved in a complaint, the Board may take preliminary disciplinary action; but does await the completion of criminal court action before rendering a final resolution of the case. This policy causes a substantial increase in the time needed for resolution.

Quality Review Programs of
Other States and Other Arizona
Regulatory Programs

The State Board of Accountancy is exceptional in its attempt to assure that registrants are complying with accountancy laws and rules. Among Arizona professional regulating bodies only two other quality review programs exist and among other State Boards of Accountancy the Arizona Board has been nationally recognized as a leader in developing its quality review program.

An Auditor General survey of 19 Arizona professional regulatory bodies revealed that the State Board of Accountancy is one of only three professional regulatory bodies that conduct quality reviews as well as investigation of complaints. Table 16 lists the 19 professional regulatory bodies surveyed.

TABLE 16

SUMMARY OF PROFESSIONAL QUALITY REVIEW
PROGRAMS AMONG ARIZONA PROFESSIONAL
REGULATORY BODIES

<u>Professional Regulatory Body</u>	<u>Maintain Quality Review Program*</u>	
	<u>Yes</u>	<u>No</u>
STATE BOARD OF ACCOUNTANCY	X	
State Bar of Arizona		X
State Board of Barber Examiners		X
State Board of Chiropractic Examiners		X
State Board of Cosmetology		X
State Dental Board		X
State Board of Education**		X
State Board of Funeral Directors and Embalmers	X	
Board of Medical Examiners		X
State Naturopathic Board of Examiners		X
State Board of Nursing		X
Board of Optometry		X
Arizona Board of Osteopathic Examiners in Medicine and Surgery		X
Arizona State Board of Pharmacy	X	
Board of Physical Therapy Examiners		X
State Board of Psychologist Examiners		X
State Board of Technical Registration		X
Arizona State Veterinary Medical Examiners Board	-	<u>X</u>
Total	<u>3</u>	<u>16</u>

* A quality review program is defined as a systematic review of registrants to determine if they are in compliance with the applicable statutes and regulations. This review is conducted even though a formal complaint may not have been received by the agency.

** A teacher assessment program is conducted by individual school districts for their use.

Nationally, the Arizona State Board of Accountancy has been recognized as a leader among other state boards of accountancy. The U.S. Securities and Exchange Commission has reported to Congress, "A few states, notably Arizona, Colorado and Florida have begun relatively ambitious monitoring, review and enforcement programs." An Auditor General survey of the 50 state accountancy boards revealed that only eight boards have quality review programs. These states are:

ARIZONA	North Dakota
Colorado	Oregon
Florida	Virginia
Iowa	Washington

The Board's Quality Review
Program For Public Filings
Has Proven To Be An
Effective Means Of Identifying
Substandard Accounting Work

During 1978, the State Board of Accountancy resolved 60 investigations of which 26 were quality reviews of public filings. Of these 26 quality review investigations, nine resulted in the Board imposing some form of discipline on the registrant who performed the audit or prepared the financial statement that was filed with the public agency. The Board's resolution of the 26 quality reviews of public filings and complaint investigations completed during 1978 are summarized in Table 17.

TABLE 17

SUMMARY OF BOARD RESOLUTION
OF THE 26 QUALITY REVIEWS OF
PUBLIC FILINGS AND COMPLAINT
INVESTIGATIONS COMPLETED
DURING 1978

<u>Board Resolution</u>	<u>Quality Reviews of Public Filings</u>	<u>Complaint Investigations</u>
Revocation	-	3
Suspension	2	-
Consent Order or Other Sanction	4	4
Cease and Desist Order	1	3
Advisory Warning	2	6
No Action	<u>17</u>	<u>18</u>
Number of Quality Reviews of Public Filings Completed	<u>26</u>	<u>34</u>

As shown in Table 17, the quality review program for public filings has been comparable to the investigation of complaints in the identification of accounting work sufficiently substandard to require some form of discipline.

State Board Of Accountancy

Interprets Law To Preclude Quality

Reviews Of Private Filings

Members of the State Board of Accountancy stated that, in accordance with Arizona Revised Statute (ARS 32-744), without a complaint, audit reports and financial statements used by private entities are not accessible to the board for its quality review program. ARS 32-744 reads, in part:

"All statements, schedules, working papers and memoranda made by a certified public accountant or public accountant incident to or in the course of professional service to clients, except reports submitted to a client, shall be and remain the property of the certified public accountant or public accountant in the absence of an express agreement between the certified public accountant or public accountant and the client to the contrary."

When the Board initiated the quality review program in 1976, it determined that commercial or private filings were beyond their authority to review; and, therefore, limited the program to filings with public agencies.

As discussed on pages 33 to 36, individuals could be financially harmed who rely on audit reports and financial statements that deviate from generally accepted accounting principles and auditing standards. McKesson-Robbins, Incorporated, Equity Funding Corporation of America and the Lincoln Thrift Association are national and state examples of harm that can occur. This potential for financial harm is not limited to the public filings now available for review by the Arizona State Board of Accountancy.

Lending institutions, private corporations and suppliers rely on the opinion of independent auditors regarding the fairness and accuracy of financial statements. Inaccurate attest work could result in credit being extended or other decisions being made erroneously, based on the auditor's opinion.

Arizona State Board of Accountancy members have expressed concern regarding the current limitations of quality review and complaint investigation. Mr. D. Jay Ryan, President of the Board, stated on June 19, 1979:

"The public is not completely protected because private filings cannot be reached without a complaint. We (The Board) don't know that they (audits, etc.) even exist unless the banker, for example, supplies us with a copy. Whether our subpoena power would permit a general 'fishing expedition' in a CPA's files, private company's books or bank records I cannot say at this time."

Mr. Archie Walker, member of the State Board of Accountancy, stated on June 19, 1979:

"The substantial amount of work performed by CPA's relates to commercial business. Our economic system is dependent upon financing. For the system to work, the financial statements of the various organizations have to be reliable. To enhance the public protection from substandard work, the Board should become more active in obtaining commercial audits for review. Based upon the results of the Board's investigative activities to date, the need for such a review exists."

Mr. Mike Marusich, Vice-president of the Board on March 23, 1979, stated:

"The best method of controlling private filings is through mandatory periodic peer review conducted by another licensee."

Legislative Council Opinion States
Audit Reports, Financial Statements
And Supporting Working Papers Made By Any
Certified Accountant Are Accessible To The Board.

In a memorandum to the Auditor General dated May 24, 1979, the Legislative Council stated that for purposes of conducting quality review of a certified accountant's work, the State Board of Accountancy does have access to audit reports, financial statements and supporting work papers.

The Legislative Council cited ARS 32-749, as amended in the 1979 legislative session, which states in part:

"Certified public accountants and public accountants practicing in this state shall not be required to divulge, nor shall they voluntarily divulge information which they have received by reason of the confidential nature of their employment. Information derived from or as a result of such professional source shall be deemed confidential, but this section shall not be construed as modifying, changing or affecting the criminal or bankruptcy laws of this state or the United States, nor shall it be construed to limit the authority of this state or agency of this state to subpoena and use such information in connection with any investigation, public hearing or other proceeding."

The Legislative Council noted that the State Board of Accountancy is granted broad powers to administer the regulation of Certified Public Accountants and Public Accountants and according to ARS 32-703, "...prescribe...rules of conduct appropriate to establish and maintain a high standard of integrity and dignity in public accounting."

Further, the Legislative Council cited a 1974 case concerning the scope of investigations:

"In Atchison, T. and S. F. Ry. Co. v. Kansas Com'n on Civil Rights, 215 Kan. 911, 529 p. 2d 66b (1974), the court addressed the scope of investigatory powers of the Kansas Commission on Civil Rights. The Court Noted:

'(i)nvestigation' is appropriately used with regard to nonjudicial functions of an administrative agency and the seeking of information for future use rather than proceedings in which action is taken against someone (citations omitted). An 'investigation' is nonadvisory and contemplates a procedure much less formal and more flexible than applies even to an administrative hearing 529 p. 2d at 673.

'The court specifically recognized that the commission was '...granted broad powers of investigation even though a formal complaint is not filed.' 529 p. 2d at 672...

(Thus) in the absence of voluntary production of audits, financial statements and working papers for the board's review, the board could initiate proceedings and compel the production of the items by subpoena (ARS 32-743)."

The Legislative Council also concluded that exceptions from generally accepted auditing standards and accounting principles noted during a mandatory peer review program would also be accessible to the Board for disciplinary action.

The State Board of Accountancy has also been denied access to financial statements filed with the Department of Transportation. Prequalification procedures for bidding on state highway construction contracts include filing financial statements by contractors. These statements are considered confidential by the Department of Transportation and are available only to certain stated parties; consequently, the statements were not released to the Board for quality review purposes.

In behalf of the Board, the Department of Transportation on November 17, 1977, requested an Attorney General opinion regarding the confidentiality of the contractor's financial statements. The Attorney General ruled on May 24, 1979:

"It appears to us that the financial statements submitted by contractors pursuant to A.C.R.R. R17-3-04 seeking prequalification for public contracts are clearly received by the Department of Transportation in connection with its public duty to evaluate bids and award contracts for highway construction. We therefore conclude that the financial statements submitted by contractors fall within the scope of 'public records and other matters' under ARS 39-121.

* Appendix XII is full text of the Legislative Council opinion.

"ARS 39-121 provides public records and other matters in the office of any officer at all times during office hours shall be open to inspection by any person..."

In Matthew v. Pyle, the Arizona Supreme Court held that a public official may deny public access to a document that falls within the category of 'other matters' as distinguished from 'public records' in the strict meaning of that term if in the official's judgment the document contains matters that are confidential or of such a nature that disclosure would be detrimental to the state... No statute makes the prequalification files confidential, therefore, the Department of Transportation must be prepared to articulate to a reviewing court that the prequalification files are 'other matters' which public policy demands be treated as confidential. This office repeatedly has advised that any doubts in such a determination of confidentiality should be resolved in favor of public disclosure... (Emphasis added)

A.C.R.R. R17-3-04, part 7, indicates that the Department of Transportation has determined that it would be detrimental to the interests of the state to disclose the contents of such files, including the financial statements therein. This interpretation of the rule is necessary to avoid concluding that the rule is contrary to ARS 39-121 and therefore invalid. As the matter now stands, therefore, we can conclude that the financial statements filed by the contractors...are confidential and not required to be disclosed...A.C.R.R. R17-3-04, part 7, indicates that disclosure will be made (only) to the persons indicated in the rule, and the Accountancy Board is not listed."

The Attorney General included the following suggestion in the opinion* to the Department of Transportation:

"...in view of your indication that you would like to cooperate with the State Board of Accountancy, we suggest that you consider amending the rule. This option seems particularly appropriate in view of both the strong public policy supporting disclosure under ARS 39-121 and in view of the fact that the State Board of Accountancy is not directly concerned with the contractor's business affairs but, rather, is simply trying to police the accountancy profession by examining the statements prepared by the accountant for compliance with professional standards." (Emphasis added)

* Appendix XIII contains the full text of the Attorney General opinion.

CONCLUSION

In 1976, the Board of Accountancy initiated a quality review program for audit reports and financial statements filed with public agencies. This quality review program has proven to be an effective means of identifying substandard accounting work. However, the quality review program has not been extended to include audit reports and financial statements performed and prepared for private organizations and corporations because the Board believes that they do not have the legal authority to conduct such review without a complaint being lodged with the Board against the accountant. As a result, substandard accounting work performed for private and nonprofit organizations and corporations may go undetected with possible financial harm to the public. According to the Legislative Council, the Board may have access to audit reports and financial statements performed and prepared for private organizations and corporations. Therefore, it appears that the Board can expand its quality review program to include areas not currently subject to review.

RECOMMENDATION

It is recommended that consideration be given to the following:

- The State Board of Accountancy request an Attorney General opinion regarding the Board's legal authority to expand its quality review program to include audited financial statements performed for commercial and nonprofit organizations and corporations and prepared by certified accountants.
- Within 90 days after receiving the Attorney General opinion, the State Board of Accountancy should formulate a policy regarding the expansion of its quality review program.
- The State Board of Accountancy communicate to the Senate Committee on Commerce and Labor and the House of Representatives Committee on Commerce the Board's policy on expanding its quality review program.

The Legislative Council suggested several legislative changes to accompany an expansion of the Board's quality review program. Included in these suggestions were: 1) immunity to be given to Board members or employees for actions taken in good faith during the course of a quality review, and 2) for the protection of the client, the Board members or employees be prohibited from disclosing any information obtained as a result of a quality review except pursuant to a hearing as provided in Arizona Revised Statutes, Title 32, Chapter 6.

FINDING IV

THE ARIZONA STATE BOARD OF ACCOUNTANCY HAS BEEN SUBSTANDARD IN ITS ENCOURAGEMENT AND USE OF PUBLIC INPUT IN ITS OPERATIONS. INFORMATION REGARDING PROPOSED RULES, REGULATIONS AND LEGISLATIVE CHANGES HAS PRIMARILY BEEN PROVIDED TO REGISTRANTS AND NOT THE CONSUMER.

The Arizona State Board of Accountancy has primarily limited encouragement of public input in its rule and regulation promulgation and in drafting proposed legislation to registrants of the Board. Compared to the encouragement of public participation used by other Arizona regulatory boards and commissions, the State Board of Accountancy's actions regarding public input have been minimal and need to be expanded to include potential and actual consumers of the accountants' service.

Board Actions Regarding

Public Input

The State Board of Accountancy notifies registrants of rule and regulation promulgation, disciplinary actions taken, certificates granted and other information regarding regulation of interest to licensed accountants. ARS 32-703.B defines the Board's responsibility regarding notification of registrants on promulgation of rules and regulations and states:

"At least 30 days prior to the promulgation of any such rule or amendment, the board shall mail copies of the proposed rule or amendment to each holder of a certificate with a notice advising him of the proposed adoption date of the rule or amendment and requesting that he submit his comments thereon at least 10 days prior to such proposed adoption date."

The Board has complied with both ARS 32-703 and the Arizona Administrative Procedures Act (ARS 41-1002) that requires an agency to file a notice of rule changes with the Secretary of State at least 20 days prior to the proposed adoption date.

While not statutorily required, the Board has adopted another method of communicating information to registrants. The Arizona State Board of Accountancy, ASBA Update, a quarterly news bulletin, contains accounting related news including disciplinary action, certificates granted and discussion of accounting issues. This bulletin is mailed to registrants of the Board as well as eight state agencies, hearing officers, Arizona university accounting departments, the American Institute of Certified Public Accountants, three federal agencies, the Arizona Society of CPAs, complaint committee members, two legislators, the Governor and one accountant not certified by the Board. In addition, board actions, notably disciplinary proceedings, have been reported in Arizona newspapers. Beginning in January 1978, the Board began to regularly issue news releases to the media when major cases were resolved.

While the Board is in compliance with applicable Arizona statutes that require it to notify registrants and the general public of proposed rules or regulations, it is minimal when compared to other Arizona regulatory boards and commissions in its efforts to encourage public input. A survey of Arizona regulatory boards and commissions conducted by the Office of the Auditor General revealed that various methods are employed by these regulatory bodies to encourage public input and participation in the promulgation of rules and regulations and in the development of legislative proposals. The State Board of Accountancy, however, employs only two of these methods of encouragement. Table 18 summarizes the various methods used by Arizona regulatory bodies to encourage public input and participation in the promulgation of rules and regulations and in the development of legislative proposals.

TABLE 18

SUMMARY OF METHODS USED BY ARIZONA
REGULATORY BODIES TO ENCOURAGE PUBLIC
INPUT AND PARTICIPATION IN THE PROMULGATION
OF RULES AND REGULATIONS AND DEVELOPING
LEGISLATIVE PROPOSALS

AGENCY	METHOD OF ENCOURAGING PUBLIC INPUT AND PARTICIPATION									
	PROMULGATING RULES					DEVELOPING LEGISLATIVE PROPOSALS				
	Informs Affected Registrants Prior To Hearing	Advertises in News Media	Informs Consumer Groups	Holds Pre-adoption meetings other than hearings		Informs Affected Registrants Prior to Adoption	Contacts Professional Associations	Advertises in News Media	Holds Pre-adoption Meetings	Solicits Consumer Group Participation
STATE BOARD OF ACCOUNTANCY	X ^A					X				
Professional Regulatory Agencies										
State Bar of Arizona	X	X				X		X		
State Board of Barber Examiners	X					X			X	
State Board of Chiropractic Examiners	X	X					X			
State Board of Cosmetology	X	X	X	X		X			X	X
State Dental Board	X									
State Board of Funeral Directors and Embalmers	X	X						X		
Board of Medical Examiners	X					X		X		
State Naturopathic Board of Examiners	X						X			
State Board of Nursing	X	X				X	X	X		
Board of Optometry							X			
Arizona Board of Osteopathic Examiners in Medicine and Surgery										
Arizona State Board of Pharmacy	X						X			
Board of Physical Therapy Examiners	X						X			
State Board of Podiatry Examiners	X					X	X			
State Board of Psychologist Examiners	X		X			X	X		X	
State Board of Technical Registration							X			
Arizona State Veterinary Medical Examiners Board	X									
State Board of Education			X ^C	X ^C		X	X		X	
SUBTOTAL	15	5	3	2		8	12	3	4	1
Other Regulatory Agencies										
Arizona Commission of Agriculture and Horticulture	X	X	X							
Arizona State Athletic Commission	X						X			
Arizona Atomic Energy Commission		X								
State Banking Department, Collection Agencies	X									
Registrar of Contractors	X					X	X		X	X
Division of Mobile and Manufactured Housing Standards	X					X	X			X
State Dairy Commissioner	X									
State Board of Dispensing Opticians	X									
State Egg Inspection Board	X						X			
Department of Insurance	X					X				
Department of Liquor Licenses and Control	X	X					X			
Board of Nursing Care Institution Administrators	X					X	X			
Arizona Racing Commission	X									
State Real Estate Department	X	X								
Structural Pest Control Board	X					X				
SUBTOTAL	14	4	1			5	6		1	2
TOTAL	29	9	4	2		13	18	3	5	3

A Statutes require notification to registrants

B Agency does not draft legislative proposals

C Agency creates task forces of professional and lay persons to develop proposals

It should be noted that of the above Arizona regulatory bodies the State Board of Accountancy is the only one that is statutorily required to notify registrants of proposed rules and regulations.

Limited Public Awareness

Of the Board

A survey conducted in 1978 by Mariscal and Company revealed limited accounting service consumer awareness of the State Board of Accountancy and its functions. This limited consumer awareness is a possible indication of inadequate communication between the Board and the consuming public.

Mariscal and Company surveyed 625 accounting service consumers to ascertain among other things, consumer awareness of the State Board of Accountancy and its functions. The Mariscal survey revealed that of those consumers responding 31.7 percent had knowledge of the Board, 22.8 percent were able to identify at least one of the Boards functions, and only 3.4 percent knew that the Board was responsible for establishing accounting regulations.

Methods For Improving

Public Participation

Mr. Ernest Gellhorn, former Dean of Arizona State University College of Law and a recognized authority on administrative procedure law, has formulated recommendations for improving the Federal Administrative Procedures Act.* Many of these recommended actions are equally applicable to state regulatory bodies. According to Mr. Gellhorn:

- "1. Agency obligations. Minimum constitutional requirements are insufficient reasons for agencies to fail to explore appropriate procedures for providing effective notice to the affected public. (Emphasis added)
2. Meeting public notice needs. Agencies should be required to provide identified, accessible sources of information about proceedings in which public participation is likely to be effective. At a minimum, each agency should:

* Ernest Gellhorn, "Public Participation in Administrative Proceedings," Yale Law Journal, Volume 81, No. 3 (January 1972) pp 398-401.

- "
- a. Strive to provide notice as far in advance of the proceeding as possible; and
 - b. Prepare a separate bulletin issued periodically, identifying the proceeding and providing relevant
3. Attracting and focusing public attention. The public can be made aware of important agency proceedings in many ways, such as press releases to news media; requirements that applicants directly inform users; special notice to governmental bodies, citizen groups or trade associations and separate agency listing of significant matters.

Coverage in the news media is perhaps the most effective way of reaching the average citizen, and public interest groups and agencies should make special efforts to encourage reporting of their activities. Factual press releases written in lay language should explain the significance of the proceedings and the opportunities for public participation. Releases describing important proceedings with a local geographical impact should be sent to area news media. In major matters, agencies might consider public service advertisements and announcements over local broadcasting facilities. Direct mailings are yet another alternative." (Emphasis added)

Under ARS 41-2354 (The Sunset Law), one factor that shall be considered in determining the need for continuation or termination of each agency is:

"The extent to which the agency has encouraged input from the public before promulgating its rules and regulations and the extent to which it has informed the public as to its actions and their expected impact."

In our opinion the State Board of Accountancy has not adequately encouraged public input. State Board of Accountancy members concede that improvements in their notice to the public of Board actions are needed and have agreed to extend the distribution of the quarterly bulletin, ASBA Update to credit and financial trade associations, news media and other accounting groups. While such action constitutes a beginning, additional remedial steps can and should be taken.

CONCLUSION

While the State Board of Accountancy has complied with applicable Arizona statutes regarding public input, it is minimal when compared to other Arizona regulatory bodies in its efforts to encourage public input and has limited encouragement and use of public input primarily to registrants and not the consumer. As a result, there appears to be limited consumer awareness of the State Board of Accountancy and its functions.

