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SECURITIES AND EXCHANGE COMMISSION

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Form 19b-4

Proposed Rule Changes

By

Public Company Accounting Oversight Board

In accordance with Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of the Proposed Rule Change

(a) Pursuant to the provisions of Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") is filing with the Securities and Exchange Commission ("SEC" or "Commission") proposed rule changes consisting of new Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*, an amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*, and an amendment to the Board's interim independence standards. The proposed rule changes are attached as Exhibit A to this rule filing.

(b) The proposed rule changes will have a direct effect on Rule 3523 because they will amend that rule. As amended, Rule 3523 will no longer apply to the provision of tax services to persons in financial oversight roles during the portion of the audit period that precedes the professional engagement period. The proposed rule changes will also have a direct effect on the Board's interim independence standards by superseding *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* ("ISB No. 1"), ISB Interpretation 00-1, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant*, and ISB Interpretation 00-2, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant, An Amendment of Interpretation 00-1*.

(c) PCAOB-2005-02, Ethics and Independence Rules Concerning Independence, Tax Services and Contingent Fees (August 2, 2005); PCAOB-2005-02, Amendment No. 1, Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees (November 23, 2005); PCAOB-2006-01, Amendment No. 2 to Rule Filings with Respect to the PCAOB's Proposed Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees (March 28, 2006); PCAOB-2006-02, Implementation Schedule for Certain Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees (October 31, 2006); PCAOB-2007-01, Implementation Schedule for Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles (April 3, 2007); PCAOB-2007-03, Implementation Schedule for Rule 3523 (July 24, 2007); PCAOB-2008-02, Implementation Schedule for Rule 3523 (April 22, 2008).

2. Procedures of the Board

(a) The Board approved the proposed rule changes, and authorized them for filing with the SEC, at its open meeting on April 22, 2008. No other action by the Board is necessary for the filing of the proposed rule changes.

(b) Questions regarding this rule filing may be directed to Bella Rivshin, Associate Chief Auditor (202-207-9180; rivshinb@pcaobus.org) or Jacob Lesser, Associate General Counsel (202-207-9284; lesserj@pcaobus.org).

3. Board's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

(a) Purpose

Section 103(a) of the Act directs the Board, by rule, to establish "ethics standards to be used by registered public accounting firms in the preparation and issuance of audit reports, as required by th[e] Act or the rules of the Commission, or as may be necessary or appropriate in the public interest or for the protection of investors." Moreover, Section 103(b) of the Act directs the Board to establish such rules on auditor independence "as may be necessary or appropriate in the public interest or for the protection of investors, to implement, or as authorized under, Title II of th[e] Act."

As discussed more fully in Exhibit 3, the Board adopted Rule 3526, *Communication with Audit Committees Concerning Independence*, because it believed that the accounting firm should discuss with the audit committee before accepting an initial engagement pursuant to the standards of the PCAOB any relationships the accounting firm has with the issuer that may reasonably be thought to bear on its independence. The proposed rule is intended to build on the communication requirements in ISB No. 1 and provide the audit committee with information – including information about the firm's relationships with persons in financial reporting oversight roles at the company – that may be important to its determination about whether to hire the firm as the company's auditor. The rule also requires a registered firm on at least an annual basis after becoming the issuer's auditor to make a similar communication and also affirm to the audit committee of the issuer, in writing, that the firm is independent. The

Board intends for these communications to provide the audit committee with sufficient information to understand how a particular relationship might affect independence and to foster a robust discussion between the firm and the audit committee. The rule also includes a new requirement for the firm to document the substance of its discussion with the audit committee.

Also, as discussed more fully in Exhibit 3, the Board adopted amendments to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*, to exclude the portion of the audit period that precedes the beginning of the professional engagement period. The Board believes that it is not necessary for the rule to restrict the provision of tax services during the portion of the audit period that precedes the professional engagement period. The Board also added a note to Rule 3523 that states that in an engagement for an audit client whose financial statements for the first time will be required to be audited pursuant to the standards of the PCAOB, the provision of tax services to persons covered by Rule 3523 before the earlier of the date that the firm (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.

The proposed rule changes also amend the PCAOB interim independence standards because Rule 3526 will supersede the Board's interim independence requirement, *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees*, and two related interpretations.

(b) Statutory Basis

The statutory basis for the proposed rules is Title I of the Act.

4. Board's Statement on Burden on Competition

The Board does not believe that the proposed rule changes will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule changes would apply equally to all registered public accounting firms.

