



State of Arizona  
Office  
of the  
Auditor General

PERFORMANCE AUDIT

**ARIZONA  
STATE BOARD  
OF  
ACCOUNTANCY**

Report to the Arizona Legislature  
By Debra K. Davenport  
Acting Auditor General  
September 1999  
Report No. 99-20

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STATE OF ARIZONA  
OFFICE OF THE  
**AUDITOR GENERAL**

DEBRA K. DAVENPORT, CPA  
ACTING AUDITOR GENERAL

September 28, 1999

Members of the Arizona Legislature

The Honorable Jane Dee Hull, Governor

Ms. Ruth R. Lee, Executive Director  
Arizona 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 May 27, 1997, resolution of the Joint Legislative Audit Committee. The performance audit was conducted as part of the Sunset review set forth in A.R.S. §§41-2951 through 41-2957.

The report addresses how the Board handles complaints against certified public accountants, public accountants, and registered accounting firms. First, the Board needs to study ways to increase its speed in handling complaints. Although many complaints are resolved within a reasonable time, almost half of them take over a year to be resolved. Second, the report addresses the public's access to key information about registrants. We recommend that the Board consider asking the Legislature to change its statutes to allow the public better access to information concerning whether registrants have been disciplined by the Board. Finally, the Board should review its Quality Review Program (Program) and consider either changing or eliminating it. The Program currently appears to uncover mostly minor technical violations and reviews the work of only a small portion of the Board's registrants.

As outlined in its response, the Board has agreed to implement the recommendation that it study its complaint-handling process. Based on that study the Board will decide whether to implement most of the other recommendations.

My staff and I will be pleased to discuss or clarify items in the report.

This report will be released to the public on September 29, 1999.

Sincerely,

A handwritten signature in cursive script that reads "E. William Thomson".

E. William Thomson, Director  
Performance Audit Division

Enclosure

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## SUMMARY

The Office of the Auditor General has conducted a performance audit and Sunset review of the Arizona State Board of Accountancy pursuant to a May 27, 1997, resolution of the Joint Legislative Audit Committee. The audit was conducted as part of a Sunset review as set forth in Arizona Revised Statutes §§41-2951 through 41-2957.

The former Auditor General and the current Acting Auditor General are certified public accountants and registrants of the Board. Consequently, to avoid the appearance of a conflict of interest or impropriety, they recused themselves from this audit. Additionally, none of the Auditor General staff assigned to the audit were Board registrants.

### Background

The Arizona State Board of Accountancy, overseen by a seven-member Board appointed by the Governor, is responsible for establishing and enforcing qualifications and accounting standards for certified public accountants, public accountants, and registered accounting firms. The Board exercises this responsibility by:

- Processing certifications and administering certified public accountant examinations.
- Registering certified public accountants, public accountants, and accounting firms biennially.
- Ensuring that registrants obtain continuing professional education.
- Conducting quality reviews of financial statements completed by registrants and filed with select state agencies.
- Receiving, investigating, and resolving complaints made against registrants.

**The Board Sometimes Does Not Handle Complaints in a Timely Manner (See pages 7 through 10)**

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*Half of the complaints received by the Board take more than six months to resolve.*

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Although the Board resolves many complaints within a reasonable number of days, some take considerable time to resolve. Some complaints take over a year to be resolved. The Board could benefit from studying ways to further speed complaint-handling processes. Specifically, the Board may wish to focus its study on complaints resolved by formal discipline or requiring investigators. Additionally, the approval process for minutes received from the Tax Practice and Auditing Standards Committee should be reviewed to determine if a more timely approach is appropriate.

**Public's Access to Information Is Limited (See pages 11 through 14)**

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*Statutes block the public from accessing key information about CPAs.*

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Statutory language and Board practices impede access to public information. Providing unimpeded public access to information is an important component of regulatory boards' responsibilities. Arizona Revised Statutes prohibit the Board from releasing important information about its registrants, such as dismissed complaints, pending complaints, and complaints resolved by letters of concern. Additionally, problems with the Board's automated telephone answering system and public viewing requirements present further obstacles to members of the public who wish to obtain information about registrants.

The Board could improve access to public information by seeking changes to statutes that prevent the release of information contained in letters of concern. Additionally, changes would allow the Board to disclose the number and nature of pending and dismissed complaints. If statutory changes are made, the Board will need to develop a public information policy specifying which information staff will automatically provide to the general public. In developing this policy, the Board will need to protect the confidentiality of registrants' clients, as well as the integrity of ongoing investigations. Finally, the Board should investigate the feasibility of adding an option to its telephone answering system so it is easier for the public to obtain information about registrants and

stop requiring members of the public to obtain a notarized statement when viewing registrants' files for personal use.

**Board Needs to Consider Changing or Eliminating Its Quality Review Program  
(See pages 15 through 20)**

As currently implemented, the Board's Quality Review Program appears to mostly identify minor technical deficiencies, encompasses only a limited number of registrants, and is duplicative for some Program registrants.

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*Current Quality Review Program produces minimal results.*

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Contract investigators the Board hires limit their review to public filings at nine participating state agencies, including the Departments of Banking, Insurance, and Transportation. Consequently, only registrants who prepare public filings at one of the nine participating public agencies are subject to program review. Most of the deficiencies noted by investigators are minor in nature, and the Board closes the vast majority of resulting complaints without action. Additionally, the Quality Review Program is redundant for those Board registrants who have completed American Institute of Certified Public Accountants (AICPA) peer review requirements.

The Board should review the Program's effectiveness and make changes where warranted. Specifically, the Board should consider reorienting the program to a peer review approach or eliminating it. As a part of this effort, the Board should consider promulgating rules or requesting that the Legislature clarify the Program's statutory authority to conduct a peer review program.

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# INTRODUCTION AND BACKGROUND

The Office of the Auditor General has conducted a performance audit and Sunset review of the Arizona State Board of Accountancy (Board) pursuant to a May 27, 1997, resolution of the Joint Legislative Audit Committee. This audit was conducted under the authority vested in the Auditor General by Arizona Revised Statutes §§41-2951 through 41-2957.

The former Auditor General and the current Acting Auditor General are certified public accountants and registrants of the Board. Consequently, to avoid the appearance of a conflict of interest or impropriety, they recused themselves from this audit. Additionally, none of the Auditor General staff assigned to the audit are Board registrants.

