CALIFORNIA BOARD OF ACCOUNTANCY

PEER REVIEW OVERSIGHT COMMITTEE
2017 Annual Report

Table of Contents

I. Message from the Committee Chair 1
II. Background 2
III. PROC Responsibilities 2
IV. PROC Committee Members 3
V. Legislation and Regulations 3
VI. Board-Recognized Peer Review Program Providers 4
American Institute of Certified Public Accountants (AICPA) 4
a. CalCPA 4
b. National Peer Review Committee (NPRC) 4
c. Other State Societies 5
VII. Activities and Accomplishments 5
a. Program Oversight 5
i. AICPA 5
A. AICPA Peer Review Board (PRB) 5
B. AICPA Peer Review Program Annual Report on Oversight 5
C. AICPA PRB Oversight Report Acceptance of CalCPA Peer Review Administration 6
D. AICPA PRIMA 6
E. AICPA Educational Framework for Peer Reviewers 7
F. AICPA Annual Peer Review Conference – Peer Reviewer Training 9
ii. CalCPA 9
A. CalCPA PRC 9
B. CalCPA Report Acceptance Body (RAB) 9
C. CalCPA Administrative Site Visit Conducted by the CBA PROC 9
D. CalCPA Peer Review Annual Report on Oversight 10
iii. NPRC 11
A. NASBA CAC 11
B. NASBA CAC Report on the AICPA NPRC 11
iv. Other State Societies 12
b. Administrative Functions 12
i. PROC Committee Meetings 12
ii. PROC Oversight Checklists 13
A. Revisions to PROC Oversight Checklists 13
iii. Approval of Board-Recognized Peer Review Program Providers 14
iv. Withdrawal of Board Recognition of a Peer Review Program Provider 15
c. Other Activities 15
i. AICPA Proposed Evolution of Peer Review Administration 15
ii. California Peer Review Program Flowchart 16
iii. Oversight of Peer Review-Related Updates 17
iv. Revisions to the PROC Procedures Manual 17

VIII. Statistics 17
a. Statistical Monitoring and Reporting Activity 17
b. Peer Reviewer Population 22
IX. Observations 24
X. Conclusion 25

I. Message from the Committee Chair

I am pleased to present the California Board of Accountancy (CBA) with the Peer Review Oversight Committee's (PROC) 2017 Annual Report. It has been a pleasure to serve as Chair this past year, and I am honored to again serve as Chair this upcoming year.

Over the last year, the PROC has undertaken several important initiatives to improve its oversight of the peer review process. The PROC has endeavored to further evaluate and refine the Administrative Site Visit process used to evaluate the California Society of Certified Public Accountants (CalCPA) administration of the peer review program. During the PROC September 2017 Administrative Site Visit to CalCPA, the PROC implemented comprehensive Administrative Site Visit oversight procedures and concluded that CalCPA, as an administering entity (AE), met the American Institute of Certified Public Accountants' (AICPA)[1] Peer Review Program Standards, adopted by the CBA.

The PROC has been vigilant with oversight activities associated with the AICPA Enhanced Audit Quality (EAQ) initiatives and the evolution of the peer review program over the past year. The PROC assessed two AICPA EAQ initiatives that actualized in 2017; the May 2017 launch of the AICPA Peer Review Integrated Management Application (PRIMA) and the Benchmark Model for AEs. The PROC recognizes that PRIMA functions as a tool to streamline the national peer review process; allows accounting firms, reviewers, and AEs to communicate in real-time via notifications; and looks forward to using PRIMA as a data extrapolation tool to enhance peer review-related statistics. The PROC also reviewed the AICPA Benchmark Model for AEs, designed to monitor and promote transparency and are actively working to integrate the Benchmark Model in the overall PROC oversight responsibilities in 2018.

Tasked by the CBA in 2017, the PROC embarked on developing a process to evaluate the California peer reviewer population. The PROC communicated with AICPA and CalCPA regarding the California peer reviewer population and determined a need to establish a framework to monitor the peer reviewer population in California. The PROC plans to work collaboratively with both AICPA and CalCPA to establish and implement an applicable peer reviewer population monitoring framework in 2018.

With the on-going evolution of the peer review administration, the PROC successfully updated and revised the PROC Procedures Manual (PROC Manual) to remain relevant. The PROC specifically updated sections relating to committee membership qualification and oversight responsibilities within the PROC Manual. On that note, the PROC has successfully welcomed two new members in 2017: Sharon Selleck, CPA and Fiona Tam, CPA. In 2018 the PROC will continue to actively work on

[1] The California Board of Accountancy use of the acronym 'AICPA' is referring to the American Institute of Certified Public Accountants, and is not referring to the Association of International Certified Professional Accountants, a partnership between AICPA and the Chartered Institute of Management Accountants.

recruiting new individuals, and staff are working to increase outreach regarding the recruitment process.

I would like to thank the CBA for the opportunity to lead the PROC over this coming year and look forward to another successful year.

Sincerely,

Jeffrey De Lyser, CPA

II. Background

In 2009, the CBA sponsored Assembly Bill (AB) 138 (Chapter 312, Statutes of 2009) implementing mandatory peer review. AB 138 was signed by Governor Arnold Schwarzenegger and became effective on January 1, 2010. AB 138 requires all California-licensed firms, including sole proprietorships, providing accounting and auditing services, to undergo a peer review once every three years as a condition of license renewal. Effective January 1, 2012, Senate Bill 543 (Chapter 448, Statutes of 2011) removed the sunset language included in the original enabling legislation, making mandatory peer review permanent in California. Peer review, as defined by Business and Professions Code (BPC) section 5076(b)(1), is a study, appraisal, or review conducted in accordance with professional standards of the professional work of a firm, and may include an evaluation of other factors in accordance with the requirements specified by the board in regulations.

III. PROC Responsibilities

The PROC derives its authority from BPC section 5076.1. The purpose of the PROC is to provide recommendations to the CBA on any matter upon which it is authorized to act to ensure the effectiveness of mandatory peer review.

