STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

TENNESSEE STATE BOARD OF ACCOUNTANCY

Performance Audit Report

September 2015

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September 3, 2015

The Honorable Ron Ramsey
Speaker of the Senate
The Honorable Beth Harwell
Speaker of the House of Representatives
The Honorable Mike Bell, Chair
Senate Committee on Government Operations
The Honorable Jeremy Faison, Chair
House Committee on Government Operations
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable Julie Mix McPeak, Commissioner
Department of Commerce and Insurance
12th Floor, Davy Crockett Tower
500 James Robertson Pkwy
Nashville, Tennessee 37243-0565

Ladies and Gentlemen:

We have conducted a performance audit of selected programs and activities of the Tennessee State Board of Accountancy for the period January 1, 2013, through December 31, 2014. This audit was conducted pursuant to the requirements of Section 4-29-111, *Tennessee Code Annotated*, the Tennessee Governmental Entity Review Law.

Our audit disclosed a finding which is detailed in the Objectives, Methodologies, and Conclusions section of this report. Management of the Tennessee State Board of Accountancy has responded to the audit finding; we have included the response following the finding. We will follow up the audit to examine the application of the procedures instituted because of the audit finding.

This report is intended to aid the Joint Government Operations Committee in its review to determine whether the Tennessee State Board of Accountancy should be continued, restructured, or terminated.

Sincerely,

Deborah V. Loveless

Deborah V. Loveless, CPA
Director

DVL/jw
15/047

State of Tennessee

Audit Highlights

Comptroller of the Treasury Division of State Audit

Performance Audit
Tennessee State Board of Accountancy
September 2015

AUDIT SCOPE

We have audited the Tennessee State Board of Accountancy (the board) for the period January 1, 2013, through December 31, 2014. Our audit scope included a review of internal control and compliance with laws and regulations in the areas of continuing professional education requirements, peer reviews, professional privilege tax, complaint handling, board funding, open meetings, National Association of State Boards of Accountancy (NASBA) participation, and information systems. Managements of the board and the Department of Commerce and Insurance are responsible for establishing and maintaining effective internal control and for complying with applicable laws and regulations.

For our sample design, we used nonstatistical audit sampling, which was the most appropriate and cost-effective method for concluding on our audit objectives. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient, appropriate audit evidence to support the conclusions in our report. We present more detailed information about our methodologies in the individual report sections.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusion based on our audit objectives.

CONCLUSIONS

FINDING

Under its current structure, the Tennessee State Board of Accountancy is limited in its ability to oversee the peer review program in Tennessee

We found the board's Peer Review Oversight Committee is inactive and has never served in an oversight capacity as required by state law. In addition, Section 62-1-201(b)(3), *Tennessee Code Annotated*, prohibits the board from accessing any documents relating to peer reviews. Because the Peer Review Oversight Committee is inactive and the board cannot view peer review reports issued by peer reviewers for Tennessee firms under any circumstances, the board cannot effectively regulate the firms and protect the public interest of those Tennessee citizens who procure their services (page 12).

OBSERVATION

The following topic did not warrant a finding but is included in this report because of its effect on the operations of the board and on the citizens of Tennessee: the Tennessee State Board of Accountancy and the Department of Commerce and Insurance disagreed on the reasonableness and importance of the department's complaint handling standard operating procedures (page 17).

MATTER FOR LEGISLATIVE CONSIDERATION

This performance audit identified an area in which the General Assembly may wish to consider statutory changes to improve the efficiency and effectiveness of the board's operations. Specifically, the General Assembly may wish to revise Section 62-1-201, *Tennessee Code Annotated*, requiring peer review results and documentation to be kept confidential from the board, which potentially hampers the board's authority to effectively regulate the profession (page 12).

Performance Audit
Tennessee State Board of Accountancy

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Performance Audit
Tennessee State Board of Accountancy

INTRODUCTION

PURPOSE AND AUTHORITY FOR THE AUDIT

This performance audit of the Tennessee State Board of Accountancy was conducted pursuant to the Tennessee Governmental Entity Review Law, *Tennessee Code Annotated*, Title 4, Chapter 29. Under Section 4-29-237, the board is scheduled to terminate June 30, 2016. The Comptroller of the Treasury is authorized under Section 4-29-111 to conduct a limited program review audit of the agency and to report to the Joint Government Operations Committee of the General Assembly. This audit is intended to aid the committee in determining whether the board should be continued, restructured, or terminated.

ORGANIZATION AND STATUTORY RESPONSIBILITIES

The mission of the Tennessee State Board of Accountancy is to protect the public interest by ensuring that persons professing special competencies in accountancy or those offering assurance regarding financial statement presentation have demonstrated their qualifications to do so. The board's vision is to protect the public, enhance communications with licensees, and proactively respond to the demands of today's changing world. The board licenses Certified Public Accountants (CPAs), registers accounting firms, and assists individuals who file complaints against CPAs or those claiming to be CPAs.

The Governor appoints the 11 board members, who serve staggered three-year terms. As outlined in Section 62-1-104, *Tennessee Code Annotated*,

