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PCPS achievements & prospects : report

Special Committee to Study the Objectives, Policies, and Procedures of the Private Companies Practice Section

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may 1984

pcps

achievements & prospects

*report of the
special committee
to study the objectives,
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of the private companies
practice section*

AICPA American Institute of Certified Public Accountants

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***report of the
special committee
to study the objectives,
policies, and procedures
of the private companies
practice section***

Special Committee to Study the Objectives, Policies, and Procedures of the PCPS

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Richard C. Rea, who was also appointed to the committee, was unable to participate directly in its deliberations because of illness. However, Mr. Rea maintained an active interest in the committee's proceedings. He received and reviewed all material, including drafts of the report, considered by the committee and conveyed his views and comments for the committee's consideration.

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Foreword

This report is an evaluation of the achievements of the Private Companies Practice Section (PCPS) of the Division for CPA Firms during its first five years and presents a program to aid its future growth. The PCPS is a vital element of the profession's voluntary quality assurance program for CPA firms, an unprecedented program of self-regulation by a profession highly conscious of its public obligations. The section's ability to attract as members a significant proportion of AICPA members practicing in local firms, including sole practitioners, is vital to its future prospects and effectiveness.

The report is the product of a special committee appointed early in 1983 to review the objectives, organizational structure, and functions of the PCPS and to determine whether the objectives and programs of the PCPS are appropriately responsive to the needs of AICPA members serving private company clients. The committee completed the portion of the report containing its recommendation to aid the future growth of the PCPS in late 1983 and presented its findings as an interim report to the AICPA Board of Directors and Council and to the PCPS Executive and Peer Review Committees. Subsequently, the committee prepared an addendum to its report to identify some problems relating to the structure of the division and to suggest some solutions to those problems.

The PCPS Executive Committee accepted the recommendations in the interim report and, as indicated in the letter from the chairman of that committee published with this report (Appendix B), has begun to implement the recommendations. The implementation of the recommendations will, we believe, make the PCPS relevant and attractive to more firms and increase its reach and effectiveness. Firms that have not yet joined the division are invited to consider the report and the benefits of membership in the division for the firm, the profession, and the public.

The committee, under the able leadership of A. Marvin Strait, completed its work under a tight time schedule. We appreciate the dedicated efforts of committee members on this important project. Through the preparation and issuance of this report, the committee has made a valuable contribution to the Institute and to the profession.

Bernard Z. Lee
Chairman of the Board

Philip B. Chenok
President

New York
May 1984

PCPS: Achievements and Prospects

May 1984

In January 1983, Rholan E. Larson, chairman of the American Institute of Certified Public Accountants, acting at the direction of the AICPA Board of Directors, appointed the Private Companies Practice Section Structure Committee to

comprehensively review the objectives, membership requirements, and organizational structure and functions of the Private Companies Practice Section (PCPS), including the activities of its Executive, Peer Review, and Technical Issues Committees, to determine whether the section's objectives and programs are appropriately responsive to the needs of AICPA members having private company clients, and to report their findings and recommendations to the Board of Directors.

This is the PCPS Structure Committee's report based on its review and evaluation of the Private Companies Practice Section of the AICPA Division for CPA Firms.

A Blueprint for Increased Effectiveness

Independent public accountants in public practice have been given an opportunity to participate in a voluntary program, administered by their peers, to maintain and improve the quality of practice in CPA firms.¹ A profession that relies on such a program must be ever vigilant to protect its interest and to retain public trust. It must be willing to consider and to adopt program innovations required by changing circumstances. To that end, we present here, in summary, a blueprint for such changes designed to enhance the strengths and minimize the perceived weaknesses of the PCPS and the Division for CPA Firms.

General Assessment

The PCPS plays a vital role in the profession's voluntary quality assurance program for CPA firms. It has been a force in improving the quality of the audit and accounting practices of its members. It should expand its focus to all areas of practice to help improve the quality of practice in areas such as MAS and tax.

1. The term, "CPA firms," as used in this report and in describing the constituency of the Division for CPA Firms, encompasses firms of all sizes, including sole practitioners engaged in the professional practice of public accounting without regard to whether they employ professional staff.

Objectives of the PCPS

The stated objectives of the PCPS should be revised. Improving the quality of services for all types of clients should be emphasized as the primary objective. Although the authority to impose sanctions should be retained, the reference to sanctions as a means to achieve an effective system of self-regulation should be eliminated from the objectives. The educational aspects of programs to help firms improve the quality of their practices should be recognized in the objectives. The statement of the advocacy objective should be modified to emphasize the current PCPS approach to professional and technical advocacy.

Attracting More Members

The division can attract a greater percentage of AICPA members in practice. All firms represented in the AICPA membership should be part of the division. A better understanding of the needs and desires of all firms should enable the division to attract more firms through a vigorous membership promotion program. The division should motivate small firms to become members by developing attractive programs and realistic requirements relating to their practices. Users of the services of CPA firms (clients) and third-party users of financial statements should be better informed about the nature and significance of membership in the division through public information programs developed for those purposes.

More Relevant Peer Review Requirements

Peer reviews should be more appropriately designed for the various types of member firms. The division should establish arrangements to help minimize apprehension about peer reviews and to reduce the economic burden of peer reviews for all firms. We recommend that

- The existing forms of peer reviews should be retained for firms with significant audit practices, but efforts should continue to find ways to reduce the cost of both the initial and subsequent peer reviews.
- A new type of optional off-site peer review should be developed for firms whose accounting and audit practices are limited to review and compilation, and transitional procedures should be developed for firms that have accepted audit engagements for the first time.
- Prospective member firms should be offered optional, premembership, consulting peer reviews on a confidential and educational basis to help them prepare for membership and to overcome the fear of peer reviews.
- A peer review barter bank should be established for the barter of peer review hours to afford firms the option of defraying costs by providing an equivalent number of peer review hours to other firms.
- Member firms should be offered a peer review deferred payment arrangement under which they could pay for their peer reviews over the three-year peer review cycle.

Member Services — Untapped Opportunities

Member services should be considerably expanded. New approaches should be developed covering a wide range of potential services, including assistance in building an MAS practice, consultations on computer hardware and software utilization, assistance in the development of a tax practice, and assistance in practice management. A committee should be established as the primary instrument for expanding the services available to firms. It should establish subgroups of firms based on features such as size and type of practice. Separate subgroups should be established for multi-office firms, large single-office firms, medium-size single-office firms, and small firms including sole practitioners. Assistance and support of the SECPS should be obtained for the program. Quality control standards and procedures should be developed for tax and MAS practices, and peer reviews of such areas of a firm's practice should be made available on an optional basis.

A Forum for PCPS Firms

Providing a forum for advocacy on behalf of private companies practice firms, an important function of the PCPS, should be continued and expanded.

A Response to an Emerging Need

Before discussing in detail our blueprint for changes, we will briefly review the history of the PCPS, its objectives, and its present structure.