5. Board's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The Board released the proposed rules for public comment on July 24, 2007. See Exhibit 2(a)(A). The Board received 16 written comment letters relating to its proposed rule changes. See Exhibits 2(a)(B) and 2(a)(C).

The Board has carefully considered all comments it has received. In response to the written comments received, the Board has clarified and modified certain aspects of the proposed rule changes. The Board's response to the comments it received and the changes made to the rules in response to these comments are summarized in Exhibit 3 to this filing.

6. Extension of Time Period for Commission Action

The Board does not consent to an extension of the time period specified in Section 19(b)(2) of the Securities Exchange Act of 1934.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Board or of the Commission

Not applicable.

9. Exhibits

Exhibit A – Text of the Proposed Rules

Exhibit 1 – Form of Notice of Proposed Rule for Publication in the Federal Register.

Exhibit 2(a)(A) – PCAOB Release No. 2007-008 (July 24, 2007)

Exhibit 2(a)(B) – Alphabetical List of Comments

Exhibit 2(a)(C) – Written comments on the rules proposed in PCAOB Release No. 2007-008

Exhibit 3 – PCAOB Release No. 2008-003 (April 22, 2008)

10. Signatures

Pursuant to the requirements of the Act and the Securities Exchange Act of 1934, as amended, the Board has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Public Company Accounting Oversight Board

By: 
J. Gordon Seymour
General Counsel
and Secretary

Date: April 24, 2008

Exhibit A – Text of the Proposed Rules

Language deleted by the proposed rule changes is set forth in brackets.
Language that is added is underlined.

RULES OF THE BOARD

* * *

SECTION 3. PROFESSIONAL STANDARDS

* * *

Part 5 – Ethics

* * *

Subpart I – Independence

* * *

Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles

A registered public accounting firm is not independent of its audit client if the firm, or any affiliate of the firm, during the [audit and] professional engagement period provides any tax service to a person in a financial reporting oversight role at the audit client, or an immediate family member of such person, unless –

(a) the person is in a financial reporting oversight role at the audit client only because he or she serves as a member of the board of directors or similar management or governing body of the audit client;

(b) the person is in a financial reporting oversight role at the audit client only because of the person's relationship to an affiliate of the entity being audited

–

(1) whose financial statements are not material to the consolidated financial statements of the entity being audited; or

(2) whose financial statements are audited by an auditor other than the firm or an associated person of the firm; or

(c) the person was not in a financial reporting oversight role at the audit client before a hiring, promotion, or other change in employment event and the tax services are –

(1) provided pursuant to an engagement in process before the hiring, promotion, or other change in employment event; and

(2) completed on or before 180 days after the hiring or promotion event.

Note: In an engagement for an audit client whose financial statements for the first time will be required to be audited pursuant to the standards of the PCAOB, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.

* * *

Rule 3526. Communication with Audit Committees Concerning Independence

A registered public accounting firm must –

(a) prior to accepting an initial engagement pursuant to the standards of the PCAOB –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client or persons in financial reporting oversight roles at the potential audit client that, as of the date of the communication, may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (a)(1) on the independence of the registered public accounting firm, should it be appointed the issuer's auditor; and

(3) document the substance of its discussion with the audit committee of the issuer.

(b) at least annually with respect to each of its issuer audit clients –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in financial reporting oversight roles at the audit client that, as of the date of the communication, may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (b)(1) on the independence of the registered public accounting firm;

(3) affirm to the audit committee of the issuer, in writing, that, as of the date of the communication, the registered public accounting firm is independent in compliance with Rule 3520; and

(4) document the substance of its discussion with the audit committee of the issuer.

Amendment to PCAOB Interim Independence Standards

Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees* ("ISB Standard No. 1"), ISB Interpretation 00-1, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant*, and ISB Interpretation 00-2, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant, An Amendment of Interpretation 00-1*, are superseded by Rule 3526.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. PCAOB-2008-03)

[Date]

Public Company Accounting Oversight Board; Notice of Filing of Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence, Amendment to Interim Independence Standards, and Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles.

Pursuant to Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), notice is hereby given that on April 24, 2008, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission") the proposed rule changes described in items I, II, and III below, which items have been prepared by the Board. The Commission is publishing this notice to solicit comments on the proposed rules from interested persons.

I. Board's Statement of the Terms of Substance of the Proposed Rule Change

On April 22, 2008, the Board adopted Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*, an amendment to the Board's Interim Independence Standards, and an amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*. The proposed rule change text is set out below. Language deleted by the amendment to Rule 3523 is in brackets. Language that is added by the amendment to Rule 3523 is underlined.