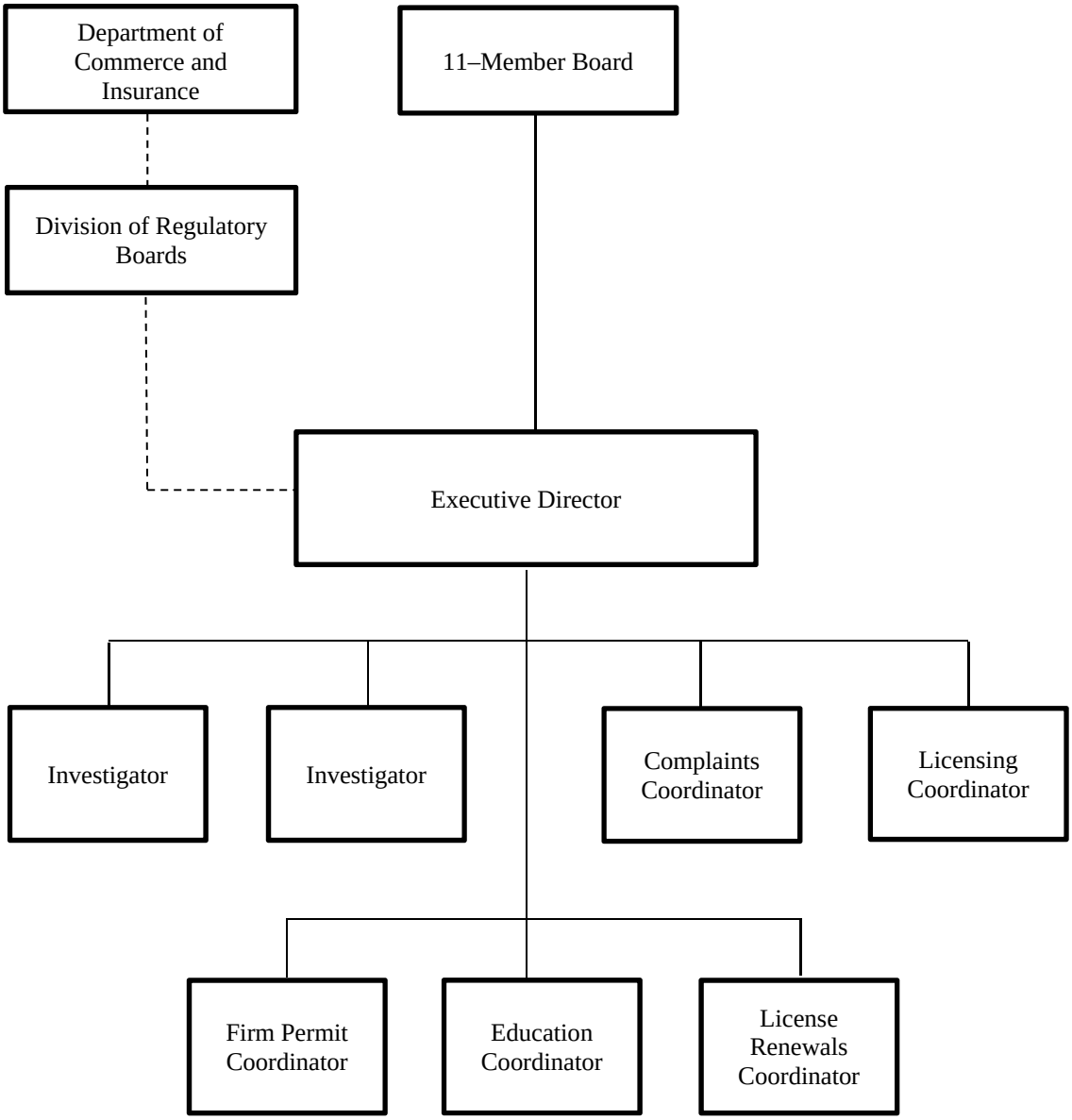
> nine of the members shall be certified public accountants holding a certificate issued by, and residing in, the state of Tennessee. One member shall be an attorney licensed to practice in the highest court of the state. One member shall be a public member possessing expertise in one or more significant portions of the board's regulated activities. Neither the attorney nor the public member shall be the holder of a certified public accountant's certificate or license to practice as a public accountant.

In addition, the statute states that the Governor should strive to ensure that at least one member is 60 years old or older and that at least one member is a member of a racial minority. Based on our review of board minutes, the board meets at least four times a year.

The board appoints an Executive Director, who is an active CPA in the State of Tennessee. The Executive Director oversees seven employees who are responsible for carrying out the board's mission on a daily basis, such as maintaining and securing all necessary records and files; ensuring adequate meeting space for the board meetings; implementing the board's policies and procedures; informing the board about state policies and procedures; and addressing any other matters delegated by the board. The board is administratively attached to the Department of Commerce and Insurance, Division of Regulatory Boards. The board's business unit code is 335.10. We present an organizational chart of the board on the following page.

The Tennessee State Board of Accountancy also works with the Tennessee Society of Certified Public Accountants (TSCPA) and the National Association of State Boards of Accountancy (NASBA) to enhance the accounting profession. TSCPA works to enhance the success of its members who are CPAs through service, support, and advocacy. NASBA, which represents 55 states and U.S. territories, works to enhance the effectiveness and advance the common interests of all the State Boards of Accountancy by creating a forum for accounting regulators and practitioners to address issues relevant to the viability of the accounting profession. Officials from TSCPA regularly attend board meetings; NASBA has attended board meetings in the past.

Tennessee State Board of Accountancy
Organizational Chart
February 2015



AUDIT SCOPE

We have audited the Tennessee State Board of Accountancy (the board) for the period January 1, 2013, through December 31, 2014. Our audit scope included a review of internal control and compliance with laws and regulations in the areas of continuing professional education requirements, peer reviews, professional privilege tax, complaint handling, board funding, open meetings, National Association of State Boards of Accountancy (NASBA) participation, and information systems. Managements of the board and the Department of Commerce and Insurance are responsible for establishing and maintaining effective internal control and for complying with applicable laws and regulations.

For our sample design, we used nonstatistical audit sampling, which was the most appropriate and cost-effective method for concluding on our audit objectives. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient appropriate audit evidence to support the conclusions in our report. We present more detailed information about our methodologies in the individual report sections.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusion based on our audit objectives.

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendation(s) in the prior audit report. The prior audit report was dated September 2007. In this report, there were two findings. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDINGS

The current audit disclosed that the Department of Commerce and Insurance and the Tennessee State Board of Accountancy have corrected the previous audit findings concerning the department's improper restriction of the board's expenditures and the board's need to expedite complaint processing.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

GENERAL BACKGROUND INFORMATION

The board's responsibilities include issuing CPA licenses to individuals who meet the appropriate requirements and issuing firm permits to individuals and entities that provide accounting services to Tennesseans. In order to become a licensed CPA in Tennessee, an individual must meet certain requirements to sit for the Uniform CPA Examination,[1] which is administered by the National Association of State Boards of Accountancy. Specifically, a candidate must earn at least 150 semester hours of coursework from a regionally accredited college or university, with at least 24 semester hours earned in accounting and at least 24 semester hours earned in general business. The candidate must also pass an ethics examination given by the American Institute of Certified Public Accountants. Once the candidate passes both examinations, he or she must submit an application for licensure to the board and must demonstrate one year of work experience in the accounting field. To maintain and renew an active license, a CPA must meet specific continuing education requirements.