The AICPA organized the AICPA Division for CPA Firms in September 1977. The creation of the division represented the profession's effort to establish a voluntary quality assurance program within the AICPA for CPA firms. The division consists of two autonomous and largely independent sections, the SEC Practice Section (SECPS) and the Private Companies Practice Section (PCPS). In addition to providing a voluntary quality assurance program for CPA firms that serve primarily private company clients, the PCPS provides a means to better serve local practitioners and to afford them a more effective voice within the profession. The division, now in its sixth full year, represents firms with which about 43 percent of AICPA members in public practice are affiliated.

Creation of the Division for CPA Firms

Forming the division was a major initiative in the development of a voluntary quality assurance program for the profession, focusing on firms rather than individual CPAs. The concept underlying the division was first accepted in 1975 by the AICPA Special Committee to Study Proposals to Restructure the Profession (the Mancher committee), chaired by Harry Mancher. In its report to the AICPA Board of Directors in July 1976, the Mancher committee recommended that a structure be established within the AICPA for CPA

firms as entities. The board accepted the recommendation and instructed staff to explore ways to implement it. However, the concept embodied in the recommendation was controversial, and no immediate actions were taken to implement the recommendation.

A year later, in response to external pressures, the AICPA set up a voluntary quality assurance program for CPA firms. In May 1977, a proposal to establish two divisions for CPA firms, an SEC practice division and a private companies practice division, won the support of the board, and ad hoc groups were designated to implement the proposal. The proposal, modified as a single division with two sections, was approved by Council in the fall of 1977, and the Division for CPA Firms became operational in 1978.

Objectives of the PCPS

The organizational document for the PCPS, as approved by Council, established its objectives, basic membership requirements, organizational structure, and functions. Its objectives are to

- Improve the quality of services by CPA firms to private companies through the establishment of practice requirements for member firms.
- Establish and maintain an effective system of self-regulation of member firms by means of mandatory peer reviews, required maintenance of appropriate quality controls, and the imposition of sanctions for failure to meet membership requirements.
- Provide a better means for member firms to make known their views on professional matters, including the establishment of technical standards.

Organizational Structure

The activities of the PCPS are governed by the PCPS Executive Committee (PCPSEC), a twenty-one-member committee drawn from representatives of member firms. PCPSEC members are appointed for staggered three-year terms by the AICPA chairman with the approval of the AICPA Board of Directors and the existing PCPSEC. A nominating committee, drawn from seven PCPS member firms and elected by the AICPA Council, submits a slate of candidates. In selecting candidates, the nominating committee is guided by the principle that the PCPSEC should include at all times at least fourteen representatives of member firms with no SEC clients. The chairman is elected by the PCPSEC from among its members to serve at the pleasure of the PCPSEC and is limited to three one-year terms.

The Peer Review Committee (PRC) is responsible for administering the peer review program. Its broad assignment entails establishing standards for reviews, reporting on reviews, recommending sanctions and discipli-

nary proceedings, and recording reviews. The PRC is a fifteen-person committee appointed by the PCPSEC from individuals selected from member firms. Its objectives are to determine that member firms are maintaining and applying quality controls in accordance with established standards.

The PCPS is authorized to set up a public oversight board like the Public Oversight Board of the SECPS, but it has not exercised that option.

The PCPSEC can impose sanctions on member firms either on its own initiative or on recommendation of the PRC. It has established procedures and due process for the implementation of sanctions, but it has not yet imposed formal sanctions. Although the PRC is not authorized to impose sanctions, it can and does require firms that receive unsatisfactory peer review reports to agree to certain conditions before their reports are accepted. The conditions include additional CPE requirements, accelerated peer reviews, and revisits by review captains or submission of documents to the PRC to see that appropriate corrective steps have been taken.

In addition to the committees established or authorized by the PCPS organizational document, the PCPSEC has a technical issues committee (TIC) to monitor technical developments and present the views of PCPS members on those developments to other AICPA components. The TIC is a twelve-person committee appointed by the PCPSEC from PCPS member firms. The PCPSEC has also established task forces, such as those on (a) member services, (b) public relations, (c) insurance requirements, and (d) nominations. The PRC also has several task forces.

The AICPA president designates a staff director for the PCPS and assigns other staff. The administrative and other costs of the PCPS staff and normal meeting costs are met out of the AICPA's general budget. Special projects are paid for by PCPS membership dues.

Membership Requirements

For a CPA firm to be eligible for membership in the PCPS, a majority of its partners (or equivalents) must be members of the AICPA. (A sole practitioner is a "partner" in this context and must be a member of the AICPA.) Firms seeking membership must submit an application together with certain required nonfinancial information and agree to abide by the membership requirements. A firm may resign from the division if at the time of its resignation it is not undergoing a peer review or is not the subject of an investigation. A firm's membership may be terminated by the action of the executive committee for failure to abide by membership requirements.

Member firms must comply with the following requirements:

- Ensure that a majority of the members of the firm are CPAs, that the firm can legally engage in the practice of public accounting, and that each partner (or equivalent) resident in the United States and eligible for AICPA membership is a member of the AICPA.

- Adhere to quality control standards established by the AICPA.
- Submit its accounting and audit practice to peer reviews conducted in accordance with review standards established by the PRC every three years or at such additional times as designated by the PCPSEC.
- Assure that each professional in the firm resident in the United States, including CPAs and non-CPAs, participates in at least twenty hours of continuing professional education every year and in at least 120 hours every three years.
- Maintain at least the minimum amounts and types of accountant's liability insurance prescribed by the PCPSEC.
- Pay established dues, comply with the established rules and regulations of the PCPS, cooperate with the PRC, and comply with sanctions.
- File with the PCPS for each fiscal year designated nonfinancial information for inclusion in a public file.

Benefits of Membership

The benefits of PCPS membership generally relate to improving the quality of member firms' accounting and audit practices and the advocacy function. PCPS membership is viewed as demonstrating a commitment to support the profession's voluntary quality assurance program. The overriding attraction is a form of accreditation of the quality of a firm's practice. Other benefits include a quarterly newsletter, *The PCPS Reporter*, and an annual conference.

The Issues Considered

The primary objectives of the PCPS are to promote high-quality practice among member firms for the benefit of the public and of users of the financial statements of private companies and to serve as an advocate in professional and technical matters on behalf of its members. In our review of the PCPS, the strategic question for its growth and the growth of the Division for CPA Firms was whether they serve the needs of practitioners. Areas of concern were these.

Structure and Objectives

- Should the Division for CPA Firms be restructured?
- Should the PCPS give greater emphasis to the educational aspects of its programs as a means of improving the quality of practice of its member firms?

- Should a primary objective of the PCPS be to gain wide recognition of the commitment of its member firms to quality practice and to serve as an advocate on their behalf?
- Should the authority to impose sanctions be modified or eliminated?

Membership

- Should the constituency of the PCPS be viewed as all firms, including sole practitioners, in the AICPA membership regardless of size and type of practice or should the field of membership be more narrowly circumscribed?
- Can the division make membership more attractive to small firms by making membership requirements more relevant to such firms or should a separate membership group be created for such firms?
- Should the division undertake a comprehensive membership promotion program?