RULES OF THE BOARD

* * *

SECTION 3. PROFESSIONAL STANDARDS

* * *

Part 5 – Ethics

* * *

Subpart I – Independence

* * *

Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles

A registered public accounting firm is not independent of its audit client if the firm, or any affiliate of the firm, during the [audit and] professional engagement period provides any tax service to a person in a financial reporting oversight role at the audit client, or an immediate family member of such person, unless –

(a) the person is in a financial reporting oversight role at the audit client only because he or she serves as a member of the board of directors or similar management or governing body of the audit client;

(b) the person is in a financial reporting oversight role at the audit client only because of the person's relationship to an affiliate of the entity being audited
–

(1) whose financial statements are not material to the consolidated financial statements of the entity being audited; or

(2) whose financial statements are audited by an auditor other than the firm or an associated person of the firm; or

(c) the person was not in a financial reporting oversight role at the audit client before a hiring, promotion, or other change in employment event and the tax services are –

(1) provided pursuant to an engagement in process before the hiring, promotion, or other change in employment event; and

(2) completed on or before 180 days after the hiring or promotion event.

Note: In an engagement for an audit client whose financial statements for the first time will be required to be audited pursuant to the standards of the PCAOB, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.

* * *

Rule 3526. Communication with Audit Committees Concerning Independence

A registered public accounting firm must –

(a) prior to accepting an initial engagement pursuant to the standards of the PCAOB –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client or persons in financial reporting oversight roles at the potential audit client that, as of the date of the communication, may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (a)(1) on the independence of the registered public accounting firm, should it be appointed the issuer's auditor; and

(3) document the substance of its discussion with the audit committee of the issuer.

(b) at least annually with respect to each of its issuer audit clients –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in financial reporting oversight roles at the audit client that, as of the date of the communication, may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (b)(1) on the independence of the registered public accounting firm;

(3) affirm to the audit committee of the issuer, in writing, that, as of the date of the communication, the registered public accounting firm is independent in compliance with Rule 3520; and

(4) document the substance of its discussion with the audit committee of the issuer.

Amendment to PCAOB Interim Independence Standards

Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees* ("ISB Standard No. 1"), ISB Interpretation 00-1, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant*, and ISB Interpretation 00-2, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant, An Amendment of Interpretation 00-1*, are superseded by Rule 3526.

II. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Board included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rules. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Board's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

Section 103(a) of the Act directs the Board, by rule, to establish "ethics standards to be used by registered public accounting firms in the preparation and issuance of audit reports, as required by th[e] Act or the rules of the Commission,

or as may be necessary or appropriate in the public interest or for the protection of investors." Moreover, Section 103(b) of the Act directs the Board to establish such rules on auditor independence "as may be necessary or appropriate in the public interest or for the protection of investors, to implement, or as authorized under, Title II of th[e] Act."

As discussed more fully in Exhibit 3, the Board adopted Rule 3526, *Communication with Audit Committees Concerning Independence*, because it believed that the accounting firm should discuss with the audit committee before accepting an initial engagement pursuant to the standards of the PCAOB any relationships the accounting firm has with the issuer that may reasonably be thought to bear on its independence. The rule is intended to build on the communication requirements in *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* ("ISB No. 1") and provide the audit committee with information – including information about the firm's relationships with persons in financial reporting oversight roles ("FROR") at the company – that may be important to its determination about whether to hire the firm as the company's auditor. The rule also requires a registered firm on at least an annual basis after becoming the issuer's auditor to make a similar communication and also affirm to the audit committee of the issuer, in writing, that the firm is independent. The Board intends for these communications to provide the audit committee with sufficient information to understand how a particular relationship might affect independence and to foster a robust discussion between the firm and the audit committee. The rule also includes a

new requirement for the firm to document the substance of its discussion with the audit committee.

Also, as discussed more fully in Exhibit 3, the Board adopted amendments to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*, to exclude the portion of the audit period that precedes the beginning of the professional engagement period. The Board believes that it is not necessary for the rule to restrict the provision of tax services during the portion of the audit period that precedes the professional engagement period. The Board also added a note to Rule 3523 that states that in an engagement for an audit client whose financial statements for the first time will be required to be audited pursuant to the standards of the PCAOB, the provision of tax services to persons covered by Rule 3523 before the earlier of the date that the firm (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.

The proposed rule changes also amend the PCAOB interim independence standards because Rule 3526 will supersede the Board's interim independence requirement, ISB No. 1, and two related interpretations.