In addition, any individual or entity that engages in the practice of public accounting must register annually and obtain a firm permit from the board. The firm must have a resident manager who holds an active Tennessee CPA license. If the firm offers attest services,[2] it must have a peer review[3] completed once every three years in order to renew its permit to continue its practice.

Tables 1 and 2 containing the statuses of all CPAs and all firms, respectively, in the State of Tennessee, as of April 21, 2015, are exhibited on the following page. The tables were provided by board staff.

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[1] The Uniform CPA Examination is developed by the American Institute of Certified Public Accountants to assess the knowledge and skills that entry-level accountants need to practice public accountancy.

[2] According to Section 62-1-103, *Tennessee Code Annotated*, the word "attest" means providing "any audit or other engagement performed in accordance with the Statements on Auditing Standards (SAS); any review performed in accordance with Statements on the Standards for Accounting and Review Services (SSARS); [and] any examination performed in accordance with the Statements on Standards for Attestation Engagements (SSAE)…." Any report issued, including compilation reports, indicating the service was performed in accordance with these standards falls under the definition of "attest." These standards are issued by the American Institute of Certified Public Accountants. In this report, we will refer to attest engagements as accounting and auditing services.

[3] Peer reviews are quality control reviews where an experienced, independent CPA or group of CPAs examine one or more aspects of the professional work completed by the CPA firm to ensure the firm followed the appropriate professional standards identified in footnote 1.

Table 1

CPA Licensee Statuses as of April 21, 2015	
Status	**Number of Licensees**
Applications in Process	28
Withdrawn	21
Expired Applications	197
Denied	5
Probation	3
Active	10,440
Inactive	4,139
Disabled	48
Active Military	2
Retired	175
Suspended	3
Expired-Grace*	173
Retired-Over 65	894
Expired License	2,296
Closed	2,981
Revoked	56
Deceased	2,695
Total	**24,156**

Table 2

Firm Permit Statuses as of April 21, 2015	
Status	**Number of Firms**
Applications in Process	7
Withdrawn	10
Expired Applications	7
Denied Applications	13
Probation	1
Active	2,100
Expired-Grace*	3
Expired License	187
Closed	1,978
Revoked	18
Total	**4,324**

* This status indicates that a licensee did not renew by December 31, 2014. The license is currently in a 12-month grace period before it expires.

CONTINUING PROFESSIONAL EDUCATION REQUIREMENTS

General Requirements

The board requires Certified Public Accountants (CPAs or licensees) to obtain 80 hours (with a minimum of 20 hours per year) of continuing professional education (CPE) biennially by their license renewal date. The 80 hours of CPE must include at least 40 hours of technical subject matter (i.e., accounting, accounting ethics, attestation, taxation, or management advisory services) as well as 2 hours of state-specific ethics. Licensees who are engaged in attest functions must have at least 20 of their 80 hours in Accounting and Attestation while those providing expert witness testimony are required to have 20 of their 80 hours of CPE in the area in which the court deems the licensee an expert. If a licensee knows that he or she will not comply with the CPE requirements by the December 31 license renewal date, the licensee may request an extension from the board's Executive Director.

According to Rule 0020-05-.07, *Rules of Department of Commerce and Insurance, Division of Regulatory Boards, Tennessee State Board of Accountancy*, "the Board may, upon written request, extend the time up to six (6) months within which license holders must comply with the requirements of this chapter for reasons of poor health, military service, foreign service or other good cause." Licensees must still meet CPE subject matter and hour requirements and must file for the extension before December 31. CPAs who do not meet the CPE requirements are subject to penalties, including additional CPE hours and fines.

The board only recognizes CPE courses provided by an approved CPE program sponsor. CPE program sponsors must be registered with the National Association of State Boards of Accountancy (NASBA) or the board, or fall into one of five automatically approved categories:

- professional accounting organizations (e.g., the American Institute of Certified Public Accountants and the Tennessee Society of Certified Public Accountants);
- universities and colleges;
- firms or entities offering in-firm or in-house educational programs for their employees without charge;
- governmental entities; or
- self-study programs from a provider that is a member of NASBA's Quality Assurance Service.

CPE Audits

When licensees attend CPE courses, the CPE program sponsor provides the CPAs with documentation certifying the subject matter and hours earned. It is the licensees' responsibility to maintain all documentation to prove they met all CPE requirements. This documentation is subject to audit by the board. Each year, the board conducts an audit of a sample of licensees who renewed their license to determine if the licensees complied with CPE requirements and

received CPE from an approved sponsor. After board staff select the sample, they send letters to the licensees selected for audit to request copies of all CPE documentation for the previous two-year licensure period. The board permits licensees to submit their documentation by the following methods: the online CPETracking tool created by NASBA,[4] email, mail, fax, or personal delivery. The board conducts the CPE audit by reviewing the licensees' CPE documentation.

Results of Audit Work

The objectives of our review of the board's responsibilities over continuing professional education requirements were to determine if

- the board staff properly conducted CPE audits and whether the CPETracking tool was effective in performing these audits; and
- the Executive Director granted CPE extensions in accordance with Rule 0020-05-.07.

To gain an understanding of the CPE audit process, we interviewed the Executive Director,[5] the Firm Permit Coordinator, and the Education Coordinator, and we conducted a survey of other state boards to compare their audit process with Tennessee's process.

To determine if the board properly conducted CPE audits and whether the CPE tracking tool was effective in performing these audits, we obtained the following items:

- the 2014 CPE Audit Report Presentation, dated September 9, 2014;
- copy of the letter of notification sent to a licensee subject to the CPE audit, dated May 7, 2014;
- instructions for CPE documentation submission;
- the letter to notify the licensee after failure to respond to the CPE audit;
- the summary of the board's CPE requirements and guidelines, as of March 30, 2015;
- completed CPE tracking worksheets;
- CPE tabulation worksheets;
- CPE categories; and
- the 2012-2013 CPE audit report.

We observed the CPE audit process for CPA licensees who submitted documentation through email delivery for the December 31, 2014, renewal date. Also, we obtained a list for the most recent completed CPE audit of 173 licensees who renewed on December 31, 2013, and who submitted their CPE documentation using NASBA's CPETracking tool. We tested a

[4] To assist the State Boards of Accountancy and licensees in all jurisdictions, NASBA created the CPETracking online tool that allows licensees to document their CPE hours earned and upload and store their CPE documentation.