The roles and responsibilities of the PROC, as defined by the CBA, are:

a. Hold meetings as necessary in order to conduct business and report to the CBA regarding the effectiveness of mandatory peer review.
b. Ensure that Board-recognized peer review program providers (Provider) administer peer reviews in accordance with the standards set forth in Title 16, California Code of Regulations (CCR) section 48:

    - Conduct an annual administrative site visit.
    - Attend peer review board meetings, as necessary but sufficient to evaluate and assess the effectiveness of the program.
    - Attend peer review committee meetings, as necessary but sufficient to evaluate and assess the effectiveness of the program.
    - Attend meetings conducted for the purposes of accepting peer review reports, as necessary but sufficient to evaluate and assess the effectiveness of the program.

- Conduct reviews of peer review reports on a sample basis.
- Attend, on a regular basis, peer reviewer training courses.

c. Evaluate any *Application to Become A Board-recognized Peer Review Provider* and recommend approval or denial to the CBA.
d. Refer to the CBA any Provider that fails to respond to any request.
e. Collect and analyze statistical monitoring and reporting data from each Provider on an annual basis.
f. Prepare an Annual Report to the CBA regarding the results of its oversight.
g. Evaluate the peer reviewer population.

IV. PROC Committee Members

The PROC is comprised of seven members, all of whom must possess and maintain a valid and active license to practice public accountancy issued by the CBA. Members are appointed to two-year terms and may serve a maximum of four consecutive terms.

Current members	Term Expiration Date	Maximum Term Date
Jeffrey De Lyser, CPA, Chair	March 31, 2019	March 31, 2021
Kevin Harper, CPA, Vice-Chair	March 31, 2019	March 31, 2023
Renee Graves, CPA	November 30, 2019	November 30, 2023
Sharon Selleck, CPA	March 31, 2019	March 31, 2025
Fiona (Liang) Tam, CPA	November 30, 2019	November 30, 2025
Vacant	--	--
Vacant	--	--

In 2017, the CBA re-appointed Jeffrey De Lyser, CPA as Chair at its November 17-18, 2017 meeting and Kevin Harper, CPA, as Vice-Chair of the PROC at its January 18, 2018 meeting. In 2017, the PROC welcomed Ms. Sharon Selleck and Ms. Fiona Tam as new members to the PROC. The PROC is actively looking for new members as membership terms expire.

V. Legislation and Regulations

In an effort to streamline the CBA Peer Review Program, the CBA has considered a proposal to amend CCR section 45 regarding a requirement for accounting firms to report to the CBA.

The proposed amendment will decrease the CBA's population of licensed CPAs required to have a peer review. The proposed amendment will require only accounting firms and CPAs operating as sole proprietors performing auditing and attest services to have peer reviews and complete the required Peer Review Reporting form as part of the license renewal application process. The projected outcome would result in a decrease of barriers for CPAs performing general accounting services to renew their license timely.

The proposed amendment is actively being reviewed by the CBA and staff projects approval and changes will take effect in 2019.

VI. Board-Recognized Peer Review Program Providers

American Institute of Certified Public Accountants (AICPA)

The AICPA Peer Review Program is currently the only CBA-recognized Peer Review Program Provider. Through regulation, the CBA established that the AICPA Peer Review Program meets the standards outlined in, CCR section 48. Further, the CBA accepts all AICPA-approved entities authorized to administer the AICPA Peer Review Program.

The AICPA Peer Review Program provides for a triennial review of a firm's accounting and auditing services performed by a peer reviewer who is unaffiliated with the firm being reviewed to ensure work performed conforms to professional standards. There are two types of peer reviews. System Reviews are designed for firms that perform audits or other similar engagements. Engagement Reviews are for firms that do not perform audits but perform other accounting work such as compilations and/or reviews. Firms can receive a rating of pass, pass with deficiency, or fail. Firms that receive ratings of pass with deficiency or fail must perform corrective actions.

a. CalCPA

CalCPA administers the AICPA Peer Review Program in California. As an administering entity, CalCPA is responsible for ensuring that peer reviews are performed in accordance with the AICPA's Standards for Performing and Reporting on Peer Reviews. The CalCPA Peer Review Committee (PRC) monitors the administration, acceptance, and completion of peer reviews. CalCPA administers the largest portion of peer reviews to California-licensed firms.

b. National Peer Review Committee (NPRC)

The NPRC administers the AICPA peer review program for firms that meet any of the following three criteria:

- The firm is required to be registered with and subject to permanent inspection by the Public Company Accounting Oversight Board (PCAOB).
- The firm performs engagements under PCAOB standards.
- The firm provides quality control materials (QCM), or is affiliated with a provider of QCM, that are used by firms that it peer reviews.

The National Association of State Boards of Accountancy (NASBA) Compliance Assurance Committee (CAC) provides oversight of the NPRC.

c. Other State Societies

California-licensed accountancy firms with their main office located in another state are required to have their peer review administered by the AICPA's administering entity for that state. In most cases, the administering entity is the state CPA society in that state.

VII. Activities and Accomplishments

Following are the activities and accomplishments of the PROC during 2017.

a. Program Oversight

The PROC is charged with providing oversight of all CBA-recognized peer review program providers to ensure that peer reviews are being administered in accordance with the standards adopted by the CBA. During 2017, the PROC performed multiple activities to assess the effectiveness of the AICPA's Peer Review Program and its administering entities in California, the CalCPA, and the NPRC.

i. AICPA

A. AICPA Peer Review Board (PRB)

The AICPA PRB is responsible for maintaining, furthering and governing the activities of the AICPA Peer Review Program, including the issuance of peer review standards, and peer review guidance, while being mindful of the profession's covenant to serve the public interest with integrity and objectivity.

During 2017, PROC members observed each of the open AICPA PRB meetings as part of the PROC oversight activity.

