

**REVISED RULE MAKING
NO HEARING(S) SCHEDULED**

Mandatory Quality Review Program for Public Accountancy

I.D. No. EDU-30-10-00003-RP

PURSUANT TO THE PROVISIONS OF THE State Administrative Procedure Act, NOTICE is hereby given of the following revised rule:

Proposed Action: Amendment of section 70.10 of Title 8 NYCRR.

Statutory authority: Education Law, sections 207(not subdivided), 6501(not subdivided), 6504(not subdivided), 6506(6) and 7410

Subject: Mandatory quality review program for public accountancy.

Purpose: To establish the requirements for the mandatory quality review program for public accountancy.

Substance of revised rule: The Commissioner of Education proposes to add a new section 70.10 to the Regulations of the Commissioner of Education, relating to establishing a mandatory quality review program in public accountancy. The following is a summary of the proposed amendment:

Subdivision (a) of section 70.10 of the Regulations of the Commissioner of Education establishes a mandatory quality review program requiring all applicants seeking a firm registration or renewal of a registration, other than a sole proprietorship or firms with two or fewer professionals, to participate in a quality review of the firm's attest services no more frequently than once every three years.

Subdivision (b) of section 70.10 of the Regulations of the Commissioner of Education defines terms used in section 70.10 including accounting professional, quality review report, review, review team, reviewer, sponsoring organization and team captain.

Subdivision (c) of section 70.10 of the Regulations of the Commissioner of Education indicates those firms that must participate in a quality review. This subdivision also requires any firm not required to participate in mandatory quality review to annually submit a written notification of exemption to the Department. Any firm that begins providing attest services or otherwise becomes subject to mandatory participation in the quality review program is required to notify the Department of its change in status within 30 days and to provide the Department with evidence that it has enrolled in an acceptable quality review program within one year of the earlier of the firm's initial registration or the firm's initial performance of services requiring a quality review. Such firms must have a quality review performed within 18 months of the date the services were first provided.

Subdivision (d) of section 70.10 of the Regulations of the Commissioner of Education establishes a Quality Review Oversight Committee (QROC) to oversee the mandatory quality review program. The QROC will consist of five members who must be New York licensed CPAs and hold a current registration with the Department. Members will serve five year terms except those first appointed will serve staggered terms so that an equal number of terms terminate annually. Responsibilities of the QROC include: receiving and approving quality review plans of entities seeking to be sponsoring organizations; monitoring sponsoring organizations to determine that each sponsoring organization is providing an acceptable level of oversight over reviewers, review teams and firms participating in the quality review program; inform the Department of issues and /or problems relating to the quality review program; annually

report to the Department that the sponsoring organization holds qualifications necessary to continue as an approved sponsoring organization; annually assess the effectiveness of the quality review program; annually report on any recommended modifications to the quality review program; review each quality review report submitted by a firm to determine that the firm is complying with applicable professional standards and ensure that any documents received from a firm or reviewer, sponsoring organization or entity administering peer review outside the state of New York shall be confidential and not constitute a public record and shall not be subject to disclosure under article six and six-A of the Public Officers Law.

Subdivision (e) of section 70.10 of the Regulations of the Commissioner of Education defines the approval process for sponsoring organizations. Sponsoring organizations must submit a plan of administration that establishes committees and provides assurances that sufficient professional staff exist for the operation of the quality review program; provide assurances that the sponsoring organization will notify firms and reviewers of the latest developments in quality review standards and the most common deficiencies in quality reviews conducted by the sponsoring organization; establish procedures to resolve any disagreement between the firm and the reviewer that may arise out of the performance of a quality review; acknowledge that the sponsoring organization is subject to evaluation and periodic review; establish procedures to evaluate and document performance of each reviewer and to disqualify a reviewer who does not meet the standards for quality review; establish procedures to ensure that the sponsoring organization submits timely reports to the QROC; establish procedures to maintain the confidentiality of documents received from the firm or reviewer unless any such document is admitted into evidence in a hearing held by the Department; and provide annual reports to the QROC on the results of the quality review program, including number of reviews conducted; the number of firms complying with the quality review standards, the number of firms having some deficiencies, the number of firms not in compliance with the quality review standards.

Subdivision (f) of section 70.10 of the Regulations of the Commissioner of Education defines the process to be followed to approve and assign team captains and review teams. The sponsoring organization must provide a list of reviewers to the Department and from that list the Department must develop a roster of approved reviewers. Sponsoring organizations must perform procedures to test that review team members, including the team captain are licensed or otherwise authorized to practice in any state and that the review team and team captain meet a minimum set of competencies to commence a quality review. Competencies include specified experience performing attest services, participation in acceptable training, and knowledge of professional standards, rules and regulations appropriate to the industries included in the review.

Subdivision (g) of section 70.10 of the Regulations of the Commissioner of Education provides that the Department may upon notice and with the opportunity to be heard, remove a reviewer and/or review team member from the roster of approved reviewers for failure to meet the requirements of subdivision (f) or for having been subject to disciplinary action.