[5] The board's Executive Director retired on May 1, 2015, near the end of audit fieldwork. The board hired a new Executive Director effective August 10, 2015.

nonstatistical random sample of 60 licensees to determine if the CPE audit was affected when licensees submitted their documentation using the NASBA CPETracking tool.

We also obtained a listing of the 18 licenses that expired on December 31, 2013, and 12 licenses that expired on December 31, 2014, that received extensions. We performed testwork on these 30 extensions to determine if the board complied with Rule 0020-05-.07.

Based on the procedures performed, we determined that

- the board properly conducted CPE audits and the CPETracking tool was effective for conducting CPE audits; and
- the Executive Director granted CPE extensions in accordance with Rule 0020-05-.07.

PEER REVIEWS

Background

In general, to ensure that accounting firms hired to conduct accounting and auditing engagements properly conduct these engagements in accordance with standards established by the accounting profession's standard-setting bodies, firms must have a system of quality control in place and undergo a peer review to ensure firms provide quality services to citizens. According to the American Institute of Certified Public Accountants (AICPA),

> Peer reviews help to monitor a CPA firm's accounting and auditing practice (practice monitoring). The goal of the practice monitoring, and the program itself, is to promote quality in the accounting and auditing services provided by . . . CPA firms. This goal serves the public interest. . . .

Accounting firms in Tennessee that perform accounting and auditing services must have a peer review at least once every three years to ensure the firm's work product meets generally accepted accounting and auditing standards. When a firm registers for a firm permit in Tennessee, the firm has 30 days to enroll in a board-approved peer review program. The board has approved any peer review program conducted by the Tennessee Society of Certified Public Accountants (TSCPA), AICPA, or other state society administering the AICPA Peer Review Program. Firms are responsible for contracting with a TSCPA-approved peer reviewer.

During a review, a peer reviewer examines a firm's work papers and quality control procedures to ensure that the firm properly performed its work and issued the appropriate report. In Tennessee, TSCPA administers the peer review program and is responsible for approving entities who will conduct peer reviews. Peer reviewers follow the AICPA's *Standards for Performing and Reporting on Peer Reviews*. If a peer review finds that a firm produced substandard work, the firm will be required to take remedial steps. Remediation may include items such as additional continuing professional education or another peer review of one or more subsequent accounting and auditing services. While the TSCPA has the authority to stipulate

that a firm perform certain remedial actions, only the Tennessee State Board of Accountancy has the power to suspend or revoke a firm's permit.

Pursuant to Section 62-1-201, *Tennessee Code Annotated*, the board's Peer Review Oversight Committee, which consists of three licensed CPAs, one member from each of Tennessee's grand divisions, is responsible for overseeing the state's peer review program, including TSCPA's administration of the program, and recommending to the board what actions to take against firms that had unfavorable peer reviews; it also states that "neither the board nor any third party, other than the oversight body [the Peer Review Oversight Committee], shall have access to documents furnished or generated in the course of the review."

Results of Audit Work

In gaining our understanding of the board's peer review process and responsibilities, we determined that the Peer Review Oversight Committee has never performed oversight responsibility as required by Section 62-1-201, *Tennessee Code Annotated*, and was rendered inactive by the board in 2009.

Prior to 2009, the Peer Review Oversight Committee performed peer reviews and oversaw the state's peer review program. In 2009, the board decided to remove the committee's responsibility to perform peer reviews because it became difficult for a three-person committee to manage the workload. TSCPA agreed to allow any firm to enroll in its peer review program regardless of the firm's membership status with TSCPA.

If the Peer Review Oversight Committee were active, its responsibilities would include evaluating peer reviewers' determinations and recommendations; assisting with selecting and training peer reviewers; and reporting on the peer review program's effectiveness to the board, among other responsibilities. The TSCPA currently performs these duties, with the exception of training for peer reviewers, which is provided through the AICPA. Furthermore, if the Peer Review Oversight Committee were active, it could recommend that the board open a complaint against a firm based on the firm's peer review results, but under current law the committee could not provide any details to the board relating to the peer review.

The objectives of our review of the board's peer review responsibilities were to determine

- the effect of an inactive Peer Review Oversight Committee on the board's ability to oversee accounting professionals within the state; and
- how National Association of State Boards of Accountancy (NASBA) members' statutory requirements governing the confidentiality of peer review results compare to Tennessee's requirements.

To gain an understanding of the board's statutory requirements governing peer reviews and the Peer Review Oversight Committee's responsibilities, we interviewed members and staff of the Tennessee State Board of Accountancy as well as TSCPA management. We attended the January 16, 2015, board meeting, where a TSCPA speaker presented information on peer

reviews. Additionally, we obtained statutes and Board of Accountancy rules for 54 jurisdictions of the United States and its territories who were members of NASBA,[6] which we then analyzed and compared to Tennessee. We obtained and reviewed

- AICPA's *Standards for Performing and Reporting on Peer Reviews*;
- TSCPA's application for firms' admission into the peer review program; and
- TSCPA's *Peer Review Annual Report on Oversight*, dated December 23, 2014.

We emailed surveys to the 54 jurisdictions to determine if these jurisdictions had an active Peer Review Oversight Committee (or equivalent) and to ascertain their committee's responsibilities to their respective Board of Accountancy. The results of our survey revealed a significant number of other State Boards of Accountancy across the United States, 35 of 54 (65%), have the authority to view peer review reports, and other related documents, of firms that operate within their jurisdictions. One jurisdiction did not require peer reviews, and for another jurisdiction, we could not determine if the board could view peer review reports and other documents.

Based on the procedures performed, we determined that

- without an active Peer Review Oversight Committee, the Tennessee State Board of Accountancy is limited in its ability to oversee the peer review process to ensure that peer reviews are conducted in accordance with the AICPA's *Standards for Performing and Reporting on Peer Reviews* and, thus, cannot effectively oversee and regulate accounting professionals within the state (see Finding); and
- unlike the majority of other jurisdictions, Tennessee statute prohibits the board from viewing the results of peer reviews, including peer review reports, letters of peer review acceptance, or information relating to whether a firm passed or failed a peer review, which prevents the board from using a critical resource (the peer review results) in regulating the profession (see Finding).