RECOMMENDATION

It is recommended that consideration be given to the following:

- The State Board of Accountancy adopt methods to encourage public input and participation in the promulgation of rules and regulations and development of legislative proposals. Consideration should be given to the methods being used by other Arizona regulatory bodies and the recommendations presented by Mr. Gellhorn.

FINDING V

THE ARIZONA STATE BOARD OF ACCOUNTANCY CAN REDUCE OPERATING COSTS BY APPROXIMATELY \$28,000 OVER A FOUR-YEAR PERIOD. IN ADDITION, STATE GENERAL FUND INTEREST EARNINGS CAN BE INCREASED BY AS MUCH AS APPROXIMATELY \$27,000 IN FOUR YEARS.

The Arizona State Board of Accountancy can reduce operating costs approximately \$28,000 over a four-year period by 1) adopting a biennial registration cycle, and 2) automating registration and the maintenance of investigative files. These cost saving options are summarized below.

<u>Method of Realizing Cost Savings</u>	<u>Estimated Cost Savings Over A Four-Year Period</u>
Adopt a biennial registration cycle	\$17,840
Automate registration and maintenance of investigative files	<u>10,500</u>
Total	<u>\$28,340</u>

As a result of converting to a biennial registration cycle, earlier collection of revenue will generate increased interest earning up to approximately \$27,000 for the state general fund in four years.

Adopt A Biennial Registration Cycle

Arizona law requires Certified Public Accountants, Public Accountants, accounting partnerships and professional corporations to register with the State Board of Accountancy each year before December 31. ARS 32-730 states in part:

"The Board shall each year require every certified public accountant, every public accountant, every partnership and professional corporation to register with the board and pay a registration fee of not less than five nor more than 50 dollars not later than December 31." (Emphasis added)

Each year the Administrative Office of the State Board of Accountancy processes approximately 2,100 registrations. According to the Executive Director of the Administration Office approximately 16 percent of the Administrative Office workload is attributable to registration activities. However, the State Board interprets ARS 32-730 to require all registrants to register during the month of December.* As a result, most of the Administrative Office registration workload is concentrated in the months of November, December and January. Consequently, a disproportionate amount of Administrative Office staff resources are devoted to registration activities during those months. Table 19 summarizes the annual workload distribution for the Administrative Office.

* The Legislative Council in an April 20, 1979, opinion stated that the Board of Dental Examiners could not impose a mandatory staggered registration system because Arizona law specified that fees must be paid on or before June 30 each year. Based upon that Legislative Council opinion, it appears that the State Board's interpretation of ARS 32-730 is correct.

TABLE 19

SUMMARY OF THE ANNUAL WORKLOAD DISTRIBUTION*
FOR THE ADMINISTRATIVE OFFICE OF THE STATE
BOARD OF ACCOUNTANCY

During the Month of	Percentage of Workload Attributable To			
	General Administration and Board Activities	Complaints and Violations	Examination and Certification	Registration
January	30%	13%	32%	25%
February	30	10	46	14
March	32	12	49	7
April	32	12	49	7
May	42	12	35	11
June	55	14	15	16
July	35	12	47	6
August	34	12	48	6
September	33	12	49	6
October	31	12	50	7
November	30	11	28	31
December	<u>30</u>	<u>12</u>	<u>3</u>	<u>55</u>
Average Annual Percentage of Workload	<u>34%</u>	<u>12%</u>	<u>38%</u>	<u>116%</u>

* Workload distribution is based upon an estimate prepared by the Executive Director of the State Board of Accountancy.

Because of the above demonstrated cyclical nature of the registration workload the Administrative Office employs part-time help primarily to assist in processing registrations. According to the Executive Director, these part-time positions would not be necessary if the number of annual registrations could be reduced and the registration workload could be spread evenly throughout the year. One means to reduce the number of annual registrations and equalize the registration workload throughout the year could be to adopt a biennial registration cycle with staggered registration dates. Currently 13 states, including California and New York, are registering accountants, accounting partnerships and professional corporations on a biennial basis. Table 20 summarizes those states that have adopted a biennial registration cycle.

TABLE 20

SUMMARY OF STATES THAT HAVE
ADOPTED A BIENNIAL REGISTRATION
FOR ACCOUNTANTS, ACCOUNTING
PARTNERSHIPS AND PROFESSIONAL CORPORATIONS

California	Oregon
Georgia	Pennsylvania
Hawaii	South Carolina
Indiana	Vermont
Massachusetts	Virginia
New Jersey	Wisconsin
New York	

By adopting a biennial registration cycle similar to that used by these states the Arizona State Board of Accountancy would realize cost savings of approximately \$17,840 over a four-year period as follows:

<u>Means of Achieving Cost Savings</u>	<u>Estimated Cost Savings Over A Four-Year Period Through Biennial Registration</u>
Elimination of part-time and temporary help positions	\$17,040
Reduced materials and postage expenses	<u>800</u>
	<u>\$17,840</u>

According to the Executive Director of the Administrative Office a biennial registration cycle has advantages other than reducing costs. For example, registration fees would be easier to collect and the Registration Clerk could be used for other Office activities; thus, perhaps eliminating the need for future staff increases.

The Executive Director did, however, point out that the elimination of annual registrations would deprive the Board of its most effective means of identifying changes in address, telephone number, employer and professional associations for registrants. For example, during the December 1978, registration cycle, the following registrant changes were identified:

Address	-	220
Telephone number	-	161
Employer	-	152
Professional association	-	144

It should be noted that the members of the State Board of Accountancy expressed confidence that some other means of identifying changes in registrant status besides the annual registration process could be developed. One such option might be the State Board of Accountancy's Rule 4-1-55, which requires registrants to notify the Board of changes in address and states in part:

"...notice shall be given to the Board, within 30 days, of any address change or the address of any office opened for the practice of public accounting in this state... (and) the closing of any such offices."

Earlier Collection of Revenues

Will Generate Increased Interest Earnings

Revenues collected and deposited in both the State Board of Accountancy (90 percent of revenues) and the State general fund (10 percent of revenues) are invested until needed to finance state government operations. All interest earned from such investments is retained in the general fund. As a result of converting to a biennial registration cycle, additional interest earnings of as much as approximately \$27,000 will be generated in four years.

The increase in interest earnings will result because revenue collected utilizing a biennial registration cycle in one year will exceed the amount needed to finance that year's operations. The additional amount can be invested until needed, thus generating interest earnings. Depending upon the method used for converting to a biennial registration cycle, estimated additional interest earnings range from \$23,040 to \$27,360 assuming a nine percent* rate of return on investments.

Automate Registration and

Maintenance of Investigative Files

If two of the Administrative Office processes - registration and the maintenance of investigation files - were automated, costs savings up to \$10,500 could be obtained over a four-year period.

Currently, there are several alternative methods of automating registration and maintenance of investigative files. A review of these alternatives revealed that each offers varying degrees of cost savings, and equipment and file control features as shown in Table 21.

* According to the State Treasurer, the annual rate of return on investments for 1979 is projected to be nine percent.

TABLE 21

COMPARISON OF COST SAVINGS, EQUIPMENT
AND FILE CONTROL FEATURES AND SYSTEM
FLEXIBILITY FOR THE ALTERNATIVE METHODS
OF AUTOMATING REGISTRATION AND MAINTENANCE
OF INVESTIGATIVE FILES

	<u>Alternative Methods</u>			
	Purchase of Word Processor	Computer Processing Using Department of Administration Input Terminal	Computer Processing Using Department of Administration Input Format	Time Sharing on Department of Administration Word Processor
Estimated Cost Savings Over Four Years*	\$22,800	\$22,800	\$22,800	\$22,800
Estimated Four Year Cost of Implementation**	<u>19,800</u>	<u>12,300</u>	<u>15,000</u>	<u>18,000</u>
Net Cost Savings	<u>\$ 3,000</u>	<u>\$10,500</u>	<u>\$ 7,800</u>	<u>\$ 4,800</u>
Equipment and File Control Features	Board controls all processing functions	Department of Administration controls input and printing	Department of Administration controls key punching, input and printing	Board controls all processing functions except printing process
System Flexibility Capabilities	Limited	Future complex processing possible	Future complex processing possible	Dependent upon rental agreement with Department of Administration

* The four-year cost savings of \$22,800 are realized by the replacement of one full-time clerical position costing \$9,000 per year with a part-time position costing \$3,300 per year. Annual cost savings of \$5,700 over a four-year period equal \$22,800.

** A significant dispersion of estimated implementation costs was obtained. The indicated amounts represent the low estimates.

The cost savings shown in Table 21 represent the expected results of automating only two processes - registration and maintenance of investigative files. Additional cost savings may be realized if other processes are also automated.

CONCLUSION

The State Board of Accountancy can reduce personnel, material and postage expenses approximately \$28,000 over a four-year period by adopting a biennial registration cycle and automating registration and the maintenance of investigative files. In addition, conversion to biennial registration will result in increased interest earnings for the State general fund by as much as approximately \$27,000 in four years.

RECOMMENDATION

It is recommended that consideration be given to the following:

1. Amendment of ARS 32-730, which requires annual registration, to allow the State Board of Accountancy to adopt a less frequent registration schedule.
2. Approval of the State Board of Accountancy budget to include costs for automating the processing of data.
3. State Board of Accountancy review the methods of automated data processing and implement the method with the maximum costs savings and flexibility to suit the future needs of the Board.

OTHER PERTINENT INFORMATION

ENTRANCE INTO THE PROFESSION

An individual can become a Certified Public Accountant (CPA) or a Public Accountant (PA) in Arizona either by passing an examination and completing other requirements or through reciprocity.

For both certification through examination and reciprocity an individual must meet requirements concerning education, experience, age, residency and moral character.

Initial Certification In Arizona

In order to be considered for initial certification as a CPA or PA in Arizona an individual must have completed the requirements for a bachelor's degree.

Education. According to Arizona Revised Statute (ARS) Section 32-723 before an individual can be allowed to take the written examination in accounting and related subjects, the person must either present satisfactory evidence (a college transcript) that:

- 1) "...he has successfully completed, or will successfully complete within ninety (90) days after the examination, the courses required for a bachelor's degree from the universities or state colleges of this state, or from a college or university maintaining standards comparable to those of the universities or state colleges of this state." The transcript must include at least 24 semester hours in accounting courses, or (Emphasis added)
- 2) "...he has successfully completed...the courses required for a bachelor's degree and passes an examination prepared by the accounting or other faculties of the state universities, under the supervision of the Board. The examination shall be in the subjects of elementary and intermediate accounting theory and related subjects."

Examination. After presenting satisfactory evidence of meeting the above education requirements, an individual may take the uniform CPA examination which is prepared and graded by the American Institute of Certified Public Accountants (AICPA) and used by all 50 state boards of accountancy. The CPA examination contains four subjects; auditing, theory of accounts, commercial law and accounting practices.

- To become a CPA an individual must pass all four subjects.
- To become a PA, an individual must pass either the accounting practice subject or all of the other three subjects.

As demonstrated in Table 22 the average applicant will take the CPA examination numerous times before completing the examination requirement.

TABLE 22
EXAMINATION STATISTICS FOR INDIVIDUALS
WHO INITIATED THE CPA EXAMINATION PROCEDURE IN
ARIZONA DURING 1974 or 1975*

<u>Examination Requirement Completed</u>	<u>1974</u>	<u>1975</u>
First Attempt	17%	14%
Second Attempt	16%	15%
Third Attempt	12%	10%
Fourth Attempt	7%	9%
More than four attempts	<u>6%</u>	<u>7%</u>
Pass Ratio	58%	55%
Fail Ratio	<u>42%</u>	<u>45%</u>
Adjusted Pass Ratio**	<u>59%</u>	<u>60%</u>

* Statistics from 1974 and 1975 were used because candidates have had several opportunities to pass the examination.

** Adjusted to delete from the fail ratio those individuals who have continued the examination procedure into the November 1978 or May 1979 exam.

It should be noted that an individual will receive "conditional" credit for passing accounting practice or any two subjects in one attempt. To use the "conditional" credit, the candidate must pass the remaining subject(s) within the next six consecutive examinations.

Experience. According to ARS 32-721 a person must have "been employed as a full-time staff accountant, either before or after passing the examination for certified public accountant, for a minimum of two years in the office of a certified public accountant or public accountant, within private industry or a government agency..." to become a CPA or PA. The employment shall be experience in the practice of accounting, including examinations of financial statements and reporting on examined financial statements by formal audit opinion or other communication. A person with a master's or more advanced degree in accounting which includes at least 30 semester hours of accounting and related courses, of which at least 12 of those semester hours are graduate level accounting courses, can substitute this additional education for one year of the required experience. The State Board of Accountancy verifies an applicant's experience by contacting the employer(s) involved.

Other Requirements of Certification. An individual must also meet age, residency and other requirements before a CPA or PA certificate will be issued. These requirements are:

- a) 18 years of age,
- b) residency in Arizona,
- c) good moral character,
- d) has not engaged in any conduct which would be grounds for revocation, suspension or other disciplinary action under the accountancy law.
- e) completed an examination in professional ethics and Arizona accountancy law and rules

The Board, in its evaluation of an applicant's age, residency, moral character and violations of the accountancy laws, relies extensively upon the application form prepared by the applicant. The Board accepts age and residency as declared on the application. Moral character and any violations of the accountancy law are evaluated through three questions concerning 1) violations of professional standards, 2) convictions for a felony or crime of which an essential part is dishonesty, deceit or fraud, and 3) rejections of applications for fidelity bonds. In an attempt to deter the applicant from providing false information the applicant must sign an affidavit stating the information provided is true and complete.

In addition, the Board also requests reference letters from five individuals, including at least one CPA, to evaluate moral character. According to the Executive Director of the Board, during her tenure, reference letters have never been the sole reason for denying a certificate.

The professional ethics examination is a self-study course in professional ethics offered by the California CPA Foundation for Education and Research. According to current Board members, the purpose of the ethics exam is to acquaint applicants with professional standards of ethics.

The Arizona Accountancy Law and Rules examination consists of a take-home questionnaire and a copy of the accountancy law and rules. Applicants can read the laws and rules, complete and return the questionnaire to the Board. The objective of the examination, according to Board members, is to make applicants aware of accountancy laws and rules.

Applicants who meet these requirements of education, examination, experience and other areas are granted a certificate as a CPA or PA. This certificate, together with annual registration, allows the individual to use the legally reserved titles of "Certified Public Accountant" or "Public Accountant."

Reciprocity

The process for obtaining a CPA or PA certificate through reciprocity in Arizona differs only slightly from the process for initial certification.

Reciprocity is defined by the Council of State Governments as an arrangement where "licensed practitioners from one state will be licensed by the other without further examination." The Arizona State Board of Accountancy recognizes a verified license from another state in lieu of the uniform CPA examination. Experience, age, residency and other requirements are reviewed by the Board using the same procedure as in the initial certification process.

The timeliness of granting reciprocity is a measure of the ease of entry into a profession. Table 23 displays the approval rate and timeliness of granting CPA reciprocity in Arizona during 1978.

TABLE 23

ARIZONA APPROVAL RATE AND TIMELINESS OF GRANTING
CERTIFIED PUBLIC ACCOUNTANT CERTIFICATES DURING
CALENDAR YEAR 1978

	<u>Number</u>	<u>Percentage</u>
Total applications for reciprocity reviewed during 1978	60	100%
Number refused during 1978	(2)	(4)
Number tabled during 1978	(1)	(2)
Total number of reciprocity applications approved	<u>57</u>	<u>94%</u>
Number of reciprocity applications approved within 60 days	17	30%
Number of reciprocity applications approved in 60 days or more	<u>40</u>	<u>70</u>
Total number of reciprocity applications approved	<u>57</u>	<u>100%</u>
Reasons for approvals taking 60 days or more		
Delays in obtaining confirmation of certification	3	7%
Delays in obtaining confirmation of experience	10	25
Applicant did not take ethics examination	7	18
Delayed because of Board policy to consider reciprocity only every other month	13	32
Other	<u>7</u>	<u>18</u>
Total	<u>40</u>	<u>100%</u>

As Table 23 indicates, 70 percent of the applicants were not granted reciprocity within 60 days of application. In 32 percent of the cases delayed beyond 60 days (13), the delay was caused by the Board's current policy of reviewing reciprocity applications only at every other monthly Board meeting.

Similar Requirements In Other States

Arizona certification requirements are similar to those of other states. Each state uses the uniform CPA examination and requires a minimum age, and all but four require residency. Moral character is evaluated in each state and an examination in professional ethics is required by 35 states.

The major differences among the state requirements for certification are in the education and experience required. Eleven states including Iowa, Oklahoma and Oregon require less education and experience; whereas, six others, including Indiana, New Jersey and Wyoming require more.*

Equal Employment Opportunity

Responsibilities of Licensing Authorities

The Federal Equal Employment Opportunity Act, promulgated federal regulations and recent case law, define equal employment opportunity responsibilities of state licensing authorities such as the State Board of Accountancy. Under the Equal Employment Opportunity Commission regulations, licensing tests which have a discriminatory adverse impact on minorities must be validated to demonstrate the relationship between the test and job performance. In a court decision involving a selection test used by the Duke Power Company the court noted the dangers of using tests, diplomas, or degrees "as fixed measures of capability." The decision continued, "history is filled with examples of men and women who rendered highly effective performance without the usual badges of accomplishment in terms of certificates, diplomas or degrees." Further, "diplomas and tests are useful servants, but congress has mandated the common-sense proposition that they are not to become masters of reality." The major thrust of the decision appears to be, "nothing in this act precludes the use of testing or measuring procedures. Congress has not recommended that the less qualified be preferred over the better qualified...what congress has considered is that any tests used must measure the person in the job and not the person in the abstract."

* Appendix II contains a comparison of state licensing requirements.

Advice from Albert Maslow, chief of the Personnel Measurement Research and Development Center, U.S. Civil Service Commission, should be considered by licensing boards. He says, "I am convinced that we need to sharpen our ability to develop and demonstrate the rational relationship between the job requirements and the measurement system used to certify or qualify people for an occupation. A number of techniques are available to improve the process of job analysis to get a much more exact fix on the critical requirements for the work to be done. I would urge, therefore, that, especially in examinations for occupational knowledge and proficiency, you insist, at the very least, on a clear-cut showing of how one proceeds from the decision as to the skills and abilities required for effective performance to the decision that certain tests or other measures will ensure that the applicant can adequately perform in that occupation. The entire decision-making process, from setting minimum standards to making a final certification on the basis of appraisal data, must be very carefully analyzed step by step to make sure that it does not inadvertently lock out certain segments of our population."*

It should be noted that the AICPA examination is currently being studied by the National Association of State Boards of Accountancy (NASBA). According to Mr. Elmer Thierman, Arizona State Board of Accountancy member and delegate to NASBA, two independent committees are studying the content and administration of the examination. Study of the examination content will include the method and extent a person is tested in such areas as auditing, tax accounting practice, commercial law and economics. Study of the examination administration will include the adequacy of security measures, proctoring methods and provisions for handicapped examinees.

* Appendix XIV contains a Legislative Council memorandum dated May 15, 1979, describing state licensing authorities responsibilities and interpretation of EEO law.

RESPONSE TO THE OFFICE OF THE AUDITOR GENERAL ON ITS PERFORMANCE AUDIT OF
THE ARIZONA STATE BOARD OF ACCOUNTANCY

DATED: July 25, 1979

INTRODUCTION

Since the Board's inception in 1919, it has continually strived to protect the public and insure a minimum quality of accounting services. In recent years, its enforcement of generally accepted accounting principles and standards has been expanded through the use of a quality review program. This program has been greatly aided through the cooperation of other state agencies, especially the Securities Division of the Arizona Corporation Commission.

Even more recently, the regulatory efforts of the Board have been advanced through the enactment of new legislation. For instance, the 1979 amendments give the Board the power to require 40 hours of continuing professional education annually, to establish reporting requirements and to impose administrative penalties for violations of its laws and rules and regulations.

Due to its new powers, the Board anticipates expanding its already successful efforts to protect the public and guarantee a minimum quality of accounting services.

RESPONSE TO CONCLUSIONS AND RECOMMENDATIONS

1. The Arizona State Board of Accountancy concurs with the conclusion and recommendation of the Auditor General that it would be in the public interest to limit the attest function to individuals approved by the State Board of Accountancy. The Board, however, feels that the consumer is provided substantial protection from financial harm by the present statutory framework. This is supported by the Auditor General's Report. On page 44, the report states, "Practical restrictions imposed by business and federal and state law restrict the attest function to titled accountants, and result in minimal practice of the attest function by non-titled accountants in Arizona." The report, on page 41, finds the proportion of the non-titled accountant's practice which represents the attest function to be so insignificant that it is less than one-third of one percent of his practice. Combined, these facts suggest that the consumer is provided substantial protection by the present practical and legal limitations on the non-titled accountant's performance of the attest function.
2. The Arizona State Board of Accountancy concurs with the conclusion and recommendation of the Auditor General that the public accountant classification is unnecessary, and that the classification should be eliminated through designation as a "dying class."

