

HOUSE BILL REPORT

HB 1597

As Reported by House Committee On:
Commerce & Labor
Appropriations

Title: An act relating to the public accountancy act.

Brief Description: Changing the public accountancy act.

Sponsors: Representatives Conway (co-prime sponsor), Clements (co-prime sponsor), Wood and B. Chandler .

Brief History:

Committee Activity:

Commerce & Labor: 2/21/01, 2/26/01 [DPS];

Appropriations: 3/6/01, 3/8/01 [DP2S(w/o sub CL)].

Brief Summary of Second Substitute Bill

- Revises regulation of certified public accountants, including phasing out the issuance of new CPA certificates in favor of licensing only, but allowing certificate holders as of June 30, 2001, to renew their certificates as "inactive certificates."
- Changes the definition of "reports on financial statements" to exclude services that non-licensees are permitted to provide.
- Requires a majority of owners of CPA firms to be licensed persons, and allows certain out-of-state licensees to practice in Washington without a Washington license.
- Grants authority to the board to provide consumer protection and alerts, and to investigate Washington licensees when a complaint is made by the board of accountancy of another state.

HOUSE COMMITTEE ON COMMERCE & LABOR

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 8 members: Representatives Clements, Republican Co-Chair; Conway,

Democratic Co-Chair; B. Chandler, Republican Vice Chair; Wood, Democratic Vice Chair; Hunt, Kenney, Lisk and McMorris.

Staff: Chris Cordes (786-7103).

Background:

The Board of Accountancy administers a licensing program for persons and firms that engage in the practice of public accounting. Generally, public accounting involves the use of accounting or auditing skills and includes such services as reporting on financial statements, performing tax planning or preparing tax returns, and providing management advisory or consulting services.

A licensed certified public accountant (CPA) may practice public accounting only in a licensed CPA firm. A person holding a valid CPA certificate, but not a license, may use the CPA designation as long as he or she meets certain conditions and does not hold himself or herself out as practicing public accounting.

Board membership. The board has seven members appointed by the Governor: four members must hold valid CPA certificates and must have been in public practice for at least 10 years; two members must have held valid CPA certificates for a least 10 years; and one member must represent the public. The executive director is also appointed by the Governor and must hold a certificate.

Board duties. As part of administering the licensing program, the board administers the CPA examination at least twice a year, issues certificates and licenses, investigates complaints, and sets fees to cover the cost of the program.

Certification and licensing. CPA certificates are issued to persons who meet specified requirements, including good character, and educational and examination requirements. The board may waive the education requirements for certain qualified persons.

Individuals and firms that wish to practice public accounting must obtain a license. For individuals to be eligible for a license, the individual must be certified, must maintain the required continuing professional education, and must have at least one year of experience. Under board rules, this experience must consist of 2,000 hours under the direct supervision of a licensed CPA actively engaged in public accounting. The experience must require the exercise of independent judgment and involve such services as accounting and auditing, issuance of reports on financial statements, and preparation of tax returns. The firm must participate in a board-approved peer or quality review program, or be a commercial or government organization that has filed a sponsorship agreement.

For a firm to be eligible for a license, the principal purpose of the firm must be to

furnish public accounting services, and certain members of the firm must be licensed. Only persons licensed in Washington or another state may hold corporate stock in a CPA corporation. Each office of the firm must be registered.

Certificates, licenses, and registrations are renewed every three years, subject to maintaining specified requirements.

Out-of-state CPAs are permitted to practice temporarily in Washington on business incidental to a regular practice. By rule, these CPAs may not maintain an office in Washington, advertise in Washington, or collect more than 10 percent of gross annual billings from Washington clients.

Washington certificates or licenses are issued to CPAs with an out-of-state certificate or license that permits the practice of public accountancy in the other state if the other state grants reciprocity to Washington CPAs with certificates or licenses.

Disciplinary actions. The board may take action for various causes, including if there is fraud in obtaining a certificate or license or in representing oneself as a CPA, a conviction of a crime, or failure to maintain requirements for certification or licensing.

Penalties. The board may revoke, suspend, or not renew a certificate or license or impose a \$1,000 fine and investigation and legal costs for violations of the CPA licensing law. If the board has reason to believe a person is violating the CPA licensing law, it must certify the facts to the prosecuting attorney. A violation of the CPA licensing law is also a misdemeanor subject to a maximum fine of \$1,000 or imprisonment up to six months, or both.

Summary of Substitute Bill:

Board membership. Beginning June 30, 2001, the Board of Accountancy membership is increased from seven to nine members by adding two members representing the public, including one member qualified to represent the interests of clients of licensees.

The executive director of the board must be a licensed CPA.