[6] The National Association of State Boards of Accountancy's (NASBA) membership consists of 55 jurisdictions of the United States and its territories. While we reviewed statutes and Board of Accountancy rules for 54 jurisdictions, we did not include Puerto Rico in our work because the documents we obtained were written in Spanish.

Finding – Under its current structure, the Tennessee State Board of Accountancy is limited in its ability to oversee the peer review program in Tennessee

Condition

The Tennessee State Board of Accountancy cannot fulfill the requirements of Section 62-1-201, *Tennessee Code Annotated*, without an active Peer Review Oversight Committee and therefore is unable to effectively regulate the accounting profession.

Cause

According to the Executive Director, it has been extremely difficult for the board to fill the East and West Tennessee positions. He stated that there has been almost no interest from applicants in East Tennessee. The Executive Director has advertised the East Tennessee position since January 2015 with no responses as of May 1, 2015. In 2014, the Executive Director had to advertise for the West Tennessee position for five months before he could fill the position. According to the Executive Director, on April 9, 2015, he obtained a list of qualified licensees from the TSCPA and planned to contact each eligible member directly.[7]

Effect

Without an active oversight body, the board has a limited ability to ensure that peer reviews are conducted in accordance with the AICPA's *Standards for Performing and Reporting on Peer Reviews* and cannot know why a firm has performed poorly. Due to the absence of the Peer Review Oversight Committee and the board's statutory restriction from viewing peer review reports, the board cannot properly regulate firms providing accounting and auditing services in Tennessee. Allowing the board to view peer review reports could alleviate this issue.

Recommendation

If the board continues to have difficulties filling the positions on the Peer Review Oversight Committee, the board should consider alternatives, which might include working with the General Assembly to amend Section 62-1-201, *Tennessee Code Annotated*, to allow the board to view peer review reports and documents.

Legislative Consideration

Section 62-1-201, *Tennessee Code Annotated*, requires that peer review documents be kept in confidence from the board, under all circumstances. In the interest of transparency to the Tennessee businesses and citizens who procure services from accounting firms, the General Assembly may wish to consider revising the statute so that the board has the ability to view peer review report results and other necessary documents, to facilitate the board's ability to regulate the profession.

[7] We do not know the current status of this plan because the Executive Director retired on May 1, 2015.

Management's Comment

We concur with the finding.

The Board and management will discuss and consider the noted recommendation of working with the General Assembly to revise Section 62-1-201, *Tennessee Code Annotated*, requiring peer review results and documentation to be kept confidential from the Board. The Board will be asked to consider their support for this recommendation at the next Board meeting in October 2015.

Due to stringent requirements to serve on a PROC, it has been difficult to locate individuals to serve in this role. The Board and management will discuss options related to the PROC in conjunction with the above recommendation at the next Board meeting in October 2015.

PROFESSIONAL PRIVILEGE TAX

Pursuant to Section 67-4-1702(3)(A), *Tennessee Code Annotated*, individuals who engage in certain professions in Tennessee, including accountants, are required to pay the professional privilege tax of $400, due annually on June 1, to the Tennessee Department of Revenue. When a CPA fails to pay the professional privilege, the board suspends the CPA's license until he or she resolves the tax delinquency with the Department of Revenue.

The objective of our review of this section was to determine if CPAs with active licenses paid the professional privilege tax due to the Department of Revenue before the board renewed their licenses.

To gain an understanding of the professional privilege tax requirements for active CPAs, we reviewed several sections within Title 67, Chapter 4, Part 17, *Tennessee Code Annotated*. From a population of 7,248 active licenses renewed on December 31, 2014, we tested a nonstatistical random sample of 25 active licenses to determine if the CPAs paid their professional privilege tax before the board renewed the license. We verified with the Department of Revenue, Taxpayer Services Division, to determine whether these active licensees were current on their privilege tax payments.

Based on the procedures performed, we determined that the CPAs with active licenses that renewed on December 31, 2014, paid their professional privilege tax before the board renewed their licenses.

COMPLAINT HANDLING PROCESS

The board is tasked with the mission of protecting the public interest by ensuring the reliability of financial information produced by those individuals and firms professing competencies in accountancy. Effective protection of the public interest requires the board to handle complaints timely and to proactively search for violations involving the accounting profession. Any member of the public or the board staff itself may initiate complaints against individuals and firms. The board, in conjunction with the Department of Commerce and Insurance, handles the complaints in accordance with the *Department of Commerce and Insurance, Division of Regulatory Boards, Complaint Handling Standard Operating Procedure*. According to the department's Standard Operating Procedure,

> . . . the Program Director or designee [state board's Executive Director] shall conduct an initial review of the complaint to determine: (1) whether the complaint has been filed with the correct program and (2) whether the complaint is a high priority matter (e.g., the alleged conduct poses an imminent danger to the public health, safety or welfare) . . . Within five (5) business days of receiving the complaint, the Complaint Coordinator shall: . . . Send a copy of the complaint, via U.S. mail, to the Respondent, unless otherwise advised by the Program Attorney [Department of Commerce and Insurance's General Counsel] after consultation with the Program Director. . . . Investigation requests shall be completed [by the board] and written investigation reports shall be sent to the Program Attorney within thirty (30) calendar days of referral. If additional time is needed for completion of investigations requests, then the investigator shall make such request by email to . . . the Attorney who requested the investigation. The request shall specify how much additional time is needed and must be made within twenty-five (25) calendar days of when the matter was referred.

The board members and staff and the Department of Commerce and Insurance's Office of General Counsel play an integral role in resolving complaints filed against CPAs and accounting firms in Tennessee. The complaint handling process begins when the board receives a completed complaint form. Completed complaint forms may be mailed, emailed, or dropped off at the board's office. Once the complaint forms are received, the board's Executive Director must first determine if the complaint is worth pursuing. The Executive Director then reviews all complaints to determine what the alleged violations are and if they pose an imminent danger.[8] After the Executive Director reviews the complaints, he gives the forms to the complaint coordinator. The complaint coordinator enters the complaint into the Regulatory Boards Case/Complaint System, where a complaint number is assigned. Occasionally, a complaint is erroneously opened. For example, a complaint coordinator mistakenly opens two complaints for the same alleged violation, or mistakenly opens a complaint for unlicensed practice against a licensee when, in fact, the licensee is active. In these and other unique scenarios, the complaint may be closed by the board's complaint coordinator due to administrative error, which means

[8] Imminent danger to the public health, safety, or welfare could include situations that require law enforcement involvement, potentially violent respondents, or other ongoing litigation efforts.

that neither the formal complaint process nor board presentation is required to resolve the complaint.