3. The Board concurs with the Auditor General's conclusion that substandard accounting work performed for private and nonprofit organizations and corporations which make no filings with public agencies may go undetected with possible financial harm to the public. While the Board has initiated vigorous enforcement actions concerning public corporations offering securities to the investing public (usually involving public filings with securities agencies), expansion of investigation and quality review programs to include private firms would further facilitate detection of substandard work in that area and substantially reduce the possibility of financial harm to investors and grantors of credit resulting from misleading information.

Until now, there have been two barriers to such an expansion of the Board's investigation and quality review programs. First, until law amendments effective this month, the public accountant's working papers and client files were privileged materials, and it was questionable whether the Board could subpoena or compel release of such private information. See A.R.S. §32-749 (1976). Second, the Board has been limited in the number of investigations it undertakes by lack of funds. Action has been taken concerning both of these barriers.

Legislation enacted in 1979 (and effective July 22, 1979) amends A.R.S. § 32-749 and clarifies the Board's position that its subpoena power, as a state agency, was not frustrated by the privilege extended to public accountant's working papers. Additionally, the 1979 legislation, which was drafted by the Board and actively promoted by it through the legislative process, clarifies the Board's power to hire investigators (A.R.S. § 32-702) and to issue investigative subpoenas (A.R.S. § 32-743). Thus, the Board now has a firmer legal basis for expanding its investigation and review programs.


To further facilitate the expansion of the investigation and quality review programs, the Board has increased fees which, subject to legislative appropriation, will provide more funds for the programs.

4. The Arizona State Board of Accountancy concurs with the conclusion and recommendation of the Auditor General that a maximum effort to encourage public awareness and input has not been evident in the past experience of the Board when rule or legislative amendment has been proposed.

A small administrative staff and limited budget have been restrictive factors in the Board's activities. Since 1977, the Board has endeavored, through the publication of a quarterly Newsletter and the establishment of an expanded mailing list, to provide more information for the public regarding the activities of the Board. The Board also intends to make more use of the news media through both press releases and advertisements.

5. The Arizona State Board of Accountancy concurs with the conclusion and recommendation of the Auditor General that biennial registration and automation of registration and other procedures would result in substantial savings.

The Board is now studying the various automated systems which are available with the intention of implementing the method which it deems to be the most efficient and flexible.


Mike Marusich, CPA, President

Dated July 25, 1979

APPENDICES

32-701. Board of accountancy; membership

A. There shall be a state board of accountancy which shall consist of four certified public accountants and one public member appointed by the governor. One member shall be appointed each year for a term of five years, to begin and end July 3, or until his successor is appointed and qualified. Not less than three members shall be in active public practice as certified public accountants. No more than one member shall be from any one accounting firm.

B. Members of the board shall be citizens and residents of the state. ~~and Four MEMBERS shall be certified public accountants certified under the provisions of this chapter AND ONE MEMBER SHALL BE A PUBLIC MEMBER WHO IS NOT A HOLDER OF A CERTIFICATE ISSUED PURSUANT TO THIS CHAPTER.~~

C. Vacancies occurring from any cause other than expiration of a term shall be filled by appointment by the governor for the unexpired term. No person who has served a complete term shall be eligible for reappointment until after the lapse of one year. Appointment to fill an unexpired term shall not be considered as a complete term.

32-701.01. Definitions

IN THIS CHAPTER, UNLESS THE CONTEXT OTHERWISE REQUIRES:

1. ~~The term "Board", as used in this chapter,~~ means the board of accountancy created by section 32-701, except ~~as to~~ IN matters pertaining to the qualification, licensing and disciplining of public accountants; ~~then the term "board" shall mean~~ MEANS a body consisting of a quorum of the board of accountancy and a quorum of the public accountants advisory committee created by section 32-704, subsection A.

2. "CONVICTION" MEANS A JUDGMENT OF CONVICTION BY ANY STATE OR FEDERAL COURT OF COMPETENT JURISDICTION IN A CRIMINAL CAUSE, REGARDLESS OF WHETHER AN APPEAL IS PENDING OR COULD BE TAKEN, AND INCLUDES ANY JUDGMENT OR ORDER BASED ON A PLEA OF NO CONTEST.

3. "DISCIPLINARY ACTION" MEANS ANY OTHER REGULATORY SANCTIONS IMPOSED BY THE BOARD IN COMBINATION WITH, OR AS AN ALTERNATIVE TO, REVOCATION OR SUSPENSION OF A CERTIFICATE OR REGISTRATION, WHICH MAY INCLUDE:

(a) IMPOSITION OF AN ADMINISTRATIVE PENALTY IN AN AMOUNT NOT TO EXCEED TWO THOUSAND DOLLARS FOR EACH VIOLATION OF THIS CHAPTER OR REGULATIONS PROMULGATED THEREUNDER.

(b) IMPOSITION OF RESTRICTIONS ON THE SCOPE OF REGISTRANTS' ACCOUNTING PRACTICE, INCLUDING, WITHOUT LIMITATION, RESTRICTION OF AUDIT OR ATTEST FUNCTION PRACTICE, RESTRICTION OF TAX PRACTICE, OR RESTRICTION OF MANAGEMENT ADVISORY PRACTICE.

(c) IMPOSITION OF PEER REVIEW AND PROFESSIONAL EDUCATION REQUIREMENTS.

(d) IMPOSITION OF PROBATION REQUIREMENTS BEST ADAPTED TO PROTECT THE PUBLIC WELFARE WHICH MAY INCLUDE A REQUIREMENT FOR RESTITUTION PAYMENTS TO ACCOUNTING SERVICES CLIENTS OR TO OTHER PERSONS SUFFERING ECONOMIC LOSS RESULTING FROM VIOLATIONS OF THIS CHAPTER OR REGULATIONS PROMULGATED THEREUNDER.

4. "FEDERAL SECURITIES LAWS" MEANS THE SECURITIES ACT OF 1933, THE SECURITIES EXCHANGE ACT OF 1934, THE PUBLIC UTILITY HOLDING COMPANY ACT OF 1935 AND THE INVESTMENT COMPANY ACT OF 1940, AS AMENDED.

5. "PRACTICE OF ACCOUNTING AS A CERTIFIED PUBLIC ACCOUNTANT OR AS A PUBLIC ACCOUNTANT" MEANS THE PROVISION OF ANY ACCOUNTING SERVICES, INCLUDING RECORDING AND SUMMARIZING OF FINANCIAL TRANSACTIONS, ANALYZING AND VERIFYING FINANCIAL INFORMATION, REPORTING OF FINANCIAL RESULTS TO AN EMPLOYER, CLIENTS OR OTHER PARTIES AND THE RENDERING OF TAX AND MANAGEMENT ADVISORY SERVICES TO AN EMPLOYER, CLIENTS OR OTHER PARTIES.

Sec. 3. Section 32-702, Arizona Revised Statutes, is amended to read:

32-702. Organization; compensation

A. The board shall annually ~~at its first meeting following July 3~~ elect from its membership a president, a secretary and a treasurer and all or any of such officers may sign and approve claims filed against the state board of accountancy fund for payment of all expenses incurred under this chapter.

B. A majority of the board shall constitute a quorum for the transaction of business. The board shall have a seal which shall be judicially noticed, and shall keep records of its proceedings. The board may employ clerks, examiners, INVESTIGATORS and assistants in the performance of its duties, whose compensation shall be as determined pursuant to section 38-611.

C. The members of the board shall receive compensation as determined pursuant to section 38-611.

32-703. Rule making powers of board; exemption

A. The board may adopt, and amend from time to time, RULES AND REGULATIONS PERTAINING TO PERSONS CERTIFIED OR REGISTERED BY THE BOARD CONCERNING THE FOLLOWING MATTERS: ~~for the orderly conduct of its affairs and for the administration of this chapter. The board may also prescribe, and amend from time to time, rules of conduct appropriate to establish and maintain a high standard of integrity and dignity in public accounting.~~

1. ESTABLISHMENT AND MAINTENANCE OF HIGH STANDARDS OF COMPETENCE, INDEPENDENCE AND INTEGRITY IN THE PRACTICE OF ACCOUNTING AS A CERTIFIED PUBLIC ACCOUNTANT OR AS A PUBLIC ACCOUNTANT AS REQUIRED BY GENERALLY ACCEPTED AUDITING STANDARDS, GENERALLY ACCEPTED ACCOUNTING PRINCIPLES AND, IN THE CASE OF PUBLICLY HELD CORPORATIONS, OR ENTERPRISES OFFERING SECURITIES FOR SALE, IN ACCORDANCE WITH STATE OR FEDERAL SECURITIES AGENCY ACCOUNTING REQUIREMENTS.

2. ESTABLISHMENT OF REPORTING REQUIREMENTS WHICH WOULD REQUIRE REGISTRANTS TO REPORT ANY SUSPENSION OR REVOCATION OF RIGHT TO PRACTICE BEFORE THE FEDERAL SECURITIES EXCHANGE COMMISSION OR OTHER GOVERNMENT AGENCIES, CRIMINAL CONVICTIONS, CIVIL JUDGMENTS INVOLVING NEGLIGENCE IN THE PRACTICE OF ACCOUNTING AS A CERTIFIED PUBLIC ACCOUNTANT OR AS A PUBLIC ACCOUNTANT AND JUDGMENTS OR ORDERS AS DESCRIBED IN SECTION 32-741, SUBSECTION A, PARAGRAPHS 7 AND 8.

3. ESTABLISHMENT OF BASIC REQUIREMENTS FOR CONTINUING PROFESSIONAL EDUCATION OF CERTIFIED PUBLIC ACCOUNTANTS AND PUBLIC ACCOUNTANTS, EXCEPT THAT SUCH REQUIREMENTS SHALL NOT EXCEED FORTY CLASSROOM HOURS IN ANY CALENDAR YEAR.

4. ADOPTION OF PROCEDURES CONCERNING DISCIPLINARY ACTIONS, ADMINISTRATIVE HEARINGS AND CONSENT DECISIONS.

5. ADOPTION OF REGULATIONS CONCERNING THE DEFINITION OF TERMS AND FOR THE ORDERLY CONDUCT OF THE BOARD'S AFFAIRS AND THE EFFECTIVE ADMINISTRATION OF THIS CHAPTER.

8. In addition to the requirements of title 41, chapter 6, at least ~~sixty~~ THIRTY days prior to the promulgation of any such rule or amendment, the board shall mail copies of the proposed rule or amendment to each holder of a certificate with a notice advising him of the proposed adoption date of the rule or amendment and requesting that he submit his comments thereon at least ~~thirty~~ TEN days prior to such proposed adoption date. Such comments shall be advisory only. Failure of any certificate holder to receive such rule, amendment or notice shall not affect the validity of any such rule or amendment.

§ 32-704. Public accountants' advisory committee; membership; powers and duties

A. There shall be a public accountants' advisory committee which shall consist of four members appointed by the governor. One member shall be appointed each year for a term of four years, to begin and end July 3, or until his successor is appointed and qualified. Not less than three members shall be in active public practice as public accountants. Three members of the committee shall constitute a quorum for the transaction of business.

B. Members of the committee shall be citizens and residents of the state and shall be public accountants who hold certificates to practice under the provisions of this chapter.

C. Vacancies occurring from any cause other than expiration of a term shall be filled by appointment by the governor for the unexpired term. No person who has served a complete term shall be eligible for reappointment until after the lapse of one year. Appointment to fill an unexpired term shall not be considered as a complete term.

D. The public accountants' advisory committee shall advise and aid the board in matters affecting public accountants, and no action shall be taken as to matters pertaining to the qualification, licensing and disciplining of public accountants except on a majority vote of the board and committee, as a body. The committee shall be kept informed of contemplated acts of the board primarily affecting public accountants and shall have access to the files of the board pertaining to public accountants for the purpose of carrying out its duties.

E. The remuneration of members of the committee shall be as determined pursuant to § 38-611 for time spent in attending regular and special meetings.

§ 32-705. Disposition of fees

All monies received by the board under the provisions of this chapter shall be paid to the state treasurer monthly. The state treasurer shall deposit ten per cent thereof in the general fund and ninety per cent in the board of accountancy fund for the payment of salaries and other expenses of the board when appropriated for such purposes.

32-721. Certified public accountant; qualifications

A. A certificate of certified public accountant shall be issued by the board to any person who:

1. Has attained the age of eighteen years, is of good moral character, ~~and who~~ is a resident of this state.

2. Has not ENGAGED IN ANY CONDUCT WHICH WOULD CONSTITUTE GROUNDS FOR REVOCATION OR SUSPENSION OF A CERTIFICATE OR OTHER DISCIPLINARY ACTION PURSUANT TO SECTION 32-741, SUBSECTION A. ~~been convicted of a violation of this chapter.~~

3. Has met the requirements to take the examination provided in section 32-723.

4. Has, within a period of time specified in the rules of the board, obtained a grade of seventy-five per cent in each subject of the examination for certified public accountant in this state, or in any state, territory or possession, which uses the questions and grading facilities of the American institute of certified public accountants.

5. Has been employed as a full-time staff accountant, either before or after passing the examination for certified public accountant, for a minimum period of two years in the office of a certified public accountant or public accountant, within private industry or a government agency, which employment ~~shall have~~ HAS exposed the applicant to and provided him with experience in the practice of accounting, including examinations of financial statements and reporting thereon, or has completed one year of the experience as set forth herein and holds a master's, or more advanced degree in accounting or business administration from a college or university recognized by the board, provided that the academic transcript showing completion of the degree program shall include a minimum of thirty semester hours in accounting, business administration, economics and such related subjects as the board shall determine to be appropriate, of which a minimum of twelve semester hours of credit shall be in graduate-level accounting courses. THE BOARD MAY ACCEPT PART-TIME EMPLOYMENT IN A PERIOD OF FOUR YEARS OR MORE AS A SUBSTITUTE FOR THE REQUIREMENT OF TWO YEARS OF FULL-TIME EMPLOYMENT IF SUCH PART-TIME EMPLOYMENT PROVIDES THE APPLICANT WITH EQUIVALENT EXPERIENCE IN THE PRACTICE OF ACCOUNTING.

32-722. Public accountant; qualifications

A. A certificate as a public accountant shall be issued by the board to any person who:

1. HAS ATTAINED THE AGE OF EIGHTEEN YEARS, is of good moral character and is a resident of this state.

2. HAS NOT ENGAGED IN ANY CONDUCT WHICH WOULD CONSTITUTE GROUNDS FOR REVOCATION OR SUSPENSION OF A CERTIFICATE OR OTHER DISCIPLINARY ACTION PURSUANT TO SECTION 32-741, SUBSECTION A.

~~2~~ 3. Has met the requirements to take the examination provided in section 32-723.

~~3~~ 4. Has obtained a grade of seventy-five per cent or more in the subject of "accounting practice" or seventy-five per cent or more in each of the remaining subjects given in the examination provided in section 32-723.

~~4~~ 5. Further qualifies under section 32-721. paragraph 5.

§ 32-723. Certified public accountant examination; qualifications

A. Examination of persons applying for certificates under this chapter shall be held within the state, as the board decides, at least once each year. The time and place for holding an examination shall be advertised for not less than three consecutive days, not less than thirty days prior to the date of the examination, in at least one daily newspaper of general circulation published in the state.

B. No person shall be permitted to take the examination unless he qualifies under one of the following:

1. He presents satisfactory evidence that he has successfully completed, or will successfully complete within a period of ninety days after the examination, the courses required for a bachelor's degree from the universities or state colleges of this state, or from a college or university maintaining standards comparable to those of the universities or state colleges of this state. The academic transcript presented shall include a minimum of twenty-four semester hours in accounting courses of which twelve semester hours must be in intermediate accounting theory, or advanced accounting, or cost accounting, or auditing theory and practice, or income taxes, or any combination thereof, or advanced accounting courses equivalent thereof, and shall include an additional eighteen semester hours in related economics and business administration courses, or courses satisfactory to the board of accountancy. As used in this paragraph, related courses refer to economics, corporation finance, business law, mathematics and advanced English composition, or other courses closely related to the subject of accounting and satisfactory to the board.

2. He presents satisfactory evidence that he has successfully completed, or will successfully complete within a period of ninety days after the examination, the courses required for a bachelor's degree and passes an examination prepared by the accounting or other faculties of the state universities, under the supervision of the board. Such examination shall be in the subjects of elementary and intermediate accounting theory and the related subjects of principles of economics, business law, English composition and business mathematics. The examinations shall have a difficulty equivalent to the final examinations prepared for these respective courses in the universities and state colleges.

3. He is the holder of a valid and unrevoked certificate as a public accountant issued by the state of Arizona and makes application to take any of the examinations offered prior to December 31, 1976.

C. The subjects in which applicants may be examined are:

1. Theory of accounts.
2. Accounting practice.
3. Auditing.
4. Commercial law.
5. Such other subjects as the board may adopt.

D. All examinations provided for in this section shall be in writing upon forms provided by the board and may be held under the

joint auspices and control of the board and the American institute of certified public accountants. The board may make such use of all or any part of the uniform certified public accountants' examination and advisory grading service, or both, as it deems appropriate to assist it in performing its duties hereunder.

E. All examination papers shall be graded by a majority of the board or by the board of examiners of the American institute of certified public accountants. Each subject shall be graded separately. Within a reasonable time after the examination the board shall notify each candidate of his grading. All examination papers shall be preserved for one year after the candidates have been notified of their grading and any candidate shall, upon written request to the board within such year, have access to his examination papers.

F. A candidate who successfully passes an examination in the subject of accounting practice in its entirety or in any two or more subjects shall be deemed to have received a "condition" and shall have the right to be reexamined in the remaining subjects at subsequent examinations held by the board, and if he passes in the remaining subjects within a period of time specified in the rules of the board he shall be considered to have passed the examination in its entirety, except that examinations held during the time a candidate is temporarily in the armed forces shall not be counted unless the candidate sits for such examinations.

G. Any candidate who has successfully passed an examination in the subject of accounting practice in its entirety or any two or more subjects in any state which uses the questions and grading facilities of the American institute of certified public accountants and whose requirements to take the examination are as high as those required in this state shall be deemed to have received a "condition" and may be given credit in his Arizona examination for those subjects in which he has so passed, provided such credits are still in effect as determined by the rules of the board, and he may have the right to be reexamined only in the remaining subjects at subsequent examinations held by the board and if he passes in the remaining subjects within a period of time specified in the rules of the board he shall be considered to have passed the examination in its entirety.

H. Any candidate who has taken two examinations and has failed to receive a "condition" may be required, before being accepted for further examinations, to furnish evidence satisfactory to the board that he has made further diligent study in the failed subject or subjects.

I. The board may permit an Arizona applicant for the Arizona examination to take the examination for certified public accountant outside of this state under the auspices and control of any other state board of accountancy and the American institute of certified public accountants giving an examination for certified public accountants.

J. The board may make rules and regulations regarding the scope of the examinations, the method and time of filing applications and all other rules and regulations necessary to carry into effect the purposes of this section.

As amended Laws 1960, Ch. 68, § 10; Laws 1970, Ch. 119, § 7; Laws 1973, Ch. 130, § 3.

32-727. Certified public accountant or public
accountant; reciprocity; qualifications

A. The board may waive the examination of and may issue a certificate of certified public accountant or public accountant to any person who is the holder of a valid and unrevoked certificate, from the state or foreign country of original issue, as a certified public accountant or public accountant ~~issued by a state or foreign country which extends the same privilege of reciprocity to certified public accountants or public accountants of this state~~, provided that the applicant meets the requirements set forth in section 32-721, ~~subsection A~~, paragraphs 1, 2 and 5 AND THE EDUCATIONAL REQUIREMENTS EXISTING IN THIS STATE AT THE TIME THE APPLICANT WAS ISSUED HIS ORIGINAL CERTIFICATE.

B. Nothing in this section shall be construed as invalidating the certificate to practice as a certified public accountant or the certificate of authority to practice as a public accountant issued under prior laws of this state.

§ 32-729. Examination and certificate fee

The board shall establish and collect a uniform fee from each applicant for each examination held pursuant to § 32-723, such fees to be determined by the board to cover reasonable costs of the examination, and from each applicant for a certificate to be issued under § 32-727. No additional fee shall be required from an applicant entitled to a certificate after having successfully passed the examination. If an applicant for examination is refused permission to take the examination, or if an application for a certificate by reciprocity is rejected by the board, one-half of the fee shall be returned to the applicant.

As amended Laws 1970, Ch. 119, § 10; Laws 1973, Ch. 130, § 5.

32-730. Annual registration

A. Except for the provisions set forth in subsection B, the board shall each year require every certified public accountant, every public accountant, every partnership and every professional corporation to register with the board and pay a registration fee of not less than five nor more than fifty dollars not later than December 31. In the administration of this section, registrants for less than one year shall be charged on a pro rata quarterly basis for the remainder of the year registered.

B. The registration fee for certified public accountants and public accountants may be reduced or waived by the board for registrants who have attained the age of sixty-five or who have become totally disabled to a degree precluding the continuance of their practice for six months or more prior to the due date of any renewal fee.

