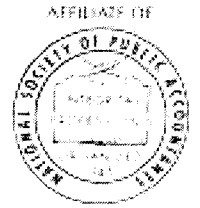


HAWAII ASSOCIATION OF PUBLIC ACCOUNTANTS

Organized August 7, 1943
P.O. BOX 61043
HONOLULU, HAWAII 96839



January 19, 2010

Chairperson Doreen Griffith and Members
State of Hawaii Board of Public Accountancy
P.O. Box 3469
Honolulu, Hawaii 96801-3469

RE: 2007 and 2008 CPA Temporary Permits to Practice

Dear Chair Griffith and Members:

The Hawaii Association of Public Accountants (HAPA) conducted a study to assess the demand and process involved with the issuance of temporary CPA permits to out-of-state CPAs during 2007 and 2008. The study was based upon temporary permit information provided to HAPA by the Department of Commerce and Consumer Affairs (DCCA) in response to our request. As noted below, the results of this study were not what we expected, and, in some cases, reflect poorly on the CPA profession as a whole.

The following are HAPA's findings and requests for action by the Board of Public Accountancy.

Summary of Findings:

The study revealed what HAPA regards as three systemic problems which need to be addressed in considering CPA "no notice, no fees" mobility legislation in Hawaii as currently advocated by the Hawaii Accountants Coalition and the Hawaii Society of Certified Public Accountants (HSCPA):

- **Non-compliance with Hawaii tax laws:** Approximately 70% of outside CPA firms whose owners and/or employees obtained a temporary permit to practice in Hawaii did not obtain Hawaii General Excise Tax (GET) license numbers.

Without the GET license numbers, the firms would not have been able to pay Hawaii General Excise taxes on their Hawaii source income. This also raises serious questions whether the firms and their owners and employees filed income tax returns and paid taxes due on Hawaii source income.

- **Non-compliance with Hawaii business registration requirements:** Of the outside CPA firms who did not obtain Hawaii GET numbers, none of those sampled had registered to do business with the Department of Commerce and Consumer Affairs as required by Hawaii laws.
- **Non-compliance with statutory definition of Incidental Practice:** Many of the applicants receiving temporary permits to practice appear to be ineligible for temporary permits under the definitions of Incidental Practice contained in Hawaii Revised Statutes §466-7(c) and Hawaii Administrative Rules §16-71-10.

Action Requested:

HAPA requests that the Board of Public Accountancy investigate each of the above findings, take appropriate action, and inform HAPA of the Board's findings and actions taken.

Discussion of Findings:

Non-Compliance with Hawaii Tax Laws:

As described in more detail in the attached letter dated December 16, 2009 to the State of Hawaii Director of Taxation, Kurt Kawafuchi, HAPA found that approximately 70% of out-of-state CPA firms had not obtained Hawaii GET license numbers. The redacted documents upon which we based our study did not provide sufficient information to determine whether the firm owners and/or employees who received temporary individual permits to practice in Hawaii filed and paid their Hawaii individual income tax obligations. The failure of out-of-state CPA firms to obtain GET licenses, however, raises questions whether the firms as well as the individual temporary permit holders paid their Hawaii taxes. If they did not file and pay, then local CPA firms and their employees are at a competitive disadvantage in the Hawaii market.

The failure to follow Hawaii tax laws raises consumer protection questions regarding the quality of advice out-of-state CPA firms are providing to their Hawaii clients. We wish to emphasize that failure of an out-of-state CPA firm to obtain a Hawaii GET license number greatly impairs the ability of the Hawaii Department of Taxation to identify and collect any taxes owed by out-of-state practitioners.

Non-Compliance with Hawaii Business Registration Requirements:

Using the list of firms with no Hawaii GET license numbers (see attachment to letter to Director Kawafuchi), we sampled to obtain an indication of compliance with Hawaii business registration requirements using the DCCA Business Registration Division website.¹ None of the sampled firms on the "no GET list" showed up as having registered to do business in Hawaii as required by Hawaii laws. The failure of out-of-state CPA firms to register to do business in Hawaii fails to inform the public of who is authorized to do business in the State of Hawaii, and the form of entity and other information concerning out-of-state CPA firms.

Incidental Practice:

As you know, a certified public accountant licensed in another state may apply for a temporary permit to practice in Hawaii for work incidental to their mainland practice if they meet certain requirements under Hawaii Revised Statutes §466-7(c) and Hawaii Administrative Rules (HAR) §16-71-10. HAR §16-71-10 describes "incidental practice" as follows:

§16-71-10 Incidental to person's practice in such other state or country.
The phrase "incidental to the person's practice in such other state or country" used in section 466-7(c)(4), HRS, shall mean services rendered in this State by a non-licensee for work performed for a client outside the State such as the audit of a Hawaii subsidiary of an out-of-state parent corporation, or an audit of a Hawaii branch or division of an out-of-state partnership, joint venture, or individual proprietorship. [Eff 5/12/78; am and ren §16-71-10, 6/25/81; am and comp 6/8/84; am and comp 10/23/87; am and comp 2/22/94; comp 6/3/95; comp 1/22/01] (Auth: HRS §466-4) (Imp: HRS §466-7)

¹ The address for the website used for this limited test is <http://hbe.ehawaii.gov/documents/search.html>.