## Board Responsibilities

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*Board examines, certifies, and monitors CPAs, PAs, and registered accounting firms.*

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The Arizona State Board of Accountancy was created in 1919 to establish and enforce standards of qualification and accounting practice for certified public accountants (CPAs), public accountants (PAs), and accounting firms. Together, this group is referred to as registrants. Under A.R.S. §§32-721 through 32-751, the Board’s specific responsibilities include:

- **Examination and Certification**—The Board administers the uniform CPA examination of the American Institute of Certified Public Accountants (AICPA). The Board processed 362 new CPA applications and certified 365 CPAs in fiscal year 1999.
- **Registration**—The Board oversees the biennial registration of CPAs, PAs, and accounting firms. In fiscal year 1999, 7,824 CPAs, 16 PAs, and 762 firms were regulated by the Board.<sup>1</sup>

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<sup>1</sup> Public accountants (PAs) were required to meet less stringent examination requirements than CPAs. PA status is no longer granted to new applicants.

- **Continuing Education**—During biennial registration the Board is responsible for ensuring that registrants have obtained continuing education. CPAs in public practice must obtain 80 hours of continuing professional education every two years.
- **Quality Review**—The Board’s investigators review a sample of audits and financial statements prepared by registrants to determine if they comply with professional standards. If the audits and financial statements do not comply, the Board can initiate complaints.
- **Complaints**—The Board receives, investigates, and resolves complaints against registrants. Typical complaints include the unauthorized use of the “CPA” title by nonregistrants, discrepancies on income tax returns, and registrants’ failure to complete required continuing professional education. However, the Board also spends a great deal of time resolving a relatively small number of complaints against large firms. These major cases involve significant litigation or potential litigation and extensive legal resources. The Board opened 222 complaints in fiscal year 1999.

## **Organization and Staffing**

The Board is comprised of seven members appointed by the Governor to five-year terms. The Board consists of five certified public accountants and two public members. Ten full-time employees and two full-time Assistant Attorneys General assist the Board.

Under Arizona Administrative Rules, the Board also supports five advisory committees. These volunteer professional committees, not composed of Board members, provide specialized reviews and recommendations to the Board. Committees examine issues related to professional standards, CPA certification, professional education, pending legal issues (such as complex cases), and taxes. Committees also review complaints, initiate investigations, and recommend disciplinary action to the Board.

## **Funding and Budget**

The Board is funded through revenue collected from licenses and fees. Additional funding is derived from fines and forfeits. In fiscal year 1998, the Board collected revenues of \$1,076,629. Expenditures in fiscal year 1998 amounted to \$1,225,057. The Board is a 90/10 agency, remitting 10 percent of its gross revenues to the State General Fund. Remittances to the State General Fund in fiscal year 1998 amounted to \$116,963. (See Table 1, page 4)

## **1979 Report Follow-up and Update**

Auditor General staff revisited the concerns identified in the 1979 performance audit report of the Board (Auditor General Report No. 79-5). The 1979 report contained four recommendations, as follows:

- Designating the public accountant classification as a “dying class” and eliminating provisions for any new registrants under the “PA” classification while permitting existing registrants to retain their certificates.
- Adopting additional methods for encouraging public input.
- Amending statutes to require less frequent registration and budget approval for implementing automated data processing.
- Formulating a policy for expanding the quality review program.

The Board has made progress on the first three issues. Statutory provisions regarding issuance of a PA certificate were repealed in 1980 and the Board position formerly held by a public accountant is now designated for a member of the public. In addition to adding the second public member position, the Board has opened an Internet Web site and issues news releases when major cases are resolved. The Board now licenses registrants on a biennial basis and has implemented an automated data proces-

**Table 1**

**Arizona State Board of Accountancy  
Statement of Revenues, Expenditures, and Changes in Fund Balance  
Years Ended June 30, 1997, 1998, and 1999  
(Unaudited)**

	1997	1998	1999
Revenues:			
Licenses and fees	\$ 855,213	\$ 928,448	\$ 924,911
Fines and forfeits	337,691	130,707	5,550
Charges for goods and services	25,290	17,411	21,610
Other	<u>        </u>	<u>63</u>	<u>5,564</u>
Total revenues	<u>1,218,194</u>	<u>1,076,629</u>	<u>957,635</u>
Expenditures: <sup>1</sup>			
Personal services	253,080	285,011	285,310
Employee related	50,961	57,900	60,105
Professional and outside services	656,245	596,321	660,615
Travel, in-state	8,324	11,288	16,145
Travel, out-of-state	6,869	8,675	6,834
Other operating	211,255	265,862	225,454
Capital outlay	<u>30,586</u>	<u>        </u>	<u>        </u>
Total expenditures	<u>1,217,320</u>	<u>1,225,057</u>	<u>1,254,463</u>
Excess of revenues over (under) expenditures	<u>874</u>	<u>(148,428)</u>	<u>(296,828)</u>
Other financing uses:			
Net operating transfers out	5,543	5,067	2,943
Remittances to the State General Fund <sup>2</sup>	<u>125,856</u>	<u>116,963</u>	<u>100,758</u>
Total other financing uses	<u>131,399</u>	<u>122,030</u>	<u>103,701</u>
Excess of revenues under expenditures and other uses	(130,525)	(270,458)	(400,529)
Fund balance, beginning of year	<u>1,740,357</u>	<u>1,609,832</u>	<u>1,339,374</u>
Fund balance, end of year <sup>3</sup>	<u>\$1,609,832</u>	<u>\$1,339,374</u>	<u>\$ 938,845</u>

<sup>1</sup> Includes prior year administrative adjustments and special investigations, legal services, and year 2000 project expenditures that the Legislature authorized as special line items.

<sup>2</sup> As a 90/10 agency, the Board remits administrative penalties and 10 percent of other gross revenues to the State General Fund.

<sup>3</sup> Fund balance is unreserved and undesignated; however, the balance cannot be spent without legislative appropriation.

Source: The Arizona Financial Information System (AFIS) *Revenues and Expenditures by Fund, Program, Organization, and Object* and *Trial Balance by Fund* reports for the years ended June 30, 1997, 1998, and 1999.

sing system. However, as reported in Finding III (see pages 15 through 20), the current audit found that the Board still needs to make changes to the quality review program.