B. AICPA Peer Review Program Annual Report on Oversight

The AICPA Annual Report on Oversight provides a general overview, statistics and information, the results of the various oversight procedures performed on the AICPA Peer Review Program, and concludes on whether the objectives of the oversight process were met.

The AICPA 2017 Annual Report on Oversight for the calendar year 2016 has been substantially delayed due to data extraction issues relating to the new AICPA PRIMA. The PROC will review the report once it becomes available.

C. AICPA PRB Oversight Report Acceptance of CalCPA Peer Review Administration

Biennially, the AICPA PRB's Oversight Task Force (OTF) performs an onsite oversight of CalCPA's administration and report acceptance procedures established by the AICPA Peer Review Program. A member from the AICPA PRB OTF reviews files and interviews staff at the administrative office. In addition the member attends a peer review committee meeting and observes the report acceptance process of the committee members.

At its December 8, 2017 meeting, the PROC reviewed an April 3, 2017 AICPA PRB OTF issued letter of acceptance of procedures and observations conducted as part of the November 16-18, 2016 oversight site visit to the CalCPA. The AICPA PRB OTF attended onsite RAB meetings; met with the Director of Technical Services and Peer Review Managers to review the program's administration; reviewed open files requiring follow-up actions, policies, procedures for granting extensions, timelines of the scheduling process, information dissemination via internet, and noted that all were handled consistent with peer review standards.

The AICPA PRB OTF made recommendations to the CalCPA, who has maintained documentation, to establish appropriate policies and procedures to notify peer reviewers to retain certain peer review documentation prepared during the system and engagement reviews, including a complete list of documents to be retained.

The next oversight site visit to CalCPA performed by the AICPA PRB OTF is scheduled to take place in 2018.

D. AICPA PRIMA

Prior to May 2017, the AICPA managed the peer review program through a computer system known as Peer Review Information System Manager (PRISM), used mainly by the CalCPA to schedule and monitor peer reviews. Licensees and peer reviewers used PRISM as a tracking tool and peer review related documents were submitted outside of the system.

In May 2017 as part of the AICPA six-point plan to enhance audit quality, AICPA launched PRIMA to replace PRISM in an effort to improve audit quality, streamline, and meet the technological or operational needs of the AICPA peer review program and sufficiently respond to changing needs of the accounting industry released.

PRIMA went live in May 2017 as an interactive web interface platform.

PRIMA is used by accounting firms, peer reviewers, state boards of accountancy (to access the Facilitated State Board Access (FSBA)), and AEs to complete the peer review process. It allows users to perform self-service activities including initiating and tracking their peer review schedule, uploading and signing documents, and responding to discrepancies or matters in real-time.

Below are the most significant changes resulting from implementations of PRIMA for firms and peer reviewers:

- Firms and Peer Reviewers receive email notifications to log into PRIMA to view/perform work, letters, etc.
- Firms complete peer review information requests and scheduling information online
- Firms undergoing an engagement review, complete their Engagement Summary Form online (or submit to Review Captain to complete)
- For firms undergoing a system review, their Team Captain enters the population of engagements online (or submit to firm to complete)
- Findings for Further Consideration are completed electronically like Matters for Further Consideration
- A recommended report rating is generated for engagement reviews based upon the number of non-conforming engagements
- Letters to acknowledge corrective actions and implementation plans are “signed” electronically via clicking “Acknowledge” in PRIMA
- Support for corrective actions and implementation plans are sent electronically in PRIMA
- Requests for extensions, year-end changes, enrollment in the AICPA Peer Review Program, and resignations are completed in PRIMA

E. AICPA Educational Framework for Peer Reviewers

The AICPA provided trainings as part of the Enhanced Audit Quality initiative and six-point plan. The plan outlines efforts to enhancing quality of peer reviewers, to promote audit quality and demonstrate the professions ongoing commitment to quality improvement.

The AICPA is seeking to improve the quality of peer reviewers by increasing the qualifications required to perform a review, greatly enhancing the oversight of reviewers, and expediting removal of poor performers. In addition to assessing reviewer performance, the enhanced oversight program includes root cause analysis, determination of quality control policies and procedures with the strongest correlation to audit quality.

Effective May 1, 2016, peer reviewer initial qualification, ongoing qualification, and training for reviews of certain must-select engagement are offered by the AICPA annually.

In order to meet the requirement to possess current knowledge of professional standards applicable to the kind of practice to be reviewed, including quality control and peer review standards, all peer reviewers should obtain at least 40 percent of the AICPA required continuing professional education (CPE) in subjects relating to accounting, auditing, and quality control. Peer reviewers should obtain at least eight hours in any one year and 48 hours every three years.

Individuals wishing to become or remain Team Captains or Review Captains after May 1, 2016 are required to take online peer review curriculum as listed below:

- Initial Training Requirements
  - Complete a series of online peer reviewer curriculum modules, similar to self-study on demand courses and exams designed to meet NASBA's CPE Standards, a peer review curriculum "Becoming an AICPA Peer Review Team or Review Captain"
  - Complete a live seminar course titled, "Becoming an AICPA Peer Review Team Captain: Case Study Application" within 12 months after completion of the peer reviewer curriculum
- Ongoing Training Requirements
  - Option 1 – Attend the General Session of the annual Peer Review Conference
  - Option 2 – Complete the AICPA Peer Review Update on-demand self-study course with final exams designed to meet the NASBA CPE Standards
  - Option 3 – Attend an alternative conference session or complete an alternative course that has been approved by the AICPA PRB
  - Option 4 – Participate in the AICPA Peer Review Update live seminar course, an advanced reviewer training course updated annually to cover changes to peer review guidance
  - Option 5 – Participate in the AICPA Peer Review Advanced Course, a live seminar designed for experienced reviewers
- Must-Select Training Requirements
  - Option 1 – Participate in the relevant optional session of the annual Peer Review Conference
  - Option 2 – Complete the relevant Peer Review Industry Update on-demand self-study courses with final exams designed to meet the NASBA CPE Standards
  - Option 3 – Complete an alternative course of conference session that has been approved by the PRB

F. AICPA Annual Peer Review Conference - Peer Reviewer Training

The AICPA Peer Review Conference was held on August 14-16, 2017 in Nashville, Tennessee and due to the location, PROC members were unable to attend. In 2017, CalCPA offered a peer reviewer training course available to be attended in-person or via webcast on April 24, 2017, which the PROC Chair, Mr. De Lyser attended via webcast. The peer reviewer training course focused on auditing, assurance, and employee benefit plans. Mr. De Lyser reported that the training was helpful for reviewers and their attest work and noted that peer reviewers are now required to update their CPE annually.

ii. CalCPA

A. CalCPA PRC

During 2017, PROC members attended both CalCPA PRC meetings, which took place in May and November 2017.