To pursue complaints, the complaint coordinator sends letters to the complainant and the respondent[9] based on the information received from the Executive Director. The letter to the complainant informs him or her that the board received a completed complaint form and that the board will notify him or her once the complaint is resolved. The letter to the respondent includes notification that a complaint was received, the statute or board rule that was allegedly violated, and a request for a response to the complaint. For complaints that do not pose an imminent danger to the public health, safety, or welfare, the board is required to mail a copy of the complaint via U.S. mail to the respondent within 5 business days of receiving the completed complaint form. The respondent is given up to 30 calendar days to respond to the complaint letter; then the matter is referred to the department's Office of General Counsel.

The department's general counsel determines the best course of action necessary to resolve cases against respondents. The department's general counsel may request that one of the board's two investigators complete an investigation to establish the facts of the case and attempt to obtain a sworn affidavit from the respondent explaining his or her perspective of the case. Once requested to review, investigators must complete the investigation within 30 days. After all the necessary information is obtained, the general counsel will present the case to the board members with a recommendation to dismiss or close with no action; issue a letter of warning; issue a cease and desist letter; offer a consent order or agreed order; or order a formal hearing. The board members ultimately determine the appropriate penalty or disciplinary action via majority vote at one of its quarterly board meetings. Section 62-1-111, *Tennessee Code Annotated*, grants the board the authority to impose civil penalties and suspend or revoke licenses. To determine the appropriate disciplinary action and penalty, the board utilizes the applicable statutes, its rules, the recommendations of general counsel, and its settlement guidelines to render their decisions.

The objectives of our review of the complaint handling process were to determine

- that complaints, which were administratively closed were approved and properly closed;
- if the board sent notification letters to the respondents within 5 business days of receiving the complaint;
- if the board completed investigations within 30 calendar days after receipt;
- if disciplinary actions taken against respondents were in accordance with stated guidelines; and
- if the board proactively seeks to identify individuals or firms providing accounting services without a license or permit, respectively.

[9] The department's complaint handling Standard Operating Procedure uses the term "complainant" to refer to the individual or entity that initiated the complaint. It uses the term "respondent" to refer to the individual or entity against whom the complaint was filed.

To meet all of our objectives, we interviewed the applicable department and board staff to gain an understanding of the complaint handling process. We also conducted a survey of other state boards under NASBA and obtained the Ohio Board of Accountancy's *Enforcement and Disciplinary Policy Manual*, dated June 2012, and compared their process with Tennessee's process.

We obtained the Tennessee State Board of Accountancy's Regulatory Board System reports containing 214 complaint files that were opened from January 1, 2013, through December 31, 2014, to determine the number of administratively closed files. We identified eight files that were administratively closed and then performed testwork to determine the reason they were closed and whether the closure was approved by the Executive Director.

To determine if notification letters were sent to the respondent within 5 business days of the complaint and if investigations were completed within 30 calendar days, we reviewed the *Department of Commerce and Insurance*, *Division of Regulatory Boards*, *Complaint Handling Standard Operating Procedure*, version October 2014. We also obtained a list of 214 complaints that were opened from January 1, 2013, through December 31, 2014. We identified 206 of the 214 complaints that required the board to send a letter to the respondent. We then performed testwork on a nonstatistical random sample of 60 of these complaints to determine if the board sent a letter regarding the complaint to the respondent. Furthermore, we identified 139 of the 214 complaints that required an investigation and tested them to determine if the investigations were completed within 30 days.

To determine if disciplinary actions taken against the respondent were in accordance with stated guidelines, we reviewed the board's *Settlement Guidelines for Disciplinary Action*, dated October 16, 2012. We obtained a list of 191 complaints that were closed from January 1, 2013, through December 31, 2014. From this list of closed complaints, we identified 155 complaints requiring an investigation and we performed testwork on a nonstatistical random sample of 63 complaints to determine the board's disciplinary actions against the respondent. We also reviewed the board's website, which contained the 2013 and 2014 disciplinary actions archive, and we identified 36 complaints that required disciplinary action. We then performed testwork on the 36 complaints and determined that 17 complaints involved first-time offenders, 15 complaints involved repeat offenders, and 4 complaints were not repeat offenders but involved especially damaging violations to the profession or public.

To determine if the board proactively pursued individuals or firms providing accounting services without a license or permit, respectively, we obtained the documentation of the board's investigators' 2014 Preparer Tax Identification Number (PTIN) database project.[10] The investigators used this database project to look for preparers located in Tennessee who claimed they were Certified Public Accountants but were not licensed by the board. The board's investigators divided the project workload, and we obtained documentation that one investigator was currently pursuing 59 potential violations.

Based on the procedures performed, we determined that

[10] On August 12, 2015, board management informed us that they aborted this project, effective April 24, 2015.

- administratively closed complaints were appropriate and properly approved;
- the board's former and current complaint coordinator did not send notification letters to the respondent within 5 business days for 43% of the opened complaints tested (see observation);
- the board's investigators did not complete investigations within 30 days for 90% of opened investigations tested (see observation);
- the disciplinary actions were leveled against respondents in accordance with stated guidelines; and
- the board proactively sought individuals or firms providing accounting services without a license or permit, respectively.

Observation – The Tennessee State Board of Accountancy and Department of Commerce and Insurance disagreed on the reasonableness and importance of the department's complaint handling standard operating procedures

The Department of Commerce and Insurance established performance metrics for all boards under its Division of Regulatory Boards to monitor and evaluate each board's complaint processing performance based on the percentage of complaints resolved within 180 days of receipt. To ensure the 180-day performance metric is met, the department also established complaint handling standard operating procedures that define interim deadlines (e.g., requirements to send notification letters to respondents and investigation completion) to help each board monitor its progress. Through our audit work, we determined that the board met the department's 180-day performance metric; however, we noted that the Tennessee State Board of Accountancy did not always meet the following complaint handling standard operating procedure deadlines.