(b) Statutory Basis

The statutory basis for the proposed rule is Title I of the Act.

B. Board's Statement on Burden on Competition

The Board does not believe that the proposed rule changes will result in any burden on competition that is not necessary or appropriate in furtherance of

the purposes of the Act. The proposed rule changes would apply equally to all registered public accounting firms.

C. Board's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The Board released the proposed rules for public comment in PCAOB Release No. 2007-008 (July 24, 2007). The Board received 16 written comments. A copy of PCAOB Release No. 2007-008 and the comment letters received in response to the PCAOB's request for comment are available on the PCAOB's web site at www.pcaobus.org. The Board has carefully considered all comments it has received. In response to the written comments received, the Board has clarified and modified certain aspects of the proposed rule change, as discussed below.

Rule 3526. Communication with Audit Committees Concerning Independence

Under Section 301 of the Act, "[t]he audit committee of each issuer, in its capacity as a committee of the board of directors, shall be directly responsible for the appointment, compensation, and oversight of the work of any registered public accounting firm employed by that issuer...for the purpose of preparing or issuing an audit report or related work...."^{1/} PCAOB interim independence standards require the auditor to provide certain information to the audit committee about independence that could assist the audit committee in fulfilling

^{1/} The SEC has implemented this provision by adopting rules directing the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance with the audit committee requirements mandated by the Act.

these oversight responsibilities. Specifically, ISB No. 1 requires, among other things, firms to disclose at least annually to the audit committee all relationships between the auditor and its related entities and the company and its related entities that, in the auditor's professional judgment, may reasonably be thought to bear on the auditor's independence. ISB No. 1 does not, however, require the firm to provide information to the audit committee about the firm's independence in connection with *becoming* the issuer's auditor (*i.e.*, before the person or firm becomes the issuer's auditor).

As discussed in the proposing release, the Board proposed Rule 3526 because it believed that the accounting firm should discuss with the audit committee before accepting an initial engagement pursuant to the standards of the PCAOB any relationships the accounting firm has with the issuer that may reasonably be thought to bear on its independence. The proposed rule was intended to build on the communication requirements in ISB No. 1 and provide the audit committee with information – including information about the firm's relationships with persons in FRORs at the company – that may be important to its determination about whether to hire the firm as the company's auditor. The Board also proposed to include in the rule a new requirement for the firm to document the substance of its discussion with the audit committee.

All commenters were generally in favor of the Board adopting the proposed rule, and, as discussed more fully below, some recommended modifications. Commenters stated that Rule 3526 would assist audit committees in fulfilling their responsibilities and would aid them in their decision-making

process. After carefully considering the comments, the Board is adopting Rule 3526 with one modification, as described below. If approved by the SEC, Rule 3526 will supersede ISB No. 1 and two related interpretations.^{2/}

Scope of the Required Communication

The Board proposed in Rule 3526(a) to require the registered firm, prior to accepting an initial engagement pursuant to the standards of the PCAOB, to describe in writing to the audit committee^{3/} all relationships between the

^{2/} ISB Interpretation 00-1, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant*, and ISB Interpretation 00-2, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant, An Amendment of Interpretation 00-1*. The interpretations state that the responsibility to comply with ISB No. 1 rests solely with the primary auditor, but that the primary auditor should include in its report to the audit committee all of its relationships and those of its domestic and foreign associated firms that could reasonably bear on the independence of the primary auditor. Under these interpretations, if the primary auditor is relying on the work of secondary auditors not associated with the primary auditor's firm, the report of the primary auditor should either describe any such secondary auditors' relationships, or it should state that it does not do so. The treatment of secondary auditors under Rule 3526 will be similar to the treatment of secondary auditors under ISB No. 1 and the two interpretations. Secondary auditors will not need to comply with Rule 3526, but the primary auditor will need to disclose to the audit committee any relationships of the firm's affiliates that could reasonably be thought to bear on the independence of the primary auditor. As under ISB No. 1 and the related interpretations, the scope of any communications about secondary auditors under Rule 3526 should be clear to the audit committee. Accordingly, the Board expects the primary auditor's report to either include any covered relationships of any secondary auditors not affiliated with the firm or state that it does not do so. One commenter recommended that the Board consider providing an exemption for secondary auditors. Because the rule does not require communications by secondary auditors, an exemption is not necessary.