B. CalCPA Report Acceptance Body (RAB)

The CalCPA holds multiple RAB meetings per year. The RAB meetings generally occur via conference call. RAB members review and present the peer review reports subject to discussion on a general call. PROC members observe how the RAB executes its duties in the meeting to determine whether the peer review process is operating effectively in the state of California.

During 2017, PROC members observed eight RAB meetings.

C. CalCPA Administrative Site Visit Conducted by the CBA PROC

The PROC is charged with conducting, at a minimum, an annual Administrative Site Visit of each Peer Review Program Provider to determine if the provider is administering peer reviews in accordance with the standards adopted by the CBA.

As an administering entity, CalCPA is responsible for administering the AICPA Peer Review Program in compliance with the AICPA Standards, interpretations, and other guidance established by the CBA.

In 2016, the PROC undertook a significant modification of procedures involved in the Administrative Site Visit. The PROC completed a risk assessment of the CalCPA peer review administration to ensure the existing oversight process and checklist continue to work in parallel with the AICPA peer review program. The 2016 risk assessment and checklist reviews resulted in a revised Administrative Site Visit procedure

that included four checklists, to be implemented in five different phases (see section VII.b.ii., Oversight Checklists):

- PROC Administrative Site Visit Work Plan Checklist
- PROC Administrative Site Visit Risk Map and Risk Mitigating Procedures Checklist
- PROC Administrative Site Visit Summary Report
- PROC Summary of Administrative Oversight Checklist

On September 25, 2017, the PROC performed its Administrative Site Visit to CalCPA and reviewed its administration of the AICPA's Peer Review Program. The following procedures were performed as part of the PROC's oversight responsibilities:

- Reviewed existing and new peer reviewers and their qualifications to determine if AICPA's minimum standards are met
- Completed Phase 3 (*see page 13, section VII.b.ii.A., Revisions to PROC Oversight Checklists*) by reviewing all risk variables and examining all mitigating procedures
- Interviewed key CalCPA staff
- Reviewed policies and procedures used by CalCPA to govern its peer review program process
- Read correspondence and other available documentation from other oversight activities performed at CalCPA
- Reviewed a sample of peer review reports and associated files
- Discussed the peer review committee member and individual peer reviewer qualifications process with CalCPA personnel and reviewed a sample for inspection of supporting documentation
- Considered risk mitigating procedures
- Completed PROC Administrative Site Visit Summary Report and Summary of Administrative Oversight Checklist

At its December 8, 2017 meeting, the PROC discussed findings from the 2017 Administrative Site Visit to CalCPA and concluded that the CalCPA, AICPA peer review program met peer review standards adopted by the CBA.

The PROC plans to revisit and re-evaluate the PROC Administrative Site Vist procedures and checklists in 2018. The PROC will consider a two-day site visit, incorporation of recent changes to the peer review process relating to the PRIMA system, and impacts the 2018 AICPA Benchmark Model may have on CalCPA and the CBA peer review program.

D. CalCPA Peer Review Program Annual Report on Oversight

The PROC annually reviews the CalCPA Peer Review Program Annual Report on Oversight report (Report). The Report summarizes the results

of the mandated oversight of two percent of all reviews processed during the year and verification of the resumes and CPE of one third of peer reviewers.

The CalCPA Report for the calendar year 2016 has been substantially delayed due to data extraction issues relating to the new AICPA PRIMA. The PROC will review the report once it becomes available.

iii. NPRC

A. NASBA CAC

The charge of the NASBA CAC is to promote effective oversight of compliance with professional standards by CPAs and their firms. As such, the focus of the NASBA CAC is to recommend a nationwide strategy promoting a mandatory program for compliance assurance acceptable to boards of accountancy. The NASBA CAC provides oversight of the NPRC.

The PROC observed two NASBA CAC meetings held on May 19, 2017 and November 8, 2017.

B. NASBA CAC Report on the AICPA NPRC

To determine if the NASBA CAC is satisfied and can report that the AICPA NPRC has operated appropriately, the PROC annually reviews the NASBA CAC report that covers oral reports provided at each CAC meeting by NASBA representatives serving as members on the AICPA NPRC, the comprehensive oversight report prepared by the AICPA NPRC, and the administrative oversight report issued by a third party.

During its February 3, 2017 meeting, the PROC reviewed the administrative oversight report performed by a third party issued on September 13-14, 2016 covering the AICPA NPRC for the calendar year 2015. The administrative oversight program is designed to provide reasonable assurance that the AICPA peer review program is being administered in accordance with guidance as issued by the AICPA PRB. The report noted that the AICPA NPRC peer reviewer resume information verification process appeared to be in conformity with the AICPA Peer Review Program Oversight Handbook.

The NASBA CAC Report on the AICPA NPRC for the period of November 1, 2015 to October 31, 2016, has been substantially delayed. The PROC will review the report once it becomes available.

iv. Other State Societies

Most California-licensed accounting firms use CalCPA or AICPA NPRC to administer their peer reviews. There are some California-licensed firms that have their peer reviews administered by the AICPA's administering entities other than the CalCPA and the AICPA NPRC, meaning out-of-state CPA societies.