The Peer Review Process

- Should peer review standards, procedures, and reports continue to be substantially identical for all firms?
- Should greater emphasis be given to the educational benefits of peer review?
- Should peer review procedures be more appropriately designed and more affordable for small firms?
- Should peer reviews be developed for the tax and MAS areas of a firm's practice?
- Should the requirements for peer reviews subsequent to a firm's initial review be modified?

Member Services

- Should members' expectation of benefits be limited to a form of accreditation carrying a special designation and recognition?
- Should the benefits of membership be expanded to include more services?

Advocacy

- Should the PCPS have an advocacy role on behalf of its membership in professional and technical matters?
- Is an advocacy role consistent with the quality assurance function and with the overall objectives of the AICPA?

A Successful Beginning, A Challenging Future

From its inception, the division has been confronted with controversy and skepticism. It has had a successful beginning but faces a challenging future. Many concerns have been expressed about the structure, purpose, and operations of the division. The major concerns relate to whether its structure and operations meet the needs of the public accounting profession and the expectations of society. The division as a voluntary organization plays an important role as a part of the control mechanisms in our society that apply to CPAs. Its role is preventive rather than punitive.

CPAs in public practice have been assigned a significant public responsibility and have an obligation to obtain and retain public trust. In a study of control mechanisms in society, Albert K. Cohen included CPAs among those in society who have been assigned specific functions to help to control compliance with societal norms.² He contends that since those, like CPAs, assigned a guardian role may also deviate from accepted norms, any study of control mechanisms in society must also address the question: Who will guard the guardians? That question is relevant in assessing the performance of the PCPS as a vital part of the Division for CPA Firms, because the CPA profession has jealously guarded its right to regulate itself.

In *The Rise of the Accounting Profession — From Technician to Professional 1896-1936*, John L. Carey reported excerpts from 1933 testimony by Colonel Arthur H. Carter, then senior partner of Haskins & Sells, in Senate committee hearings on securities acts legislation. Colonel Carter maintained that although the role of CPAs was to audit others, CPAs were “audited” by their consciences.³ As a response to congressional concern, Colonel Carter’s answer is no longer credible or acceptable. The societal role of independent public accountants must be controlled through a combination of standards based on a consensus of those expected to abide by them and the establishment and monitoring by the profession of procedures to help assure compliance with those standards. Although the PCPS as part of the Division for CPA Firms is a part of that process, the process also includes government control elements having more punitive authority, such as state boards of accountancy and the courts. Some state boards have established programs involving reviews similar to those of the division to help enforce compliance with professional standards.

The PCPS has neither the SEC’s direct influence nor Congress’s concern for financial reporting by public companies, both of which bolster the

2. Albert K. Cohen, *Deviance and Control* (Englewood Cliffs, N.J.: Prentice-Hall, 1966).

3. John L. Carey, *The Rise of the Accounting Profession — From Technician to Professional 1896-1936* (New York: American Institute of Certified Public Accountants, 1969), pp. 186–187.

SECPS. Nonetheless, the public interest requires that all CPA firms meet acceptable standards of practice. The concerns and the regulatory programs of state licensing authorities exert direct influence on both the PCPS and the SECPS to maintain a program that helps assure that member firms meet acceptable standards of practice.

Although self-regulation — the voluntary agreement to abide by standards established and enforced by peers — is a necessary means to achieve satisfactory quality of practice, education — the process of developing educational programs designed to help firms improve the quality of their practices — is an equally vital means of achieving that objective that has been largely ignored by critics of the PCPS. By providing means through self-regulation and educational programs to help both private companies practice firms and SEC practice firms improve the quality of their practices, the Division for CPA Firms directly supports the role of the state boards. To increase the benefits and uses of its program of self-regulation, the division should work with the National Association of State Boards of Accountancy (NASBA) through existing AICPA liaison channels to gain wider acceptance and promotion of its program by state boards.

The evidence indicates that the PCPS as a part of the division for firms has been and continues to be influential in improving the quality of the audit and accounting practices of its members. It has become an essential element in the profession's voluntary quality assurance program. Its primary objectives are (1) to improve the quality of services provided by CPA firms to their clients through the establishment of practice requirements to protect the public interest and (2) to serve as an advocate on behalf of its members. Until now, however, the focus of the efforts to improve the quality of services has been almost exclusively directed to accounting and audit services. The PCPS should expand its focus to all areas of practice in which CPA firms provide services; it should develop programs to help improve the quality of services provided in such other areas as MAS and tax practice.

Revised Objectives for PCPS

Many believe the central objective of the PCPS is to establish and maintain an effective voluntary quality assurance program for CPA firms by means of mandatory peer reviews, compliance with quality control standards, and the imposition of sanctions. Its stated objectives contribute to the perceived regulatory emphasis. The perception is unnecessary, and we believe that it is a major impediment to PCPS membership for many firms. For firms with only private company clients, the emphasis should be on educational efforts to assist firms in improving the quality of their practices in all areas.

For those firms, the objectives should be to

- Improve the quality of services by CPA firms.
- Establish and maintain an effective system of self-regulation through the establishment of review procedures and other requirements for member firms and through the educational aspects of programs to help member firms to improve the quality of their practices.
- Provide a means to represent the interests of member firms on professional matters, including the establishment of technical standards.

The first objective would emphasize the quality of services offered to all types of clients. The second objective would emphasize self-regulation without the necessity of sanctions and highlight educational aspects of programs that would encourage firms to improve the quality of their practices. Finally, the third objective would emphasize the PCPS's current advocacy approach, primarily through informed, representative committees of peers to carry out the advocacy function on professional and technical matters.

A Drive to Increase Membership

Since membership in the division is voluntary, the division's ability to attract a substantial percentage of AICPA members practicing in local firms is a significant factor in assessing its long-term viability. It can attract a higher percentage.

Current Membership Statistics

The table on page 12 shows an analysis and comparison of division membership with CPA firms (including sole practitioners) represented in the AICPA membership as of April 19, 1983. The comparison shows that although 1,718 firms (5 percent of the 34,516 firms represented by AICPA members in practice) are members of the division, 44,063 AICPA members, or 43 percent of the 102,539 AICPA members in practice, are in member firms. Firms not in the division are primarily sole practitioners and small firms with less than eleven AICPA members. Division membership represents about one-third of firms with six to ten AICPA members and just over one-half of firms with eleven to twenty-five members. Most large firms are members of the division. Since large firms tend to have a larger portion of their practice in the audit area than do smaller firms, the division undoubtedly covers a much larger proportion of audit practice than its proportion of AICPA members in practice may suggest.

Need to Expand Constituency

An examination of these statistics raises the question of whether a comparison of division membership with the total number of firms represented in the AICPA membership is a reliable indicator of the division's success or failure in meeting its objectives. We believe that to achieve those objectives, the division's constituency should include all firms regardless of size and type of practice. However, the statistics suggest that the division needs to examine carefully the nature of the practices of firms with less than six AICPA members, a very small percentage of which have joined the division to date, to design a program that realistically meets their needs. A better understanding of the nature of the practices of this group should enable the division to attract a much greater number as members, a necessary first step in meeting its primary objective of improving the quality of practice. The division's program should not repel any firms from joining and receiving the benefits of membership.