### **Audit Scope and Methodology**

Audit work conducted focused on determining if the Board provides adequate information to the public regarding registrants, the effectiveness of the Board's quality review program, and whether the Board adequately tracks, investigates, and resolves complaints. To do so, Auditor General staff:

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*Auditors reviewed 107 complaint files in-depth.*

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- Randomly selected a sample of 107 files for complaints received by the Board in fiscal year 1998. Files reviewed included complaints regarding taxes, professional education, CPA titles, and audit/accounting practices. The staff then analyzed selected files to determine whether complaints were processed in a timely manner, reviewed the actions recommended by committees, and compared the final action taken by the Board with committee recommendations.
- Interviewed representatives from accountancy boards in 15 other states (Georgia, Missouri, Illinois, Michigan, New York, Oklahoma, Virginia, West Virginia, Wisconsin, Ohio, California, North Carolina, Texas, Oregon, and Tennessee).
- Attended four full Board meetings and four committee meetings.
- Conducted an extensive review of literature, including professional journal articles, books, Internet Web sites, and reports from other states.
- Reviewed performance audits conducted on similar boards in four other states.
- Interviewed representatives of the Arizona Society of Certified Public Accountants, the American Institute of Certified Public Accountants, and the National Association of State Boards of Accountancy.

The audit presents recommendations in three areas:

- The need for statutory changes to allow better public access to complaint information.
- The need for the Board to improve some aspects of the complaint-handling process.
- The need for the Board to review the quality review program to determine if the current program is the most effective method available.

This audit was completed in accordance with government auditing standards.

The Auditor General and staff express appreciation to the members of the Arizona State Board of Accountancy, the Board's representatives from the Office of the Attorney General, the Executive Director of the Board, and the Board's staff members for their cooperation and assistance throughout the audit.

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## FINDING I

# THE BOARD SOMETIMES DOES NOT HANDLE COMPLAINTS IN A TIMELY MANNER

Many of the complaints filed with the Board take a considerable amount of time to resolve. While 180 days for complaint resolution is a reasonable standard for occupational regulatory boards, only about half of the complaints received in fiscal year 1998 were resolved within that time. These lengthy processing times are caused by many factors, including registrants' legal tactics, investigative hurdles, and administrative practices in referring complaints to the Board for final resolution. Because the causes are so varied, more study is needed to determine what might be done to speed up the process.

The Board is responsible for investigating and resolving complaints against CPAs, PAs, and registered public accounting firms. Complaints are often made regarding tax services performed by registrants, alleged violations of accounting and auditing standards, inappropriate use of the CPA designation, and registrants' failure to meet continuing education requirements. If a complaint needs further investigation before it can be addressed, it is assigned to one of the Board's investigators. Board staff may also assign complaints to the Board's committees or the Office of Administrative Hearings to make recommendations for Board action. Ultimately, all complaints are eventually heard and resolved by the full Board.

### Many Complaints Take Six Months or More to Resolve

While many complaints received by the Board are resolved quickly, others take a considerable time to resolve. Auditors' examination of complaint resolution processes followed by regulatory boards in many professions has shown that 180 days is a reasonable benchmark. When compared to such a benchmark, the processing times for many of the complaints the Board filed are longer. As shown in Table 2 (see page 8), the Board

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*Board takes more than six months to resolve half of the complaints it receives.*

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**Table 2****Arizona State Board of Accountancy  
Days Needed to Resolve Closed Complaints  
Year Ended June 30, 1998**

Days to Resolve <sup>1</sup>	Nature of Complaint Allegations				Total Number of Complaints Reviewed	Percentage of Resolutions by Number of Days
	Auditing and Accounting Standards	Tax Practices	Continuing Education	Use of CPA Designation		
0-180	14	6	11	12	43	50%
181-360	3	8	17	10	38	44
Over 360	<u>2</u>	<u>1</u>	<u>1</u>	<u>1</u>	<u>5</u>	<u>6</u>
Total	<u>19</u>	<u>15</u>	<u>29</u>	<u>23</u>	<u>86</u> <sup>2</sup>	<u>100</u> %

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<sup>1</sup> Resolution calculated from the date the complaint is received to the Board's decision.

<sup>2</sup> Auditor General staff were unable to independently identify open and close dates for 21 of the 107 complaints initially reviewed.

Source: Auditor General staff analysis of 107 complaints filed with the Board during the year ended June 30, 1998.

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took over 180 days to resolve half of the complaints it received in the fiscal year ending June 30, 1998, based on a file review of 107 complaints.

Some of the complaints that take a long time to resolve involve serious situations posing a financial risk to the public. For example, one complaint involving a certified public accountant who pleaded guilty to criminal charges in a U.S. District Court took approximately a year and a half to resolve. Prosecutors had accused the accountant of taking part in a scheme that defrauded investors in Arizona and California out of \$10 million. The registrant eventually agreed to terminate his certificate.

## **Reasons for Lengthy Processing Times Are Varied**

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*Complaints delayed for a variety of reasons.*

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There are many reasons why complaints can be delayed in processing. Auditor General staff reviewed nine of the most lengthy cases received by the Board during fiscal year 1998. Auditors found that these complaints were delayed for various reasons that included postponements, lengthy negotiating periods, and processing delays. For example:

- One complaint, which accused a registrant of accounting standards violations, took over a year to resolve. An investigator worked on this complaint for three months. Additionally, the registrant requested to postpone an informal interview twice, adding two more months. Finally, the registrant's attorney attempted to negotiate a settlement for over four months. The registrant eventually signed a consent order that required his future work to be reviewed prior to its release.
  
- A second complaint, which accused a registrant of tax preparation problems, took over a year to resolve. The complaint was initially closed without action within three months, but was reopened, deliberated again, and assigned to an investigator after the complainant notified a legislator about her dissatisfaction with the initial outcome. The complaint was further delayed during the holiday season when almost three months elapsed between the Board's vote to issue a letter of concern and the date the Board President signed the letter.

Because there is no single clear explanation for the Board's slow handling of some complaints, it is difficult to identify potential remedies. The Board's complaint-handling process already incorporates some best practices. For example, the Board uses professional rather than voluntary investigators. An audit conducted of another regulatory board has shown that using voluntary investigators can be another source of problems. In addition, the Board already monitors whether investigators are reporting their results to the Board within a statutorily mandated time period.