The PROC reviews, on a sample basis, the AICPA oversight visit reports as part of the oversight activity of out-of-state administrative entities each year. All AICPA oversight visit reports were reviewed and accepted by the AICPA PRB OTF.

For 2017, the PROC reviewed the AICPA's oversight reports for five AEs, a total of ten states including: Nevada, which administers Nevada, Utah, Wyoming, and Nebraska; New Jersey; Florida; Texas; and the CalCPA which administers Alaska, Arizona, and California. The oversight reports concluded with no findings for the New Jersey, Florida, Texas, and California. There were eight findings identified in the AICPA oversight report for Nevada.

The PROC discussed about possibly revising procedures on how to perform future oversight activities on out-of-state AEs found not adhering to professional standards set by AICPA, as there are potentially negative impacts to the CBA's mobility program.

The PROC has expressed a need to monitor AEs that received findings in the AICPA report. The PROC is working on developing a framework that would include communication with AICPA and monitoring of subsequent AICPA oversight reports to ensure remedial actions are taken to address findings.

b. Administrative Functions

i. PROC Committee Meetings

The PROC holds meetings as necessary in order to conduct business and report to the CBA regarding the effectiveness of mandatory peer review.

The PROC held the following meetings:

- February 3, 2017 – Sacramento, CA
- May 5, 2017 – Burbank, CA
- August 25, 2017 – Sacramento, CA (Cancelled)
- December 8, 2017 – Sacramento, CA

A representative of the PROC attended five CBA meetings and reported on PROC activities.

ii. PROC Oversight Checklists

The PROC has developed oversight checklists which serve to document the members' findings and conclusions after performing specific oversight activities. The checklists, listed herein, are included in the PROC Manual and additional checklists will be developed as necessary. Members submit the completed checklists to staff to document PROC oversight activities.
Present Checklists:

- Summary of Peer Review Committee Meeting
- Summary of Peer Review Subcommittee Meeting
- Summary of Administrative Site Visit
- Summary of Peer Reviewer Training Course
- Peer Review Board Meeting Checklist
- Peer Review Program Provider Checklist
- Summary of Oversight of Out-of-State Peer Review Administering Entity
- Summary of Compliance Assurance Committee Meeting

A. Revisions to PROC Oversight Checklists

The PROC established a standing agenda item for its meetings to allow opportunities to review existing PROC checklists. In 2016, the PROC reviewed and updated all of the PROC checklists to ensure completeness and relevance with the continuously evolving peer review program.

During 2017, the PROC continued its efforts to review and revise the PROC's checklists. The PROC applied the revised checklists, including the revised PROC Administrative Site Visit procedures and checklists.

Prior to revisions, the Administrative Site Visit activity included a singular checklist of expectations to be met. The PROC found that the single checklist alone was not sufficient nor comprehensive and did not provide guidelines or standards to properly assess the Administrative Site Visit. The revised Administrative Site Visit activity includes four checklists required to be implemented in five different phases. The four checklists are as follows:

- PROC Administrative Site Visit Work Plan Checklist
  – An overall planning checklist for the entirety of the site visit activity, which provides the necessary steps to plan for the site visit, how to apply and execute practical tests, and an opportunity to bring forth findings

- PROC Administrative Site Visit Risk Map and Risk Mitigating Procedures Checklist
  – An itemized list of executable procedures to reference and determine whether the risk mitigating procedures set in-place by the AE

functions are as intended

- PROC Administrative Site Visit Summary Report
  – A summary report of the Administrative Site Visit, allowing the PROC to narrate the scope and purpose of the visit, the activities performed as part of the oversight, and conclude all findings

- PROC Summary of Administrative Oversight Checklist
  – A revised PROC Administrative Site Visit Checklist, allows the PROC to verify that all necessary oversight activities were completed, determine if the AE is administering peer reviews in accordance to standards adopted by the CBA, and provide a summary report to the CBA

As previously mentioned, the Administrative Site Visit is implemented in five phases annually in order to ensure key deadlines are met and for inclusion in the PROC Annual Report. The phases are as follows:

Phase 1: Assignment of the two-person administrative site visit team (**May**)

Phase 2: Period for sending initial contact letter to the AE confirming arrangements of the oversight visit and requesting documents and information necessary to effectively complete the risk assessment (**May/June**)

Phase 3: Placing on the PROC agenda an item soliciting input from the PROC on risks and associated testing (**August**)

Phase 4: General period during which to conduct the administrative site visit (**September/October**)

Phase 5: Time period for the two-person administrative site visit team to submit the Peer Review Oversight Committee Administrative Site Visit Summary Report and Administrative Site Visit Summary Checklist (**October/November**)

iii. Approval of Board-Recognized Peer Review Program Providers

At such time that the CBA receives an Application to Become a CBA-recognized Peer Review Program Provider, the PROC will review the application and documentation using the Peer Review Program Provider Checklist and determine if the program meets the requirements outlined in, CCR section 48. Based on the review, the PROC will provide a recommendation to the CBA that the application be approved or denied.

iv. Withdrawal of Board Recognition of a Peer Review Program Provider

The PROC has not made any recommendations to the CBA concerning the withdrawal of CBA recognition of a peer review program provider.

c. Other Activities

i. AICPA Proposed Evolution of Peer Review Administration

In February 2016, the AICPA released a paper titled, *Proposed Evolution of Peer Review Administration* (Paper). The Paper advocated plans to increase audit quality, consistency, efficiency, and effectiveness within the peer review administration.

The AICPA went on to issue multiple iterations of the Paper, with a continued focus on the reduction of AEs and increasing of audit quality. AICPA released the following additional papers:

- On July 18, 2016, AICPA released a secondary follow-up paper to supplement the discussion on the reduction of AEs and sought input from state boards of accountancy.

- On January 4, 2017, AICPA released a revised discussion paper titled, *Proposed Evolution of Peer Review Administration,* revised January 2017, with a feedback deadline scheduled for June 30, 2017. The discussion paper proposed a benchmark model for AEs to increase transparency of AE performance.