Making Membership More Attractive to Small Firms

Increasing the attractiveness of PCPS membership for small firms should involve designing membership requirements with special provisions for such firms and creating subgroups for them. The PCPS should motivate small firms to become members by designing attractive programs and realistic requirements relative to their practices. Adopting that approach would enhance the effectiveness and integrity of the voluntary quality assurance program.

A Comprehensive Membership Promotion Program

We recommend that the PCPS undertake a comprehensive membership promotion program to expand its constituency and attract more firms. The approach to a comprehensive program involves publicizing the PCPS not only to prospective members but also to preparers and users of financial statements. As indicated by the analysis of membership data, the substantial number of AICPA members in practice that have not joined the division are primarily in small firms. We believe that with the changes in the voluntary quality assurance program for private companies practice firms recommended in this report, an effective comprehensive promotion program can be mounted to attract many of those firms into the program. The results would be a division that represents a majority of AICPA members in practice, which would significantly add to the thrust for quality.

Comparison of Membership in the Division for CPA Firms With AICPA Members in Public Practice as of April 19, 1983

Firm Size by Number of AICPA Members	PCPS Only		Both PCPS and SECPS		SECPS Only		Totals for the Division for Firms		AICPA Membership		Percentage* Penetration of AICPA Membership	
	Firms	Members	Firms	Members	Firms	Members	Firms	Members	Firms	Members	Firms	Members
1	139	139	17	17	1	1	157	157	23449	23449	1%	1%
2-5	540	1718	95	330	2	9	637	2057	8771	24537	7%	8%
6-10	359	2706	99	780	6	52	464	3538	1515	11131	31%	32%
11-25	221	3423	120	1934	1	20	342	5377	640	9677	53%	56%
26-50	31	1016	50	1674	—	—	81	2690	102	3384	79%	79%
51-100	—	—	13	881	—	—	13	881	15	998	87%	88%
over 100	—	—	24	29363	—	—	24	29363	24	29363	100%	100%
Totals	1290	9002	418	34979	10	82	1718	44063	34516	102539	5%	43%

*Rounded to nearest
whole percentage

Note:

The information in this table was compiled from two separate data bases. AICPA membership records and the membership records for the Division for CPA Firms. The data on AICPA members in public practice and their firm-size classifications were taken from a computer-generated analysis of AICPA membership records. The membership records for the Division for CPA Firms classify member firms based on the number of CPAs reported by those firms instead of AICPA members. For that reason, the number of AICPA members in each member firm was compiled manually from AICPA membership records to the extent feasible. However, the division's classification of member firms with one CPA was treated as equivalent to firms with one AICPA member without cross checking the classification to AICPA membership records. Other size categories include firms for which the number of CPAs reported were considered equivalent to AICPA members in the firm as follows:

Size Category	Totals in Category		Numbers Based on Division Data (CPAs)		Percentages of Totals in Category	
	Firms	AICPA Members	Firms	AICPA Members	Firms	AICPA Members
2-5	637	2057	117	340	18%	17%
6-10	464	3538	24	171	5%	5%
11-25	342	5377	6	107	2%	2%
Totals	1443	10972	147	618	10%	6%

The three largest size categories were completely reconciled to AICPA membership records. Thus, the classifications by firm size based on AICPA members is a close approximation based on the best available data.

Getting the Message to the Public

The basic rationale for membership in the division is that membership indicates to the public a commitment to provide high quality service and gives a firm credibility in the eyes of the public. Membership represents a form of accreditation that needs to be widely understood. The users of the services of CPA firms and the users of financial statements need to be informed about the significance of membership. They need to be informed about the membership requirements, the nature and significance of the peer review process, the educational benefits of membership, and the commitment to quality practice by member firms.

More Flexibility in Peer Reviews

The peer review requirement is the most difficult and most controversial membership requirement. Some believe that the fear of failing a peer review is the most significant barrier to division membership for many firms. Others believe that the costs of preparing for and undergoing peer reviews are the most significant barriers. We identified peer review as a central issue and focused on ways to make peer reviews more relevant and to reduce their cost so as to make division membership attractive to more firms.

Present Requirements

Peer reviews are designed to determine whether firms' quality control policies and procedures conform to standards established by the AICPA. Peer reviews by four types of entities are available:

- A *committee appointed review team (CART) review* is conducted by a Peer Review Committee-appointed review team.
- A *firm-on-firm review* is conducted by another CPA firm.
- An *association review* is conducted by a team authorized or appointed by an association of CPA firms.
- A *state society review* is arranged under a state society program.

PCPS peer reviews are structured essentially the same as those of the SECPS. PCPS and SECPS peer reviews are administered by the same staff under the same standards, frequently using the same peer reviewers except that PCPS peer reviews are not conducted under POB oversight as are SECPS peer reviews. Unlike the SECPS, the PCPS allowed charter members to delay their initial peer reviews to allow members more time to document their quality control policies and procedures. However, firms that join either section of the division during 1984 will be required to have their peer reviews within one year of joining.

The division now has distinctions in peer review procedures based on size of firm and type of practice. The peer review checklists and procedures of both the SECPS and PCPS differ for

- Sole practitioners.
- Firms with two to twenty professionals.
- Firms with twenty to fifty professionals.
- Firms with over fifty professionals.

The PCPS has additional categories designed to reduce the cost of peer reviews, including

- Firms having limited accounting and audit practices.
- Firms having no accounting and audit practice.

In addition, the PCPS has developed procedures for simplified, engagement-oriented reviews for firms with up to twenty professionals. Such firms may elect that their quality control systems be evaluated primarily through a review of selected accounting and audit engagements so that the documentation of compliance with quality control policies and procedures is less formal than for system-oriented reviews.

Although many member firms aggressively publicize the results of their peer reviews, the PCPS does not do so. The peer review report and the firm's annual information report are included in the firm's public membership file.

Some see the close similarity between PCPS peer reviews and SECPS peer reviews as a major strength of PCPS membership, viewing the PCPS and the SECPS as two cohesive elements of the profession's voluntary quality assurance program for CPA firms. They believe that the ability of the program to withstand regulatory or congressional challenge will depend on the ability to demonstrate the success and effectiveness of the entire peer review program. They also fear that any modification in the PCPS peer review program that would make it less demanding than the SECPS program would give PCPS membership a second-class status. In a recent survey of a group of PCPS members, the respondents overwhelmingly supported the position that the PCPS peer review standards, procedures, and reports should continue to be substantially identical to those of the SECPS. We believe that the close similarity in peer reviews and peer review procedures should be maintained for firms with significant audit practices.