C. AT THE TIME OF REGISTRATION, EVERY CERTIFIED PUBLIC ACCOUNTANT AND PUBLIC ACCOUNTANT, COMMENCING WITH THE REGISTRATION FOR THE CALENDAR YEAR ONE YEAR AFTER THE BOARD'S PROMULGATION OF CONTINUING PROFESSIONAL EDUCATION REQUIREMENTS, SHALL AS A PREREQUISITE TO ANNUAL REGISTRATION SUBMIT TO THE BOARD SATISFACTORY PROOF, IN A MANNER PRESCRIBED BY THE BOARD, THAT THE REGISTRANT HAS COMPLETED THE CONTINUING EDUCATION REQUIREMENTS ESTABLISHED BY THE BOARD. THE BOARD MAY GRANT EXEMPTION FROM CONTINUING PROFESSIONAL EDUCATION REQUIREMENTS FOR REGISTRANTS NOT ENGAGED IN THE PRACTICE OF ACCOUNTING AS A CERTIFIED PUBLIC ACCOUNTANT OR AS A PUBLIC ACCOUNTANT OR FOR OTHER GOOD CAUSE DETERMINED BY THE BOARD.

32-711. Revocation or suspension of certificate: certified public accountants; public accountants

A. After notice and OPPORTUNITY FOR hearing, the board may revoke or suspend any certificate granted under this chapter, ~~or AND may censure~~ TAKE DISCIPLINARY ACTION AS DEFINED IN SECTION 32-701.01 CONCERNING the holder of any certificate for any ~~one or any combination~~ of the following causes:

1. Conviction of a felony under the laws of any state or of the United States where civil rights have not been restored pursuant to title 13, chapter 9 or other applicable recognized judicial or gubernatorial order.

2. Conviction of any crime WHICH HAS A REASONABLE RELATIONSHIP TO THE PRACTICE OF ACCOUNTING AS A CERTIFIED PUBLIC ACCOUNTANT OR AS A PUBLIC ACCOUNTANT, INCLUDING BUT NOT LIMITED TO CRIMES INVOLVING ACCOUNTING OR TAX VIOLATIONS, DISHONESTY, FRAUD, MISREPRESENTATION, EMBEZZLEMENT, THEFT, FORGERY, PERJURY OR BREACH OF FIDUCIARY DUTY, REGARDLESS OF WHETHER CIVIL RIGHTS HAVE BEEN RESTORED. ~~, an essential element of which is dishonesty, deceit or fraud.~~

3. Fraud or deceit in obtaining a certificate as a certified public accountant or in obtaining a certificate as a public accountant under this chapter.

4. Dishonesty, fraud or gross OR CONTINUING negligence in the practice of public accounting.

5. Cancellation, revocation or suspension of certificate or other authority to practice or refusal to renew the certificate or other authority to practice as a certified public accountant by any other state or foreign country FOR ANY CAUSE OTHER THAN FAILURE TO PAY LICENSE OR REGISTRATION FEES.

6. Violation of any of the provisions of this chapter, OF TITLE 44, CHAPTER 12, ARTICLE 13 OR OF ANY FRAUD PROVISIONS OF THE FEDERAL SECURITIES LAWS.

7. FINAL JUDGMENT IN A CIVIL ACTION WHERE THE COURT MAKES FINDINGS OF ACCOUNTING VIOLATIONS, DISHONESTY, FRAUD, MISREPRESENTATION OR BREACH OF FIDUCIARY DUTY.

8. FINAL JUDGMENT OR ORDER IN A CIVIL ACTION OR ADMINISTRATIVE PROCEEDING WHERE THE COURT OR AGENCY MAKES FINDINGS OF VIOLATIONS OF ANY FRAUD PROVISIONS OF THE LAWS OF THIS STATE OR FEDERAL SECURITIES LAWS.

~~7-~~ 9. ~~Intentional~~ KNOWING violation of ~~a~~ ANY DECISION, ORDER, rule or regulation ISSUED OR promulgated by the board. ~~under the authority granted by this chapter.~~

~~8-~~ 10. Suspension or revocation for cause of the right to practice before THE FEDERAL SECURITIES EXCHANGE COMMISSION OR any OTHER governmental body or agency.

B. The board shall suspend, without notice or hearing, the certificate of any certified public accountant or the certificate of any public accountant who fails to register and pay the annual registration fee as required by section 32-730. Terms of a suspension issued under this ~~rule~~ SUBSECTION shall include a provision that the suspension shall be vacated when the registrant has paid all past due fees and penalties not to exceed ~~seventy-five~~ THREE HUNDRED FIFTY dollars. The board may waive the collection of any fee or penalty after suspension under conditions which the board deems justifiable.

C. THE BOARD SHALL, AFTER NOTICE AND HEARING, SUSPEND THE CERTIFICATE OF ANY CERTIFIED PUBLIC ACCOUNTANT OR PUBLIC ACCOUNTANT WHO FAILS TO SHOW PROOF, IN ACCORDANCE WITH SECTION 32-730, OF COMPLIANCE WITH THE CONTINUING EDUCATION REQUIREMENTS ESTABLISHED BY THE BOARD. IF THE BOARD DETERMINES THAT SUCH FAILURE WAS DUE TO REASONABLE CAUSE OR EXCUSABLE NEGLIGENCE, THE BOARD MAY REQUIRE COMPLIANCE AS EXPEDITIOUSLY AS POSSIBLE. ANY CERTIFICATE SUSPENDED PURSUANT TO THIS SECTION SHALL BE REINSTATED UPON COMPLIANCE WITH RULES AND REGULATIONS GOVERNING SUCH CASES AS ADOPTED BY THE BOARD.

32-742. Revocation or suspension of certificate; partnerships;
professional corporations

A. After notice and OPPORTUNITY FOR hearing, as provided in section 32-743, the board shall revoke the registration to practice public accounting, of a partnership or professional corporation if at any time it does not have all the qualifications prescribed by this chapter.

B. After notice and OPPORTUNITY FOR hearing, as provided in section 32-743, the board may revoke or suspend the registration to practice public accounting of a partnership or professional corporation ~~or~~ AND may ~~revoke~~ ADDITIONALLY TAKE DISCIPLINARY ACTION AS DEFINED IN SECTION 32-701.01 CONCERNING the registrant for any of the causes enumerated in section 32-741, subsection A, or for any of the following additional causes:

1. The revocation or suspension of any certificate of any shareholder, officer, director or employee of a professional corporation, or partner or employee of a partnership.

2. The cancellation, revocation, suspension or refusal to renew the authority of the partnership or any partner thereof to practice public accounting in any other state for any cause other than failure to pay an annual registration fee in such other state.

C. The board shall suspend, without notice or hearing, the registration to practice public accounting of any partnership or professional corporation which fails to register and pay the annual registration fee as required by section 32-730. Terms of a suspension issued under this rule shall include a provision that the suspension shall be vacated when the registrant has paid all past due fees and penalties not to exceed ~~seventy~~ THREE HUNDRED FIFTY dollars. The board may waive the collection of any fee or penalty after suspension under conditions which the board deems justifiable.

Sec. 11. Section 32-743, Arizona Revised Statutes, is amended to read:

32-743. Hearings before board; notice; procedure; review

A. The board may initiate proceedings under this chapter, for cause, either upon its own motion or a verified complaint.

B. A written notice stating the nature of the charge or charges against the holder of a certificate and the time and place of the hearing before the board on such charges shall be served not less than ~~thirty~~ TWENTY days prior to the date of such hearing either personally or by mailing a copy thereof, ~~registered~~ CERTIFIED mail, to the address last known to the board.

C. If, after having been served with the notice of hearing as provided for in this section, such person fails to appear at the hearing and defend, the board may proceed to hear evidence against him and may enter such order as shall be justified by the evidence, which order shall be final. ~~unless he petitions for a review thereof as provided in this section, provided, that within thirty days from the date of any order, upon a showing of good cause for failing to appear and defend, the board may reopen the proceedings and may permit such person to submit evidence in his behalf.~~

D. At any hearing such person may appear in person and by counsel, produce evidence and witnesses on his own behalf, cross-examine witnesses, and examine such evidence as may be produced against him. He shall be entitled, on application to the board, to the issuance of subpoenas to compel the attendance of witnesses on his behalf.

E. The board, or any member thereof, may issue subpoenas to compel the attendance of witnesses and the production of documents, and may administer oaths, take testimony, hear proofs, and receive exhibits in evidence in connection with AN INVESTIGATION INITIATED BY THE BOARD or upon hearing under this chapter. In case of disobedience to a subpoena the board may invoke the aid of any court of this state in requiring the attendance and testimony of witnesses and the production of documentary evidence.

F. The board shall not be bound by technical rules of evidence.

~~G. A stenographic record of the hearing shall be kept and a transcript thereof filed with the board.~~

G. HEARINGS OF THE BOARD SHALL BE RECORDED IN ACCORDANCE WITH SECTION 41-1009, SUBSECTION F.

H. At all hearings the attorney general of this state, one of his assistants, or a special assistant designated by him, shall appear and represent the board.

I. The decision of the board shall be by majority vote. ~~thereof.~~ ANY PERSON AGGRIEVED BY THE DECISION MAY APPLY FOR A REHEARING.

J. The board's decision shall be subject to review under the provisions of title 12, chapter 7, article 6.

§ 32-744. Statements and working papers as property of accountant; exception

All statements, schedules, working papers and memoranda made by a certified public accountant or public accountant incident to or in the course of professional service to clients, except reports submitted to a client, shall be and remain the property of the certified public accountant or public accountant, in the absence of an express agreement between the certified public accountant or public accountant and the client to the contrary.

§ 32-746. Fraudulent audit practices

A. A person commits fraudulent audit practices if such person while registered under the provisions of this chapter recklessly prepares, issues, delivers or files with any public agency an audit report or certificate on any financial statement which is false or fraudulent, or which fails to fairly present the financial condition or status of the person or entity reported on.

B. Fraudulent audit practices is a class 5 felony. Fraudulent audit practices in connection with any securities offering or involving the filing of financial statements with securities agencies of this state is a class 4 felony. Added Laws 1978, Ch. 201, § 538, eff. Oct. 1, 1978.

§ 32-747. Unlawful use of designation or abbreviation; classification

A. A person who has received from the board a certificate to practice as a certified public accountant, or as a public accountant issued under the laws of the state, shall be known as a "certified public accountant" or "public accountant", in accordance with his certificate and he may also use the abbreviation "C.P.A." or "P.A.", in accordance with his certificate. No other person, corporation or partnership shall assume or use any such title, designation or abbreviation or any other title, designation, sign, card or device tending to indicate that the person, corporation, partnership or firm using it is authorized to practice public accounting or is a certified public accountant or a public accountant in this state.

B. No person, corporation or partnership shall assume or use the title or designation "chartered accountant", "certified accountant", "enrolled accountant", "registered accountant", "licensed accountant", "certified tax accountant", "certified tax consultant" or any other title or designation likely or intended to be confused with "certified public accountant" or "public accountant", nor shall any person, corporation or partnership assume or use any of the abbreviations "C.A.", "E.A.", "R.A.", "C.T.A.", "C.T.C.", "L.A." or similar abbreviations likely or intended to be confused with "C.P.A." or "P.A.", but a person qualified as a certified public accountant in this state who also holds a comparable title under the laws of another country may use such title in conjunction with the title "Certified Public Accountant", or "C.P.A.".

C. Nothing in this section shall apply to, or affect or limit the right to continuous use of a partnership name, or a modification thereof, by successor firms formed by the remaining partner or partners or added partner or partners even though the persons whose names are included in the partnership name are not partners, but the successor firm shall conform to all other provisions of this chapter, nor shall the provisions of this section apply to, or affect or limit the right to continuous use of a professional corporation's name as provided pursuant to this chapter or title 10, chapter 3.¹

D. No corporation shall be permitted to practice public accounting in this state, provided that this provision shall not apply to a professional corporation incorporated under the laws of this state or properly qualified to do business within this state and which is otherwise qualified to practice accounting under the provisions of this chapter.

E. If a person or firm violates this chapter, or represents himself or itself to the public as having received a certificate or registration to practice after a certificate or registration has been revoked or suspended, the person or firm is guilty of a class 2 misdemeanor. Each day an offense is committed shall constitute a separate offense.

F. The displaying or uttering by a person of a card, sign, advertisement or other printed, engraved or written instrument or device, bearing a person's name or a firm name intended to be confused with the words "certified public accountant" or "public accountant" or an abbreviation of either shall be prima facie evidence in a prosecution, proceeding or hearing brought under this section that the person or firm whose name is so displayed caused or procured the displaying or uttering of such card, sign, advertisement or other printed, engraved or written instrument or device. As amended Laws 1978, Ch. 201, § 539, eff. Oct. 1, 1978.

¹ Section 10-901 et seq.

32-748. Reinstatement

A. Upon application in writing and ~~after hearing pursuant to notice~~ FOR GOOD CAUSE SHOWN, the board may issue a new certificate to a certified public accountant or a public accountant whose certificate ~~shall have~~ HAS been revoked, or may permit the registration of anyone whose certificate has been suspended, or may reissue a certificate or permit, or modify the suspension of any certificate to practice public accounting which has been suspended.

B. "GOOD CAUSE SHOWN" AS USED IN THIS SECTION MEANS THAT THE PERSON MAKING APPLICATION FOR REINSTATEMENT OR REISSUANCE SHALL DEMONSTRATE THROUGH SUBSTANTIAL EVIDENCE PRESENTED TO THE BOARD THAT HE IS COMPLETELY REHABILITATED WITH RESPECT TO THE CONDUCT WHICH WAS THE BASIS OF THE REVOCATION OR SUSPENSION OF HIS CERTIFICATE OR REGISTRATION. DEMONSTRATION OF SUCH REHABILITATION SHALL INCLUDE EVIDENCE:

1. THAT SUCH PERSON HAS NOT ENGAGED IN ANY CONDUCT DURING THE REVOCATION OR SUSPENSION PERIOD WHICH, IF LICENSED OR REGISTERED DURING

SUCH PERIOD, WOULD HAVE CONSTITUTED BASIS FOR REVOCATION OR SUSPENSION PURSUANT TO SECTION 32-741 OR 32-742.

2. THAT, WITH RESPECT TO ANY CRIMINAL CONVICTION WHICH CONSTITUTED ANY PART OF THE BASIS FOR THE PREVIOUS REVOCATION OR SUSPENSION, CIVIL RIGHTS HAVE BEEN FULLY RESTORED PURSUANT TO STATUTE OR OTHER APPLICABLE RECOGNIZED JUDICIAL OR GUBERNATORIAL ORDER.

3. THAT RESTITUTION HAS BEEN MADE TO ANY AGGRIEVED PARTY AS ORDERED BY A COURT OF COMPETENT JURISDICTION.

4. SUCH OTHER EVIDENCE OF REHABILITATION THAT THE BOARD DEEMS APPROPRIATE.

C. ANY PERSON MAKING APPLICATION FOR ISSUANCE OR REISSUANCE OF A REVOKED CERTIFICATE SHALL, IN ADDITION TO THE OTHER REQUIREMENTS OF THIS SECTION, COMPLY WITH ALL THEN EXISTING QUALIFICATIONS AND REQUIREMENTS FOR INITIAL CERTIFICATION FOR THE PRACTICE OF ACCOUNTING AS A CERTIFIED PUBLIC ACCOUNTANT OR AS A PUBLIC ACCOUNTANT, EXCEPT THOSE REQUIREMENTS WHICH ARE INCONSISTENT WITH THIS SECTION.

D. THE BOARD SHALL NOT ISSUE OR REISSUE A CERTIFICATE TO A CERTIFIED PUBLIC ACCOUNTANT OR PUBLIC ACCOUNTANT WHOSE CERTIFICATE HAS BEEN REVOKED PRIOR TO THE EXPIRATION OF FIVE YEARS FROM THE EFFECTIVE DATE OF REVOCATION, EXCEPT IF THE REVOCATION IS BASED ONLY ON SECTION 32-741, SUBSECTION A, PARAGRAPH 1 OR 2 AND THE CRIMINAL CONVICTION IS ULTIMATELY REVERSED ON APPEAL, THE BOARD SHALL ENTER AN ORDER VACATING SUCH REVOCATION.

**32-749. Confidential nature of information acquired
by accountants; privilege**

Certified public accountants and public accountants practicing in this state shall not be required to divulge, nor shall they voluntarily divulge information which they have received by reason of the confidential nature of their employment. Information derived from or as a result of such professional source shall be deemed confidential, but this section shall not be construed as modifying, changing or affecting the criminal or bankruptcy laws of this state or the United States, NOR SHALL IT BE CONSTRUED TO LIMIT THE AUTHORITY OF THIS STATE OR ANY AGENCY OF THIS STATE TO SUBPOENA AND USE SUCH INFORMATION IN CONNECTION WITH ANY INVESTIGATION, PUBLIC HEARING OR OTHER PROCEEDING.

§ 32-750. Injunction against unlawful act

When in the judgment of the board any person has engaged, or is about to engage, in any acts or practices which constitute, or will constitute, a violation of § 32-747, the board may make application to the appropriate court for an order enjoining such acts or practices, and upon a showing by the board that such person has engaged, or is about to engage, in any such acts or practices, an injunction, restraining order, or such other order as may be appropriate shall be granted by such court without bond.

Added Laws 1960, Ch. 68, § 23.

APPENDIX II

COMPARATIVE CHART OF STATE LICENSING REQUIREMENTS FOR CERTIFIED PUBLIC ACCOUNTANTS

State	Minimum Age Required	Residency Required*	Moral Character Evaluated	Minimum College Education Accepted**	Condition Status for Passing Subjects of CPA Examination	Years of Experience Required**	Ethics Exam Required
Alabama	19	Yes	Yes	Bachelor's	2 (a)	1-2	Yes
Alaska	19	Yes	Yes	2 Years	2 (a)	2-4	No
ARIZONA	18	Yes	Yes	Bachelor's	2 (a)	1-2	Yes
Arkansas	21	Yes	Yes	Bachelor's	2 (a)	1-2	Yes
California	18	No	Yes	2 Years	2 (a)	2-4	Yes
Colorado	None	No	Yes	Bachelor's	2 (a)	0-1	Yes
Connecticut	18	Yes	Yes	Bachelor's	2 (a)	2	No
Delaware	18	Yes	Yes	2 Years	2 (a)	1-4	Yes
Florida	18	Yes	Yes	Bachelor's	2	0-1	Yes
Georgia	18	Yes	Yes	Bachelor's(b)	2	2	No
Hawaii	18	Yes	Yes	Bachelor's	2 (a)	0-1	Yes
Idaho	18	Yes	Yes	Bachelor's	2 (a)	1	No
Illinois	21	Yes	Yes	4 Years	2 (a)	1	No
Indiana	18	Yes	Yes	Bachelor's	2	2-3	Yes
Iowa	None	Yes	Yes	None	2 (a)	1-3	Yes
Kansas	21	Yes	Yes	Bachelor's	2	0-2	Yes
Kentucky	18	Yes	Yes	Bachelor's	2 (a)	1-3	Yes
Louisiana	21	Yes	Yes	Bachelor's	2	1	No
Maine	20	Yes	Yes	Bachelor's	2 (a)	1-2	No
Maryland	18	Yes	Yes	Bachelor's	2 (a)	None	Yes
Massachusetts	18	Yes	Yes	Bachelor's	2 (a)	2-3	No
Michigan	18	Yes	Yes	Bachelor's	1	2	No
Minnesota	18	No	Yes	None	2	1-6	Yes
Mississippi	21	Yes	Yes	Bachelor's	2 (a)	1-2	Yes
Missouri	21	Yes	Yes	Bachelor's		2	Yes
Montana	None	Yes	Yes	Bachelor's	2 (a)	1	Yes
Nebraska	21	Yes	Yes	Bachelor's	2 (a)	2	Yes
Nevada	21	Yes	Yes	Bachelor's	2 (a)	1-2	Yes
New Hampshire	18	Yes	Yes	4 Years	2 (a)	1-2	No
New Jersey	18	Yes	Yes	Bachelor's	2 (a)	2-4	Yes
New Mexico	18	Yes	Yes	4 Years	2	1	Yes
New York	21	No	Yes	None	2 (a)	1-15	No
North Carolina	18	Yes	Yes	2 Years	2 (a)	1-2	No
North Dakota	18	Yes	Yes	None	2 (a)	0-4	Yes
Ohio	18	Yes	Yes	Bachelor's	1	1-2	Yes
Oklahoma	21	Yes	Yes	None	2 (a)	0-3	Yes
Oregon	18	Yes	Yes	None	2 (a)	1-2	Yes
Pennsylvania	18	Yes	Yes	Bachelor's	1	1-2	No
Rhode Island	21	Yes	Yes	Bachelor's	2 (a)	1-2	No
South Carolina	18	Yes	Yes	Bachelor's(b)	2 (a)	2-3	Yes
South Dakota	18	Yes	Yes	Bachelor's	2 (a)	1	Yes
Tennessee	18	Yes	Yes	Bachelor's(b)	2 (a)	1-2	No
Texas	18	Yes	Yes	2 Years	2	1-6	Yes
Utah	21	Yes	Yes	Bachelor's	2 (a)	1-2	Yes
Vermont	18	Yes	Yes	None	2 (a)	2	No
Virginia	18	Yes	Yes	4 Years	2 (a)	1-2	Yes
Washington	18	Yes	Yes	Bachelor's(b)	2 (a)	1-2	Yes
West Virginia	18	Yes	Yes	Bachelor's	1	None	Yes
Wisconsin	23	Yes	Yes	Bachelor's	2	1 1/2-3	Yes
Wyoming	19	Yes	Yes	Bachelor's(b)	2 (a)	3	Yes

* Residency requirement refers to actual residence or employment within the state.