With each iteration, the AICPA received comment letters from stakeholders such as NASBA and state societies including California, New York, Virginia, and Florida.

In an effort to fully evaluate the proposed changes to the peer review program, the PROC reviewed and revisited prior AICPA papers along with all publicly available comment letters during the following PROC meetings:

- August 19, 2016
- February 13, 2017
- May 5, 2017

The PROC reported its findings at the CBA's September 15-16, 2016 and July 20-21, 2017 meetings, which subsequently resulted in adoption of letters that conveyed the CBA's support of those efforts undertaken by the AICPA to enhance the effectiveness, consistency, and quality of peer reviews along with expressed concerns regarding potential increase in the cost of peer review and the peer reviewer population.

On August 31, 2017, AICPA published a paper titled, *Evolving Peer Review Administration to Enhance Audit Quality.* Similar to the AICPA January 4, 2017 revision paper, it outlined the new enhanced model for the peer review administration, with a focus on required benchmarks for AEs to meet, and is scheduled to take effect at the beginning of 2018.

The new enhanced Benchmark Model for the peer review administration subject AEs to meet benchmarks that are qualitative, objective, and have measurable criteria along with consistency. Failure to meet the established benchmarks will require a fair procedure to determine the appropriate remediation, and may result in being placed on probation or loss of qualification to be an AE.

The Benchmark Model includes:

- Benchmarks and Familiarity Mitigation
- Benchmark Violations and Fair Procedures
- AE Staffing Requirements
- Oversight and State Board Relations
- Discontinuing Program Administration

During the December 8, 2017 PROC meeting, the committee decided it will evaluate and initiate incorporating the AICPA Benchmark Model for AEs in future PROC oversight activities. The integration of the benchmarks will take place in future PROC meetings.

ii. California Peer Review Program Flowchart

At the May 5, 2017 PROC meeting, the PROC requested the development of a flowchart to depict and provide information on the recent changes to the AICPA Peer Review Program and how PRIMA works in parallel.

Staff developed the draft California Peer Review Program Flowchart (Flowchart) to mirror the AICPA PRIMA training documents currently available online in efforts to align the information distributed across the nation regarding how the AICPA peer review program functions.

Below is an outline of the peer review processes covered within the Flowchart:

Step 1: Peer Review Information
Step 2: Peer Review Scheduling
Step 3: Peer Review Process
Step 4: Peer Review Committee Acceptance Review
Step 5: Decision
Step 6: Corrective Action(s) and/or Implementation Plan

The Flowchart was reviewed during the PROC December 8, 2017 meeting and subsequently examined by CalCPA for presentation.

iii. Oversight of Peer Review-Related Updates

In 2017, the PROC continued its regular review of all peer review-related updates available on the AICPA and NASBA websites in an effort to ensure the PROC members are continuously aware of changes relating to the peer review program.

iv. Revisions to the PROC Procedures Manual

The PROC derives its authority from BPC section 5076.1. The purpose of the PROC is to provide recommendations to the CBA on any matter upon which it is authorized to act to ensure the effectiveness of mandatory peer review. The PROC Manual outlines the PROC's authority, purpose, roles and responsibilities, oversight activities, and overall expectations to effectively oversight the peer review program to ensure administration is performed in accordance with the standards adopted by the CBA, as specified under section III. PROC Responsibilities herein this report.

During its December 8, 2017 meeting, the PROC reviewed and adopted proposed revisions to the PROC Manual. The revisions reflected:

- Recent evolution of the peer review program
- PROC oversight activities
- Update the California Peer Review Program Flowchart
- Revised qualifications criteria for PROC membership

VIII. Statistics

a. Statistical Monitoring and Reporting Activity

At its August 19, 2016 meeting, the PROC discussed the possibility of enhancing the statistics reported within the PROC Annual Report and requested that an agenda item be added to allow members the opportunity to discuss peer review-related statistics as defined in Section IV.A.7 of the PROC Manual, which includes a list of data points to monitor and report on a regular basis in a mutually agreed upon format. The data points are as follows:

- Types (system vs. engagement) and numbers of reviews in process
- Types (system vs. engagement) and numbers of reviews completed by month, and cumulatively for the annual reporting period
- Types (system vs. engagement) and numbers of reviews receiving a pass, pass with deficiencies, or fail rating
- Extensions requested and status (granted, denied, and completed)

- Corrective action matters (various types: overdue peer review reports, disagreements pending resolution, etc.)
- Delinquent reviews
- Firms expelled (dropped) from the program

Staff identified the following three areas where no statistical information is currently available and will be set aside for future monitoring upon when they become available:

- Types and numbers of reviews in process
- Extensions requested and status
- Delinquent reviews

The PROC asked that staff provide statistical updates twice annually, once prior to the Administrative Site Visit to CalCPA and a final report to consider for the PROC annual report. The peer review-related statistical information provided below were reviewed at the May and December 2017 PROC meetings:

Types (system vs. engagement) and numbers of reviews completed by month, and cumulatively for the annual reporting period

i. Numbers of reviews completed by month.

Source: AICPA FSBA Website

Comments: **Table 1 – The FSBA Reviews Accepted Report**
Provides the number of both system and engagement reviews accepted on a monthly basis starting from January 1, 2013 to December 31, 2016 and includes accounting firms that chose to Opt out of the FSBA.

Table 1:

California | The FSBA Reviews Accepted Report				
MONTHS	**2013**	**2014**	**2015**	**2016**
January	261	145	148	161
February	168	110	196	159
March	90	138	120	135
April	111	138	149	120
May	170	145	133	111
June	168	132	147	139
July	137	161	117	84
August	106	124	107	94
September	172	161	131	134
October	117	137	153	87
November	85	129	95	87
December	117	137	104	111
TOTAL	**1,702**	**1,657**	**1,600**	**1,422**

- Average number of reviews completed in California annually: 1,595
- A decrease in the peer reviewer population directly correlates with the decrease in the number of peer reviews accepted

ii. Types (system vs. engagement) and numbers of reviews completed cumulatively for the annual reporting period

Source: CalCPA Peer Review Program Annual Report on Oversight (Report).