Modify Peer Reviews for Some Types of Firms

We considered whether quality control standards have broad applicability to all CPA firms and whether all PCPS members should be required to have peer reviews as now structured to determine whether they have systems

that meet the requirements of those standards. Member firms with significant audit practices should continue to have peer reviews as now structured. However, we believe an effective peer review can be performed in a simpler and more cost effective manner for firms without audit practices. We believe that for those firms, a much simpler peer review process that adheres to the profession's voluntary quality assurance program can be designed. Greater emphasis and publicity should be given to peer reviews as a part of the educational effort to assist firms in improving practice quality. Firms that now dread peer reviews with the present emphasis should welcome peer reviews as valuable educational experiences.

Make Peer Reviews More Relevant

Peer reviews should be redesigned and made more relevant for some firms, and the PCPS should establish arrangements to help eliminate apprehension about peer reviews and to reduce the economic burden of peer reviews for all firms. To accomplish those results, we recommend that

- The existing forms of peer reviews be retained for firms with significant audit practices, but efforts should continue to find ways to reduce the cost of both the initial and subsequent reviews.
- A new type of off-site peer review, limited to a review of selected reports together with the submission of report preparation and procedural checklists and in conjunction with appropriate inquiries, should be developed for firms whose accounting and audit practices are limited to review and compilation.
- A special arrangement should be developed for firms whose accounting and audit practices are primarily limited to review and compilation, with only a few audit engagements, under which such firms would be given a one-time option for one peer review cycle of either undergoing an on-site peer review or having each of its audit engagements undergo a preissuance, concurring review by a member firm, in accordance with procedures established by the PRC, while continuing the type of peer review developed for review and compilation practices.
- Procedures should be established to offer prospective members pre-membership consulting peer reviews on a voluntary, confidential, and educational basis.
- An arrangement should be established under which a firm could obtain a peer review on a barter basis through a peer review barter bank maintained by the PRC by providing an equivalent number of peer review hours for reviews of other firms designated by the PRC.
- A deferred payment arrangement should be established under which a member would be allowed to pay for its peer review over the three-year peer review cycle.

- Efforts in the division to explore ways to reduce the cost of subsequent peer reviews should be continued.

Peer reviews for review and compilation practices. The recommendation to establish a form of peer review limited to a review of selected reports, together with the required submission of appropriate checklists and inquiries, is based on the desire to design the review to fit the type of practice. An on-site peer review is unnecessary for firms whose accounting and audit practices are limited to review and compilation. An off-site review with checklists would adequately determine compliance with standards. Moreover, a firm could be required to submit a representation letter on its compliance with quality control standards.

We believe that an off-site peer review for firms with only review and compilation practices is an appropriate review for such firms and that no distinction should be made in the division's directory. No distinction is made in the present directory for differences in peer review procedures, which include no peer reviews for firms without accounting and audit practices. An explanation of the various types of practices and the forms of peer reviews should be included in the introduction to the directory.

A transitional arrangement. The recommendation to give firms with only a few audit engagements a one-time option is designed to ease the transition from an off-site review to an on-site review. The proposal would allow a firm whose accounting and audit practice is primarily limited to review and compilation, with only a few audit engagements, either to undergo an on-site peer review or to have the option during one peer review cycle, of having each of its audit engagements undergo a preissuance, concurring review by a member firm, in accordance with procedures established by the PRC, while continuing with the peer review developed for review and compilation firms. Under the proposal, the option would be available for only one peer review cycle. Therefore, a firm with only a few audit engagements could elect to have an off-site peer review and defer its on-site peer review for one full cycle if it agreed to subject its audit reports on those engagements to a preissuance review by a member firm.

Premembership consulting peer reviews. The recommendation to develop procedures to offer premembership consulting peer reviews to prospective members on a confidential and educational basis is designed to help firms overcome the fear of peer reviews. It is based on the view that the PCPS should make available to prospective member firms a risk-free educational program to prepare them for a peer review. Under the proposal, the PCPS would offer firms consulting reviews to help them improve the quality of their practices and to prepare them for membership. We proposed that the PCPS rebate a part of the cost of such reviews if a firm subsequently joins the division and undergoes a regular peer review.

Peer review barter bank. The recommendation to establish a peer review barter bank based on hours will, we believe, help overcome objections to membership that stem from the cost of peer reviews. The program, designed and administered by the PCPS, would allow firms to offset the direct cost of peer reviews by providing an equivalent number of hours for peer reviews of other firms. Firms would be required to settle their accounts within a reasonable period, perhaps eighteen months, in either equivalent hours or dollars.

Deferred payment arrangements. The recommendation to establish a deferred payment arrangement that would permit firms to pay for their peer reviews over the three-year peer review cycle should help ameliorate the economic burden of undergoing a peer review. Under the proposal, the PCPS would establish arrangements for financing the deferred payments.

Subsequent reviews. One aspect of the peer review problem relates to division members facing their second peer review. The PRC is considering the extent to which peer review procedures can be reduced for subsequent reviews. We recommend that the PRC continue to actively consider and eventually adopt such procedures where feasible.

Member Services — Untapped Opportunities

The PCPS should substantially expand its services to members, and we believe the program recommended in this report will enhance its ability to do so.

The Existing Program of the PCPS

Peer review and advocacy, which are discussed separately, are the major existing member services. The PCPSEC recently established a member services task force charged with developing and evaluating recommendations for increasing and improving the services that PCPS provides to its member firms. One problem has been identifying services that PCPS could and should provide to its members without duplicating those already being adequately provided by the AICPA and state societies. In the past, PCPS has taken initiatives that led to the development of services for all AICPA members, such as the *AICPA Audit and Accounting Manual* and a brochure designed to help local firms in recruiting staff.

Existing AICPA activities that are most closely related to PCPS member needs are those carried on by the Management of an Accounting Practice (MAP) Committee. Those activities include the MAP handbook, MAP conferences, round table discussion manuals, telephone consultation service,

and the local firm management review program. Other existing AICPA services that primarily benefit local firms include

- Continuing professional education.
- The Technical Information Service.
- *Audit and Accounting Manual*.
- *The Practicing CPA, Client Bulletin*, and the Practitioners Forum in the *Journal of Accountancy*.
- Much of the MAS publications program.
- Staff recruiting aids.
- Liability and retirement insurance programs.
- Local practitioner seminars, member forums, and member round tables.
- Computer software exchange referrals.

We are not suggesting that the PCPS should assume responsibility for some or all AICPA activities that primarily benefit local firms. Some of the benefits of coordinating such activities have already been achieved by centralizing the direction of many of those activities under the vice-president, local practitioner activities, to whom the PCPS staff reports.

Recommended Expansion of Member Services

The division is a unique organization of firms and should be particularly adaptable to providing services to firms. The AICPA now provides a wide range of services that are unique to CPA firms. As the AICPA changes in response to changing circumstances, we believe a time may well come when many of those types of services can also be offered through the division. However, we recommend that in the meantime, the PCPS develop in close coordination with existing AICPA activities a program to expand services.

Develop innovative approaches. The PCPS should develop innovative approaches to providing member services. It should not be overly constrained because some types of services are now available from other sources or because some types of services cannot be restricted to its members. An innovative approach should consider a wide range of possibilities, including

- Developing consultation services.
- Initiating public relations efforts to make users, clients, and recruits more aware of the PCPS and its membership requirements.
- Setting up a computerized listing of open opportunities to provide services to government entities or government grant recipients on a re-

gionalized, current, and reasonably comprehensive basis to apprise firms of opportunities to bid for new business.