Subdivision (h) of section 70.10 of the Regulations of the Commissioner of Education provides that a firm which has received a report that the firm has failed to design a system of quality control over its attest services or that receives a quality review report indicating that the firm has failed to perform and report on engagements in conformity with applicable standards in material respects may be referred by the QROC for disciplinary action under Education Law section 6510.

Subdivision (i) of section 70.10 of the Regulations of the Commissioner of Education defines the standards for quality reviews. In addition to setting the standards of quality reviews, this subdivision requires that for any firm undergoing a review of its system of quality control, the review team shall review the firm's continuing education records on a sample basis and consider whether the records demonstrate that the licensee who supervised the services meets the competency requirements set forth in professional standards for such services, and in paragraph 13 of subdivision (a) of section 29.10 of the Rules of the Board of Regents.

Subdivision (j) of section 70.10 of the Regulations of the Commissioner of Education defines the requirements for access to the results of quality reviews by the department. Any firm required to participate in the program shall submit to the department: a quality review report, the firm's letter of response, an acceptance letter from a sponsoring organization, a letter(s) signed by the firm accepting the documents and a letter from the sponsoring organization notifying the reviewed firm that required actions have been appropriately completed. The quality review report, the reviewed firm's letter of response and acceptance of the quality review report by the sponsoring organization must be made available to the department via a secure website within 30 days of the date of the acceptance letter. If applicable, a letter signed by the reviewed firm accepting the quality review documents with the understanding that the firm agrees to take any actions required by the reviewer must be made available to the

department within 30 days of the date the firm signs such letter. If applicable, the letter from the sponsoring organization notifying the reviewed firm that required actions have been appropriately completed must be made available to the department within 30 days to the date of the letter from the sponsoring organization. If the sponsoring organization cannot provide access to the quality review documents via a website, the firm shall provide copies of the quality review documents by mail or facsimile within 10 days of receipt of the applicable documents. Copies of equivalent quality review reports submitted in accordance with subdivision (m) must be made available to the department via a website provided by the entity administering the quality review. If it cannot be provided via a website, the firm shall provide copies by mail or facsimile.

Subdivision (k) of section 70.10 of the Regulations of the Commissioner of Education requires each reviewer and sponsoring organization, as applicable, to maintain documentation necessary to establish that each review conformed to the review standards of the relevant review program, including the review work papers, copies of the review report, and any correspondence indicating the firm's concurrence, non-concurrence, and any proposed remedial actions and related implementation. These documents must be retained by the reviewer for a period of time corresponding to the retention period of the sponsoring organization, and must be available to the Quality Review Oversight Committee. In no event, shall the retention period be less than 120 days from the date of acceptance of the review by the sponsoring organization.

Subdivision (l) of section 70.10 of the Regulations of the Commissioner of Education requires any firm that undergoes an inspection conducted by the Public Company Accounting Oversight Board ("PCAOB") as required under the Sarbanes-Oxley Act of 2002 to submit to the Department a copy of the public version of its most recent inspection report within ten days of a receipt of the notice of completion from the PCAOB.

Subdivision (m) of section 70.10 of the Regulations of the Commissioner of Education establishes that the Department, at its discretion, may accept a review report from a firm which the Department deems to be the substantial equivalent of a quality review report issued under this section. A review report will be deemed substantially equivalent provided such reviews are conducted and reported on in accordance with the quality review standards set forth in subdivision (i) of this section. Peer reviews administered by entities located outside the state of New York acceptable to the Department and any affiliated administering entities may be accepted as substantially equivalent of a quality review report issued under this section.

Revised rule compared with proposed rule: Substantial revisions were made in section 70.10(b)(5), (7), (c)(5), (f) and (f)(3).

Text of revised proposed rule and any required statements and analyses may be obtained from Christine Moore, New York State Education Department, 89 Washington Avenue, Albany, New York 12234, (518) 473-8296, email: cmoore@mail.nysed.gov

Data, views or arguments may be submitted to: Frank Munoz, Deputy Commissioner of the Professions, New York State Education Department, 89 Washington Avenue, 2nd Floor, Albany, New York 12234, (518) 474-1756, email: fmunoz@mail.nysed.gov

Public comment will be received until: 30 days after publication of this notice.

Revised Regulatory Impact Statement

Since publication of a Notice of Proposed Rule Making in the State Register on July 28, 2010, the following substantial revisions were made to the proposed rule:

Paragraphs (5) and (7) of subdivision (b) of section 70.10 of the Regulations of the Commissioner of Education were amended to replace the term "assigned" with "approved".

Paragraph (5) of subdivision (c) of section 70.10 of the Regulations of the Commissioner of Education is amended to replace the term "conducted" with "completed".

Subdivision (f) of section 70.10 of the Regulations of the Commissioner of Education is amended to replace the phrase "and assignment" with the term "approval".

Subparagraph (ii) of paragraph (3) of subdivision (f) of section 70.10 of the Regulations of the Commissioner is amended to delete the words "assignment by an approved sponsoring organization to" and to change the word "commence" to "commencing".