- From a population of 206 complaints that the board opened from January 1, 2013, through December 31, 2014, we tested a nonstatistical random sample of 60 complaints and found the board's former and current complaint coordinators did not send letters describing the complaints to the respondent within 5 business days for 26 of 60 complaints tested (43%). In one case, the Executive Director held a complaint for 44 business days in order to train a new complaint coordinator.
- From a population of 139 investigations completed for complaints opened from January 1, 2013, through December 31, 2014, we found that investigators did not complete and send the results to the department's general counsel within 30 calendar days for 125 of 139 investigations (90%). The average number of days required to complete these investigations was 73, with a range from 15 days to 158 calendar days.

The board's Executive Director informed us that the interim deadlines were arbitrary and unrealistic relative to the board. He stated that the department did not monitor for or report noncompliance with the interim deadlines and did not consult with him when determining the

interim deadlines. He further stated that he focused on resolving complaints within 180 days as a result of the department's emphasis on this performance metric. In the past, the Tennessee State Board of Accountancy had a backlog of complaints, but according to the Executive Director, the board has drastically improved in this area by hiring a second investigator and the board no longer has a backlog.

The Department of Commerce, Division of Regulatory Board's Accounting Manager, who is responsible for monitoring the board's performance metrics, informed us that the department stands by its standard operating procedures and the interim deadlines. He stated that the board should be able to meet the interim deadlines and departmental resources are available to assist them if needed. He further stated that the department does not actively measure the board's compliance with interim deadlines; however, these interim deadlines are merely guidelines to ensure the board resolves complaints within 180 days.

The Assistant Commissioner of the department's Division of Regulatory Boards stated that he will work with the board's next Executive Director to ensure that the complaint handling Standard Operating Procedure's interim deadlines are met.

BOARD FUNDING

Tennessee statute directs the board to operate self-sufficiently or be subject to a review by a joint evaluation committee of the State Legislature. Section 62-1-121, *Tennessee Code Annotated*, provides for the creation of a reserve fund for the board and mandates the board's self-sufficient operations. Section 4-29-121, *Tennessee Code Annotated*, provides further guidance for each "regulatory board, commission and entity administratively attached to the division of regulatory boards within the department of commerce and insurance," such as the Tennessee State Board of Accountancy, and states that any such board or entity that does not operate self-sufficiently "for two consecutive years shall be reviewed by a joint evaluation committee during the next legislative session following the second consecutive fiscal year during which such board, commission or entity operated at a deficit."

According to Sections 62-1-121(b) and (d), the purpose of the reserve fund is to defray expenses incurred by the board and "any part of the fund of the State Board of Accountancy remaining at the end of the fiscal year shall not revert to the general fund, but shall be carried forward until expended. . . ." Section 62-1-121(e), requires that

> The board shall budget annually…its expenditures for programs, services, allocated overhead or charge backs and other normal operating expenses as determined by the board. These expenditures so established shall be budgeted at the beginning of the year by the board, not to exceed the fees to be received by the board, including the excesses accumulated in the fund of the board. The commissioner of finance and administration shall inform the board annually, in advance for budgeting purposes, the allocation of all overhead or charge backs to the board.

The board has historically operated self-sufficiently, with certain exceptions resulting from unexpected expenditures, such as the costs incurred from the 2003 termination of its Executive Director and the ensuing litigation; however, in these instances, the reserve fund was sufficient to cover these losses.

During our audit period, the Department of Commerce and Insurance initiated the implementation of the Comprehensive Online Regulatory Enforcement (CORE) system, a $2.4 million system to replace the antiquated Regulatory Board System. The CORE system will be used by boards administratively attached to the department, including the Tennessee State Board of Accountancy, to track licensure. To cover the costs of implementing the new system, the department allocates the total cost to each regulatory board based on the number of licensees and charges each regulatory board's reserve fund.

The objective of our review of the sufficiency of the board's funding was to determine

- if the board operated self-sufficiently;
- the proper uses of the board's reserve fund; and
- how the department allocated and charged the board's reserve fund for its share of the CORE system implementation costs.

To meet all of our objectives, we interviewed the board's Executive Director, applicable department staff, and a Coordinator with the Department of Finance and Administration, Division of Budget. To determine if the board was self-sufficient, we reviewed the appropriate state statutes to gain an understanding of the board's self-sufficiency requirements as well as the proper uses of the board's reserve fund.

We also reviewed the board's budgets for fiscal years 2013 and 2014. From Edison, the state's accounting system, we obtained the board's operational and reserve fund revenues and expenditures and calculated the board's self-sufficiency based on operational revenues and expenditures for fiscal years 2013 and 2014. Although the board was self-sufficient operationally for both fiscal years, we also considered the board's reserve fund revenue and expenditure amounts for fiscal years 2013 and 2014 and analyzed their effect on self-sufficiency. To ensure we obtained a complete list of all transactions relevant to the board's reserve fund, we traced the amounts to Edison queries; the department's financial report to the Department of Finance and Administration; and the board's financial statement.

To determine the methodology the department used to allocate the costs of the CORE system implementation, we obtained a copy of the department's Fund Loan Request, Cost Approval, and Cost Allocation for the CORE system, including each regulatory board's share of the total cost of the CORE system.

Based on the procedures performed, we determined that

- the board was self-sufficient for fiscal years 2013 and 2014;

- the board's reserve fund was properly used; and
- the department appropriately allocated and charged the board's reserve fund $70,464 for CORE system design and implementation during fiscal year 2014.

OPEN MEETINGS AND NATIONAL ASSOCIATION OF STATE BOARDS OF ACCOUNTANCY PARTICIPATION

Open Meetings

Pursuant to Section 8-44-102(a), *Tennessee Code Annotated*, "All meetings of any governing body are declared to be public meetings open to the public at all times. . . ." The Open Meetings Law was enacted to ensure that all boards and councils that govern over or provide recommendations to a regulatory agency or answer to a regulatory agency properly record all meetings and that all discussions concerning board matters are open to the public. If a board is found to have conducted improper meetings and is challenged in the state's court system, the court may order an adjournment, may order an injunction against any of its actions or policy changes, will monitor the board for a year, and will require semi-annual communication. The Open Meetings Law requires governing bodies, such as the Tennessee State Board of Accountancy, to ensure that all meetings are open to the public by notifying the general public prior to each meeting, providing the agenda of each meeting in a timely manner before the meeting, and recording and releasing the minutes of each meeting.

