

LATE

Before the Senate Committee on
Commerce and Consumer Protection

Wednesday, February 17, 2010
9:15 a.m.
Conference Room 229

**In support of S.B. 2501
Relating to Public Accountancy**

Chair Baker, Vice Chair Ige, and Committee members:

My name is Terri Fujii and I am a CPA licensed in the State of Hawaii. I am also the Office Managing Partner of Ernst & Young LLP's Honolulu office.

Thank you for the opportunity to provide testimonial in **support** of S.B. 2501.

Current law provides for a quality review committee to review the work of CPA firms. However, because peer review is not mandatory in Hawaii, this provision does not result in a review of all CPAs performing audit or attest services in Hawaii. S.B. 2501 would significantly strengthen the Hawaii peer review regime by requiring that a CPA firm performing audit or other attest services in Hawaii be peer reviewed as a condition on the renewal of that CPA firm's Hawaii permit to practice. The bill would grant the Hawaii Board of Public Accountancy the authority to regulate the peer review process.

I believe that it is important for Hawaii to have a mandatory peer review system. Peer review strengthens the quality of the audit and attest services provided, protecting those who purchase such services and those who use the financial statements resulting from such services. Peer review also provides for continuous quality improvements as CPAs make changes to their processes to improve the quality of their work.

As I discuss in more detail below, many firms, including Ernst & Young, are already subject to peer review so requiring peer review in Hawaii will not significantly change the status quo for these firms. Our experience has been that peer review is such a significant means of promoting high quality professional services that expanding peer reviews to all firms providing attest services in Hawaii best promotes the public interest.

I would like to address two points. First, I would like to put the peer review process in some context. Second, I would like to explain the peer review process from the perspective of a CPA firm that performs audits of SEC issuers in more than one U.S. state.

Background on Peer Reviews

There is a broad, national consensus among the various state boards of accountancy and the representatives of the profession that periodic peer review is an important means of maintaining

and improving the quality of the professional services performed by CPA firms and thus, protecting the public.

It is therefore no surprise that peer reviews are a condition of membership in the American Institute of Certified Public Accountants (AICPA), and that nearly all U.S. states have a separate mandate that CPA firms receive periodic peer reviews.¹ That is, each state's mandate is independent of the peer review requirement that is a condition of AICPA membership. In practice, however, states coordinate their review requirements with the AICPA's review, so that CPA firms practicing in more than one state are not burdened by unnecessarily duplicative review programs.

Now that audits performed for SEC issuers are subject to inspections by the Public Company Accounting Oversight Board (PCAOB), peer reviews focus on the nonissuer accounting and auditing practice of licensed CPA firms. Peer review is the key method of external quality control review for these services.

While CPA firms are required to have internal quality control systems, external regulatory reviews such as peer reviews help to determine whether a firm's system of quality control is designed and being complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. CPA firms learn from the peer reviews that they undergo, and those lessons are a key input into firms' continual efforts to improve the quality of the professional services they render to their clients.

Because peer reviews promote quality, the chief beneficiaries of S.B. 2501 are Hawaii consumers of accounting services.

Peer Review Under the AICPA

Over 30,000 CPA firms participate in the AICPA peer review program, or "PRP." As described above, the various states with mandatory peer reviews have determined that participation in the PRP is sufficient to meet each state's specific requirement. The peer reviews conducted under the PRP are performed pursuant to the *AICPA Standards for Performing and Reporting on Peer Reviews*.²

Firms participating in the PRP are required to have a peer review once every three years of their non-issuer accounting and auditing practice. This review covers a specified one-year period.

¹ Specifically, 45 of the 55 U.S. states and territories that license CPAs have mandatory peer review. That number will grow to 47 in 2012, when Illinois and New York requirements take effect.

² The AICPA Standards for Performing and Reporting on Peer Reviews ("Peer Review Standards"), are available at http://www.aicpa.org/download/practmon/2009_stdts.pdf.

Ernst & Young's peer review is administered through the AICPA's National Peer Review Committee ("NPRC"). Firms are required to have their peer review administered by the NPRC if they are required to be registered with *and* inspected by the PCAOB or if they perform audits of non-SEC issuers pursuant to the standards of the PCAOB. (Other peer reviews are administered by state CPA societies.)