Subclause (1) of clause (a) of subparagraph (ii) of paragraph (3) of subdivision (f) of section 70.10 of the Regulations of the Commissioner of Education is amended to delete the words "manager or person with equivalent supervisory responsibilities".

The above revisions to the proposed rule do not require revisions to the previously published Regulatory Impact Statement.

Revised Regulatory Flexibility Analysis

Since publication of a Notice of Proposed Rule Making in the State Register on July 28, 2010, the proposed rule was revised as set forth in the Revised Regulatory Impact Statement herewith.

The above revisions to the proposed rule do not require any revisions to the previously published Rural Area Flexibility Analysis.

Revised Rural Area Flexibility Analysis

Since publication of a Notice of Proposed Rule Making in the State Register on July 28, 2010, the proposed rule was revised as set forth in the Statement Concerning the Regulatory Impact Statement filed herewith.

The revisions to the proposed rule do not require revisions to the previously published Rural Area Flexibility Analysis.

Revised Job Impact Statement

Since publication of the Notice of Proposed Rule Making in the State Register on July 28, 2010, the proposed rule was revised as set forth in the Statement Concerning the Regulatory Impact Statement filed herewith.

The proposed rule, as so revised, relates to the mandatory quality review program for public accountancy. The revised rule will not have a substantial adverse impact on job or employment opportunities. Because it is evident from the nature of the revised rule that it will have no impact on jobs or employment opportunities, no further measures were taken. Accordingly, a job impact statement is not required and one has not been prepared.

Assessment of Public Comment

Since publication of a Notice of Proposed Rule Making in the State Register on July 28, 2010, the State Education Department received the following comments.

COMMENT: Two commenters expressed concern that the proposed regulations require auditors performing audits for small not-for-profit entities to undergo a peer review in accordance with government auditing standards also known as the "Yellow Book" standards promulgated by the Comptroller General of the United States. The commenters believe that requiring the application of these peer review standards could raise the cost of an independent audit of small not-for-profit entities. Another commenter expressed concern that the regulation would require all NYS Charities Bureau clients to be audited according to the "Yellow Book" standard, and that the CPAs would be required to meet the "Yellow Book" Continuing Professional Education requirement.

RESPONSE: The proposed regulation implements the requirements of Chapter 651 of the Laws of 2008, which requires "a firm that performs attest services for any New York State or municipal department, board, bureau, division, commission, committee, public authority, public corporation, council, office, or other governmental entity performing a governmental or proprietary function for New York State or any one or more municipalities thereof, or performs attest services specifically required to be performed pursuant to New York State law... to undergo an external peer review in conformity with" Generally Accepted Government Auditing Standards issued by the Comptroller General of the United States. The proposed amendment does not impose any additional requirements above those imposed by statute.

COMMENT: One commenter expressed concerns over the ambiguity of the phrases "begins providing attest services" and "initial performance" of attest services.

RESPONSE: The AICPA standards define the date of performance as the date the accountant issues an attestation report. The same date will be used for purposes of the proposed amendment. The Department will clarify this in guidance.

COMMENT: One commenter expressed concerns over the use of the term "conducted" and suggested that the term "completed" be used to avoid ambiguity and conform to current professional standards. The regulation states that the peer review must be "conducted" within 18 months. The commenter would prefer the term "completed."

RESPONSE: The Department has revised the proposed regulation to use the term completed instead of conducted to avoid any ambiguity and conform to the AICPA standards.

COMMENT: One commenter recommends that the Quality Review Oversight Committee recommend to the Department the acceptance of peer review reports rated "pass with deficiencies," similar to reports rated "pass without deficiencies."

RESPONSE: The Department believes that the Quality Review Oversight Committee should review all reports with deficiencies and reserve its ability and judgment to determine if such deficiencies warrant disciplinary action. The Department believes this to be in the public's best interest.

COMMENT: One commenter suggested a change to the reporting standard to coincide with existing peer review standards by including the wording "in all material respects" in the regulation. The commenter also suggested changing the section on referrals to the Office of Professional Discipline to include the wording "in all material respects," based on the fact that this language is used in reports on financial statements and in the proposed quality review standards.

RESPONSE: The proposed regulation provides for the adoption of AICPA standards for peer review. These standards require the review team to report whether or not a firm's is complying with applicable profes-

sional standards "in all material respects." Therefore it is not necessary to include the suggested level of specificity in the proposed regulation.

COMMENT: Professional standards require that a letter of comments be issued by the review team, if deficiencies were found during a quality review and if the quality review was commenced prior to January 1, 2009. To conform to these professional standards, the commenter suggested that the Department clarify that in addition to a quality review report, the letter of comments should also be submitted to the Department for those firms falling into this category.

RESPONSE: The Department believes that because the implementation date of the quality review requirement is January 1, 2012, many of the firms submitting reports under the regulation will have had their quality reviews commenced after January 1, 2009 and this requirement will not affect many of the firms submitting reports in compliance with the regulation. However to address this concern, the Department will clarify the need to submit a letter of comments in guidance for firms that fall into this category.