** Many states have varying combinations of acceptable education and experience. The table shows the minimum college education and the range of experience accepted.

(a) Accounting Practice Section will satisfy a two-subject condition requirement.

(b) A test may be substituted for the education requirement.

APPENDIX III

UNITED STATES SECURITIES AND EXCHANGE COMMISSION'S COMMENDATION OF THE ARIZONA STATE BOARD OF ACCOUNTANCY - JULY 1978

United States Securities and Exchange Commission; Report to Congress on the Accounting Profession and the Commission's Oversight Role; July 1978; pp 237-240.

Activities of State Licensing Authorities

"As it has for the past several years, the Commission staff has continued its efforts to enhance its communication and cooperation with state licensing authorities. These efforts have been made in several areas, some of which represent new initiatives and some of which are continuations of historical practices. Since there are over 50 such autonomous bodies with jurisdiction over accountants in the U. S. alone, the process is necessarily a lengthy one. Nevertheless, we believe that progress has been made and that the pace of this progress should accelerate in the future.

A body which has been of considerable help in this area is the National Association of State Boards of Accountancy ("NASBA"). This voluntary organization includes among its members all of the U. S. licensing authorities. Although NASBA has no formal authority over its members, the organization has served as a sort of clearinghouse for the sharing of information and as a catalyst for helping to initiate various regulatory efforts at the state level. The Association has only a small full-time staff at the present time, but has been very cooperative in providing assistance to various states in setting up local enforcement programs. The Association also sponsors various regional and national meetings at which representatives of its member licensing authorities discuss topics of current interest. Members of the Commission staff have attended several of these meetings during 1978 as observers.

NASBA has been publishing for some time a monthly newsletter which highlights activities by its members. In addition, several state boards have recently begun publishing newsletters of their own. The Commission staff regularly receives and reviews copies of these publications. State boards have also been generally cooperative in providing information on request.

"It has long been commission practice that, following enforcement actions against licensed accountants, copies of pertinent documents are forwarded to the state licensing authorities for whatever action they may deem appropriate. Historically, follow-up actions by the states have been mixed. Some states regularly communicate with the Commission, request additional information (including access to investigative files, which is generally granted) and apparently pursue the matter diligently. Others conduct only limited additional inquiry and still others rarely, if ever, communicate with the Commission. Interest in disciplinary matters has been increasing noticeably, however, during the past year.

Nearly all state boards are critically lacking in resources. Many boards are staffed with only one or two full-time employees who are frequently occupied almost exclusively with administrative duties. Board members are normally practitioners who devote only a fraction of their time to regulatory activities. This situation is changing in many states, however, several boards have begun to increase their staffing substantially and to supplement their resources with voluntary assistance from practitioners.

Since a majority of the memberships of nearly all state boards is made up of practitioners, these bodies are at least partially self-regulatory in character. The responsibilities of nearly all of these authorities include a role in enforcing the accounting laws of their jurisdiction. As Chairman Williams noted at the AICPA Fifth National Conference on current SEC Developments on January 4, 1978:

'A second important area about which there is a sense of expectation and urgency is the need for enhanced professional self-regulatory and disciplinary mechanisms. Those mechanisms are vital, not only for the sake of disciplining those who have failed in their professional undertaking, but to reinforce independence. If the profession's own disciplinary proceedings are more effective, and more visible, it will strengthen the independence of the auditors, and the perception of independence, as well as warding off legislative alternatives.'

"A few states, notably Arizona, Colorado and Florida, have begun relatively ambitious monitoring, review and enforcement programs. The staff is hopeful that in the future the state licensing authorities will assume a uniformly meaningful role in the disciplinary process. (Emphasis added)

During the next year, the Commission staff will be attempting to increase substantially its knowledge concerning the resources and activities of the state licensing authorities and to effect better liaison with those bodies at several levels. The Commission's ability to influence the activities of state regulatory bodies is, of course, very limited. The staff believes, though, that substantial benefits are to be gained by enhancing coordination and communication, especially in the enforcement area."

BUD TIMS
CHAIRMAN

STAN AKERS
COMMISSIONER

JIM WEEKS
COMMISSIONER



GEORGE C. ANDERSON, JR.
EXECUTIVE SECRETARY

ARIZONA CORPORATION COMMISSION

March 1, 1979



James A. Sexton
Performance Audit Division
Auditor General's Office
Suite 600
112 North Central Avenue
Phoenix, Arizona 85004

Dear Mr. Sexton:

In response to your letter of January 24, 1979, regarding your review of the Arizona State Board of Accountancy, I provide the following information:

The only requirement for accountants to practice before the Arizona Corporation Commission Securities Division is that the accountant be a Certified Public Accountant or a Public Accountant, and not be subject to any order of the Board of Accountancy which bars him from practice before the Securities Division.

Although detailed qualifications of accountant are not required for practice before the Securities Division, detailed requirements do exist for their work product filed with the Division in connection with registration of securities, exemptions from registration and registrations of dealers in securities. Under A.R.S. 44-1895 financial statements must be prepared in accordance with Generally Accepted Accounting Principles and certified, if necessary, by an independent Public Accountant or a Certified Public Accountant. Under A.R.S. 44-1875, 44-1942 and A.R.S. 44-2066, the Commission and/or Director of Securities may request and require the filing of additional information. Oftentimes, additional information is requested from the accountant regarding financial projections, internal budgets and similar type accounting-related reports.

During the past two and one half years, the Securities Division has actively participated with the State Board of Accountancy's program to upgrade the quality of the accounting profession. This participation has taken the form of referral of substandard accounting work that has been filed with the Securities Division. The most notable example of that joint effort was the disciplinary action taken by the State Board of Accountancy against the accounting

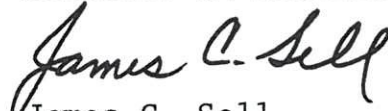
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firm of Henry and Horne. The Division relies heavily upon the State Board of Accountancy for the continued review of the quality of the independent accountant's work.

The aggressive actions taken by the State Board of Accountancy over the past two and one half years has greatly helped this Agency in upgrading the quality of the accounting work found in public registrations. The Division believes the continued aggressive action by the State Board is vital to continued protection of potential investors in Arizona. We intend to continue to participate in the Board's program of reviewing the quality of work performed by Certified Public Accountants and Public Accountants. The Division believes the continued existence of the State Board of Accountancy is vital to the protection of Arizona investors.

Very truly yours,

Matthew J. Zale
Director of Securities

A handwritten signature in dark ink, reading "James C. Sell". The signature is written in a cursive style with a large, stylized "J" and "S".

James C. Sell
Director of Regulation

JCS:pd

ARIZONA LEGISLATIVE COUNCIL

MEMO

May 31, 1979

TO: Douglas R. Norton, Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (0-79-3)

This is in response to a request made on your behalf on March 2, 1979 by Gerald A. Silva.

QUESTIONS PRESENTED:

1. Could the attest function in Arizona be restricted to licensed accountants?
2. If the answer to Question No. 1 is yes, can this be done through promulgation of rules and regulations, or would a change in statute be needed?

ANSWERS:

1. Yes.
2. A change in statute would be needed.

1. Within the accountancy profession, the attest function of an independent auditor is the performance of an audit in accordance with generally accepted auditing standards and expressing an opinion on the financial statements as to the fairness of those statements in representing the financial condition of the audited entity. Arizona State Board of Accountancy v. Keebler, (1977 Ct. App.) 115 Ariz. 239. The Generally Accepted Auditing Standards and Generally Accepted Accounting Principles of the American Institute of Certified Public Accountants have been adopted by the Arizona board of accountancy, Administrative Rules and Regulations, Rules of Professional Conduct, R4-1-56. The difference between the standards and the principles, as explained in Securities and Exchange Commission v. Arthur Young & Co. (Court of Appeals, Ninth, No. 77-1768, Jan. 31, 1979), is that the generally accepted auditing standards involve how an auditor goes about obtaining information, while the generally accepted accounting principles involve the format in which to present the information. Good faith compliance with the generally accepted auditing standards, without concealment or negligence, immunizes the certified public accountant from liability under the federal securities laws. SEC v. Young.

It is stated in the memorandum and request that the attest function is not, in this state, now limited to certified public accountants and/or public accountants, and that other states and the Securities and Exchange Commission limit the performance of the attest function to a certified public accountant.

The attest function is not limited by statute in Arizona to public or certified public accountants because neither that function nor any other accounting function is defined in the regulatory statutes, Arizona Revised Statutes Title 32, chapter 6. Public accounting is not defined.

Limitation of the attest function to licensed accountants in other states is accomplished by definitions of public accounting which include that function, and by prohibiting the practice of public accounting by one other than a licensed public or certified public accountant. California and Illinois have nearly identical definitions of public accountancy, including "professional services that involve or require an audit, examination, verification, investigation, certification, presentation or review of financial transactions and accounting records" and including a person "who prepares or certifies for clients reports on audits or examinations of books or records of accounts, balance sheets . . . financial . . . statements or reports which are to be used for publication or for the purpose of obtaining credit or for filing with a court of law or with any governmental agency . . ." California Code, Business and Professions, sec. 5051; Illinois Ann. Stats. 110 1/2 sec. 32. New York defines the professional services offered, including "any opinion on, report on, or certificate to such financial, accounting or related statement". New York Education Law, sec. 7401.

Arizona Revised Statutes section 32-721, describing the type of employment experience required for certification of public or certified public accountants, "which employment shall have exposed the applicant to and provided him with experience in the practice of accounting, including examination of financial statements and reporting thereon", has been specifically held not to describe the attest function. Board of Accountancy v. Keebler.

"It is well settled that within proper limits the legislature may regulate the profession of accountancy in the interests of the general welfare." Hilkert v. Canning (1941), 58 Ariz. 290, 291, 119 P. 2d 233. The common understanding that preparation of income tax returns is not public accounting arises in other states partly from statutes, partly from administrative interpretation of statutes, and partly from the principle that income tax returns are ultimately reviewed by public officials. While it is recognized that bookkeeping and similar technical services are private business having no bearing on the general public welfare, auditing and expression of professional opinion on financial statements on which third parties may rely is a function endowed with sufficient public interest for exercise of the police power. Op. Atty. Gen. No. 71-5 and authorities there cited.

Conclusion: The attest function can legitimately by statute be limited to public and certified public accountants.

2. Faced with insufficient guidelines or inadequate definitions in regulatory statutes, the courts may strike an entire statute, strike part and retain the enforceable part, or find some "reasonable" standard for a board to follow. Bd. of Accountancy v. Keebler; Welsh v. Bd. of Accountancy (1971), 14 Ariz. App. 432, 484 P. 2d 201; Cohen v. Bd. of Psychologist Examiners, (1978), 588 P. 2d 299 and (1977), 588 P. 2d 313. The Attorney General may offer a clarifying opinion. But the constitutional power of the legislature to legislate cannot be relinquished or delegated so as to permit an administrative agency "to range at large and determine for itself the conditions under which a law should exist and pass the law it thinks appropriate". State v. Marana Plantations (1953), 75 Ariz. 111. To the extent that Op. Atty. Gen. 71-5, in observing that any distinction between preparation of income tax returns for individuals, or for corporations and partnerships including financial statements, "must be made by the State Board as a policy matter, based upon its obvious competence and expertise in determining what does and does not constitute the practice of public accounting" conflicts with the holding of Marana that formulation of policy is for the legislature and that administrative

rules must be within the framework of policies which the legislature has sufficiently defined, it must yield to Marana. Only the legislature can define public accounting and limit its practice to public or certified public accountants, where it affects the public welfare in matters relied on by third parties.

Recent history provides examples of many such attempts to define or limit. The 1973 legislation, Laws 1973, chapter 130, led to the Keebler case. H.B. 2140 (1976) and S.B. 1203 and S.B. 1295 (1977) proposed to add to Arizona Revised Statutes section 32-747 relating to unlawful practices the following:

No person shall sign or affix his name, trade name or assumed name to any accounting or financial statement or to any opinion, report or certificate on such statement, attesting in any way to the fairness of the representations or estimates set forth in such statements where such attestation purports to result from an audit or examination of such statement, unless he holds a certificate as a certified public accountant or public accountant.

S.B. 1176 (1976) would have limited the attest function to certified public accountants by adding to Arizona Revised Statutes section 32-747:

No person may attest to the accuracy of a financial statement unless such person is certified as a certified public accountant pursuant to this chapter.

S.B. 1203 (1977) and H.B. 2126 (1978) proposed to add a definition of accounting which would have included "auditing, investigation or review of financial records in order to determine the correctness of financial statements or books of account".

Conclusion: Restriction of the attest function to public or certified public accountants could not legally be accomplished by rule or regulation of the board of accountancy.

MEMO

March 14, 1979

TO: Douglas R. Norton, Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (0-79-2)

This is, in response to a request made on your behalf on March 2, 1979 by Gerald A. Silva.

QUESTIONS PRESENTED

1. Which Arizona statutes now require a certified public accountant or public accountant to provide certain services?

2. Which Arizona statutes now specify a certified public accountant or public accountant to provide services in lieu of others?

The following statutes contain provisions requiring certified public accountants or public accountants to provide certain services or to provide certain services in lieu of others:

<u>A.R.S. Section</u>	<u>Category</u>	<u>Description</u>
5-107	required service	An application for a permit to hold a racing meeting must contain a financial statement completed and certified by a CPA. The racing commission, on its request, must be provided with a statement from an accredited CPA certifying that the net worth of any guarantor or guarantors is at least equal to the amount of the unpaid indebtedness guaranteed.
5-111.02	in lieu service	The cost of a capital improvement to a race track facility must be determined and verified upon completion of the project by an audit of the permittee's records conducted by the racing commission or by an independent CPA selected by the permittee and approved by the commission.
6-477	discretionary service	The board of a savings and loan association may appoint a CPA to audit the association's books at least once each year. This section specifies that a CPA audit is not in lieu of the required examination by the superintendent of banks.

6-478	in lieu service	Every savings and loan association must file a statement showing its financial condition and operations. This may be verified by a CPA appointed by the board in lieu of a committee of members of the association or two officers of the association.
6-523	in lieu service	Audit of credit union by CPA (mentioned in your request).
6-831	required service	Records of an escrow agent must be audited at least once each fiscal year by a CPA.
9-481	required service	Audits of cities and towns by CPA or public accountant (mentioned in your request).
9-921	required service	Police pension board must have an annual audit of the police pension fund performed by a CPA.
9-956	required service	Board of trustees of firemen's relief and pension fund must have an annual audit of the fund performed by a CPA.
9-1002.01	discretionary service	A district board of a volunteer fire district may retain a CPA to perform an annual audit of the board's books.
10-205	in lieu service	The annual accounting of a close corporation must be acknowledged by the manager of the corporation or certified by an independent public accountant.
16-454.01	in lieu service	Continuing political organizations which expend money for political purposes must submit an annual itemized financial statement prepared by a public accountant or a CPA or by the treasurer of the political organization.
23-982	required service	An audit of the books of the state compensation fund must be made at least annually by a competent and independent firm of certified public accountants who must submit the audit report to the auditor general prior to its delivery and filing.

23-1612, required service
Art.VI(d)

All receipts and disbursements of funds handled by the Vehicle Equipment Safety Commission must be audited yearly by a qualified public accountant. (This section contains the Vehicle Equipment Safety Compact which has a membership of approximately 40 states. This audit requirement does not necessarily mean that an Arizona public accountant will be required to perform this service.)

30-204 in lieu service

District and state agencies authorized to issue revenue bonds subject to approval of the state certification board must have an annual audit performed on their operation funds. Districts, state agencies and municipalities pledging any assessments, funds or property presently owned or to be provided, accumulated or acquired are also required to have an audit performed on their collateral deposits. These audits must be performed by a CPA and are in lieu of all other official audits of all operation funds or collateral deposits of the districts, state agencies and municipalities except as required by court order.

30-696, required service
Art.III(e)

All receipts and disbursements of the Western Interstate Nuclear Board must be audited annually by a certified or licensed public accountant. (This section also contains a compact ratified by certain other states. Therefore, the audit requirement would not necessarily be performed by an Arizona CPA.)

32-1052 mandatory service;
in lieu service

The superintendent of the banking department has authority to appoint a CPA or public accountant to check on the financial condition of a collection agency and to determine if certain violations have occurred. How frequently these appointments can be made is at the discretion of the superintendent, except that they cannot occur more frequently than once a year. This section also provides that a licensed collection agency may appoint a CPA or public accountant to audit its books. At the option of the superintendent, this audit can be accepted in lieu of an audit by the superintendent.

36-125.03	required service	Hospitals are required to file with the department of health services an annual financial report certified to by an independent CPA.
40-1122	required service	The board of directors of a metropolitan public transit authority must have a semiannual audit made on all books and accounts of the authority by an independent CPA.
41-175	required service	The state treasurer's office must have its accounts and securities audited annually by a CPA selected by the state board of deposit.
41-1279.01	required service	The state auditor general and chief deputy must be CPA's.
44-1872	required service	The issuer or registered dealer of securities must file a registration statement with the corporation commission which includes a statement of the facts showing that the securities are entitled to be registered by description together with a balance sheet, surplus statements and profit and loss statements prepared and certified by an independent public accountant or CPA.
44-1895	required service	Financial statements required for registration of securities by qualification must be certified if certification is necessary by an independent public accountant or CPA.
44-1941	required service	An application for registration as a securities dealer must contain a balance sheet, profit and loss and surplus statements, prepared and certified by an independent public accountant or CPA.
44-1947	required service	A securities dealer must include a balance sheet and profit and loss and surplus statements certified by an independent public accountant or a CPA in his application for renewal of registration.
44-2066.07	required service	Every real property securities dealer and issuer must file an annual report with the corporation commission containing financial statements accompanied by an opinion on the financial statements by a CPA or public accountant which is based on an audit of the dealer's or issuer's business.

44-2066.08 required service

An application for a real property securities permit must be accompanied by a balance sheet of the applicant prepared and certified by an independent public accountant or CPA.

45-581, required service
Art. VIII

All receipts and disbursements of funds handled by the Upper Colorado River Commission must be audited yearly by a qualified independent public accountant. (This audit requirement would not necessarily be performed by an Arizona public accountant.)

LETTERS FROM ARIZONA FINANCIAL INSTITUTIONS
REGARDING CREDIT POLICIES

- A - Valley National Bank
- B - First National Bank of Arizona
- C - The Arizona Bank
- D - Greater Arizona Savings
- E - First Federal Savings



VALLEY NATIONAL BANK

MEMBER FEDERAL RESERVE SYSTEM

HEADQUARTERS: PHOENIX, ARIZONA

February 7, 1979

BUD CLARK
ASSISTANT VICE PRESIDENT

PHOENIX
P. O. BOX 71 85001

Mr. James A. Sexton
Performance Audit Division
Office of Auditor General
Suite 600
112 No. Central Avenue
Phoenix, Arizona 85004

Dear Mr. Sexton:

In reply to your letter regarding Valley National Bank policy requirements for audited financial statements.

Basically our policy states that all credit facilities to business entities of \$250,000.00 or more, the borrower and guarantors (if any) must submit a minimum of three years annual financial statements with unqualified opinions by a recognized competent certified public accountant.

I believe this is the information you wanted. If not, or if clarification is required, I will be happy to cooperate.

Sincerely,

BC:sd



FIRST NATIONAL BANK OF ARIZONA

February 8, 1979

Mr. James A. Sexton
Performance Audit Division
Office of the Auditor General
Suite 600
112 N. Central Avenue
Phoenix, AZ 85004

Dear Mr. Sexton:

This letter is in answer to your inquiry of February 1, 1979 regarding financial statement requirements.

All unsecured loan applications over \$1,000 must be accompanied by a financial statement.

There is no set policy at First National Bank of Arizona requiring accompanying certified financial statements with loan applications. This lack of policy should not be construed as an indifference, but rather as flexibility for the loan officer.

As a rule of thumb, unsecured loans exceeding \$500,000 usually require a certified financial statement depending upon the customer's credit history, financial condition of company, knowledge of customer's industry, guarantees, etc.

When a certified financial statement is received the loan officer relies heavily on the figures in making the loan decision. He also trusts that the presentation adheres to the AICPA standard and is in a fair and consistent form unless otherwise noted.

Sincerely,

T. A. Zeller
Assistant Vice President
Credit Department

TAZ:rw



CLAYTON W. NIMTZ
VICE PRESIDENT

February 16, 1979

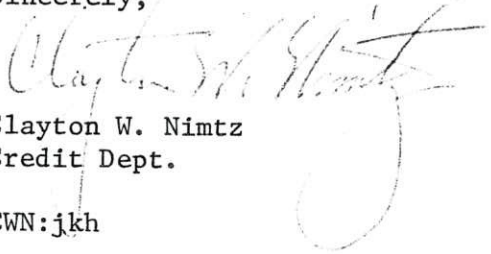
Mr. James A. Sexton
Office of the Auditor General
112 N. Central Ave. Suite 600
Phoenix, AZ 85004

Dear Mr. Sexton:

This letter will confirm your recent telephone conversation with Tony Ward in which he indicated we normally require audited statements for loan requests of \$250,000 and over.

If there is anything else that I can help you with in this regard please feel free to contact me.

Sincerely,


Clayton W. Nimitz
Credit Dept.