^{3/} One commenter recommended the Board provide guidance in situations in which an issuer does not have an audit committee. Under Section 2(a)(3) of the Act, "[t]he term 'audit committee' means – (A) a committee (or equivalent body) established by and amongst the board of directors of an issuer for the purpose of overseeing the accounting and financial reporting processes of

accounting firm or any affiliates of the firm^{4/} and the potential audit client or persons in FRORs at the potential audit client that may reasonably be thought to bear on independence. The Board also proposed to require the firm to discuss with the audit committee the potential effects of those relationships on the firm's independence. In Rule 3526(b), the Board proposed to require a registered firm on at least an annual basis after becoming the issuer's auditor to provide the same information described above and also affirm to the audit committee of the issuer, in writing, that the firm is independent in compliance with Rule 3520, *Auditor Independence*.^{5/} As described in the proposing release, the Board intended for these communications to provide the audit committee with sufficient information to understand how a particular relationship might affect independence and to foster a robust discussion between the firm and the audit committee.

the issuer and audits of the financial statements of the issuer; and (B) if no such committee exists with respect to an issuer, the entire board of directors of the issuer." Accordingly, under Rule 3526, if an audit client does not have an audit committee, the auditor would be required to make the communications to the entire board of directors.

Additionally, one commenter recommended that audit committees provide better disclosure, through the proxy, when approving non-audit services performed by the auditor. The commenter stated that providing this type of transparency will permit investors a greater ability to evaluate audit committee's fiduciary performance of shareholders. The Board does not have statutory authority to require disclosure by audit committees.

^{4/} One commenter recommended that the Board adopt a definition of affiliate of the firm. This term is already defined in Rule 3501.

^{5/} Rule 3520 states that a registered public accounting firm and its associated persons must be independent of the firm's audit client throughout the audit and professional engagement period.

Commenters generally believed that the scope of the required communications was appropriate. Several commenters noted that, to a large extent, firms are already making the kinds of communications that would be required by proposed Rule 3526. One commenter acknowledged, however, that existing communications between the firm and a potential new audit client do not include the disclosure of tax services to a person in a FROR or his or her immediate family member. Additionally, some registered firms noted that communications regarding the auditor's independence currently vary in content and timing and may, in some instances, occur only orally.

Most commenters did not believe that it was necessary for the Board to expand the scope of the required communication to include any additional matters. One commenter, however, recommended requiring the firm to confirm its independence in writing to the audit committee prior to accepting an initial engagement. Another commenter recommended revising Rule 3526(a) to require the firm to make the communications in its initial proposal to the company's audit committee.

As discussed above, the Board proposed to require firms to affirm their independence annually but did not propose a similar requirement that would apply before the firm is initially engaged as the company's auditor. Rule 3526(a) requires registered firms to make certain communications about relationships that may reasonably be thought to bear on independence before accepting an initial engagement pursuant to the standards of the PCAOB. Rather than prescribing a particular time before that point when the communications must

occur, however, the rule allows registered firms and audit committees the flexibility to make that determination. The Board understands that, in some cases, firms need time before a new engagement begins to resolve any matters that could impair their independence. If a firm were required to affirm its independence prior to accepting a new engagement, it would need to wait until it has resolved any independence issues to make the required communications. These communications are intended to assist the audit committee in fulfilling its responsibility to hire the auditor – their usefulness for that purpose may diminish if they are left until immediately before the engagement begins. Accordingly, the Board does not believe a requirement for auditors to affirm that they are independent before accepting a new engagement is appropriate.

Other commenters recommended certain exclusions from the scope of the required communications. For example, one commenter asserted that the auditor cannot be expected to know about all relationships that may reasonably be thought to bear on its independence, and recommended that the written communication to the audit committee state that the auditor's assessment is based on information provided to the auditor by the issuer. The Board does not believe that allowing auditors to include such a limitation in the communication would be appropriate. Complying with the Board's independence requirements is the responsibility of the auditor.^{6/} To fulfill this responsibility, as well as their

^{6/} Another commenter suggested that the audit committee should be able to rely on the firm to determine and resolve any independence issues, and that a requirement for the auditor to discuss these matters with the audit committee would increase the responsibilities of the audit committee with respect to independence. This commenter recommended that the Board not adopt these

related responsibility under the SEC's independence rules, auditors need to ascertain what relationships with the issuer and persons in FRORs at the issuer may reasonably be thought to bear on their independence. Moreover, some of the information the auditor must assess in order to assure its independence and that may need to be communicated under Rule 3526 – such as the firm's or its associated persons' financial interests in the audit client – can be more readily obtained by the auditor than its audit client.