## **Board Needs to Examine Complaint-Handling Process**

Some processing steps could be taken more quickly. The Board would benefit from examining its complaint-handling process and identifying ways to decrease the time needed to resolve complaints. In particular, the Board may wish to review its processes for handling cases involving investigators and those cases resulting in either disciplinary action, a consent order, or the issuance of a letter of concern because these cases tend to take the most time to resolve.

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*Committee practices may delay action on complaints.*

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As a part of this review, the Board should examine practices that its committees use to refer items for Board action. These committees provide specialized reviews and recommendations to the Board and often have responsibility for the initial phase of the complaint-handling process. For example, the Accounting and Auditing Standards Committee and the Tax Practice Committee do not refer their recommendations for resolving complaints to the Board until they have approved their committee meeting minutes at their subsequent meeting. Approval of minutes may not occur for at least a month after the committee votes on its recommendation.

## **Recommendation**

The Board should formally study its complaint-handling processes to determine if complaints could be resolved in a more timely manner. The Board may want to focus on complaints that are eventually resolved by formal discipline, require an investigator's assistance, or pass through a Board committee.

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## FINDING II

## PUBLIC'S ACCESS TO INFORMATION IS LIMITED

Because of statutory limitations and certain Board practices, the public lacks access to information about registrants that it needs to make informed decisions. Statutes currently limit information that can be disclosed about complaints regarding registrants that resulted in formal disciplinary action. Further, the public cannot find out whether complaints were filed but dismissed, or whether the Board took less formal action, such as issuing a letter of concern. Consumers' ready access to information is also limited by problems in navigating the Board's automated telephone system and obtaining access to registrants' files.

### Public Benefits from Full Information

Providing unimpeded public access to information is an important component of regulatory boards' responsibilities. Regulatory boards need to be accountable to the public for their activities. In addition to providing for accountability, public information also helps to ensure that boards meet their statutory mandates to investigate complaints, issue letters of concern to warn practitioners to improve potentially problematic, but legal, practices, and discipline statutory violators. Further, public information assists consumers to select competent and ethical professionals to handle sensitive information and perform important services, such as preparing tax returns.

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*Public can make better choices when fully informed.*

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### Statutes Limit Public Access

Arizona Revised Statutes prohibit the Board from releasing important information about its registrants. Specifically, information about dismissed complaints, pending complaints, and complaints resolved by letters of concern is confidential. Statutory

changes are needed to allow the Board to disclose registrants' full complaint histories to the public and conduct more business in open session.

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*Statutes block public from learning CPAs' full record.*

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**Statutes prevent public from learning about registrants' full histories**—Members of the public who telephone or visit the Board to inquire about a registrant cannot be told about key aspects of the registrant's complaint history. Rather, they are told whether or not a registrant was disciplined. Specifically, dismissed complaints, pending complaints, and complaints resolved by letters of concern are kept confidential in accordance with statute. However, keeping this information confidential can convey a false impression to the public if a registrant has been the subject of complaints, but was never formally disciplined.

Further, because pending complaints are confidential under state statute, the Board conducts significant portions of its meetings in executive session. Consequently, the public is significantly restricted from observing Board proceedings.

The Board also destroys its Executive Session meeting minutes after only six months. This further limits the ability of appropriate parties, such as the Auditor General's Office, to review the Board's minutes. In contrast, other state agencies retain their executive session minutes longer. For example, the State Board of Dental Examiners keeps its executive session minutes indefinitely.

**Statutory changes could protect public and clients**—Statutory changes are needed to allow the Board to disclose registrants' full complaint histories to the public and conduct more business publicly. Specifically, the following statutes should be amended:

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*Statutory changes needed to protect public.*

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- A.R.S. §32-741(F), which specifies that the letters of concern are confidential and are not public records; and
- A.R.S. §32-749(C), which requires pending and dismissed complaints to be kept confidential, except under very limited conditions.

In considering changes, the Board would need to balance its obligation to the public to disclose as much information as possible while still protecting the confidentiality of registrants and their

clients and the integrity of ongoing investigations. To accomplish this goal, a prior Auditor General report (Report No. 95-13) has recommended that regulatory boards provide information about the number and general nature of dismissed and pending complaints and information about disciplinary actions to inquiring consumers. For example, the Veterinary Medical Examining Board has a policy requiring staff to inform callers of the status of a veterinarian's license; disciplinary actions taken; and the number and nature of complaints.

### **Available Information Is Difficult to Access**

Although much of the information the Board maintains about its registrants is confidential, more could be done to make the remaining public information more accessible to the public. For example, the Board is statutorily allowed to report if a registrant's certificate has been suspended or revoked. However, when Auditor General staff posing as members of the public tried contacting the Board, they encountered two major difficulties:

- **Automated telephone system is difficult to navigate**—The Board's automated telephone system presents callers with several options. The directions include terminology that may help registrants obtain information, but is not necessarily meaningful for members of the public. For example, there is no option clearly intended and labeled for the general public to inquire about a registrant's record with the Board. As a result, members of the public may not understand which option to select to obtain consumer information. Board staff could change the current options without expending Board money.
- **Notarized statement requested to review a file**—The Board's staff requires members of the public who wish to view a registrant's files in person to provide a notarized statement. This practice is principally directed at people wishing to view the Board's records for commercial purposes, such as developing mailing lists. However, it is a cumbersome obstacle for members of the general public who want to view a limited number of files for personal use and is inconsistent with Board policy. Other occupational regula-

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*Board requires public to provide notarized statement to view files.*

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tory boards do not require the general public to provide a notarized statement.

As a result of these obstacles, members of the general public may be impeded from obtaining important information.

### **Recommendations**

1. The Legislature should consider revising the following Board statutes:
  - a. A.R.S. §32-741(F), to specify that letters of concern are not confidential and are public records; and
  - b. A.R.S. §32-749(C), to allow the number and nature of pending and dismissed complaints to be public record.
2. If statutory changes are made, the Board should develop a public information policy:
  - a. To direct staff regarding what information will be automatically revealed and available to the inquiring general public.
  - b. To protect the confidentiality of accused registrants and their clients and the integrity of ongoing investigations.
3. The Board should maintain its Executive Session minutes longer as do other occupational regulatory boards.
4. The Board should change the options in its automated telephone answering system so that callers have a direct way to obtain information about registrants.
5. The Board's staff should follow Board policy by no longer requiring members of the public to provide a notarized statement when viewing registrants' files for noncommercial use.