Comments: **Table 2 –** Uses numbers reported in the CalCPA Reports issued in 2014, 2015, 2016, and 2017, each report reflects numbers from the prior year, under **section IV, Results of Peer Reviews Performed.** The numbers reported by CalCPA includes statistics generated annually from January through October.

The current year numbers provided by CalCPA were reported as of October 19, 2017 and does not include firms that opted out of FSBA and peer reviews accepted by the NPRC or out-of-state administering entities.

Table 2:

California | Peer Reviews Performed During the Calendar years 2013-2016 by Types and Report Rating				
Type of Review	**2013**	**2014**	**2015**	**2016**
System	507	582	532	464
Engagement	1,102	1,077	1,022	938
Total	**1,609**	**1,659**	**1,554**	**1,402**

Types (system vs. engagement) and numbers of reviews receiving a pass, pass with deficiencies, or fail rating

Source: CalCPA Report

Comments: **Table 3 –** Uses numbers reported in the CalCPA Reports issued in 2014, 2015, 2016, and 2017, each report reflects numbers from the prior year, under **section IV, Results of Peer Reviews Performed by Type of Peer Review and Reporting and Rating Issued**. The numbers reported by CalCPA includes statistics generated annually from January through October.

The current year numbers provided by CalCPA were reported as of October 19, 2017 and does not include firms that opted out of FSBA and peer reviews accepted by the NPRC or out-of-

state administering entities.

Provides in percentage the relative changes between the numbers of reviews versus engagements performed during the calendar years 2013 through 2016.

Table 4 – Using numbers from **Table 3**, it indicates relative changes in percentage for the total reporting grades, including both system and engagement reviews performed during the calendar years 2013 through 2016.

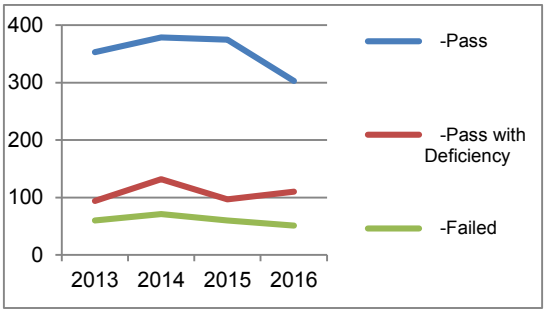
Table 3:

California | Reviews Performed by Type of Peer Review and Reporting and Rating Issued								
Review Types	**2013**		**2014**		**2015**		**2016**	
SYSTEM REVIEWS	**QTY**	**%**	**QTY**	**%**	**QTY**	**%**	**QTY**	**%**
Pass	353	70%	379	65%	375	70%	303	65%
Pass with Deficiency	94	18%	132	23%	97	18%	110	24%
Failed	60	12%	71	12%	60	12%	51	11%
Total System	507		582		532		464	
ENGAGEMENT REVIEWS								
Pass	773	70%	870	81%	885	86%	720	77%
Pass with Deficiency	218	20%	142	13%	80	8%	110	12%
Failed	111	10%	65	6%	57	6%	108	11%
Total Engagement	1,102		1,077		1,022		938	
Summary Total	**1,609**		**1,659**		**1,554**		**1,402**	

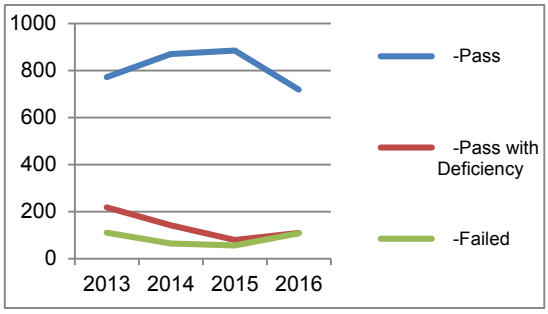
Table 4:

California | Reviews Performed by Type of Peer Review and Reporting and Rating Issued								
Report Ratings	**2013**		**2014**		**2015**		**2016**	
Systems/Engagements	**QTY**	**%**	**QTY**	**%**	**QTY**	**%**	**QTY**	**%**
Pass	1,126	70%	1,249	75%	1,260	81%	1,023	73%
Pass with Deficiency	312	19%	274	17%	177	11%	220	16%
Failed	171	11%	136	8%	117	8%	159	11%
Summary Total	**1,609**		**1,659**		**1,554**		**1,402**	

Graph 3.a - System Reviews



Graph 3.b - Engagement Reviews



Corrective action matters (various types: overdue peer review reports, disagreements pending resolution, etc.)

Source: CalCPA Report

Comments: **Table 5 –** Uses numbers reported in the CalCPA Reports issued in 2014, 2015, 2016, and 2017, each report reflects numbers from the prior year, under **section VII. Summary of Required Follow-up Actions,** with prior year numbers and identifies the types of follow-up actions that have been required. The numbers reported by CalCPA includes statistics generated annually from January through October.

The PRC is authorized by the AICPA Peer Review Program Standards to decide on the need for and nature of any additional follow-up actions required as a condition of acceptance of the firm's peer review. During the report acceptance process, the PRC evaluates the need for follow-up actions based on the nature, significance, pattern, and pervasiveness of engagement deficiencies. The PRC also considers the comments noted by the reviewer and the firm's response thereto. If the firm's response contains remedial actions which are comprehensive, genuine, and feasible, then the committee may decide to not recommend further follow-up actions. Follow-up actions are remedial and educational in nature and are imposed in an attempt to strengthen the performance of the firm. A review can have multiple follow-up actions.