Another commenter recommended that the Board exclude tax services to a person in a FROR from the required communications because the commenter believed that compliance with Rule 3523, as amended, should adequately address any independence concerns regarding such services. As discussed in the proposing release, Rule 3526 is intended to require disclosure of not only whether the firm provided any specifically prohibited services or maintained any specifically prohibited relationships, but also whether any of the firm's relationships or services may reasonably be thought to bear on independence under the SEC's general standard of auditor independence^{7/} and AU sec. 220,

requirements. As discussed above, the rule is intended to provide audit committees with information to assist them in carrying out their responsibilities to oversee the audit engagement, but auditors remain responsible for complying with the independence requirements. Nothing in the rule adds to, or otherwise modifies, the responsibilities of the audit committee.

^{7/} 17 C.F.R. § 210.2-01(b). Under that standard, an accountant is not independent if "the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant's engagement." In considering this general standard, the SEC "looks in the first instance to whether a relationship or the provision of service creates a mutual or conflicting interest between the

Independence.^{8/} Because auditors will need to consider the relevant facts and circumstances in order to make such a determination, the Board does not believe that *per se* exemptions are appropriate.

Some commenters suggested that, in certain circumstances, firms would be restricted in the information they could provide to the audit committee about relationships with persons in FRORs due to legal limitations imposed by confidentiality and privacy laws. Specifically, one commenter was concerned that the auditor would not be able to disclose to the audit committee information about tax services rendered to a person in a FROR prior to obtaining a consent from that person. Another commenter recommended that the Board address the need for obtaining such a consent in its final release, while another recommended that the Board provide an exemption in circumstances where applicable legal restrictions impede an auditor's ability to comply fully with the disclosure requirement.

Under ISB No. 1, auditors have been required to disclose to the audit committee relationships with the company and its related entities and to discuss

accountant and the audit client; places the accountant in the position of auditing his or her own work; results in the accountant acting as management or an employee of the audit client; or places the accountant in a position of being an advocate for the audit client." 17 C.F.R. § 210.2-01, preliminary note.

^{8/} AU sec. 220, *Independence*, requires that "[i]n all matters relating to the assignment, an independence in mental attitude is to be maintained by the auditor..." AU sec. 220 notes that "[i]t is of utmost importance to the profession that the general public maintain confidence in the independence of independent auditors" and that public confidence in the auditor's independence "would be impaired by evidence that independence was actually lacking, and it might also be impaired by the existence of circumstances which reasonable people might believe likely to influence independence."

the auditor's independence with the audit committee. Accordingly, the required communications could include discussion of tax or other services provided to an entity or person other than the company itself. The Board understands that firms are subject to certain confidentiality requirements in the tax context^{9/} and that other restrictions could arise outside of that context, depending on the facts and circumstances that a particular relationship presents. The Board is not, however, aware that firms have encountered difficulty in communicating with audit committees, as required by ISB No. 1 or any other professional practice standard, as a result of such privacy requirements.

As described above, Rule 3526 is a general requirement that, like ISB No. 1, requires disclosure of certain relationships that may be relevant to the audit committee's oversight of the engagement. It does not set forth a list of relationships that must always be disclosed or mandate specific information that must be communicated when disclosure is required. Rather, Rule 3526 allows firms significant flexibility to determine how to comply with the requirements to describe a covered relationship and discuss the potential effects of that relationship on the firm's independence. Accordingly, while the Board will monitor the application of the rule in this regard, it does not believe that the recommended exception is necessary or appropriate at this time.

^{9/} See 26 U.S.C. § 7216; 26 C.F.R. § 301.7216-3 (prohibiting disclosure or use of tax return information without written consent of taxpayer that meets specified requirements); 26 C.F.R. § 301.7216-1 (defining "tax return information" to mean "any information, including, but not limited to a taxpayer's name, address, or identifying number, which is furnished in any form or manner for, or in connection with, the preparation of a tax return of the taxpayer").

The Board also received several comments on its proposal not to include the words "in the auditor's professional judgment" in the rule's description of the scope of the required communications. ISB No. 1 requires disclosure of certain relationships that "in the auditor's professional judgment may reasonably be thought to bear on independence." In the proposing release, the Board explained that it believed that omitting the reference to the auditor's professional judgment would clarify the requirement by reminding auditors of the need to focus on the perceptions of reasonable third parties when making independence determinations.