CWN:jkh



122 NORTH CENTRAL AVENUE • PHOENIX, ARIZONA 85004 • (602) 258-5955

February 2, 1979

DONALD E. GOUGH
Vice President
Mortgage Loan Department

James A. Sexton
Performance Audit Division
State of Arizona
Office of the Auditor General
112 N. Central Ave.
Phoenix, Az. 85004

Dear Mr. Sexton:

Thank you for your February 1, 1979 letter requesting information concerning certified financial statements that we would require on loan applications.

Normally, on a residential loan application we would not require a certified financial statement even if the borrower was a corporation. We would require a certified financial statement where we are considering a loan on an income producing property where the amount of the loan exceeds \$100,000 whether the borrower be a corporation, individual, or partnership. On occasion, we have deviated from this policy; but, normally the above is our requirements.

I trust that this will answer your February 1, 1979 inquiry.

Very truly yours,

A handwritten signature in dark ink, appearing to read "Donald E. Gough", written over a horizontal line.

Donald E. Gough
Vice President



**FIRST
FEDERAL
SAVINGS**

3003 NORTH CENTRAL AVENUE / PHOENIX, ARIZONA 85012

E. L. THOMAS
EXECUTIVE VICE PRESIDENT

February 7, 1979

Mr. James A. Sexton
Performance Audit Division
Office of the Auditor General
112 N. Central Avenue, Suite 600
Phoenix, Arizona 85004

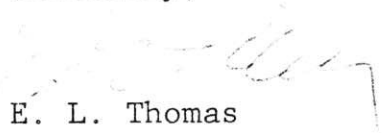
Dear Mr. Sexton:

This is written in answer to your inquiry of February 1, 1979, addressed to Larry Cerato of First Federal Savings.

It is the policy of First Federal Savings to require audited financial statements, accompanied by an opinion of a certified public accountant, when credits to an individual borrower exceed \$1,000,000. On occasion this policy may be waived with the approval of the Executive Loan Committee.

I trust that this is the information you desire.

Sincerely,


E. L. Thomas

ELT:lr

cc: Larry Cerato

ARIZONA LEGISLATIVE COUNCIL

MEMO

April 13, 1979

TO: Douglas R. Norton, Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (0-79-19)

This is in response to a request made on your behalf on March 27, 1979 by Ms. Coni Good.

QUESTION PRESENTED:

Do bookkeeping and similar technical services offered by accountants involve sufficient public interest to need legislative regulation and so interfere with the normal right of an individual to deal with anyone he chooses?

This state has long regulated the profession of public accounting. Within proper limits, the legislature can regulate the profession of accountancy in the interest of general welfare (Hilkert v. Canning, 58 Ariz. 290, 119 P.2d 233 (1942)).

No statutory definition of the practice of public accounting exists in this state. Further, no Arizona court has defined the practice of public accounting.

The attorney general of this state has considered the question of whether preparation of income tax returns comes within the definition of the practice of public accounting.

In Op. Atty. Gen. No. 71-5 (1970), the attorney general concluded that the board of accountancy would have to "determine whether or not the preparation of income tax returns comes within the purview of public accounting." The attorney general determined that preparation of income tax returns would not fall under the practice of public accounting. The attorney general concluded that:

1. Freedom to follow any lawful occupation not injurious to others is a fundamental American liberty, secured by the Federal and State Constitutions alike (Quoting from 10 A.L.R.2d 1425 at page 1444, et seq.).

2. The public convenience, prosperity, health, morals or safety was not advanced nor was danger from incompetency decreased by restricting the preparation of income tax returns to certain persons.

3. The preparation of tax returns is not a function of the practice of accounting which is endowed with public interest sufficient to justify regulation, citing State v. Bookkeepers Business Service Co., 53 Tenn. App. 350, 382 S.W.2d 559 (1964), which quoted from the Journal of Accountancy, December, 1960.

In the Bookkeepers case a Tennessee statute (Tenn. Code Ann. section 62-127) defined the practice of public accounting to include "compiling tax returns". The court determined that the effect of broadly construing a statute which defined the practice of public accounting to include compiling tax returns "...would make the statute unconstitutional as an unwarranted regulation of private business and the right of a citizen to pursue the ordinary occupation of bookkeeper and/or accountant,..."

The material quoted from the Journal of Accountancy in the Bookkeepers case indicated agreement with the proposition that only the "traditional function of certified public accountants - the auditing and expression of an opinion on financial statements, on which third parties may rely - remains...endowed with sufficient public interest to justify legal restriction of the right to perform it to certified public accountants and licensed public accountants."

The conclusions reached by the attorney general have been emphasized because they are pertinent to the discussion of the question of whether bookkeeping falls within the purview of public accounting thereby justifying regulation of bookkeeping activities.

This state does not purport to regulate the practice of bookkeeping. The practice of bookkeeping has generally been considered separate and different from the practice of public accounting.

For example, "public accountant" is defined in 1 C.J.S. Accountant p. 636 (1936) as:

One engaged in rendering accounting or auditing service, as distinguished from bookkeeping, on a fee basis, per diem or otherwise, for more than one employer but generally not possessing all the qualifications of education or experience required of a certified public accountant; . . .

Webster's Third New International Dictionary (1976) defines accountant as "one that is skilled in the practice of accounting; one that has charge of public or private accounts - distinguished from bookkeeper" and accounting as "the system of classifying, recording, and summarizing business and financial transactions in books of account and analyzing, verifying, and reporting the results" and "the body of principles, conventions, and procedures underlying accounting - distinguished from bookkeeping". Bookkeeper, on the other hand, is "one who keeps accounts: one whose business or vocation is bookkeeping - distinguished from accountant". Bookkeeping is defined as "a branch of accounting that deals with the systematic classification, recording, and summarizing of business and financial transactions in books of account".

Therefore, it is apparent the common understanding is that, though related, the practice of accounting is distinct from the practice of bookkeeping.

One court has acknowledged the relationship which exists between accounting and bookkeeping. In Jaeger Mfg. Co. v. Maryland Casualty Co., 683 Iowa 151, 300 N.W. 680 (1941), the court declared that "[E]very accountant must do some form of work that is also done by bookkeepers, and every bookkeeper must perform acts of accounting."

Though the distinction between accounting and bookkeeping was not the central issue in the following cases, the courts often remarked on this distinction while reaching their decisions on the major issue.

The court in Roberts v. Hosking, 95 Mont. 562, 28 P.2d 199 (1933) quoted, with agreement, the definition of "public accountant" found in the Encyclopedia Britannica:

The term . . . is sometimes adopted by bookkeepers, but this is an erroneous application of the term; it properly describes those competent to design and control systems of accounts required for the record of the multifarious and rapid transactions of trade and finance.

In Knight Drug Co. v. Naismith, 73 Ga. App. 793, 38 S.E.2d 87 (1946), the concurring opinion agreed that it is ". . . within the legitimate province of a bookkeeper to balance and post books, without obtaining a license as a certified public accountant, or registering as a public accountant, . . ."

A California court, in Accounting Corp. of America v. State Board of Accountancy, et al, 34 Cal. 2d 186, 208 P.2d 984 (1949), determined that public accountancy involved "[P]roficiency in the examination, analysis and evaluation of financial records . . .".

More recent court cases have concluded that bookkeeping is to be distinguished from accounting and does not possess the requisite qualities which require legal regulation.

The Supreme Court of Florida, in Mercer v. Hemmings, 194 So.2d 579, (1967) appeal dismissed 389 U.S. 46, 19 L.Ed.2d 50, 88 S.Ct. 236, (rehearing denied 389 U.S. 999, 19 L.Ed.2d 506, 88 S.Ct. 465,) cited with agreement the conclusion of the trial court that "ordinary or routine accounting services such as are or may lawfully be performed by bookkeepers" should be distinguished from the services that the defendant firm, Price Waterhouse, sought to provide which were:

. . . services that only certified public accountants or public accountants are qualified and eligible to perform, consisting of the examination and auditing of the books, statements and other records prepared and kept by others, and the preparation of reports of such examinations and audits, including certificates and expressions of opinions.

In People v. Hill, 66 Cal. App. 3d 324, 136 Cal. Rptr. 30 (1977), the defendant was not licensed as a public accountant or certified public accountant, but the defendant used the term "accounting" to describe his business. The defendant had argued that his activities were within the bookkeeping exemption of the California Accountancy Act. The court dismissed his argument by saying "[T]here is a great difference between bookkeeping and accounting. Had appellant advertised himself as "bookkeeper" or "bookkeeping" instead of "accounting," he would have been well within the law." Further, it is noteworthy that the court in Hill commented that:

. . . the trend of courts is to view . . . that accountancy is no longer a profession in which only its members are interested, but that it is a profession in which the public has an interest.

However, it is evident that the only accounting function which is sufficiently endowed with public interest to justify legal restriction is the auditing and expression of opinion on financial statements on which third parties rely.

A final case, Texas State Board of Public Accountancy v. Fulcher, 515 S.W.2d 950 (1974), involved a defendant who was not a certified public accountant or a licensed or registered public accountant but who used the term "accountants" in his business. In addition to the preparation of tax returns and furnishing bookkeeping services the defendant:

. . . renders general accounting services to the public, which include preparation of financial statements and reports, and designing and implementing accounting and bookkeeping systems. He does not make and prepare certified audits nor does he affix his signature to financial reports or statements in such a manner as to indicate that they are based upon a certified audit.

The court held that the defendant had violated the accountancy act by using "accountants" in his business when he was not properly licensed or registered according to the act. In reaching that decision the court concluded that the accountancy act was constitutional and that the act:

. . . does not amount to an unwarranted regulation of private business and the right of a citizen to pursue an ordinary occupation. It does not abridge rights of private property and does not infringe upon rights of contract in matters of purely private concern bearing no perceptible relation to the public welfare.

A quick, random survey of state statutes indicated that, if a state defined the practice of public accounting in any manner, bookkeeping or a general description of bookkeeping services was excluded from the definition. (See Alaska, Alaska Stat. section 08.04.570; California, Business and Professions Code, section 5052 (West); Illinois, Ill. Ann. Stat. ch. 110 1/2, section 35 (Smith-Hurd); Tennessee, Tenn. Code Ann. section 62-162; Florida, Fla. Stat. Ann. section 473.011; South Carolina, S.C. Code, vol. 23, ch. 1, section 1-2.) A more thorough state survey could be conducted if you believe it would be helpful.

The auditing and expression of opinion on financial statements are functions of an accountant which, according to many legislative bodies, are properly regulated by statute to protect the public interest. Many legislatures have not made the same determination with regard to the functions of a bookkeeper. Absent a legislative finding that the protection of the public health, safety or welfare necessitates statutory regulation of the functions performed by a bookkeeper, no statutory regulation is permissible.

CONCLUSION

Bookkeeping and other technical services offered by accountants do not involve sufficient public interest to require legislative regulation. However, the traditional function of accountants, the auditing and expression of any opinion, is properly a subject for legislative regulation to protect the public welfare. One may certainly argue and conclude that legislative regulation of bookkeeping and similar technical services offered by accountants would interfere with the normal right of an individual to deal with anyone he chooses absent a legislative finding that the regulation of bookkeepers is necessary to protect the public welfare. We did not locate any other court decision which expressed this conclusion as forthrightly as the Tennessee case quoted in your request.

cc: Gerald Silva
Performance Audit Manager

APPENDIX IX

RESULTS OF AN AUDITOR GENERAL SURVEY OF THE ARIZONA ACCOUNTING PROFESSION

This survey was conducted to compare characteristics of the accounting profession by the segments Certified Public Accountants, Public Accountants and non-titled accountants.

Surveys were sent to all Certified Public Accountants, Public Accountants and accounting firms registered with the State Board of Accountancy on January 22, 1979 and to other non-titled accountants listed in the 1978 yellow pages in the cities and counties of Phoenix, Tucson, Yuma, Cochise County, Flagstaff, Prescott, Navajo County, Gila County and Sedona. Mr. David Gordon, President of the Arizona Society of Practicing Accountants, generously provided a mailing list of non-titled accountants who were members of that association. The number of surveys sent and returned are scheduled below.

	<u>Number Sent</u>	<u>Number Returned</u>	<u>Percentage Returned</u>
Certified Public Accountants	1,948	936	48%
Public Accountants	91	46	51
Non-Titled Accountants	541	154	28
Miscoded Responses	<u>-</u>	<u>6</u>	<u>-</u>
Total	<u>2,580</u>	<u>1,142</u>	<u>44</u>

SURVEY FOR REVIEW OF THE
STATE BOARD OF ACCOUNTANCY

1. Are you a (select one only):

Certified Public Accountant?	1) <u>936</u>
Public Accountant?	2) <u>46</u>
Non-licensed accounting practitioner?	3) <u>154</u>

2. Are you currently practicing in (select one only) :

Public practice?	1) <u>TABLE 1</u>
Private industry?	2) <u>TABLE 1</u>
Government?	3) <u>TABLE 1</u>
Education?	4) <u>TABLE 1</u>
Retired?	5) <u>TABLE 1</u>
Other?	6) <u>TABLE 1</u>

3. Are you currently a resident of Arizona and practicing in the State?

Yes	1) <u>TABLE 1</u>
No	2) <u>TABLE 1</u>

4. Have you obtained:

A bachelor's degree with 24 or more semester hours in accounting and 18 or more additional semester hours in related business administration and economic courses?	1) <u>TABLE 2</u>
A bachelor's degree with up to 24 semester hours of accounting?	2) <u>TABLE 2</u>
A bachelor's degree without any semester hours in accounting?	3) <u>TABLE 2</u>
None of the above?	4) <u>TABLE 2</u>

5. Approximately how many classroom hours of accounting continuing education do you attend per year?

(Enter Number) TABLE 3

6. To your knowledge, have you been the subject of a complaint investigation conducted by the State Board of Accountancy since January 1, 1976?

Yes	1) <u>TABLE 4</u>
No	2) <u>TABLE 4</u>

7. To your knowledge, have you been the subject of a quality control investigation conducted by the State Board of Accountancy since January 1, 1976?

Yes	1) <u>TABLE 4</u>
No	2) <u>TABLE 4</u>

8. If you were the subject of a complaint and/or quality control investigation, how would you rate the manner in which your case was handled?

Excellent
Satisfactory
Neutral or no opinion
Poor
Unacceptable

- 1) TABLE 5
2) TABLE 5
3) TABLE 5
4) TABLE 5
5) TABLE 5

9. If you feel the State Board of Accountancy did not handle your case adequately, please explain:

IF YOU ARE EMPLOYED IN A PUBLIC PRACTICE IN ARIZONA, PLEASE ANSWER QUESTIONS TEN THROUGH SIXTEEN, OTHERWISE GO ON TO QUESTION SEVENTEEN

10. Other than yourself, how many professional staff persons are employed by your firm?

Certified Public Accountants
Public Accountants
Non-licensed accounting practitioners
with bachelor's degree and 24 or
more hours in accounting
Non-licensed accounting practitioners
who are college graduates in other
area of study
Non-licensed accounting practitioners
who are non-college graduates
Bookkeepers

- 1) TABLE 6
2) TABLE 6
3) TABLE 6
4) TABLE 6
5) TABLE 6
6) TABLE 6

11. The following represent approximately what percentage of the total client fees for professional services provided by your firm?

Auditing (to express an opinion on
financial statements)
Other auditing
Income, estate and gift tax work
Other tax work (sales, payroll, etc.)
Accounting/bookkeeping
Management consulting services
Other

- 1) TABLE 7
2) TABLE 7
3) TABLE 7
4) TABLE 7
5) TABLE 7
6) TABLE 7
7) TABLE 7

TOTAL

100%

Survey for Review of the
State Board of Accountancy
Page Three

12. The following clients represent approximately what percentage of the total fees paid for professional services provided by your firm?

Corporations
Partnerships
Sole proprietorships
Individuals

- 1) TABLE 8
2) TABLE 8
3) TABLE 8
4) TABLE 8

TOTAL 100%

13. Approximately what percentage of your business clients have the following gross receipts?

Less than \$ 50,000
\$ 50,000 up to \$ 100,000
\$100,000 up to \$ 250,000
\$250,000 up to \$ 500,000
\$500,000 up to \$1,000,000
Over \$1,000,000

- 1) TABLE 9
2) TABLE 9
3) TABLE 9
4) TABLE 9
5) TABLE 9
6) TABLE 9

TOTAL 100%

14. Approximately what percentage of your individual clients have the following annual incomes?

Less than \$ 5,000
\$ 5,000 up to \$ 10,000
\$10,000 up to \$ 20,000
\$20,000 up to \$ 50,000
\$50,000 up to \$100,000
Over \$100,000

- 1) TABLE 10
2) TABLE 10
3) TABLE 10
4) TABLE 10
5) TABLE 10
6) TABLE 10

TOTAL 100%

15. What are your hourly rates for services?

Auditing (to express an opinion on
financial statements)
Other auditing
Income, estate and gift tax work
Other tax work
Accounting/bookkeeping
Management consulting services
Other

- 1) TABLE 11
2) TABLE 11
3) TABLE 11
4) TABLE 11
5) TABLE 11
6) TABLE 11
7) TABLE 11

16. What is your malpractice insurance coverage?
(Enter \$ 0 if you do not carry malpractice insurance.)

(Enter Number)

ANSWERS NOT
USABLE

17. Any additional comments you may have regarding the regulation of the accounting profession in Arizona are welcomed.

	ARIZONA RESIDENT			NON-RESIDENT
	CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT	
Public Practice	475	23	145	643
Private Industry	191	6	3	200
Government	46	4	2	52
Education	18	-	-	18
Retired	19	4	1	24
Other	21	2	1	24
Total	770	39	152	961

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL
MARCH 1979

TABLE 2 EDUCATION LEVEL OBTAINED
BY ACCOUNTANTS

EDUCATION OBTAINED	ARIZONA RESIDENT			EDUCATION OBTAINED	NON-RESIDENT		
	CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT		CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT
No Answer	1	3	-	No Answer	2	-	1
Bachelor's Degree with 24 hours of accounting and 18 hours of related courses	701	22	65	Bachelor's Degree with 24 hours of accounting and 18 hours of related courses	129	2	-
Bachelor's Degree with up to 24 hours of accounting	32	1	14	Bachelor's Degree with up to 24 hours of accounting	7	1	1
Bachelor's Degree with no accounting	4	-	2	Bachelor's Degree with no accounting	3	-	-
None of the above	33	13	71	None of the above	8	2	-
Total	771	39	152	Total	149	5	2
			962				156

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL

MARCH 1979

TABLE 3 CONTINUING EDUCATION
CURRENTLY BEING TAKEN
BY ACCOUNTANTS

CONTINUING EDUCATION HOURS TAKEN PER YEAR	ARIZONA ACCOUNTANTS			CONTINUING EDUCATION HOURS TAKEN PER YEAR	ARIZONA ACCOUNTANTS IN PUBLIC PRACTICE			
	CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT		CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT	Total
0-15	346	31	60	437	72	12	56	140
15-30	174	6	32	212	103	4	28	135
31-45	241	4	25	270	180	3	24	207
46-60	109	2	18	129	78	2	18	98
More than 60	66	3	19	88	42	2	19	63
Total	936	46	154	1136	475	23	145	643

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL

MARCH 1979

TABLE 4 INVESTIGATIONS CONDUCTED
BY THE BOARD

ACCOUNTANTS SUBJECT TO A
COMPLAINT INVESTIGATION

	ARIZONA RESIDENT		
	CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT
Yes	43	-	1
No	724	38	150
Total	767	38	151
			956

ACCOUNTANTS SUBJECT TO A
QUALITY CONTROL INVESTIGATION

	ARIZONA RESIDENT		
	CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT
Yes	27	1	-
No	736	37	149
Total	763	38	149
			950

OUT-OF-STATE RESIDENT

	OUT-OF-STATE RESIDENT		
	CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT
Yes	-	1	2
No	149	4	-
Total	149	5	2
			156

OUT-OF-STATE RESIDENT

	OUT-OF-STATE RESIDENT		
	CERTIFIED PUBLIC ACCOUNTANT	PUBLIC ACCOUNTANT	NON-TITLED ACCOUNTANT
Yes	-	-	-
No	148	5	2
Total	148	5	2
			155

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL

MARCH 1979

TABLE 5 OPINION OF INVESTIGATIONS
CONDUCTED BY THE BOARD

	ARIZONA PRACTITIONER'S OPINION OF THE INVESTIGATION PROCESS AS APPLIED TO HIS CASE			
	<u>CERTIFIED PUBLIC ACCOUNTANT</u>	<u>PUBLIC ACCOUNTANT</u>	<u>NON-TITLED ACCOUNTANT</u>	<u>Total</u>
Excellent	10	-	1	11
Satisfactory	18	1	-	19
Neutral or no opinion	7	-	-	7
Poor	10	-	-	10
Unacceptable	12	-	-	12
No Answer	5	-	-	5

TABLE 6 TABULATION OF THE SIZES
OF FIRMS WHICH EMPLOY
ACCOUNTANTS IN PUBLIC PRACTICE

	ARIZONA ACCOUNTING PRACTITIONER'S FIRM SIZE			
	<u>CERTIFIED PUBLIC ACCOUNTANT</u>	<u>PUBLIC ACCOUNTANT</u>	<u>NON-TITLED ACCOUNTANT</u>	<u>Total</u>
Sole Practitioner	75	7	40	122
From 2-5 Staff	138	11	86	235
From 6-12 Staff	122	1	12	135
From 13-25 Staff	63	-	1	64
Over 25 Staff	77	-	-	77
Total	475	19	139	633