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## FINDING III

# BOARD NEEDS TO CONSIDER CHANGING OR ELIMINATING ITS QUALITY REVIEW PROGRAM

The Board's Quality Review Program (Program), begun as a way to ensure that registrants are doing work that complies with professional standards, needs to be reexamined. As currently implemented, the Program has limited effect in that it mostly identifies minor technical deficiencies and encompasses only a limited number of registrants. Additionally, it is duplicative for some registrants who already face a similar requirement for peer review. Therefore, the Board should consider either reorienting the Program toward a peer review approach or, given its current limitations, eliminating it altogether.

### Background

The Board's Quality Review Program was initiated in 1976 as a means of ensuring that practitioners' accounting practices are in compliance with generally accepted auditing standards and accounting principles. If these standards and principles, as specified by the American Institute of Certified Public Accountants, are not followed, an accountant can substantially misrepresent an entity's financial position. The general public, relying upon this information, would then reach inaccurate conclusions, invest or extend credit to the entity, and increase the likelihood that financial harm would occur.

Under the Program, the Board assigns contract investigators to review audits and financial statements filed with participating public agencies, including the Departments of Banking, Insurance, and Transportation.<sup>1</sup> After reviewing all of the applicable filings, investigators then conduct a more detailed examination of those filings that appear to violate generally accepted auditing

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*Poor-quality accounting practices can harm the public.*

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<sup>1</sup> The other participating public agencies are the Arizona Corporation Commission, Department of Health Services, Department of Library and Archives, Department of Racing, Office of the State Treasurer, and State Board for Private Post-secondary Education.



standards and accounting principles. The results are forwarded to Board staff, who generally open a complaint against the registrant. As with any other complaint, the Board eventually deliberates whether a violation has occurred and if disciplinary action is warranted. The Board projects that it will expend approximately \$88,500 for investigators to conduct quality reviews in fiscal years 2000 and 2001.

### **Effect of Current Program Limited**

Although the Program has a long history, its current effect is limited. Most of the deficiencies noted by the investigators are minor in nature, and as a result, the vast majority of complaints are closed without action. Further, only a small percentage of registrants are subject to this review, and many of them already face another, similar requirement.

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*Current program principally identifies minor violations.*

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***Program uncovers minor technical violations***—Most of the deficiencies currently noted by the investigators are minor in nature. Auditor General staff analyzed information on filings assigned for review in 1997 and 1998 for the Arizona Departments of Banking and Transportation, which accounts for the majority of Program reviews during this period.<sup>1</sup> Eighty-nine percent of the complaints opened as a result of quality reviews at the Department of Banking and 93 percent of the complaints opened as a result of the quality reviews at the Department of Transportation were closed because the Board found that the violations were too minor to warrant disciplinary action or, in some instances, because the Board lacked jurisdiction over the filing's preparer (for example, the preparer may have been a CPA in another state).

***Program's benefit is limited***—The Program effectively applies to only a small percentage of total registrants. In fact, auditors found that only 163 of the Board's more than 7,500 registered practitioners and firms were subject to Program reviews (based

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<sup>1</sup> Filings from the Departments of Banking and Transportation accounted for 65 percent of the 1,381 filings assigned for Program reviews in 1997 and 1998. These two departments also accounted for 66 percent of the 129 subsequent detailed reviews of those filings that appeared to violate generally accepted auditing standards and accounting principles.

on analysis of filings assigned for review at the Departments of Banking and Transportation in 1997 and 1998).

***Program sometimes redundant***—The Program is also potentially duplicative for some of the Board’s registrants. Registered firms that choose to belong to the American Institute of Certified Public Accountants (AICPA) and that perform attest work (auditing and expressing an opinion on financial statements on which third parties rely) are already subject to peer review once every three years. Currently, approximately 65 percent of the Board’s registrants are AICPA members.

### **Board Needs to Consider Modifying or Eliminating Program**

Because of the Program’s limited impact, the Board needs to consider whether the Program should be modified or eliminated. The Board could implement a peer review requirement that could extend to those not already covered by such a requirement. Otherwise, it should consider discontinuing the Program altogether.

***Board could implement a comprehensive peer review program***—Auditor General staff identified several states that use a peer review approach at the state level to systematically monitor and educate practitioners in order to maintain high-quality performance throughout the profession. In addition, the American Institute of Certified Public Accountants has its own program. There are some variations in how peer review programs are structured. For example:

- Oregon’s accountancy board requires each CPA and PA providing attest services to participate in a board-approved peer review program, either individually or as part of a firm, as a condition of permit/license renewal. It is the licensee’s responsibility to comply with the peer review program when scheduled. A CPA or PA is exempt from the peer review requirement if he or she biennially represents to the board that he or she does not engage in performing attest services and does not intend to engage in performing such services for the

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*Other states require peer reviews.*

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next two years. The licensees need only submit a signed form to the board stating that they obtained a peer review and giving the name of the reviewing organization.

- Ohio's accountancy board requires all registrants providing attest services to undergo a board-approved peer review program at least once every three years, at the registrant's expense, and submit the findings to the board. Based upon review of the peer reviewer's findings, the board may impose remedial actions. In the event the registrant is unwilling or unable to comply with established standards, or the registrant's professional work is deemed egregious, the board may take disciplinary action.
- Texas' accountancy board requires registrants providing attest services to be peer reviewed every three years at their own expense by either the AICPA, the state's professional society, or a national association of CPA practitioners, and report the results to the board. If a registrant receives two consecutive negative reviews, the board will examine the registrant's accounting practices more closely.
- The American Institute of Certified Public Accountants requires all of its members engaged in the practice of public accounting to be enrolled in an approved practice monitoring program, such as the AICPA's peer review program, in order to retain their membership in the organization. Members in the peer review program need to have independent reviews of their accounting and auditing practices at least once every three years and take remedial action if needed. If a member refuses to cooperate, fails to correct material deficiencies, or is found to be so seriously deficient in his/her performance that education and remedial corrective actions are not adequate, the member's enrollment in the AICPA's peer review program may be terminated or some other action taken.