Board duties. A requirement is added for the board to publish consumer alerts and public protection information regarding violations of the CPA licensing law.

The requirement for the board to administer examinations twice a year is deleted, along with the detailed provisions regarding the exam structure. The board is required to transition to a new exam structure or media for administering the exam.

Certification and licensing. Beginning July 1, 2001, no new certificates as a CPA will be

issued. Licenses to practice public accounting will be issued under the criteria currently applying to certification as a CPA, except that the board may no longer waive the education requirement for becoming a licensee. Specific competency and experience requirements are added, including a requirement for one year of experience gained through the use of various accounting skills while employed in government, industry, or public practice.

A CPA holding a certificate on June 30, 2001, will be able to continue holding the certificate if he or she maintains continuing professional education requirements and does not practice public accounting. A CPA holding a certificate who wishes to practice public accounting must transition to a license. If the application for a license is made by June 30, 2004, the CPA must have one year of experience in accounting, meet competency requirements, and have completed required continuing professional education. The experience may be gained at any time and must be gained through use of certain skills including accounting, issuing reports or financial statements, or tax or financial advisory skills. After June 30, 2004, current certificate holders will be subject to the requirement that the one year of experience be gained in the prior eight years.

Licensing for firms is modified to:

- delete the requirement that the principal purpose of the firm be to furnish services consistent with the CPA licensing law;
- add a requirement that a majority of firm owners must be natural persons who are licensees in Washington or another state and to delete the prohibition against nonlicensees holding stock interests in a CPA corporation. Nonlicensed owners of firms must be natural persons and be active participants in the firm. They are subject to the board's discipline and, for resident nonlicensees, to the board's ethics CPE requirements; and
- require a licensed firm to meet competency standards established by the board.

A licensed firm that falls out of compliance with firm ownership requirements must take corrective action in a reasonable period of time as determined by the board.

For an applicant licensed in another state or country to be issued a license under the reciprocity provisions, the applicant must meet Washington's "good character" requirements. The licensee must notify the board in 30 days if the out-of-state license has lapsed or become invalid.

The provision allowing "incidental" practice by an out-of-state CPA is deleted. The board may allow an out-of-state licensed individual CPA (with a principal place of business in another state) with substantially equivalent education, examination, and experience, or from a state with substantially equivalent standards, to have license privileges without the need to obtain a license. These individuals must notify the board of their intent to enter Washington and are subject to jurisdiction and discipline in Washington.

The board may accept the designation of "substantial equivalency" to national standards made by the National Association of State Boards of Accountancy.

Disciplinary actions. The board is given additional authority to take action:

- against a nonlicensee owner who commits fraud or dishonesty while representing himself or herself as holding an interest in a licensed firm;
- for failure of a nonlicensee owner to comply with statute or rules; and
- for failure to comply with board orders.

A Washington licensee who uses its CPA title or provides services in another state is subject to discipline in Washington for an act committed in the other state if the licensee would be subject to discipline in the other state. The board is required to investigate complaints made by the board of another state.

Penalties. The maximum civil fine for violations of the CPA licensing law is increased from \$1,000 to \$10,000. The board may order full restitution to injured parties. The board may take action against a firm's license for a nonlicensee owner's failure to comply with the CPA licensing law or rules. The board is permitted to enter into stipulated agreements with first time violators and is not required to certify these to the prosecuting attorney.

The maximum fine for a misdemeanor violation is increased from \$1,000 to \$10,000. A new felony crime is added, punishable by a maximum fine of \$10,000 or imprisonment for up to two years, or both, for using a professional CPA title intended to deceive the public after entering into a stipulated agreement with the board.

Substitute Bill Compared to Original Bill:

The substitute bill: (1) deletes references to an "inactive certificate" status. Instead, new certificates will not be issued after June 30, 2001, and current certificate holders who wish to practice public accounting will be required to transition to a license. These CPAs will have three years to obtain a license on showing that they have one year of relevant experience and have completed the required continuing professional education. After the three year window, these CPAs must meet the one-year experience requirement within the previous eight years; (2) adds that a licensed CPA firm that falls out of compliance with the new ownership requirements must immediately take corrective action within the time period set by the Board of Accountancy; (3) deletes the current authority for "incidental" practice privilege and the original bill's provisions allowing the board to grant a three-year license to certain out-of-state CPAs. Instead, the board will allow an out-of-state licensee to practice public accounting in Washington without a need to obtain a license if the licensee has a principal place of business in another state and meets "substantially equivalent" requirements. These CPAs must notify the board of their intent to enter Washington and are subject to the board's jurisdiction and discipline; (4) adds that a Washington licensee who uses the "CPA" title or practices in another state is

subject to discipline in Washington for an act committed in the other state if the licensee would be subject to discipline in the other state. The board must investigate complaints from the board of another state; (5) increases the maximum misdemeanor fine for a violation of the accountancy law to \$10,000; and (6) makes various technical changes.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Substitute Bill: Ninety days after adjournment of session in which bill is passed.