Some commenters supported the proposed exclusion of the words "in the auditor's professional judgment" from Rule 3526. Other commenters, however, believed that the absence of the reference to judgment could confuse, rather than clarify, the requirement and noted that it is reasonable and appropriate for audit committees to rely on the accounting firm's judgment as to what matters should be disclosed. One of these commenters contended that this aspect of the Board's proposal is inconsistent with the Board's recent focus on the importance of the use of auditor judgment. Conversely, one commenter did not object to the absence of a reference to judgment, provided that the adopting release contain an acknowledgement that the auditor must apply judgment in determining which matters are required to be communicated to the audit committee.^{10/}

^{10/} Additionally, one commenter recommended including the reference to judgment and also referring to the SEC's general standard of auditor independence and the preliminary note to the SEC's independence rules in the proposed rule or the adopting release. Footnote 9 of the Board's adopting release refers to the general standard and the preliminary note.

As the Board explained in the proposing release, auditors will need to apply judgment to determine whether a relationship may reasonably be thought to bear on independence. After considering commenters' views, the Board continues to believe that adding specific reference to the auditor's professional judgment is unnecessary and inappropriate in this instance. While the Board agrees that auditors must exercise sound judgment in carrying out their responsibilities, it does not believe that specific reference to judgment in this rule is necessary to encourage auditors to do so. Judgment is called for in applying any reasonableness standard to particular facts and circumstances, and Rule 3526 is no different. Determining what relationships may reasonably be thought to bear on independence requires consideration of how a third party – not the auditor – would view the relationship, which is consistent with the SEC's general standard of auditor independence and AU sec. 220. A reference to "in the auditor's professional judgment" could suggest otherwise, however, and therefore could discourage the necessary analysis. Accordingly, the Board has determined not to add the phrase to Rule 3526.

Time Period Covered by Rule 3526(a)

In the proposing release, the Board solicited comment on whether the initial communication in Rule 3526(a) should be limited to relationships that existed during a particular period, and, if so, how long that period should be. Commenters provided a wide variety of recommendations in this area. Some commenters stated that the initial communication should not be limited to relationships that existed during a particular period. Some of these commenters

noted that establishing a specific period could result in arbitrary exclusion of certain relationships and recommended that the audit committee and auditor be responsible for determining the relevant time frame.

Other commenters recommended that the time period be limited to the audit and professional engagement period because, according to these commenters, the relevant relationships are those that exist currently or will continue to exist. One of these commenters stated that requiring communication of relationships that existed prior to this period would cause an unnecessary burden on the firm to identify and communicate these matters and on the audit committee to consider such information, because the firm was not subject to the auditor independence rules with respect to the audit client before the beginning of the audit and professional engagement period. One commenter recommended that the required time period should, at a minimum, be the audit period and that the rule should require auditors to consider communicating relationships that existed before that time. Finally, one commenter recommended that the time period should be no longer than two years prior to the commencement of the audit period, and two commenters recommended that the proposed rule should cover a time period of at least three years.

After considering these comments, the Board has determined that the initial communication required by Rule 3526(a) should not be limited to relationships that existed during a particular time period. While the Board agrees that a relationship that existed during the audit and professional engagement period may be more likely to bear on independence than a relationship that

ended substantially before that time, it does not believe that the passage of time is the only factor relevant to a determination of whether a relationship may reasonably be thought to bear on independence. The nature of the relationship must also be considered. For example, if the firm customized and implemented the company's financial reporting system, that relationship, depending on the circumstances, might reasonably be thought to bear on independence even if the engagement to design the system was concluded before the beginning of the audit and professional engagement period. Determining whether a particular relationship is covered by Rule 3526(a) will, therefore, depend on the relevant facts and circumstances.

The Board is making one modification to the rule in response to a comment recommending that Rule 3526 make clear that the relationships required to be disclosed are those that may reasonably be thought to bear on independence as of the date of the communication. Because the relevant relationships are those that continue to bear on independence at the time of the communication, the Board has modified the rule by adding the words "as of the date of the communication" where appropriate. This clarification should help firms distinguish relationships that are covered by the rule from those that are not.

This modification should also clarify that, if a relationship may reasonably be thought to bear on independence as of the date of the communication, it must be disclosed regardless of whether it was disclosed in a prior year. Some commenters suggested that auditors should not be required to repeat a previously made disclosure. The Board believes that an earlier disclosure may

reduce the amount of information that needs to be disclosed, but it does not obviate the need for disclosure altogether. If the nature of the relationship and the potential effects of the relationship on independence remain substantially unchanged, a reference to the earlier disclosure will generally be sufficient when disclosure is required. Moreover, as discussed above, after some amount of time, the length of which depends on the nature of the relationship, a relationship may no longer reasonably be thought to bear on independence and, therefore, would no longer need to be disclosed.