A peer review approach could potentially broaden the Program's impact over Arizona practitioners. Already, approximately 65 percent of the registrants in Arizona are potentially subject to peer review once every three years as a result of belonging to the American Institute for Certified Public Accountants. A state peer review requirement could extend a similar requirement to those who are not AICPA members. It could be

designed in such a way as to allow Arizona practitioners to use the results of the AICPA peer reviews or the reviews of other Board-approved organizations. Those registrants not currently subject to peer review would need to arrange and pay for a peer review or request an exemption based upon some valid criteria, such as not having performed any audits or prepared any financial statements during the review period. In this way, the Board would be ensuring that all of its active registrants receive systematic feedback on their accounting practices and recommendations for improvement, if needed, and also eliminate the need for the Board to expend several thousand dollars a year for contract investigators to review the work of a limited number of registrants.

To encompass all CPAs and PAs preparing audits or financial statements but not currently subject to a peer review requirement, the Program would also need to apply to audits and financial statements beyond those filed with the nine Arizona agencies. The Board has not widened the existing Program to include audits and financial statements prepared for private organizations and corporations because it believes it lacks legal authority to examine supporting documentation and work papers. A.R.S. §§32-703(A)(1) and 32-749(B)(1) generally authorize the Board to adopt rules for the Board and private professional organizations to conduct practice review programs approved by the Board, including quality and peer reviews, and to access supporting documentation in conjunction with these programs. However, these statutes are not as clear as they could be. Therefore, the Board should also consider promulgating rules or asking the Legislature to clarify its statutory authority regarding the Program.

***Another option would be to eliminate the Program***—Given the limited effect of the Program as currently implemented, if the Board should decide it does not want to reorient the Program to a peer review approach, then it may want to consider eliminating it altogether. Several states, including Michigan, Missouri, and Oklahoma, do not operate or require peer review or other quality review programs.

## **Recommendations**

1. The Board should consider changing its Quality Review Program to a peer review approach to increase its impact on Arizona practitioners. In order to do so, the Board should consider promulgating rules or requesting a clarification of its statutory authority by the Legislature. Specifically, A.R.S. §32-703(A)(1) and 32-749(B)(1) should be clarified to allow the Board to require registrants to participate in peer reviews.
2. If the Board should decide against changing the Program to a peer review approach, it should then consider eliminating the Program altogether.

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## SUNSET FACTORS

In accordance with A.R.S. §41-2954, the Legislature should consider the following 12 factors in determining whether the Arizona State Board of Accountancy should be continued or terminated.

**1. The objective and purpose in establishing the Board.**

The purpose of the Arizona State Board of Accountancy is to “regulate and license accountants and accounting firms in the interest of protecting the citizens of Arizona from inept and unlawful accounting practices.” To carry out this responsibility, a seven-member board is statutorily empowered to:

- Examine candidates seeking certification as CPAs;
- Certify persons and register firms meeting statutory requirements as certified public accountants or certified public accountant firms;
- Initiate and process complaints alleging incompetent, unethical, or unprofessional conduct and discipline Board-certified practitioners; and
- Monitor practitioners through its quality review program to ensure adherence to professional standards of practice.

**2. The effectiveness with which the Board has met its objective and purpose and the efficiency with which it has operated.**

The Board has generally met its primary purpose and objectives in an effective and efficient manner. Specifically:

- **Examination**—The Board contracts with an examination service for on-site administration of the AICPA

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*Board is generally effective and efficient.*

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- CPA Examination to those applicants who meet the examination qualifications set out in statutes.
- **Certification**—The Board processes initial applications for certification in accordance with time frames established in statutes and rules. Auditors reviewed a random sample of 30 initial applications and found that the Board issued, on average, certificates within 34 days of receiving the completed application materials. Additionally, the Board has streamlined the renewal process by going from an annual to a biennial renewal schedule.
- **Complaint handling**—Although the Board resolves many of its complaints in a timely manner, it could still improve in this area. Auditors reviewed a sample of 107 complaints and found that half took over 180 days to resolve. Therefore, the Board should study its complaint-handling processes to determine if complaints could be resolved in a more timely manner (see Finding I, pages 7 through 10).

**3. The extent to which the Board has operated within the public interest.**

The Board generally operates in the public interest. Specifically, it certifies CPAs and PAs to ensure that they meet certain competency requirements and conduct their work in accordance with AICPA standards. The Board also registers CPA firms. Additionally, it receives and resolves complaints against certificate holders. The Board also handles internally identified complaints generated as a result of its quality review program and certification renewal process. Finally, it monitors CPAs' work through its quality review program.

Notwithstanding the Board's general efforts, the Board could better operate in the public interest by facilitating the public's access to information. Test calls made by auditors and a visit to review information in person showed that the Board readily released information about licensure status and complaints resulting in formal disciplinary action. However, the Board could do more to in-

form the public by seeking an amendment to its statutes and rules to allow disclosure of its complaint deliberations, as well as the number and general nature of all pending and dismissed complaints. Finally, the Board could simplify its automated telephone information system to make it more user-friendly. (For further discussion, see Finding II, pages 11 through 14.)

**4. The extent to which rules adopted by the Board are consistent with the legislative mandate.**

In compliance with A.R.S. Title 41, Chapter 6, the Board comprehensively reviewed and revised its administrative rules, which became effective in November 1998. Although current rules are generally consistent with statutes, personnel from the Auditor General's Office and Governor's Regulatory Review Council (GRRC) identified several statutes still requiring Board rules. For example:

- The Board needs to identify those colleges, universities, and courses appropriate for a bachelor's or more advanced degree in accounting or business administration for those individuals requesting certification as certified public accountants A.R.S. §§32-721(A)(5) and 32-723(B).
- The Board needs to establish equivalency requirements to use in certifying applicants by reciprocity A.R.S. §32-727(A)(2)(b).
- The Board needs to establish standards for deciding when to issue a letter of concern to registrants A.R.S. §32-741(F).

**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.**

The recent five-year rule review undertaken by the Board was completed in accordance with the Administrative Procedures Act. Proposed rule changes were posted on

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*Some rules needed.*

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the Board's Web site and copies sent to all registrants prior to a public hearing. Additionally, notices and agendas of upcoming Board and committee meetings addressing proposed rule changes were posted at various locations around the State and provided to persons requesting them. During these meetings, public comment was allowed on the proposed rule change.

In addition to keeping the public informed about rules, the Board also provides the public with access to a variety of other information through its Web site and a biannual newsletter. For example, these two sources identify:

- Names of currently certified accountants and registered accounting firms;
- Enforcement actions taken by the Board since publication of its last newsletter; and
- Board action on initial and renewal certification/registration requests.