National Association of State Boards of Accountancy

As required by statute, the board must be a member of the National Association of State Boards of Accountancy (NASBA) and actively participate in its events. According to Section 62-1-105(f), *Tennessee Code Annotated*,

> The board shall join professional organizations and associations to promote the improvement of the standards of the practice of accounting and for the protection and welfare of the public. In order to be informed about the operations and practices of other Boards of Accountancy desiring reciprocal exchange and in order to be advised regarding the progress of accountancy throughout the country and to promote uniformity in the regulation of accountancy, the board, executive director and staff shall, at the discretion of the board, travel and attend national and regional meetings of the National Association of State Boards of Accountancy (NASBA) and other appropriate professional meetings at the expense of the board. Travel shall be subject to and in accordance with the comprehensive travel regulations as promulgated by the department of finance and administration and approved by the attorney general and reporter.

Pursuant to Section 62-1-105(f), *Tennessee Code Annotated*, members and staff of the board must submit travel expense requests to attend NASBA events. The denial of travel expense

requests would place a financial burden on individual board members and staff and prevent the board from meeting the requirement of Section 62-1-105(f) to attend NASBA events.

Results of Audit Work

The objectives of our review of this section were to determine if

- the board complied with the state's Open Meetings Law; and
- the board actively participated in NASBA events.

To determine if the board complied with the Open Meetings Law, we reviewed Sections 8-44-101, et seq., and 10-7-501, et seq., *Tennessee Code Annotated*. We also interviewed the Assistant to the Comptroller for Public Finance and Open Records Counsel concerning public meeting requirements, commonly referred to as sunshine regulations, and how other state agencies interpret the Open Meetings Law. We obtained the January 31, 2014, presentation given to the Tennessee State Board of Accountancy, titled "You are My Sunshine, My Only Sunshine," which provided a summary of the public meetings regulations for governing bodies in the State of Tennessee.

To gain an understanding of the board's involvement in NASBA, we reviewed Section 62-1-105(f), which mandates the board's membership and participation in NASBA. We obtained a list of the NASBA events attended by board members and staff from January 1, 2013, through December 31, 2014.

Based on the procedures performed, we determined that

- the board held quarterly, public meetings, and thus the board complied with the Open Meetings Law; and
- board members, the Executive Director, and board staff attended NASBA's 11 meetings during calendar years 2013 and 2014, and thus actively participated.

INFORMATION SYSTEMS

The Department of Commerce and Insurance (the department) provides information system (IS) services to all regulatory boards, including the Tennessee State Board of Accountancy. To assist them in their duties, board staff use the following systems:

- Regulatory Board System[11]
- FileNet

[11] Regulatory Board System will be replaced by the CORE system, scheduled to be implemented in the fall of 2015.

The Regulatory Board System (RBS) is a system that is also used to store information about the board's licensees, firms, and complaints. Board staff enter information into RBS, which can be processed further to assist staff in their day-to-day duties. For example, when the board receives a new licensure application from a CPA candidate, board staff image the application into FileNet[12] and enter all of the candidate's information into RBS so that staff can monitor the CPA's licensure requirements, such as continuing professional education.

The objective of our review of RBS was to determine if the department and the board followed state information system policies and industry best practices.

We interviewed applicable department and board staff to gain an understanding of the IS environment over RBS. Additionally, we obtained state and departmental policies and other documents to assess the evidence that IS controls were in place during our audit. To determine industry best practices, we reviewed policies of the Department of Finance and Administration, Office for Information Resources, as well as the United States Government Accountability Office's *Federal Information System Controls Audit Manual*, which presents a methodology for auditing IS controls in federal and other governmental entities. We tested a population of three employees who separated from employment from January 1, 2013, through January 31, 2015, to determine if the department and the board followed state information system policies and industry best practices. Two employees were department employees and the other was a board employee.

Based on the procedures performed, we determined that the department and the board followed state information system policies and industry best practices.

[12] The FileNet system stores the imaged documents relating to information about the board's licensees, firms, and complaints. When the board receives information, such as a response to a complaint, board staff scan or upload the document into the FileNet system, and the scanned image becomes electronically available for other staff members to view. FileNet is an image repository system; it does not process information.

APPENDICES

Appendix 1

Tennessee State Board of Accountancy Staff and Board Member Positions by Gender and Ethnicity February 3, 2015 (Source: State Audit Information Systems)								
Title	**Gender**		**Ethnicity**					
	Male	Female	American Indian	Asian	Black	Hispanic	White	Other
Admin Assistant 1	0	1	0	0	0	0	1	0
Admin Assistant 2	1	1	0	0	0	0	2	0
Admin Assistant 3	0	1	0	0	0	0	1	0
Admin Services Assistant 4	0	1	0	0	0	0	1	0
Board Member	8	3	0	0	0	0	11	0
Executive Director	1	0	0	0	0	0	1	0
Investigator	2	0	0	0	0	0	2	0
Totals	12	7	0	0	0	0	19	0

Appendix 2

Performance Measures Information

As stated in the Tennessee Governmental Accountability Act, "accountability in program performance is vital to effective and efficient delivery of government services, and to maintain public confidence and trust in government." In accordance with this act, all executive branch state agencies are required to submit annually to the Department of Finance and Administration a strategic plan and program performance measures. The Tennessee State Board of Accountancy's priority goals, as of February 28, 2015, are as follows.

Performance Standards and Measures

Performance Standard 1: Provide efficient licensure and enforcement services for regulated industries.

Purpose of the Goal: To increase the percentage that meet or decrease average licensure processing time.

***Measuring the Goal*:** Percentage that met or decreased average licensure time.			
	Baseline	**Current**	**Target**
Percentage	85%	79.05%	90%

Source: Department of Commerce and Insurance.

Purpose of the Goal: To increase the percentage of complaints resolved or referred to formal hearing within 180 days of receipt

***Measuring the Goal*:** Percentage of complaints that were resolved or referred to formal hearing within 180 days of receipt.			
	Baseline	**Current**	**Target**
Percentage	75%	89.08%	80%

Source: Department of Commerce and Insurance.