- Providing group discount purchasing contracts.
- Providing data bank listing of available consulting and correspondent services from other member firms and a listing of CPAs seeking to relocate.
- Providing prototype press releases, such as releases relating to accomplishments of the division.

Develop specific services. The PCPS should consider developing specific services, such as

- *Providing assistance in developing MAS practices and in the administration of such practices.* MAS is one of the fastest growing areas of practice. It is an area that is very suitable to many local practitioners because of their closeness to, and familiarity with, their clients. The PCPS should form a committee to work closely with the MAS Executive Committee in establishing a program designed to help firms without MAS practices establish them.
- *Providing assistance in computer hardware and software utilization.* The rapid advance in information technology makes such assistance of vital importance to many firms.
- *Providing assistance in the development of tax practices.* Such a program should not be designed to deal with the technical aspects of a tax practice. It should provide assistance in the administration of a tax practice, provide help in tax planning, provide consulting services, and help to develop CPE material unique to a tax practice. The PCPS should form a committee to coordinate the section's activities with the tax division and the CPE division, arranging with those divisions to develop special materials for its use.
- *Providing assistance in the management of a practice area.* The PCPS should work closely with the AICPA MAP Committee to develop special programs to help firms in the management of their practices.

Peer reviews for tax and MAS practices. Peer reviews and quality control standards are now limited to accounting and audit practices. We recommend that peer review standards and procedures be developed for tax and MAS practices to provide the service of peer reviews of those areas of practice on an optional basis to firms requesting such reviews. The benefits of a peer review should be extended on an optional basis to the tax and MAS areas of practice because of the significance of those areas of practice to many firms in relation to the firm as a whole. Many firms would find a peer review of their tax and MAS practice areas a useful evaluation that would help improve the quality of their practices.

Restructuring to expand member services. Since we believe that a primary goal should be to expand the services that the PCPS provides its members, we recommend that a structure be established to achieve that goal. The PCPSEC should establish a committee, under its existing authority, to coordinate the development of member services and invite the SECPSEC to assist and support the effort through a formal, coordinating mechanism. The committee to develop member services should establish subcommittees for groups of firms based on similarities and commonalities, such as size and type of practice. We propose that separate subcommittees initially be established for multi-office firms, large single-office firms, medium-size single-office firms, and small firms including sole practitioners. The primary purpose of the subcommittees would be to develop for the firms in their areas services of the type provided to its members by an association of CPA firms, such as audit and accounting manuals, practice management assistance, exchanges of industry expertise, technical conferences and forums, sponsoring CPE courses tailored to the needs of firms in the subgroups, and tailoring some other services available through the Institute to the needs of firms in the subgroups.

Advocacy — Giving Local Practitioners a Voice

The professional and technical advocacy as now performed by the PCPS can and should operate more effectively.

Existing Program of the PCPS

One of the PCPS' objectives is to

provide a better means for member firms to make known their views on professional matters, including the establishment of technical standards.

In general, the PCPSEC carries out that objective for nontechnical issues, and the technical issues committee does so for technical issues. The modification in the statement of that objective recommended in this report is intended to give greater emphasis to the current approach to professional and technical advocacy.

After two years of performing both the professional and technical advocacy functions on its own, the PCPSEC in November 1979 established the TIC and charged it to

identify and develop substantive comments on major technical issues that would have a significant effect on private companies and the CPA firms that serve them.

Originally, TIC comments required PCPSEC clearance before they could be communicated. However, in September 1980, the PCPSEC authorized the TIC to present views on behalf of the PCPS to other components of the Institute without the PCPSEC's prior approval. The PCPSEC specified the AICPA committees to which the TIC could address its comments and established certain procedural requirements.

An Expanded Advocacy Role

Professional advocacy through the PCPSEC and technical advocacy through the technical issues committee are working reasonably well and should continue. The TIC should consider expanding its role by steps, such as issuing technical alerts to draw members' attention to technical requirements and rallying members in support of TIC advocacy positions.

The PCPS should consider and develop innovative approaches to making its professional and technical advocacy more effective. It should develop approaches to

- Espouse positions in addition to reacting to proposals of others.
- Obtain the views of its membership more directly through member forums and develop closer liaisons with member firms.
- Increase local firms' participation in, and influence on, standards-setting bodies.
- Increase the positive attention and responsiveness of standards-setting bodies to the needs of private companies and the CPAs who serve them.

Addendum

Reason for Addendum

We completed the preceding part of the report in 1983 and presented it as an interim report to the AICPA Board of Directors and to the PCPS Executive and Peer Review Committees. The PCPS Executive Committee accepted our recommended program of action to increase the effectiveness and appeal of the PCPS presented in the interim report and approved it in principle. The section has moved quickly to begin implementation of most of the specific recommendations in the report. Understandably, implementation of some of the recommendations will take time, and others were rejected after the section had considered them and explored the feasibility of their implementation.

In the review and evaluation of the PCPS, we considered other problems, many of which cannot be adequately addressed solely within the PCPS. We explored the concept of a unitary division as a possible solution to some of those problems and discussed that concept with the SECPS Review Committee, an AICPA special committee established to review the SEC Practice Section, and with other groups. The unitary division concept, as we viewed it, would entail restructuring the Division for CPA Firms into a unified division, without separate sections, to conduct the voluntary quality assurance or self-regulation program for CPA firms and to provide firm-oriented services on an expanded scale. The division would have a single balanced executive committee, with adequate safeguards to protect the integrity and autonomy of the self-regulation program for SEC practice firms and to assure continuation of the advocacy function on behalf of private companies practice firms.

We believe the concept of a unitary division merits further consideration as a long-term approach to more fully achieving the objectives of self-regulation. But, under the present structure, other initiatives can be taken to address some of the problems we have identified.

In this addendum we suggest, for further consideration, some short-term initiatives to deal with some of the problems confronting the division and to more fully achieve some of the objectives of the division.

Source of Problems

The AICPA Division for CPA Firms was established in 1977 as two autonomous and largely independent sections, the PCPS and the SECPS, in recognition of differences in the practices and in the needs of different types of firms. Although both sections are structured to improve the quality of the accounting and audit practices of member firms, the SECPS also emphasizes the special requirements of firms that serve SEC clients. Members of the SECPS are subject to special membership and oversight requirements relating to their SEC practice. The two sections have developed similar programs and share a common objective. Both rely primarily on peer review programs for improving the quality of practice, and their basic structure, programs, and operations are similar.

Among the reasons for establishing the PCPS as a separate and autonomous section were to serve the needs of local practitioners and to give them a more effective voice in the profession. The PCPS has been effective in achieving those objectives. Both sections of the division have worked reasonably well in achieving their primary objectives and have afforded firms of all sizes the opportunity to participate in the profession's program for improving the quality of practice in CPA firms through self-regulation.