Additionally, the Board holds monthly public meetings to discuss regulatory issues impacting certificate holders. These meetings comply with open meeting laws. Meeting notices are adequately posted and open (as opposed to executive session) meeting minutes are made available. The Board also provides consumers with information about certified professionals and registered firms by telephone or review of Board files.

**6. The extent to which the Board has been able to investigate and resolve complaints that are within its jurisdiction.**

A.R.S. §§32-741 through 32-751 provide for the regulation of registrants including the Board's authority, to investigate and resolve complaints regarding unlawful and unprofessional practice by practitioners and accounting firms. In fiscal year 1999, the Board opened 222 complaints against practitioners and firms. Complaints are investigated by advisory committees and contract investigators. If violations are found, the advisory committees

make disciplinary recommendations to the Board, including certificate/registration suspension or revocation, administrative penalties, restriction on scope of practice, peer review, continuing professional education, decree of censure, and probation. Additionally, they may recommend a letter of concern in those instances where the evidence does not warrant disciplinary action, but where continuation of the action under investigation may ultimately result in Board action against the practitioner.

However, our review found that the Board is not always timely in its resolution of complaints (see Finding I, pages 7 through 10). Specifically, a review of 107 complaints found that half took over 180 days to resolve.

**7. The extent to which the Attorney General of any other applicable agency of state government has the authority to prosecute actions under enabling legislation.**

A.R.S. §32-743(H) authorizes the Attorney General's Office to appear and represent the Board at all hearings. The Board is assigned two Assistant Attorneys Generals who provide counsel to the Board at their meetings, and represent the Board in disciplinary matters.

**8. The extent to which the Board has addressed deficiencies in its enabling statutes which prevent it from fulfilling its statutory mandate.**

Over the last five years, more than a dozen pieces of Board-initiated legislation have been enacted. They cover such issues as reciprocity, registration, and continuing education. Specific changes to the Board's statutes approved during the 1999 legislative session included:

- Increasing the education requirement to qualify for certified public accountant from 120 to 150 semester hours;
- Modifying partnership qualifications in CPA or Public Accountant (PA) firms so that only a majority of accounting firm ownership remains in the hands of CPAs or PAs and allows others to participate as part-

ners as long as they participate in management of the firm; and

- Restricting CPAs and PAs to performing the attest function (performing an audit and expressing an opinion on an organization's financial statements) only when working in a registered firm.

The Board also unsuccessfully sought legislation in both 1995 and 1996 requiring background checks of certification applicants. Finally, Board policy currently allows registrants to use their CPA and PA designations if they work for accounting firms, including corporations. However, Arizona accountancy law does not include corporations in its definition of firm. Therefore, the Board should seek statutory change to A.R.S. §32-701.01(6) to include "corporation" in the definition of firm.

**9. The extent to which changes are necessary in the laws of the Board to adequately comply with the factors listed in the sunset review statute.**

To better inform consumers, the Legislature should consider modifying A.R.S. §32-749(C) to allow for public disclosure of the number and general nature of pending and dismissed complaints. Additionally, it should consider modifying A.R.S. §32-741(F) to allow for public disclosure of letters of concern (see Finding II, pages 11 through 14 ).

Also, to better ensure consumer advocacy on the Board, the Legislature should consider modifying A.R.S §32-701(A) to increase the Board's public membership to closer to 50 percent. Currently, it is at 29 percent.

Finally, if the Board expands its Quality Review Program, it should consider requesting a clarification of its statutory authority by the Legislature. Specifically, A.R.S. §32-703(A)(1) and 32-749(B)(1) should be clarified to allow the Board to require registrants to participate in peer reviews (see Finding III, pages 15 through 20).

**10. The extent to which the termination of the Board would significantly harm the public health, safety, and welfare.**

Because Arizona law limits the Board's authority to regulating only the use of the CPA and PA titles, termination of the Board would not significantly jeopardize the public's health, safety, and welfare. However, the Board does provide certain benefits. Specifically, it,

- Sets minimum education, examination, and experience requirements for certified practitioners;
- Helps ensure that CPAs and CPA firms conform to professional standards of conduct by investigating and resolving complaints, and conducting quality reviews of state agencies' public filings;
- Provides the public with information regarding certified practitioners' qualifications and complaint history; and
- Provides oversight over CPAs and firms that perform audits and that express opinions on the financial statements of an organization.

**11. The extent to which the level of regulation exercised by the Board is appropriate and whether less or more stringent levels of regulation would be appropriate.**

Arizona law already provides less regulation than most states impose. Under Arizona accountancy law, any individual may provide the public with the same accounting services provided by CPAs and PAs. Arizona law restricts only the usage of the titles "certified public accountant," "public accountant," their abbreviations, and similar titles to persons who have demonstrated a minimum level of skill and competency; and prohibits CPAs and PAs working for nonregistered accounting firms from providing attest services.

12. **The extent to which the Board has used private contractors in the performance of its duties and how effective use of private contractors could be accomplished.**

The Board contracts with approximately 10 to 12 CPA investigators at any one time. These investigators allow the Board to initiate quality reviews and complaint investigations in a timely and cost-effective manner using investigators with the appropriate type of expertise. The Board also contracts out the CPA examination administration using the procurement process. Finally, the Board did look into the possibility of contracting with a private law firm to investigate and litigate major cases. However, the Board has chosen to pay for the establishment of a litigation unit within the Attorney General's Office as it is believed this will be more cost-effective.

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## Agency Response



ARIZONA STATE BOARD OF ACCOUNTANCY  
3877 North Seventh Street, Suite 106  
Phoenix, Arizona 85014  
(602) 255-3648 Phone (602) 255-1283 Fax



September 21, 1999

Bill Thomson, Director  
Performance Audit Division  
2910 N. 44<sup>th</sup> Street-410  
Phoenix, Arizona 85018

Re: Sunset Review

Dear Mr. Thomson:

Enclosed is a response submitted on behalf of the Arizona State Board of Accountancy (Board) to the report of the Performance Audit and Sunset Review of the Board. We appreciate the opportunity to respond to the observations and recommendations contained in the report.