Table 5:

California | Summary of Required Follow-up Actions Under AICPA and CalCPA Peer Review Program				
Type of Follow-up Action	**2013**	**2014**	**2015**	**2016**
Submit proof of CPE taken	355	240	160	235
Submit copy of monitoring report	22	32	25	4
Submit to Team Captain (TC) revisit-general	32	27	29	24
Submit to TC review of sub engagements with work papers	63	70	73	91
No longer perform any audit engagements	30	48	40	31
Totals	**502**	**417**	**327**	**385**

Firms expelled (dropped) from the program

Source: AICPA FSBA Website

Comments: **Table 6 –** Uses numbers from the March 20, 2017 FSBA report regarding the number of firms dropped between January 1, 2013 to December 31, 2016**:**

Table 6:

FSBA Dropped and Terminated Firms					
ACTION	**2013**	**2014**	**2015**	**2016**	**TOTAL**
DROPPED	63	97	52	92	371

b. Peer Reviewer Population

During the March 2016 CBA meeting, the PROC was tasked to follow-up on issues relating to peer reviewer population. The PROC discussed the peer reviewer population during its August 19, 2016 and December 8, 2016 meetings, and determined that a letter of inquiry regarding existing peer reviewer population should be sent to AICPA and CalCPA to determine if statistics and oversight framework to evaluate the peer reviewer population existed.

During its May 5, 2017 meeting, the PROC reviewed and approved a letter of inquiry to the AICPA and CalCPA regarding peer reviewer population. The CBA approved the letter at its May 18-19, 2017 meeting, and the letter was sent to AICPA and CalCPA on May 31, 2017.

In response to the PROC May 31, 2017 letter of inquiry regarding peer reviewer population statistics, written responses were received from James W. Brackens,

CPA, CGMA, Vice-President of Ethics and Practice Quality at AICPA, on July 10, 2017 and from Linda McCrone, CPA, CalCPA Technical Division Director, on July 26, 2017.

Upon review of AICPA and CalCPA's responses, the CBA approved a follow-up letter signed by CBA Immediate Past President, Alicia Berhow at the September 14-15, 2017 CBA meeting. The letter was sent on September 25, 2017 requesting clarification regarding peer reviewer population statistics in California.

In response to the CBA September 25, 2017 follow-up letter to AICPA and CalCPA regarding peer reviewer population, written responses were received from Mr. Brackens, on October 30, 2017 and Ms. McCrone, on October 30, 2017.

The PROC and CBA staff reviewed all written responses from AICPA and CalCPA regarding the peer reviewer population and have determined that the responses received did not provide sufficient information to effectively assess the present state of the peer reviewer population in California. The PROC continues to have concerns relating to the following key elements within responses received from AICPA and CalCPA:

- Aging Peer Reviewer Population:
  - No identification of benchmarks to determine an "appropriate ratio of enrolled firms to active peer reviewers"
  - The national ratio of enrolled firms to active reviewers was approximately 15 to 1
  - AICPA focuses on geographic areas where ratio of enrolled firms to peer reviewers are lower than the national norm of 15 to 1
  - California's ratio of enrolled firms to active reviewers was approximately 30 to 1, double the national ratio
  - The AICPA's Peer Review Customer Satisfaction Survey was anonymous and will not provide clarity on what makes up 60 percent of peer reviewers intending to retire before 2020
  - AICPA noted that 30 percent of total number of peer reviewer population were considered "high volume reviewers" as they perform 80 percent of the peer reviews nationally

- Specialized Industries:
  - AICPA currently does not track or maintain statistical information that identifies the number of peer reviewers performing engagement reviews, system reviews, system reviews under must-select, i.e., Employee Retirement Income Security Act of 1997 (ERISA) or single audits
  - CalCPA noted that the CBA should distinguish the difference between system reviews and engagement reviews, as system reviews require more time and resources, and that the population of peer reviewers performing

system reviews may be of concern

During the December 8, 2017 PROC meeting, the PROC decided to propose an initial peer reviewer population monitoring framework, as seen below, along with a draft letter addressed to AICPA and CalCPA which will be presented at the January 18, 2018 CBA meeting.

The letter to AICPA and CalCPA proposes collaboration with the CBA's PROC in the development of a data collection framework to effectively assess the California peer reviewer population statistics, especially pertaining to reviews in must-select industries:

- Number of individuals performing peer reviews
- Number of peer reviews performed by each peer reviewer
- Number of peer reviews performed by peer reviewers in specialized industries
- Number of individuals added to the peer review population over the past year
- Number of individuals who ceased performing peer reviews over the last year
- Number of individuals intending to cease performing peer reviews over the next three years

IX. Observations

Based on PROC members' 2017 oversight actions and attendance at the various peer review bodies' meetings cited in this report, the PROC offers the following findings to the CBA.

AICPA

The PROC found the AICPA PRB to give ample consideration to the quality of the profession, and exhibit a high level of technical knowledge and diligence in striving to improve the quality of the peer review program and peer reviewers through their handling of a variety of issues that the program faces. The PROC found the agenda items for the meetings to be relevant and appropriate, and that the AICPA PRB members execute their duties in a knowledgeable and professional manner understanding the importance of the peer review program to the accounting profession and the public that it serves.

CalCPA

Through participation in PRC and RAB meetings, and the Administrative Site Visits, the PROC found the CalCPA to give ample consideration to the quality of the profession, and exhibit a high level of technical knowledge and diligence in striving to improve the quality of the peer review program and peer reviewers through their handling of a variety of issues that the program faces. The PROC found the agenda items for the meetings to be relevant and appropriate, and the CalCPA to execute their duties in a knowledgeable and professional manner understanding the importance of the peer review program to the accounting profession and the public

that it serves.

NPRC

Through the participation in the CAC meetings, who oversights the NPRC, the PROC found nothing that suggested that the NPRC did not meet standards established by the AICPA.

X. Conclusion

Based on its oversight activities, the PROC concluded that the AICPA Peer Review Program, including its administering entities, CalCPA and NPRC, function effectively in accordance to standards adopted by the CBA.