AICPA peer reviews are scoped based on the level of assurance services provided by the CPA firm. Firms providing audits pursuant to the rules of the PCAOB, the Statements on Auditing Standards, or Government Auditing Standards, or firms providing examinations of prospective financial information under the Statement on Standards for Attestation Engagements, receive "system reviews." (Firms providing certain other attest services may receive "engagement reviews.")

The system review is a process designed to determine whether the firm's system of quality control for its accounting and auditing practice is designed and complied with so as to provide the firm with reasonable assurance that it is performing and reporting in conformity with applicable professional standards in all material respects.

In a system review, the reviewer will study and evaluate a CPA firm's quality control policies and procedures that were in effect during the peer review year. This includes interviewing firm personnel and examining administrative files. To evaluate the effectiveness of the system and the degree of compliance with the system, the reviewer will test a reasonable cross-section of the firm's engagements, with a focus on high-risk engagements and significant risk areas where the possibility is the greatest that the engagements may not have been performed and/or reported on in accordance with professional standards in all material respects.

Because the system review is focused on high-risk engagements, not every office of a large firm will be tested under the peer review process. However, the peer review is scoped so that the reviewer obtains an understanding of the firm's system of quality control for its accounting and auditing practice, which is applied across all of the firm's offices. In addition, the reviewer must visit a sufficient number of the firm's practice offices so as to obtain "a reasonable basis for its conclusions regarding whether the reviewed firm's quality control policies and procedures are adequately communicated throughout the firm and whether its system of quality control was complied with during the year under review based on a reasonable cross section of the reviewed firm's accounting and auditing practice, with greater emphasis on those offices with higher assessed levels of peer review risk." Peer Review Standards, at § 1000.56.

Therefore, it is just not accurate to state that certain CPA firms make a decision to exclude their Hawaii offices from consideration during a peer review. If the independent peer reviewer determines that a Hawaii office of a CPA firm presents a higher risk of a quality control failure, then engagements in the Hawaii office or elements of the system of quality control contributing to the higher risk will be subjected to peer review procedures.

A requirement that the Hawaii office be inspected during a peer review would be contrary to the risk-based AICPA PRP process. Currently, no states require that a AICPA peer review specifically address one or more of a firm's in-state offices as a condition of satisfying the state's peer review program. Such a requirement should not be a condition of peer review in Hawaii.

Conclusion

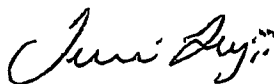
We believe that peer review should be mandatory in Hawaii to protect the consumers. Every firm providing audit and attest services should be subject to peer review. Were S.B. 2501 to pass, we believe that the Hawaii Board of Public Accountancy should use the AICPA PRP outlined above, either on its own or as supplemented by the PCAOB inspection, under rules promulgated pursuant to revised Section 466-13(b)(1), as satisfying the Hawaii peer review requirement. Working with the AICPA PRP is the most effective and efficient way to implement a peer review program in Hawaii, as it will permit the Board to focus its resources on managing the peer review process for those CPA firms which are not members of the AICPA. The State Board will also not have to reinvent the wheel and develop a peer review program as there is a well established program in place. The ACIPA PRP is used by all other licensing jurisdictions requiring peer review and has been in existence for over 20 years.

If the bill is passed and signed into law, its impact on firms that are not currently peer reviewed could be mitigated by the Board's authority under Section 466-13(b) of the bill to set the standards and requirements for peer reviews. For example, the Board could provide extensions of time, as needed, to these firms for preparing for the review and for responding to the findings.

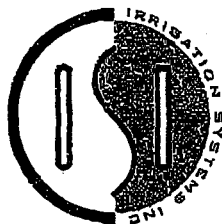
The extensive experience of firms already subject to peer reviews has been that peer reviews are critical to consumer protection by ensuring that firms maintain and improve their quality control systems. Those who rely on the work performed by CPA firms should have confidence in that work, and peer reviews both promote and help to justify that confidence. The benefits of a well-managed peer review program to the public far outweigh the burdens placed on CPA firms to undergo peer reviews.

Therefore, I **support** S.B. 2501, and thank the Chair, the Vice Chair, and the rest of the Committee's members for consideration of the above.