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL
MARCH 1979

TABLE 7 AVERAGE PERCENTAGE OF TOTAL CLIENT FEES
DERIVED FROM THE SPECIFIED SERVICE BY THE
SIZE OF THE FIRM

	CERTIFIED PUBLIC ACCOUNTANT FIRM SIZE					PUBLIC ACCOUNTANT FIRM SIZE				
	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff
Auditing to Express Opinion	13.7	8.3	21.3	25.1	49.5	21.4	.5	1.8	-	1.3
Other Auditing	2.4	2.6	3.9	3.8	4.5	3.4	1.2	3.2	-	2.4
Income, Estate and Gift Taxes	46.7	35.0	30.1	32.1	22.5	33.2	31.3	29.5	-	30.2
Other Taxes	5.1	7.8	7.0	6.6	2.4	6.1	7.5	9.5	-	8.7
Accounting/Bookkeeping	21.7	38.2	29.0	22.1	11.3	26.7	59.5	52.3	-	55.1
Management Services	7.1	6.9	6.9	8.2	8.9	7.4	-	3.7	-	2.3
Other	3.3	1.2	1.8	2.1	.9	1.8	-	-	-	-
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	-	100.0%

	NON-TITLE ACCOUNTANT FIRM SIZE				
	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff
Auditing to Express Opinion	.7	.2	-	3.0	.3
Other Auditing	-	1.4	.2	57.0	1.3
Income, Estate and Gift Tax	40.6	31.3	27.6	5.0	33.5
Other Tax	8.2	9.1	9.2	20.0	8.9
Accounting/Bookkeeping	46.6	50.5	53.5	15.0	49.4
Management Services	3.1	5.7	9.0	-	5.2
Other	.8	1.8	.5	-	1.4
	100.0%	100.0%	100.0%	100.0%	100.0%

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL

MARCH 1979

TABLE 8 AVERAGE PERCENTAGE OF TOTAL
PROFESSIONAL FEES DERIVED FROM
SPECIFIED CLIENTS BY FIRM SIZE

	CERTIFIED PUBLIC ACCOUNTANT FIRM SIZE					PUBLIC ACCOUNTANT FIRM SIZE				
	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff
Corporations	43.4	41.3	44.8	45.0	71.6	14.0	27.7	15.0	-	-
Partnerships	11.8	12.6	14.0	14.4	10.0	8.0	15.2	10.0	-	-
Sole Proprietors	19.9	21.9	20.0	19.0	7.0	39.9	28.2	75.0	-	-
Individuals	24.9	24.2	21.2	21.6	11.4	38.1	28.9	-	-	-
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	-	-

	NON-TITLED ACCOUNTANT FIRM SIZE				
	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	
Corporations	18.4	26.6	24.5	15.0	-
Partnerships	4.6	7.8	7.2	2.0	-
Sole Proprietors	38.3	36.1	50.8	23.0	-
Individuals	38.7	29.5	17.5	60.0	-
	100.0%	100.0%	100.0%	100.0%	-

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL
MARCH 1979

Table 9 AVERAGE PERCENTAGE OF BUSINESS
CLIENTS WITH THE SPECIFIED
YEARLY GROSS ANNUAL RECEIPTS
BY FIRM SIZE

Business Clients	CERTIFIED PUBLIC ACCOUNTANT FIRM SIZE				PUBLIC ACCOUNTANT FIRM SIZE			
	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	Over 25 Staff	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	Over 25 Staff
Yearly Gross Receipts								
Less Than								
\$ 50,000	26.1	14.6	6.6	4.4	95.0	9.5	-	-
50,000 to								
100,000	16.8	15.4	12.6	5.0	2.5	23.0	60.0	-
100,000 to								
250,000	13.3	25.6	22.6	9.7	2.5	30.5	25.0	-
250,000 to								
500,000	17.6	23.0	23.1	11.7	-	24.5	15.0	-
500,000 to								
1,000,000	9.8	11.5	18.5	16.6	-	9.3	-	-
Over								
1,000,000	16.4	9.9	16.6	52.6	-	3.2	-	-
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	-

Business Clients	NON-TITLED ACCOUNTANT FIRM SIZE			
	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	Over 25 Staff
Yearly Gross Receipts				
Less than				
\$ 50,000	39.1	23.6	27.9	5.0
50,000 to				
100,000	28.5	23.2	22.8	60.0
100,000 to				
250,000	19.8	24.9	18.1	30.0
250,000 to				
500,000	7.4	15.8	17.1	3.0
500,000 to				
1,000,000	3.1	6.5	8.7	2.0
Over				
1,000,000	2.1	6.0	5.4	-
	100.0%	100.0%	100.0%	100.0%

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL

MARCH 1979

TABLE 10 AVERAGE PERCENTAGE OF INDIVIDUAL
CLIENTS WITH SPECIFIED YEARLY
INCOME BY FIRM SIZE

Individual Clients	CERTIFIED PUBLIC ACCOUNTANT FIRM SIZE					PUBLIC ACCOUNTANT FIRM SIZE				
	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff
Yearly Income										
Less than \$ 5,000	1.7	1.3	1.9	.7	.4	4.0	1.6	-	-	-
5,000 to 10,000	8.2	5.0	3.8	3.2	1.5	15.1	4.1	-	-	-
10,000 to 20,000	25.6	21.0	11.9	9.1	5.2	25.1	29.0	-	-	-
20,000 to 50,000	47.0	50.6	43.8	40.1	21.5	46.5	53.3	-	-	-
50,000 to 100,000	12.7	16.1	27.8	35.8	38.5	8.3	9.1	-	-	-
Over 100,000	4.8	6.0	10.8	11.1	32.9	1.0	2.9	-	-	-
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	-	-	-

Individual Clients	NON-TITLED ACCOUNTANT FIRM SIZE				
	<u>Sole Practitioner</u>	<u>From 2-5 Staff</u>	<u>From 6-12 Staff</u>	<u>From 13-25 Staff</u>	<u>Over 25 Staff</u>
Yearly Income					
Less than \$ 5,000	5.6	4.7	3.6	-	-
5,000 to 10,000	13.9	11.8	6.8	5.0	-
10,000 to 20,000	49.0	33.7	33.6	20.0	-
20,000 to 50,000	27.0	37.8	37.6	60.0	-
50,000 to 100,000	3.3	10.8	11.2	10.0	-
Over 100,000	1.2	1.2	7.2	5.0	-
	100.0%	100.0%	100.0%	100.0%	-

SURVEY OF THE ACCOUNTING PROFESSION
BY THE OFFICE OF THE AUDITOR GENERAL
MARCH 1979

TABLE 11 AVERAGE HOURLY FEES
CHARGED FOR SPECIFIED
SERVICE BY FIRM SIZE

CERTIFIED PUBLIC ACCOUNTANT FIRM SIZE						PUBLIC ACCOUNTANT FIRM SIZE					
Type of Service	Practitioner	From Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff	Type of Service	Practitioner	From Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff
Attest						Attest					
Audit Fee	\$28.10	\$36.20	\$38.20	\$39.40	\$44.40	Audit Fee	\$35.00	\$35.00	-	-	-
Other						Other					
Audit Fee	32.90	34.20	36.10	42.50	45.50	Audit Fee	33.30	26.00	-	-	-
Income, Estate						Income					
Gift Tax Fee	34.80	36.20	38.50	44.20	47.30	Tax Fee	29.40	33.30	-	-	-
Other						Other					
Tax Fee	32.10	33.30	37.50	40.20	49.90	Tax Fee	33.30	26.40	-	-	-
Accounting/						Accounting/					
Bookkeeping Fee	22.20	24.60	26.30	29.30	30.00	Bookkeeping Fee	26.40	18.60	\$15.00	-	-
Management						Management					
Service Fee	38.00	39.00	39.20	45.90	49.80	Service Fee	45.00	33.10	-	-	-
Other						Other					
Fee	\$32.20	\$33.90	\$37.50	\$40.60	\$49.90	Fee	\$25.00	\$22.50	-	-	-

NON-TITLED ACCOUNTANT FIRM SIZE						
Type of Service	Sole Practitioner	From 2-5 Staff	From 6-12 Staff	From 13-25 Staff	Over 25 Staff	
Attest						
Audit Fee	\$26.70	\$27.00	-	\$35.00	-	
Other						
Audit Fee	21.70	26.30	\$40.00	35.00	-	
Income Tax						
Fee	23.90	28.00	35.00	40.00	-	
Other Tax						
Fee	20.20	23.60	29.40	20.00	-	
Accounting/Bookkeeping Fee	19.80	20.80	30.00	20.00	-	
Management Service Fee	30.00	30.40	31.00	50.00	-	
Other						
Fee	\$18.20	\$25.10	\$17.30	\$75.00	-	

APPENDIX X

CASE STUDIES OF INVESTIGATIONS RESOLVED BY THE STATE BOARD OF ACCOUNTANCY DURING 1978

The following appendix contains a summary of the complaint and quality control investigations which were resolved by the Board of Accountancy during the calendar year 1978. A summarized version of each case, the total number of days expended during the investigation, the Board's resolution and the source of the alleged violation are presented for evaluation.

CASE STUDIES OF INVESTIGATIONS
RESOLVED BY THE STATE BOARD OF
ACCOUNTANCY DURING 1978

Case #	Description	Total Time to Process	Resolution				Source				
			Consent Order/Other	Cease and Desist Order	Warning	No Action Taken	Public Filings or Review Investigator	Staff or Board Member	Other Agency Referral	Public Complaint	News-paper Articles
1	Audit was not conducted in accordance with generally accepted auditing standards. Audit workpapers did not include sufficient evidence to support unqualified opinion. Assets were materially overstated, significant accounting policies were not disclosed and affiliated party transactions were not disclosed.	788				X			X		
2	While acting as a fiduciary, registrant commingled trust money with personal finances. Registrant did not properly account for trust investments, receipts, disbursements and income taxes.	1254				X					X
3	Audit was not conducted in accordance with generally accepted auditing standards and financial statements were not presented in conformity with generally accepted accounting principles. Assets were materially overstated and a statement of changes in financial position was not prepared.	988				X					X
4	Registrant did not perform duties of comptroller by not maintaining significant accounting records. Registrant had been convicted of mail fraud, securities fraud, interstate transportation of money which was obtained by fraud and aiding and abetting. Convictions were subsequently overruled.	489				X					X
5	Unaudited financial statements were not accompanied by a disclaimer opinion and were not marked unaudited. Accounting records did not support financial statements. A statement of changes in financial position was not included.	867				X				X	

CASE STUDIES OF INVESTIGATIONS
RESOLVED BY THE STATE BOARD OF
ACCOUNTANCY DURING 1978

Case #	Description	Total Time to Process	Resolution					Source					
			Revocation	Suspension	Consent Order/Other Sanction	Cease and Desist Order	Advisory Action Warning	No Action Taken	Public Filings Review Investigator	Staff or Board Member	Other Agency Referral	Public Complaint	News- paper Articles
6	Audited financial statements did not include a statement of changes in financial position or the necessary footnotes required by generally accepted accounting principles.	868			X					X			
7	Audited financial statements were presented in accordance with generally accepted accounting principles. Audit was not conducted in conformity with generally accepted auditing standards. Assets were materially overstated, other deficiencies existed. Intentional misrepresentation was not uncovered.	348		X							X		
8	Audit was conducted to conform with federal regulations rather than generally accepted accounting principles. Auditors report should have noted the differences.	682					X					X	
9	Although audited financial statements contained minor deficiencies, case was dropped because registrant entered into a consent agreement for another violation.	348						X		X			
10	Auditor's opinion did not include qualifications which were presented in footnotes to financial statements. A statement of changes in financial position was not included and consolidated statements for parent and subsidiary were not presented.	466			X						X		
11	Board investigated registrant's role in deficient audit conducted by registrant's partner. Investigation concluded partner was totally responsible. (Partner entered into a consent order)	378									X		

CASE STUDIES OF INVESTIGATIONS
RESOLVED BY THE STATE BOARD OF
ACCOUNTANCY DURING 1978

Case #	Description	Total Time to Process	Resolution				Source				
			Consent Order/Other Sanction	Cease and Desist Order	Advisory Warning	No Action Taken	Public Filings Review Investigator	Staff or Board Member	Other Agency Referral	Public Complaint	News-paper Articles
12	Same as Case 8	217			X					X	
13	Same as Case 8	496			X					X	
14	Same as Case 8	455			X					X	
15	Same as Case 8, except that the opinion was modified	217			X					X	
16	Although several deficiencies were discovered in financial statements of a municipality, the case was dropped because registrant died during investigation.	336				X					
17	Investigator uncovered only minor format deficiencies on a municipal audit. Recommendations were sent to the registrant.	189			X						
18	On municipal and educational audits several deviations from generally accepted accounting principles were found, including - combination of funds, inadequate notes to financial statements and failure to include a statement of changes in financial position.	307								X	
19	On a municipal audit deviations from generally accepted accounting principles were as follows - inadequate disclosure through notes to financial statements. Generally accepted auditing standards were violated with respect to auditor's opinion which did not state responsibility for several supplemental schedules.	306	X								
20	On a municipal audit several deviations from generally accepted accounting principles were uncovered including - combination of funds, restrictions on cash remained undisclosed, budget information was not presented, improper accounting for one fund, and inadequate foot-	340	X								

CASE STUDIES OF INVESTIGATIONS
RESOLVED BY THE STATE BOARD OF
ACCOUNTANCY DURING 1978

[illegible]

CASE STUDIES OF INVESTIGATIONS
RESOLVED BY THE STATE BOARD OF
ACCOUNTANCY DURING 1978

Case #	Description	Total Time to Process	Resolution					Source				
			Revocation	Suspension	Consent Order/Other Sanction	Cease and Desist Order	No Advisory Action Taken	Public Filings Review Investigator	Staff or Board Member	Other Agency Referral	Public Complaint	News-paper Articles
30	Board did not uncover any violations on an education audit.	245					X			X		
31	Board discovered only minor errors on an education audit. Discoveries were forwarded to the auditor for informative purposes.	273					X			X		
32	Use of CPA title without being licensed, individual agreed not to use title.	91				X						X
33	Alleged substandard reporting by a nonlicensed accounting entity. Board has no jurisdiction over unlicensed entities.	39					X				X	
34	Alleged ethics violation. CPA was operating out of the same office as a nonlicensed person. Board ruled no violation occurred.	42					X				X	
35	Client filed complaint against CPA when a refund check paid by CPA did not have sufficient funds. CPA later paid in full.	273					X				X	
36	CPA was holding records in lieu of a fee. Records were returned.	68					X				X	
37	On a routine accounting engagement, CPAs did not uncover embezzlement. Board ruled no jurisdiction because audit steps were not performed.	110					X				X	
38	Only minor deficiencies were uncovered in an investigation of a municipal audit. Discoveries were forwarded to auditors.	130					X				X	
39	During investigation of municipal audit, the auditor died causing the Board to drop the case.	1					X				X	
40	The municipal audit was not reviewed because registrants were censured in another investigation.	1					X				X	

CASE STUDIES OF INVESTIGATIONS
RESOLVED BY THE STATE BOARD OF
ACCOUNTANCY DURING 1978

Case #	Description	Total Time to Process	Resolution					Source																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																						
			Revocation	Suspension	Consent Order/Other Sanction	Cease and Desist Order	Advisory Warning	No Action Taken	Public Filings Review Investigator	Staff or Board Member	Other Agency Referral	Public Complaint	News-paper Articles																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																	
41	Client claimed registrant could have prepared a tax return in a more advantageous manner while remaining within the law. Board ruled no basis for action.	139																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																												

CASE STUDIES OF INVESTIGATIONS
RESOLVED BY THE STATE BOARD OF
ACCOUNTANCY DURING 1978

Case #	Description	Total Time to Process	Resolution				Source						
			Revocation	Suspension	Consent Order/Other Sanction	Cease and Desist Order	No Advisory Action Taken	Public Filings Review Investigator	Staff or Board Member	Other Agency Referral	Public Complaint	News-paper Articles	
56	A complaint against a registrant was received by the Board and by several other agencies, including the Attorney General. Board determined the complaint was a civil matter and should be properly handled by one of the other agencies. Complaint involved registrant's personnel policies.	68					X				X		
57	A client brought charges against the CPA for not paying an interest fee on a late tax filing. The Board ruled that the complaint was a fee dispute even though many CPAs will pay interest and penalty fees.	67					X				X		
58	A creditor of a CPA brought charges against the CPA for not paying the full amount owed. The Board ruled that they have no jurisdiction over fee squabbles or registrants' debt.	14					X				X		
59	A nonlicensed person was using the CPA title. The person agreed not to use title.	11					X			X			
60	Board considered an education audit which was performed by an unlicensed accounting firm. Board has no jurisdiction over unlicensed accountants.	1					X			X			
TOTAL			3	2	8	4	8	35	19	3	7	26	5

APPENDIX XI

COMMENTS RECEIVED FROM A CERTIFIED PUBLIC ACCOUNTANT REGARDING THE EXTENT AND SCOPE OF THE BOARD'S QUALITY REVIEW PROGRAM.

"I encouraged the Board to get tougher, but I am now concerned that infractions are causing extremely severe penalties for the sake of publicity and to prove the 'need' for the Board. The penalties are being assessed against a very limited population (those firms and individuals submitting statements or reports to State Agencies). The press releases are distorted and cause much damage to those subject to Board action. We in the profession are not told what caused the penalties so we are not being educated as to potential pitfalls. Instead, we are threatened and intimidated to the point that I am not accepting engagements that require reports to be filed with a State Agency. My continuing education and quality control efforts are as good or better than most firms and much better than most sole practitioners, but I refuse to subject myself to potential bad publicity and damage to my career simply because the Board is trying to justify its existence to the Legislature and seeking to intimidate the small firms.

Now that the profession is aware of the Board's power (or at least the power of the Attorney General's Office) why doesn't the Board start holding seminars where reporting errors, etc. which led to the various consent orders may be exposed (concealing names of CPAs and clients) so that we may learn from the errors. Also, the Board should limit news releases (preferably eliminate them) so that distortions, half truths, and only one side of the story are prevented.

In conclusion, I do not believe you can upgrade the public accounting profession through intimidation or even legislation. It must be by an aware and concerned body of professionals who keep current and insist on improving their profession. Legal action should be limited to criminal activities such as fraud, conspiracy to defraud, embezzlement, etc. and the board should regulate by educating those whom they find lacking in professional knowledge."

ARIZONA LEGISLATIVE COUNCIL

MEMO

May 25, 1979

TO: Douglas R. Norton, Auditor General
FROM: Arizona Legislative Council
RE: Request for Research and Statutory Interpretation (O-79-41)

This is in response to a request made on your behalf by Gerald A. Silva in a memo dated May 8, 1979.

FACT SITUATION:

The board of accountancy regularly scrutinizes, through its quality review program, audits and financial statements filed with public agencies. The board's investigator, when conducting a quality review, compares the filings to a preliminary review checklist containing the basic elements of generally accepted auditing standards and accounting principles. The investigator reports any exceptions from these standards and principles to the board for its consideration and action. However, the program provides for a review of only a portion of the work performed by accountants certified and registered with the board. The members of the board believe that, without a complaint, audits and financial statements used by private entities are not accessible to the board for its quality review program and that due to this inaccessibility substandard work may go undetected, causing financial harm to members of the public. The basis for the board's belief is Arizona Revised Statutes section 32-744, which states:

All statements, schedules, working papers and memoranda made by a certified public accountant or public accountant incident to or in the course of professional service to clients, except reports submitted to a client, shall be and remain the property of the certified public accountant or public accountant, in the absence of an express agreement between the certified public accountant or public accountant and the client to the contrary.

QUESTIONS PRESENTED:

1. Based on legal precedent, is the Board correct in its understanding that audits, financial statements and working papers supporting them are not accessible for purposes of quality review as now conducted with public filings?
2. If, instead of quality review as now conducted, mandatory peer review were implemented, would the exceptions noted in the review be accessible to the Board for possible disciplinary action?

ANSWERS:

1. No.
2. Yes.

1. Arizona Revised Statutes section 32-744, set forth above, is a restatement of the general rule regarding an accountant's right to retain certain data.

Working papers, drafts, notes, calculations, and typed final accounts brought into being by an accountant in the course of auditing a client's account and ascertaining its tax liability, have been held to be the property of the accountant and a proper subject of an order against such accountant for their production in an action to which the accountant is a party... However, correspondence conducted by an accountant as agent for a client for the purpose of settling a tax liability has been held to be the property of the client. (1 AM. JUR. 2d Accountants section 12 (1962).)

Based upon the above cited summation of the law, the board has correctly concluded that audits, financial statements and working papers supporting the audits and financial statements are the property of private concerns, such as lending institutions and other corporations. However, the right of access by the board to this material may only be ascertained by an examination of the board's regulatory powers and the accountant-client privilege.

There was no accountant or accountant-client privilege at common law. "Absent a statute specifically denominating accountant-client transactions as privileged, no privilege attaches to such transactions." 8 Wigmore, Evidence section 2286 (McNaughton rev. 1961).