Problems and Objectives

In reviewing the operations of the PCPS, we identified several problems that require closer cooperation between the two sections. Among the areas of concern are

- Perceptions of a divided profession.
- Public awareness of the program.
- Recognition of the commonalities among practice units.
- Reduction of administrative overlap.
- Communication and relationships among firms.
- Acceptance of peer review program by state boards.
- Existence of a division in name only.
- Mix of firms represented on the executive committees.

Perceptions of a divided profession. The structure of the division contributes to erroneous perceptions that the practicing profession consists of two groups of members that provide different quality levels of service and to the politically divisive but erroneous perceptions of first and second class practices. It also fosters other undesirable views of the division, such as one consisting of a large firm section and a small firm section. We are concerned that many firms may believe quality control standards and peer review were developed to meet the needs of large firms that practice before the SEC and, as a result, have not joined the division.

Public awareness of the program. The AICPA should make the public aware of the nature of the program without distinctions based on the section of the division to which firms belong. In his May 1983 address to Council reporting on the accomplishments of the SECPS, the chairman of that section's Public Oversight Board, John J. McCloy, said

The accounting profession's self-regulatory program is perhaps one of its best-kept secrets. Bankers, financial analysts, businessmen in general and perhaps even the majority of clients know very little about this constructive program on which the profession has embarked.

The Public Oversight Board agrees with that view. In its 1982-83 report on the SECPS, it stressed the "need for a public relations program," stating that "the subject of education and public relations merits urgent attention."

We are concerned that some users of financial statements may consider the two sections to be indicative of different levels of service. Users of accounting and audit services of CPA firms and the users of financial statements should view all member firms as equally competent to provide high quality services. The structure of the division makes it difficult, from a public information perspective, to develop a comprehensive, well-coordinated

program to convey to the financial community the meaning of membership in the division without distinctions based on the section of the division to which firms belong.

Recognition of commonalities among practice units. Accounting and audit practice in CPA firms is not neatly divided between firms that serve only SEC clients and firms that do not serve SEC clients. The structure of the division, however, fosters the erroneous perception that practice is so divided. Many firms have both types of clients; none serve SEC clients exclusively. As shown in this report, all SECPS member firms, excluding ten relatively small firms that have elected to join only the SECPS, are also members of the PCPS. More than half of the firms that belong to the SECPS have no SEC clients and do not practice before the SEC. On the other hand, over 100 firms that do have SEC clients are members of the PCPS only. Perhaps, those firms believe that the major portion of their practice is with private companies or that SECPS peer review is too regulatory. Although firms have added procedures that apply only to SEC engagements, they do not have separate quality controls for SEC engagements and for private company engagements.

Reduction of administrative overlap. The structure of the division makes it necessary to develop separate programs in each section to deliver the same types of services, which leads to administrative overlap and higher cost. The peer review program, the centerpiece of self-regulation in both sections, provides a perfect example. Although the two separate programs have similar standards and procedures and draw from the same reviewer pool, they require separate peer review manuals, more committee meetings, and more staff time in their administration.

Communication and relationships among firms. Improved communication and increased participation would contribute to mutual understanding, trust, and harmony within the accounting profession. More extensive communication among firms of all sizes would be helpful, and the two sections would benefit from more joint participation in projects and programs designed for large segments of the profession.

Acceptance of peer reviews by state boards. Many state licensing authorities are developing peer review programs to determine whether firms in their jurisdictions are adhering to professional standards. They are also using peer reviews as a principal part of their "positive enforcement programs." Those developments increase the need for, and the benefits of, one comprehensive, well-coordinated national peer review program that would be acceptable to state boards of accountancy for use in carrying out their regulatory responsibilities. Since many CPA firms have interstate practices subject to multiple jurisdictions, the existence of varying types of

state peer reviews or quality assurance programs may be ineffective, inappropriate, and duplicative. One uniform national peer review program acceptable to state licensing authorities is in the best interest of the profession and the public.

Existence of a division in name only. Some of the common problems that confront the two sections of the division cannot be adequately addressed because the two sections are independent of each other and have no unifying structure. The division is a division in name only.

Mix of firms represented on the executive committees. Although large firms are members of the PCPS, the organizational document of the section severely limits the participation of representatives of large firms on its executive committee. Similarly, the organizational document of the SECPS restricts participation of representatives of small firms on its executive committee.

Joint Coordinating Committee

The two sections need to work closely together to resolve some of the common problems confronting them, such as the need to develop an effective public information program. In the past, the two sections have cooperated occasionally through ad hoc groups to develop joint programs. There is a need for a permanent organizational structure to facilitate and encourage greater coordination between the two sections in identifying and dealing with problems common to the two sections. We recommend that the executive committees of the two sections form a joint permanent coordinating committee consisting of persons selected from members of the two executive committees, including the chairmen of those committees. The coordinating committee should be assigned the responsibility of exploring ways to improve the coordination between the two sections and ways to deal with common problems. It should work with the National Association of State Boards of Accountancy and should spearhead efforts to make the division's program acceptable to state boards of accountancy.

Other Suggested Initiatives

Some other suggested initiatives to more fully achieve the objectives of self regulation are to

- Conduct a joint public information program.
- Establish a joint peer review committee, with subcommittees for SEC practice firms and for private companies practice firms.
- Issue a joint peer review manual covering the requirements for both sections.
- Publish a joint newsletter.

Joint public information program. The suggestion for a common public information program relates to the need to make the division's programs better known to the users of financial statements. To make such a program effective it should be done as a joint activity.

Joint peer review committee and peer review manual. The suggestions that the two sections establish a joint peer review committee, with appropriate subcommittees, and issue a common peer review manual, address the same problem. They both relate to the need to improve coordination between the peer review programs of the two sections, to overcome some of the administrative overlap, to strengthen the administration of the programs, and to dispel some erroneous perceptions about the programs. They also relate to the need to make the division's peer review program more acceptable to state boards.

Joint newsletter. The suggestion to publish a joint newsletter relates to the need to establish closer ties between the sections. A common newsletter would contribute to improved relations among the members of both sections and help to dispel erroneous perceptions.

Restructuring the Division

Finally, as a long-term solution, the proposal to restructure the division into a more unified organization, without sections, should be considered. It would enable the division to provide an expanded range of services and ultimately make it feasible to attract all CPAs in public practice into the system.

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APPENDIX B

A Progress Report on Implementation

This letter was written before the Addendum was added and addresses only the conclusions and recommendations in the body of the report (pages 1 to 21).



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Division for CPA Firms

March 22, 1984

A. Marvin Strait, Chairman
Special Committee to Study the Objectives,
Policies, and Procedures of the PCPS
American Institute of CPAs
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Dear Marvin:

This letter is a progress report on the Private Companies Practice Section's actions in response to the conclusions and recommendations in the report of your committee, *PCPS Achievements and Prospects*. These remarks are in every sense an interim report, since some of the special committee's recommendations will take time to implement fully, and others that we have already adopted require more work by one or more PCPS committees before they can be fully effective. This letter also reflects my observations regarding the conclusions, actions, and future direction of all Private Companies Practice Section committees. The discussion in this letter follows primarily the order in which the topics are presented in Appendix A, "Index of Conclusions and Recommendations."