Respectfully submitted,



Terri Fujii, CPA



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Senate Committee on Commerce & Consumer Protection

Testimony of Steven Yoshizawa

In Support of SB 2501

Relating to Public Accountancy

Dear Chair Baker, Vice-Chair Ige and Committee Members:

I strongly support the mandatory peer review requirement for CPAs. I support mandatory peer review in order to provide a level of assurance that financial statements prepared and issued by CPAs in the State of Hawaii are uniformly prepared in accordance with established professional standards. Additionally, I support mandatory peer review, which has been mandatory since 1988 for a majority of practicing CPAs who prepare and issue financial statements in the State of Hawaii and are members of the American Institute of Certified Public Accountants ("AICPA"), as the current national debate is not whether peer review should be mandatory but should the peer review findings be made transparent and disclosed to better inform and protect the public's interest similar to the review results of the Public Company Oversight Accounting Board ("PCAOB") created under the Sarbanes-Oxley Act for publicly-held companies.

In turn, the benefits of mandatory peer review program will: (1) improve the quality of the financial statements being prepared and issued by CPAs in the State of Hawaii; (2) enhance the creditability and reliability of financial statements prepared and issued by CPAs in the State of Hawaii; and (3) most importantly, better protect us, the unsuspecting public and users of such financial statements, who incorrectly believe that all CPAs participate in a peer review or practice monitoring program to ensure that they comply with established professional standards.

For the above reasons, I urge you to support mandatory peer review for CPAs as it will provide the public with an improved level of assurance that CPA-prepared financial statements are prepared pursuant to uniform professional standards and fulfill the public's expectations.

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Judith Chock
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Testimony of Judith Chock

In Support of SB 2501

Relating to Public Accountancy

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For the above reasons, I urge you to support mandatory peer review for CPAs as it will provide the public with an improved level of assurance that CPA-prepared financial statements are prepared pursuant to uniform professional standards and fulfill the public's expectations.



Keriann Kau
98-1686 Hoolauae Street
Aiea, Hawaii 96701

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Testimony of Keriann Kau

In Support of SB 2501

Relating to Public Accountancy

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For the above reasons, I urge you to support mandatory peer review for CPAs as it will provide the public with an improved level of assurance that CPA-prepared financial statements are prepared pursuant to uniform professional standards and fulfill the public's expectations.

Keriann Kau

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LAWRENCE D. RODRIGUEZ
2110 LAUKAHI STREET
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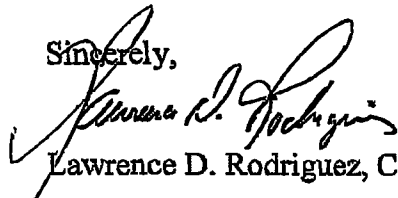
Chairman Baker
Vice Chairman Ige
Senate Committee on Commerce and Consumer Protection

I strongly support the mandatory peer review requirement for practicing Certified Public Accountants (CPAs). I support mandatory peer review in order to provide a level of assurance that financial statements prepared and issued by CPAs in the State of Hawaii are uniformly prepared in accordance with established professional standards. Additionally, I support mandatory peer review, as the current national debate is not whether peer review should be mandatory but should the peer review findings be made transparent and disclosed to better inform and protect the public's interest similar to the review results of the Public Company Oversight Accounting Board ("PCAOB") created under the Sarbanes-Oxley Act for publicly-held companies.

The benefits of mandatory peer review program will: (1) improve the quality of the financial statements being prepared and issued by CPAs in the State of Hawaii; (2) enhance the creditability and reliability of financial statements prepared and issued by CPAs in the State of Hawaii; (3) most importantly, better protect the unsuspecting public and users of such financial statements, who may incorrectly believe that all CPAs participate in a peer review or practice monitoring program to ensure that they comply with established professional standards; and (4) place CPAs who prepare and issue financial statements in the State of Hawaii on an equal playing field and enhance their competitiveness.

For the above reasons, I urge you to support mandatory peer review for CPAs as it will provide the public with an improved level of assurance that CPA-prepared financial statements are prepared pursuant to uniform professional standards and fulfill the public's expectations.

Sincerely,



Lawrence D. Rodriguez, CPA

**Christine Lyons Clarke, CPA
92-1138 Olani Street
Unit 1
Kapolei, Hawaii 96707**

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Senate Committee on Commerce & Consumer Protection

**Wednesday, February 17, 2010
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Testimony of Christine Lyons Clarke, CPA

In Support of SB 2501

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