Arizona Revised Statutes section 32-749, as amended by Laws 1979, chapter 109, section 13, provides:

Certified public accountants and public accountants practicing in this state shall not be required to divulge, nor shall they voluntarily divulge information which they have received by reason of the confidential nature of their employment. Information derived from or as a result of such professional source shall be deemed confidential, but this section shall not be construed as modifying, changing or affecting the criminal or bankruptcy laws of this state or the United States, nor shall it be construed to limit the authority of this state or any agency of this state to subpoena and use such information in connection with any investigation, public hearing or other proceeding.

This statute may be construed as creating both an accountant privilege and an accountant-client privilege. See Ernst & Ernst v. Underwriters Nat. Assur., 381 N.E. 2d 897 (1978), (Indiana accountant-client privilege statute); Ash v. H.G. Reiter Company, 78 N.M. 194, 429 P.2d 653 (1967), (separate New Mexico accountant and accountant-client privilege statutes); Dorfman v. Rombs, 218 F. Supp. 905 (1963), (Illinois accountant privilege statute); and Falsone v. United States, 205 F. 2d 734 (1953), cert. denied (1953),

346 U.S. 864, 74 S.Ct. 103, (Florida accountant-client privilege statute). (However, because of the limited applicability of the statute, which will be discussed further, no determination need be made as to what privileges are created.)

In the absence of statutory language to the contrary, accountants or clients could assert their privileges and deny the board access to audits, financial statements and working papers supporting the audits and financial statements. However, both case law and Arizona Revised Statutes Title 32, chapter 6 authorize the board to conduct a quality review of work performed by all accountants certified and registered with the board and, if necessary, to subpoena information such as audits and financial statements.

The privileges created by Arizona Revised Statutes section 32-749 are specifically limited by that section, which provides that it shall not "...be construed to limit the authority of this state or any agency of this state to subpoena and use such information in connection with any investigation, public hearing or other proceeding."

In addition, Arizona Revised Statutes Title 32, chapter 6 provides for the regulation of certified public accountants and public accountants and grants the board of accountancy broad powers to administer the provisions of that chapter and "...prescribe...rules of conduct appropriate to establish and maintain a high standard of integrity and dignity in public accounting." Arizona Revised Statutes section 32-703.

In Atchison, T. & S.F. Ry. Co. v. Kansas Com'n on Civil Rights, 215 Kan. 911, 529 P.2d 666 (1974), the court addressed the scope of the investigatory powers of the Kansas Commission on Civil Rights. The court noted:

"[i]nvestigation" is appropriately used with regard to nonjudicial functions of an administrative agency and the seeking of information for future use rather than proceedings in which action is taken against someone. (Citations omitted.) An "investigation" is nonadversary and contemplates a procedure much less formal and more flexible than applies even to an administrative hearing. 529 P.2d at 673.

The court specifically recognized that the commission was "... granted broad powers of investigation even though a formal complaint is not filed." 529 P.2d at 672.

To summarize, any accountant or accountant-client privilege which exists in Arizona is limited by the state's authority to subpoena information in connection with any investigation, hearing or other proceeding. The board of accountancy is authorized pursuant to Arizona Revised Statutes Title 32, chapter 6 to conduct a quality review program of the work of all accountants certified and registered with it. In the absence of voluntary production of audits, financial statements and working papers for the board's review, the board could initiate proceedings and compel the production of the items by subpoena (Arizona Revised Statutes section 32-743). The only privilege that could then be asserted by an accountant or a client would be the privilege against self-incrimination (U.S. CONST. amend. V; and Ariz. Const. art. 2, section 10).

2. Any exceptions from the generally accepted auditing standards and accounting principles noted during a mandatory peer review program implemented by the board of accountancy would be accessible to the board for its consideration and action as discussed above.

CONCLUSIONS:

1. Audits, financial statements and working papers supporting the audits and financial statements made by any accountant certified and registered with the board are accessible to the board for the purpose of conducting a quality review of the accountant's work.

You may wish to recommend that the statutes be amended to provide immunity to the board of accountancy, its members or employees for any action taken by them in good faith pursuant to a quality review. In addition, for the protection of the client, the board, its members or employees should be prohibited from disclosing any information obtained as a result of a quality review except pursuant to a hearing as provided in Arizona Revised Statutes, Title 32, chapter 6.

2. Any exceptions from the generally accepted auditing standards and accounting principles noted during a quality review pursuant to a mandatory peer review program would be accessible to the board for possible disciplinary action.

cc: Gerald A. Silva
Performance Audit Manager



Attorney General
STATE CAPITOL
Phoenix, Arizona 85007

Robert R. Corbin

May 24, 1979

Mr. Ron Trasente, Assistant Director
Administrative Services Division
Arizona Department of Transportation
206 South 17th Avenue
Phoenix, Arizona 85007

Re: I79-140 (R77-373)

Dear Mr. Trasente:

Your predecessor in office requested an opinion regarding disclosure by the Department of Transportation to the State Board of Accountancy of financial statements filed by contractors as part of the prequalification procedures for bidding on state highway construction contracts. According to his letter, the objective of such disclosure to the Accountancy Board is to enable the Board to review the financial statements to assist in the Board's policing of the accountancy profession and to determine if the state is being afforded adequate information upon which to rely in the prequalification procedures. The financial statements are filed by contractors seeking prequalification pursuant to A.C.R.R. R17-3-04. Part 7 of that rule provides:

Prequalification files will be considered as strictly confidential in nature. The files will be available only to the following parties:

1. Members of the Board.
2. The Director, Arizona Department of Transportation, and his bonded agents.
3. The members of the Transportation Board.
4. The Division Engineer of the Federal Highway Administration or his authorized representatives.
5. Agents of Surety, upon presentation of Application for Bond duly signed by an authorized party of the contracting firm when Application for Bond contains a clause granting Surety full access to such information.

Your specific questions and our discussion follow.

1. Are prequalification financial statements filed with this Department pursuant to the Board's rule alluded to above public records which must be made available to the public upon request?

A.R.S. § 39-121 provides:

Public records and other matters in the office of any officer at all times during office hours shall be open to inspection by any person.

A statutory definition of the "public records and other matters" which A.R.S. § 39-121 requires to be open to public inspection is not provided. We must resort, therefore, to case law definitions of "public records and other matters" to determine the availability of prequalification financial statements for inspection.

The records to be disclosed under A.R.S. § 39-121 are those made by public officers in pursuance of a duty; records required by law to be kept; records necessary to the discharge of a public officer's duty; and include writings coming into the hands of public officials in connection with their public duties. Mathews v. Pyle, 75 Ariz. 76, 251 P.2d 893 (1953); MacEwan v. Holm, 226 Or. 27, 359 P.2d 413 (1961); Atty Gen.Op. No. 76-43.

It appears to us that the financial statements submitted by contractors pursuant to A.C.R.R. R17-3-04 seeking prequalification for public contracts are clearly received by the Department of Transportation in connection with its public duty to evaluate bids and award contracts for highway construction. We therefore conclude that the financial statements submitted by contractors fall within the scope of "public records and other matters" under A.R.S. § 39-121; however, because part 7 of Rule R17-3-04 provides that prequalification files will be considered "strictly confidential in nature" and will be available only to certain named persons not including the Accountancy Board, we must consider whether this declaration of confidentiality by the Department of Transportation is a permissible exception to the public disclosure otherwise mandated by A.R.S. § 39-121.

In Mathews v. Pyle, the Arizona Supreme Court held that a public official may deny public access to a document that falls within the category of "other matters" as distinguished from "public records" in the strict meaning of that term¹ if in the official's judgment the document contains matters that are confidential or of such a nature that disclosure would be detrimental to the interests of the state. Id., 75 Ariz. at 81. The official's judgment, however, is subject to judicial review. Mathews v. Pyle, A.R.S. § 39-121.02. No statute makes the prequalification files confidential, therefore, the Department of Transportation must be prepared to articulate to a reviewing court that the prequalification files are "other matters" which public policy demands be treated as confidential. This office repeatedly has advised that any doubts in such a determination of confidentiality should be resolved in favor of public disclosure. Atty.Gen.Op. No. 76-293, October 19, 1976; Atty.Gen..Op. No. 76-43, February 13, 1976.

A.C.R.R. R17-3-04, part 7, indicates that the Department of Transportation has determined that it would be detrimental to the interests of the state to disclose the contents of such files, including the financial statements contained therein.

1. In Mathews v. Pyle, the court said:

A public record is defined as follows: "A public record, strictly speaking, is one made by a public officer in pursuance of a duty, the immediate purpose of which is to disseminate information to the public, or to serve as a memorial of official transactions for public reference." [Citations omitted.] Also a record is a "public record" which is required by law to be kept, or necessary to be kept in the discharge of a duty imposed by law or directed by law to serve as a memorial and evidence of something written, said or done.

75 Ariz. at 78.

This interpretation of the rule is necessary to avoid concluding that the rule is contrary to A.R.S. § 39-121 and therefore invalid.² As the matter now stands, therefore, we can conclude that the financial statements filed by contractors pursuant to A.C.R.R. R17-3-04 are confidential and are not required to be disclosed by A.R.S. § 39-121.³

2. If the prequalification financial statements are not public records, is there any legal means by which copies can be made available to the staff of the Accountancy Board without subjecting this Department or its officers or employees to the threat of legal liabilities?

This question is answered by A.C.R.R. R17-3-04, part 7. That section indicates that disclosure will be made to the persons indicated in the rule, and the Accountancy Board is not listed as one of those to whom disclosure may be made.

It is axiomatic that an agency must observe its own rules and regulations. Duly promulgated rules have the effect of law, are binding on the agency which promulgated them and must be followed so long as they are in force and effect. Tucson Warehouse and Transfer Co. v. Al's Transfer, Inc., 77 Ariz. 323, 271 P.2d 477 (1954); Civil Service of City of Phoenix v. Warren, 74 Ariz. 88, 244 P.2d 1157 (1952). We therefore conclude that, so long as A.C.R.R. R17-3-04 is effective in its present form, the Department of Transportation cannot voluntarily disclose the contents of a contractor's prequalification file to any person not indicated in part 7 of that rule.

2. This opinion is based on the assumption that A.C.R.R. R17-3-04 has been validly promulgated in accordance with A.R.S. §§ 41-1001 et seq. and its predecessors. We note, however, that the substantive provisions of the prequalification requirements do not appear in the Secretary of State's compilation of A.C.R.R. R17-3-04, and suggest that you notify the Secretary of State regarding this circumstance.

3. We must emphasize that this conclusion is based upon our assumption that it is in the State's interest to maintain these files as confidential.

Mr. Ron Trasente
May 24, 1979
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In view of the conclusions reached in response to your first and second questions, we deem it unnecessary to address your third and fourth questions. However, in view of your indication that you would like to cooperate with the State Board of Accountancy, we suggest that you consider amending the rule. This option seems particularly appropriate in view of both the strong public policy supporting disclosure under A.R.S. § 39-121 and in view of the fact that the State Board of Accountancy is not directly concerned with the contractor's business affairs but, rather, is simply trying to police the accountancy profession by examining the statements prepared by the accountant for compliance with professional standards.⁴

Sincerely,



BOB CORBIN
Attorney General

BC:mm

4. We express no opinion upon the applicability of A.R.S. § 32-749, declaring as confidential such information as is received by certified public accountants or public accountants as a result of their retention by a client. That issue is a subject which is more appropriately considered by the State Board of Accountancy.



ARIZONA LEGISLATIVE COUNCIL

MEMO

May 15, 1979

TO: Douglas R. Norton, Auditor General

FROM: Arizona Legislative Council

RE: Request for Research and Statutory Interpretation (O-79-35)

This is in response to a request submitted on your behalf by Gerald A. Silva in a memo dated April 27, 1979.

GIVEN FACT SITUATION:

Under the Equal Employment Opportunity Commission regulations, state licensing authorities must use validated procedures in their selection processes.

QUESTIONS PRESENTED:

- (1) What consequences might arise if a state licensing board's selection procedures, such as professional entrance exams, are not validated?
- (2) Could a selection procedure be declared unusable if it has not been validated?

ANSWERS:

- (1) Since the EEOC could not, under any conceivable interpretation of existing federal regulations, require such exams to be validated absent a finding of discriminatory adverse impact, no specific consequences can presently be anticipated.
- (2) Since the extent of the EEOC's authority over state licensing and certification functions is unclear, the EEOC's authority to declare such selection procedures unusable under any circumstances is also subject to dispute.

The Equal Employment Opportunity Commission (hereinafter EEOC), together with the U.S. Civil Service Commission (now the Office of Personnel Management), the U.S. Department of Justice and the U.S. Department of Labor, promulgated a set of federal regulations known as the Uniform Guidelines on Employee Selection Procedures in the Federal Register, Volume 43, No. 166, pp. 38290 et seq. (effective September 25, 1978). These guidelines were developed by the EEOC in the enforcement of Title VII of the Civil Rights Act of 1964, as amended. The three other federal agencies which joined with the EEOC in promulgating these guidelines also acted under the authority of Title VII as well as various related federal acts, regulations and executive orders. In Title VII, Congress authorized the "... use of any professionally developed ability test provided that such test, its administration or action upon the results is not designed, intended or used to discriminate". (See Section 703(h) 42 U.S.C. 2000 e(2)(h).)

The Uniform Guidelines were developed primarily in response to continuing disputes as to what constituted federal law in this area. The guidelines are based on the

premise that employer policies or practices which have an "adverse impact" on employment opportunities of any race, sex or ethnic group are illegal unless justified by business necessity. This general principle was adapted unanimously by the U.S. Supreme Court in Griggs v. Duke Power Company, 401 U.S. 424 (1974) and ratified by Congress in the passage of the Equal Employment Opportunity Act of 1972 which amended Title VII of the Civil Rights Act of 1964.

According to the Uniform Guidelines, "adverse impact" on equal employment opportunities means a substantially different rate of selection in hiring, promotion or other employment decision which works to the disadvantage of members of a race, sex or ethnic group. While there is no specific definition as to what constitutes a substantially different rate of selection, the federal agencies issuing the Uniform Guidelines agreed to an informal "rule of thumb" known as the 4/5ths rule. Under this rule, the agencies agreed to generally consider a selection rate for any race, sex or ethnic group which was less than 4/5ths or 80 percent of the selection rate for the group with the highest selection rate as a substantially different rate of selection. If adverse impact is found to exist under this rule of thumb, it must be justified. Such justification can, under the guidelines, come only by means of some type of validation test which demonstrates the relationship between the selection procedure or test utilized and performance on the job. It should be emphasized that the Uniform Guidelines specifically do not require that any selection procedure or process be subject to validation until a finding of adverse impact has been made.

Section 2B of the Uniform Guidelines provides that these federal regulations apply to tests and other selection procedures used as a basis in any employment decision. (See Federal Register, Volume 43, No. 166, at p. 38296.) Employment decisions are designated by the Uniform Guidelines to include licensing and certification functions to the extent that such functions may be covered under federal equal opportunity law. The Uniform Guidelines do not specify the extent of such coverage.

In March 1979, the EEOC and the three agencies which promulgated the Uniform Guidelines issued what purported to be a clarification. (See Federal Register, Volume 44, No. 43, pp. 11996 et seq.) In this clarification, the issuing agencies determined that the Uniform Guidelines applied to the licensing and certification functions of state and local governments to the extent such functions were covered by federal law. Again, however, the extent to which such functions were covered under federal law was not specified. The federal agencies have taken the position that at least some types of licensing and certification procedures which deny persons access to employment opportunity may be enjoined in an action brought pursuant to Section 707 of the Civil Rights Act of 1964, as amended. There is a body of case law contradicting the federal position.

In Woodard v. Virginia Board of Bar Examiners, et al., 420 F. Supp. 211 (1976), a black law school graduate who failed to pass the Virginia bar examination brought a class action alleging that the test was structured in a racially discriminatory fashion to deny black applicants an equal opportunity to practice law in Virginia. In holding against the plaintiff's use of Title VII to challenge the bar exam, the court found that EEOC guidelines were not applicable to professional licensing examinations. The following portion of the Woodard opinion is directly on point:

This Court is satisfied that the principles of test validation developed under Title VII do not apply to

professional licensing examinations. The EEOC guidelines in this area were developed in the context of traditional employment practices. See generally, Albemarle Paper Co. v. Moody, 422 U.S. 405, 425-35, 95 S.Ct. 2362, 45 L.Ed.2d 280 (1975); Griggs v. Duke Power Co., 401 U.S. 424, 433-36, 91 S.Ct. 849, 28 L.Ed.2d 158 (1971). See also 29 C.F.R. Section 1607 et seq. The employment tests utilized in the industrial setting are designed to measure an individual's ability to perform certain limited functions or operate particular machinery. The bar examination, however, serves a much broader purpose. A licensed attorney is presumed competent to handle any of a number of substantively divergent legal problems which may face his or her clients. Successful passage of the bar examination is intended to reflect a mastery of a wide range of substantive knowledge with which to approach such problems. The competing interests of an employer and the state as a licensing body, moreover, are also quite different. The employer, whether public or private, has the limited interest in insuring that the individual hired is capable of performing the required tasks. Whatever the magnitude of this interest, cf. Albemarle Paper Co. v. Moody, supra; Griggs v. Duke Power Co., supra, it falls short of that involved in professional licensing. The Supreme Court has recognized "that the States have a compelling interest in the practice of professions within their boundaries, and that as part of their power to protect the public health, safety, and other valid interests they have broad power to establish standards for licensing practitioners and regulating the practice of professions." Goldfarb v. Virginia State Bar, 421 U.S. 773, 792, 95 S.Ct. 2004, 2016, 44 L.Ed.2d 572 (1975) (emphasis added). See also Brown v. Supreme Court of Virginia, 359 F.Supp. 549, 554 (E.D.Va.), aff'd, 414 U.S. 1034, 94 S.Ct. 533, 38 L.Ed.2d 327 (1973); Richardson v. McFadden, supra, at p. 749.

The Court accordingly concludes that the test validation guidelines promulgated by the EEOC do not govern the instant matter, and that the job relatedness of the Virginia bar examination will be measured under the principles enunciated in Richardson v. McFadden, supra. (420 F.Supp. 211, 214 (1976))

The related case of Delgado v. McTighe, 442 F.Supp. 725 (1977), involved a class action claim by certain black and Hispanic law school graduates that an increase in the grade required to pass the Pennsylvania bar exam over the previously established level was discriminatory under Title VII in its impact on minorities. The court rejected the Title VII claim in finding that the provisions of the federal legislation applied to unlawful employment practices by employers where there was a distinct employer-employee relationship. (See Hachett v. McGuire, 445 F.2d 442 (1974), and Kyles v. Calcasieu Parish Sheriffs Department, 395 F.Supp. 1307 (1975).) Certainly, the court noted, the State Board of Bar Examiners did not function as an "employer" in any traditionally accepted sense.

The Delgado court also rejected plaintiffs' argument that Title VII had been expanded to cover those cases in which there was direct interference with an individual's employment opportunities by citing Woodard v. Virginia Board of Bar Examiners, supra, and the related case of Parrish v. Board of Commissioners of Alabama State Bar, 533 F.2d 942 (1976).

The EEOC does, as noted previously, take a conflicting view. For example, in EEOC Decision No. 75-249 (May 6, 1975), the commission found that upon a statistical showing that a disproportionately large number of Hispanics were excluded from the insurance profession by a state licensing examination, state authorities were required to show that the exam was job-related. In the same decision, the EEOC held that a state insurance department engaged in unlawful employment discrimination based on national origin by administering an insurance licensing examination only in the English language. Notwithstanding the EEOC position in this and other similar administrative decisions, research failed to indicate substantial case law support for the conclusion that Title VII applies to state and local licensing and certification functions. The courts have shown much more willingness to scrutinize Title VII testing claims in the traditional context of employer-employee relations. See Davis v. County of Los Angeles, 566 F.2d 1334 (1977) involving the use of a verbal aptitude test by a county fire department; Chance v. Board of Education, 458 F.2d 1167 (1972) involving the use of an examination in the promotion of public school teachers; and Vulcan Society v. Civil Service Commission, 490 F.2d 387 (1973) involving a test of the ability to comprehend written materials as a basis for measuring the ability to perform as a fireman.

CONCLUSION:

Since there is no formal requirement under the Uniform Guidelines for the validation of employee selection procedures absent a finding of adverse impact, no specific consequences can presently be anticipated as resulting from a failure to validate all professional licensing exams. The lack of any clarity on the extent of EEOC jurisdiction over licensing and certification functions similarly precluded a definitive answer to the second part of your question. Beyond the question of test validation,* however, is whether licensing and certification functions of state and local governments are vulnerable to challenge under Title VII of the Civil Rights Act of 1964, as amended. The small body of case law developed on this point suggests that such functions are not generally subject to a Title VII challenge. As a general rule, it would appear that the further removed a licensing and certification function is from the traditional employer-employee relationship (as is the case of a bar exam or, conceivably, a medical practices exam), the less open it would be to challenge under Title VII of the Civil Rights Act of 1964, as amended.

*Test validation, as should be now apparent, is not really the issue. The issue is whether employee selection practices result in adverse impact on the employment opportunities of a particular group or groups. Then and only then is validation of the job-relatedness of the test associated with the particular selection practice required.

cc: Gerald A. Silva
Performance Audit Manager