Testimony For: (Original bill) The purpose of this bill is to bring Washington law into line with the Uniform Accountancy Act. Although this bill is everyone's best effort to reach that goal, there are several issues that continue to need work, including how to define "equivalency" and providing for nonlicensees to have an ownership interest in CPA firms. But overall, the bill gives the board needed authority to deal with those who are not currently regulated, but who are really practicing public accounting. Moving to the model act will also allow a seamless practice between states, something that is a necessity given the way national and international companies are doing business. These companies need services that require skill sets beyond the traditional CPA expertise. To do this work, CPA firms need to attract high level associates with this non-accounting expertise and allowing these associates to have an ownership interest in the firm is one means of do this. The bill includes protections by requiring nonlicensee owners to be humans (not companies) and be actively involved in the CPA firm.

(Concerns) The bill contains some ambiguities regarding the status of certificate holders. The bill also includes new provisions on public protection that may be expensive, such as providing consumer alerts and following activities of Washington licensees in other states.

Testimony Against: This bill should not be hurried to enactment since there is no emergency requiring action this year and further study is needed. The bill might be interpreted to add new restrictions on the issuance of financial statements; these must be thought through carefully or small businesses may be adversely impacted by the need to hire new accountants. Other public interest concerns are not worked out, including the major issue of relaxing of rules on ownership of CPA firms. There may be an erosion of public confidence if CPAs are no longer viewed as independent auditors. This bill is really about expanding into new markets and increasing revenues.

Testified: (In support) Jim Boldt and Bea Naon, Washington Society of Certified Public Accountants; and Bob Underhill, Arthur Anderson.

(In support of concept, with concerns) Laurie Tish, State Board of Accountancy.

(Opposed) Carl Warren, Washington Association of Accountants and Washington State Society of Enrolled Agents; Dick Thompson; Gary Smith, Independent Business Association; Scott Salsbery; and Jim Hudspeth.

HOUSE COMMITTEE ON APPROPRIATIONS

Majority Report: The second substitute bill be substituted therefor and the second substitute bill do pass and do not pass the substitute bill by Committee on Commerce & Labor. Signed by 27 members: Representatives Sehlin, Republican Co-Chair; H. Sommers, Democratic Co-Chair; Barlean, Republican Vice Chair; Lisk, Republican Vice Chair; Alexander, Benson, Buck, Clements, Cody, Cox, Dunshee, Fromhold, Gombosky, Grant, Kagi, Keiser, Kenney, Linville, Mastin, Mulliken, Pearson, Pflug, Ruderman, D. Schmidt, Schual-Berke, Talcott and Tokuda.

Minority Report: Without recommendation. Signed by 4 members: Representatives Doumit, Democratic Vice Chair; Boldt, Kessler and Lambert.

Staff: Patricia Linehan (786-7178).

Summary of Recommendation of Committee On Appropriations Compared to Recommendation of Committee On Commerce & Labor:

The second substitute bill allows certificate holders, as of June 30, 2001, to continue to renew their certificates, but upon first renewal, requires them to use the term "inactive" when referring to their certificate, or when using their title. It grants authority to, rather than requiring, the board to provide consumer protection and alerts, and to investigate Washington licensees when a complaint is made by the board of accountancy of another state. The definition of "reports on financial statements" is changed to exclude services that non-licensees are permitted to provide. The bill also adds a definition of "natural person" to mean a living human being, makes numerous technical changes.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Second Substitute Bill: This bill contains an emergency clause and takes effect on July 1, 2001.

Testimony For: There are policy issues that are still being worked on and the fiscal note, as provided for the original version, doesn't reflect the fiscal impact of the most current version of this legislation. The change from mandatory to discretionary, for the board to pursue complaints for activities outside of Washington, will reduce the enforcement activities and reduce the fiscal impact of those activities.

Other issues that should be addressed in the fiscal note are the number of people who currently hold a certificate who will choose to become licensed, non-CPAs who will need to pay fees to license their CPA firms, and out of state CPAs who will need to register in Washington.

Testimony Against: There are significant policy issues that still need to be addressed in this legislation and the fiscal note will be affected by the policy decisions. The legislation, as currently written, will have a negative fiscal impact on people. Small businesses, who employ accountants that are not licensed, won't be able to continue using those accountants.

Testified: (In support) Representative Jim Clements, co-prime sponsor; and Jim Boldt, Washington Society of Certified Public Accountants.

(Opposed, substitute bill) Gary Smith, Executive Director, Independent Business Association.