In reviewing redacted copies of approved temporary permit applications, however, HAPA noted that temporary permits were granted to those who did not meet the "incidental practice" requirement. The following is a partial list of the explanations of incidental practice from the applicants in support of their applications for temporary permits:

- The Hawaii engagement is not material to the firm's overall revenues (and is therefore incidental).
- No new Hawaii clients will be solicited while performing the Hawaii engagement.
- The engagement requires special expertise that is not otherwise available in Hawaii. Examples of "special expertise" included, but are not limited to, the following:
 - A-133 audits and A-133 HUD audits.
 - Audits of Association of Apartment Owners.
 - Audits of a securities broker/dealer registered with the SEC.
 - Audits of Japanese owned subsidiaries requiring fluency in Japanese.
 - Audits of Medicare and Medicaid Services.
 - Supervision of auto parts physical inventories.
 - Litigation support for the mediation of a dispute over residential construction costs.
 - Audits of Pension Plans, 401(k) Plans, and ESOP Plans.
 - Audits of Union employee benefit plans.
 - Type 1 and 2 SAS 70 audits.

Most, if not all of this type of work, is already performed by Hawaii CPA firms and we do not consider this as work requiring "special expertise" that is not available from Hawaii-licensed CPAs. This takes away work and jobs for Hawaii-licensed CPAs. In our opinion, the above explanations do not meet the definition of "incidental practice".

- A number of other ownership-related justifications were given as to why an out-of-state CPA needs a temporary permit to practice in Hawaii. For example, an owner of one unit in a condominium project is a client of an out-of-state CPA firm, therefore, that out-of-state CPA firm should perform the annual audit of the related association of condominium owners. HAPA regards this justification of "incidental practice" as absurd.

Some of the approved application packets contained a letter from the Board of Public Accountancy to the applicant which stated, "Once a temporary permit has expired, the practitioner must obtain a Hawaii permit to practice public accountancy in Hawaii." Nevertheless, we noted a number of applicants paid fees for and received several (more than one) temporary permits in each year. This starts looking like a permanent permit to practice without going through the necessary application process.

After reviewing the application packets provided, HAPA was left with the impression that the applicants were allowed considerable latitude in tailoring the definition of "incidental practice" to meet their circumstances. It also appears that the Board is not following the temporary permit requirements under the Hawaii law and administrative rules.

Other Anomalies:

In copies of all approved applications provided to us, "OK" was handwritten on a space adjacent to the line labeled "Board" near the bottom of the applications. HAPA representatives who attended Board meetings in 2007 and 2008 cannot recall the Board ever reporting on reviewing and approving individual applications for temporary permits to practice during the course of the Board's public meetings or in any of its minutes of meetings. HAPA considers this significant because some of the approved applications appeared on their face to be nonsensical, incomplete, or late. Some of the anomalies noted include:

- The incidental practice line on the approved application form is blank.

- One partner in an international accounting firm received several temporary permits to practice. His cover letters accompanying his approved applications stated that he was going to perform work on captive insurance companies. Additional documentation in some of his related application packets, however, indicated that his work would actually be on Hawaii clients in industries other than insurance.

When viewed collectively, it is unclear to what degree members of the Board of Public Accountancy actually reviewed the applications. HAPA would appreciate receiving clarification as to what the Board's procedures are for reviewing and approving temporary permits to practice.

General Comments:

Our findings were not what we expected. More out-of-state individuals received temporary permits to practice than we expected. Moreover, temporary permits were issued to individuals employed by or owning a cross section of CPA firms, both large and small. In addition, we did not note evidence that processing of temporary permit applications were needlessly delayed by actions of the Hawaii Board or the DCCA. Instead, we noted in a few instances that the Boards of Accountancy for other jurisdictions occasionally were to blame because they were slow in providing a letter or other certification indicating that the applicant was in good standing. This, in turn, delayed issuance of a few temporary permits to practice.

Problems with tax compliance and business registration requirements surprised us. Frankly, we expected CPA firms and their owners and/or employees would follow Hawaii tax laws and pay Hawaii taxes on their Hawaii source income. The results of HAPA's study is an embarrassment to all CPAs. Without formally incorporating GET numbers, business registration, and income tax filing into the temporary permit application process, we believe the Hawaii Department of Taxation will have a difficult time identifying what out-of-state CPAs and CPA firms are failing to pay their fair share of Hawaii taxes.

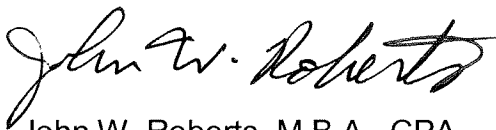
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We were also surprised with the problems in defining and applying a standard definition of "incidental practice". Since "incidental practice" was one of the reasons given in the past by the HSCPA as a reason for CPA mobility, more work needs to be done before CPA mobility legislation can be adopted in a manner that protects Hawaii consumers and is fair and equitable to Hawaii CPAs.

HAPA believes application packets or files for Hawaii temporary permits to practice contain a wealth of information that will help the Board identify and anticipate potential problems with CPA mobility before attempting to implement CPA "no notice, no fees" mobility legislation. Again, HAPA requests a review and action by the Board on the above concerns regarding temporary CPA permits granted to out-of-state CPAs.

Thank you for your consideration of the above. We look forward to hearing from you regarding the results of your own investigation.

Very truly yours,



John W. Roberts, M.B.A., CPA
HAPA State President

Enclosure: Copy of letter to the Director of Taxation, Kurt Kawafuchi,
dated December 16, 2009

cc: The Honorable Senator Colleen Hanabusa (without detailed portion of study)
The Honorable Senator Rosalyn H. Baker (without detailed portion of study)
The Honorable Senator Donna Mercado Kim (without detailed portion of study)
The Honorable Representative Calvin Say (without detailed portion of study)
The Honorable Representative Robert N. Herkes (without detailed portion of study)
The Honorable Representative Marcus R. Oshiro (without detailed portion of study)
The Honorable Representative Isaac W. Choy (without detailed portion of study)
Director Lawrence Reifurth, Department of Commerce and Consumer Affairs
(with detailed portion of study)