General Assessment and Objectives

Our committees support the general conclusions in these areas. We concur with the observation that education is equally as vital as self-regulation in achieving satisfactory quality of practice. Most of our member firms would agree that a peer review is one of the most effective educational processes, even for firms that "pass" their reviews with flying colors.

We have not taken steps to implement the recommendation that we work with NASBA to gain wider acceptance of the section's program—particularly peer review—by state boards, but we expect to do so. We are concerned that some steps state boards might take to monitor the quality of the services they regulate could duplicate the section's programs, subjecting both firms and regulators to unnecessary effort and expense. We plan to consult with both AICPA and NASBA leaders to determine the most effective approach.

We also endorse the conclusion that the PCPS should expand its focus to all areas of practice in which CPA firms provide services. We have established a Member Services Committee, which we expect to take the lead in this, working closely with the Institute's MAS and Tax Divisions and its Management of an Accounting Practice Committee.

Although we have not decided to ask Council to revise the section's formal objectives, we believe that the objectives proposed on page 10 of the report reflect more accurately the reasons for the section's existence and the goals toward which we are working. In particular, we take considerable satisfaction that, due to the cooperative spirit of our members, we have never invoked our sanctioning authority.

Membership

We recognize the importance of attracting a substantial percentage of AICPA members practicing in local firms, and we agree that our constituency should include all firms regardless of size and type of practice. At a PCPS Executive Committee meeting last year, committee members indicated overwhelmingly their belief that small practice units, including sole practitioners, should be actively encouraged to join the section.

We are giving particular attention to the recommendation that we examine the nature of smaller firms' practices in order to design a program that meets their needs. One of the first items on the Member Services Committee's agenda will be to review existing sources of information, especially the Examination Division's *Report of the Practice Analysis Task Force* (AICPA, 1984). If more information is needed, the MSC will recommend additional research that the section will sponsor. At the same time, we are increasing our efforts to recruit members of smaller firms to serve on all PCPS committees.

We are responding actively to the recommendation that the PCPS launch a comprehensive membership promotion program. In September 1983, AICPA Chairman Rholan E. Larson invited partners in local firms to consider joining the section. We received, and followed up on, over one thousand requests for information. Over one hundred new members joined, and applications are still coming in.

That invitation was not sent to sole practitioners since it seemed preferable to wait until we have—in response to your recommendations—more to offer. We plan to launch a new promotion soon, aimed mostly at smaller firms. Meanwhile, we are attempting to enlist state societies to encourage their practicing members to join.

All PCPS committees agree that we must impress the significance of PCPS membership on users of financial statements, which, for several years, has been the executive committee's primary focus. Unfortunately, we have had to move slowly because of the need to avoid implicitly disparaging nonmember firms.

The message we are projecting addresses CPAs' universal emphasis on quality practice, the profession's quality control standards, and the steps firms take to comply with the standards. Peer review is one such step, an important one. Those who rely on a CPA firm's services should satisfy themselves about the firm's quality

controls. They can always do that by direct inquiry; but, if the firm is a PCPS member, they can do it more efficiently by getting a copy of its peer review report, either from the AICPA or from the firm itself.

In recent months we have sent our members two sample speeches on quality control and a kit showing how to publicize a successful peer review. We shall soon send them a brochure explaining the significance of peer review and encourage them to distribute copies. Other materials will also be ready before long.

Our approach so far has emphasized providing public relations materials for our members to use in their communities. This is partly because we consider local public relations to be the most effective and because of current sensitivity to a centralized national campaign that might seem to be promoting just one segment of the Institute's practicing members. Nevertheless, we are planning appropriate centralized public relations activities directed at users of financial statements.

Peer Review

The members of PCPS committees accept and agree with the overall conclusions in the report about peer review. We have already changed our membership requirements to permit firms that perform no audits to have a report review instead of the conventional on-site peer review. Report review guidelines have been developed and, after some fine tuning, will be approved shortly. We expect this program to be in operation for the 1984 review season. For firms that are eligible, it should result in a significant reduction in the total cost of membership and provide a more relevant review process.

Our committees reacted favorably to the recommendation that we offer confidential premembership consulting reviews to prospective members. In the past, a number of firms have arranged something similar on their own before joining the section, often in the form of an inspection. We are still working out the details, but it is certain that we shall soon offer consulting reviews as a service of the section.

Your suggestion for a peer review barter bank has also stimulated us to action. We see some real obstacles to a formal barter system, and are unable to implement it. We could not in good faith assure a new member that its personnel would be assigned to a review team within a certain time period. However, we plan to mention the possibility, point out the opportunity to conduct firm-on-firm reviews, and remind prospective members that reviewers usually benefit as much as does the firm they review.

We have not decided to establish a deferred payment plan for peer reviews. Some of us believe that most prospective members already have adequate financing arrangements and that deferred payments at below-market interest rates would impose an unfair burden on members that do not participate.

We agree that the educational benefits of peer reviews should be emphasized and that regulatory or disciplinary aspects are generally less important. After five years of conducting reviews we have not instituted sanctioning proceedings against a single firm. It is unlikely that we shall unless we are confronted with defiance or with

a firm's lack of cooperation in adopting the corrective measures the Peer Review Committee considers necessary.

The Peer Review Committee plans to continue its efforts to reduce peer review costs, and, as noted in the preceding section, we hope to develop an effective publicity program about the benefits of peer review as an element of quality practice that is important to firms, to clients, and to users of financial statements.

Member Services

Our new Member Services Committee, composed mostly of able and dedicated alumni of our other PCPS committees, is reviewing all of your suggestions and others we added. The MSC will establish task forces to work with other AICPA divisions to develop services that would not duplicate existing services but that would be particularly useful to PCPS firms of various sizes. Though there may be some problems in using the talents and resources of other divisions without appearing to shortchange nonmember firms, we are prepared to address those problems directly and creatively.

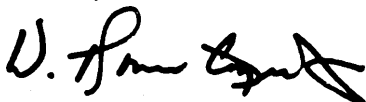
Our Member Consultation Service, scheduled to start this summer, should be especially useful when a firm develops an opportunity to serve a client in a field with which it is not familiar. The service will put the firm in touch with others who are experienced in that field and who have volunteered to consult with member firms. In addition to providing a valuable service to members, it will contribute to the PCPS's first objective—quality service to private companies.

Advocacy

In response to the report, our Technical Issues Committee is currently developing a program to increase the section's advocacy effectiveness. When the TIC makes its report, the Executive Committee will add its own ideas. We hope the result will be a more visible and effective program of technical and professional advocacy on behalf of the CPA firms that serve private companies.

The report of your committee has provided many constructive and valuable ideas for strengthening the Private Companies Practice Section and for helping it toward the first objective that Council set for it—to improve the quality of CPA firm services to private companies. On behalf of the PCPS committees, I thank you and your committee for all you have done.

Sincerely,



W. Thomas Cooper, Jr., *Chairman*
PCPS Executive Committee
Division for CPA Firms

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