I would like to take this opportunity to thank your staff for the diligent effort put forth to understand the Accountancy Board mission. Each auditor was sensitive to the every day demands put on the Accountancy Board staff and as a result allowed ample time for all responses to inquiries. The Board, its staff and all those interviewed were treated with the utmost respect.

Sincerely,

A handwritten signature in cursive script that reads "M. Susan Dwyer".

M. Susan Dwyer, CPA  
President

RRL:MSD:dt

Enclosure



Performance and Sunset Audit Response  
Arizona State Board of Accountancy  
September 21, 1999

FINDING I.

Recommendation.

The Board should formally study its complaint-handling processes to determine if complaints could be resolved in a more timely manner. The Board may want to focus on complaints that are eventually resolved by formal discipline, require an investigator's assistance, or pass through a Board committee.

Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

FINDING II.

Recommendations.

1. The Legislature should consider revising the following Board statutes:
  - a. A.R.S. § 32-741(F), to specify that the letters of concern are not confidential and are public records; and
  - b. A.R.S. § 32-749(C), to allow the number and nature of pending and dismissed complaints to be public record.

Response: In view of the board's agreement to examine the complaint process in Finding I, it is the position that the Board cannot accept or reject the recommendation until that process has been completed.

2. If statutory changes are made, the Board should develop a public information policy:
  - a. To direct staff regarding, what information will be automatically revealed and available to the inquiring general public.
  - b. To protect the confidentiality of accused registrants and their clients and the integrity of ongoing investigations.

Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented if the statutory changes are made.

3. The Board should maintain its Executive Session minutes longer as do other occupational regulatory boards.

Response: The finding of the Auditor General is agreed to and the recommendation will be implemented.

4. The Board should change the options in its automated telephone answering system so that callers have a direct way to obtain information about registrants.

Response: The options will be investigated and one of the things that will be looked at is a “direct way” to obtain information on registrants. Until the Board completes the study, it cannot agree or disagree with the audit recommendation.

5. The Board’s staff should follow Board policy by no longer requiring members of the public to provide a notarized statement when viewing registrants’ files for noncommercial use.

Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

### FINDING III.

#### Recommendations.

1. The Board should consider changing its Quality Review Program to a peer review approach to increase its impact on Arizona practitioners. In order to do so, the Board should consider requesting a clarification of its statutory authority by the Legislature. Specifically, A.R.S. §§32-703(A)(1) and 32-749(B)(1) should be clarified to allow the Board to require registrants to participate in peer reviews.

Response: The finding of the Auditor General is agreed to and the audit recommendation will be studied to determine how it can be implemented, whether by rule or statute.

2. If the Board should decide against changing the Program to a peer review approach, it should then consider eliminating the Program altogether.

Response: The audit recommendation will be considered after the Board’s study is completed.

### Sunset Factors

4. The extent to which rules adopted by the Board are consistent with the legislative mandate.

In compliance with A.R.S. Title 41, Chapter 6, the Board comprehensively reviewed and revised its administrative rules, which became effective in November 1998. Although current rules are generally consistent with statutes, personnel from the Auditor General's Office and Governor's Regulatory Review Council (GRRC) identified several statutes still requiring Board rules. For example:

- The Board needs to identify those colleges, universities, and courses appropriate for a bachelor's or more advanced degree in accounting or business administration for those individuals requesting certification as certified public accountants A.R.S. §§ 32-721(A)(5) and 32-723(B).

Response: The Board adopted a Substantive Policy Statement for clarification at its September 13, 1999 Board meeting.

- The Board needs to establish equivalency requirements to use in certifying applicants by reciprocity A.R.S. § 32-727(A)(2)(b).
- The Board needs to establish standards for deciding when to issue a letter of concern to registrants A.R.S. § 32-741(F).

Response: At its annual meeting, the Board addressed these factors. It is currently studying these and anticipates taking action in the near future.

9. The extent to which changes are necessary in the laws of the Board to adequately comply with the factors listed in the sunset review statute.

- To better inform consumers, the Legislature should consider modifying A.R.S. § 32-749(C) to allow for public disclosure of the number and general nature of pending and dismissed complaints. Additionally, it should consider modifying A.R.S. § 32-741(F) to allow for public disclosure of letters of concern.

Response: In light of the Board's response to Finding II, it is premature to consider modifying the statutes.

- Also, to better ensure consumer advocacy on the Board, the Legislature should consider modifying A.R.S. § 32-701(A) to increase the Board's public membership to closer to 50 percent. Currently, it is at 29 percent.

Response: Within the last year, the Board has doubled its public membership; however, it unanimously believes that the technical expertise of the professional members is required for the Board to fulfill its duty.

In view of the recent article in the newspaper pointing out the problems that the Governor has in filling vacancies on a lot of boards, increasing the size of the Board or its public membership would not necessarily "ensure consumer advocacy." Since the violations are technical in nature, the professionals on the Board have to take the lead in determining whether the violation took place and then the public members should weigh in more on the discipline to be handed out than the technical aspects of the case.

## Other Performance Audit Reports Issued Within the Last 12 Months

98-16	Board of Medical Examiners	99-10	Residential Utility Consumer Office/Residential Utility Consumer Board
98-17	Department of Health Services— Division of Assurance and Licensure	99-11	Department of Economic Security— Child Support Enforcement
98-18	Governor's Council on Develop- mental Disabilities	99-12	Department of Health Services— Division of Behavioral Health Services
98-19	Personnel Board	99-13	Board of Psychologist Examiners
98-20	Department of Liquor	99-14	Arizona Council for the Hearing Impaired
98-21	Department of Insurance	99-15	Arizona Board of Dental Examiners
98-22	State Compensation Fund	99-16	Department of Building and Fire Safety
99-1	Department of Administration, Human Resources Division	99-17	Department of Health Services' Tobacco Education and Prevention Program
99-2	Arizona Air Pollution Control Commission	99-18	Department of Health Services— Bureau of Epidemiology and Disease Control Services
99-3	Home Health Care Regulation	98-19	Department of Health Services— Sunset Factors
99-4	Adult Probation		
99-5	Department of Gaming		
99-6	Department of Health Services— Emergency Medical Services		
99-7	Arizona Drug and Gang Policy Council		
99-8	Department of Water Resources		
99-9	Department of Health Services— Arizona State Hospital		

## Future Performance Audit Reports

Department of Environmental Quality  
Arizona Department of Transportation—A+B Contracting