Timing of the Communications

As discussed above, the Board proposed Rule 3526(a) because it believed that auditors should communicate relevant information about independence before becoming the issuer's auditor. A few commenters expressed concern that the proposed rule could cause undue burden on private companies pursuing an initial public offering if the communication were required before the auditor accepts an engagement to assist an existing private company client in going public. According to commenters, a requirement to complete the independence assessment before the auditor could commence work related to the initial public offering might disadvantage the audit client by causing delay. One commenter stated that auditors generally begin work on the initial public offering based upon an initial review of relationships between the accounting firm and the company and complete their independence assessment before the company's registration statement is filed. This commenter suggested that the

Board reconsider the required timing of the communications in the context of an initial public offering.

After considering these comments, the Board has determined that relieving a firm whose private company audit client is pursuing an initial public offering from compliance with Rule 3526 is not necessary or appropriate. As discussed above, the rule is intended to provide audit committees with the information they need to effectively oversee the audit engagement. When a private company undertakes an initial public offering, it must, for the first time, have its financial statements audited by an auditor that is independent within the meaning of the rules of the SEC and PCAOB. Among other decisions an audit committee must make is whether to engage its existing auditor for the initial public offering or whether to retain a new auditor for that purpose. In this context, the Board believes that the communication about an existing auditor's independence – which is relevant to the existing auditor's ability to continue as the company's auditor through, and after, the initial public offering – should not be delayed until just before the registration statement is filed. Moreover, the Board believes that this evaluation will not cause an unnecessary burden because the private company is already a client of the accounting firm and therefore should already be aware of most of the relationships that would need to be communicated.

The Board also received comment on the timing of the annual communication requirement that the Board proposed in Rule 3526(b). Like ISB No. 1, proposed Rule 3526 did not specify when during the year the firm would

be required to make the annual communication.^{11/} One commenter recommended that the Board specify in Rule 3526(b) when the annual communication should take place to make sure that these critical discussions do not take place at the end of the audit engagement. The commenter recommended that the proposed rule be changed to state that firms should apply Rule 3526 as early in the audit process as practicable, preferably during the planning stage of the audit. One commenter recommended that the communication occur before substantial planning procedures commence, while another recommended that the annual communication should take place at the time the engagement letter is signed and then again near the end of the audit. Finally, one commenter recommended adding a section to Rule 3526 requiring an auditor to update the communications when he or she becomes aware of a covered, previously unknown or new relationship.

After considering these comments, the Board does not believe it is appropriate to mandate specifically when the Rule 3526(b) annual communication take place. In most cases, the communications will be more useful if they take place near the beginning of the audit process. However, by not prescribing the timing of the communication, Rule 3526(b) will allow the auditor and audit committee to determine the timing that is most appropriate in the circumstances of the particular engagement. Similarly, the Board does not

^{11/} The Board understands that, under ISB No. 1, the communication typically occurs at the end of the audit when the financial statements are issued.

believe that it is necessary for the rule to explicitly address how a firm should correct an incomplete communication.

Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles

Amendment to Rule 3523 to Exclude the Portion of the Audit Period That Precedes the Professional Engagement Period

Rule 3523, as adopted by the Board, prohibits a registered public accounting firm, or an affiliate of the firm, from providing tax services during the "audit and professional engagement period" to a person in, or an immediate family member of a person in, a FROR at the audit client. Consistent with the SEC's independence rules,^{12/} the phrase "audit and professional engagement period" is defined to include two discrete periods of time. The "audit period" is the period covered by any financial statements being audited or reviewed.^{13/} The "professional engagement period" is the period beginning when the firm either signs the initial engagement letter or begins audit procedures, whichever is earlier, and ends when either the company or the firm notifies the SEC that the company is no longer that firm's audit client.^{14/}

In circumstances in which a registered firm has been the auditor for an audit client for more than a year, the "audit period" is a subset of the "professional engagement period." However, when a registered firm accepts a new audit client, the audit period may cover a period of time before the

^{12/} 17 C.F.R. § 210.2-01(f)(5).

^{13/} Rule 3501(a)(iii)(1).

^{14/} Rule 3501(a)(iii)(2).

commencement of the professional engagement period. In such circumstances, Rule 3523, as adopted, provides that the firm is not independent of its audit client if the firm, or an affiliate of the firm, provided tax services to a person covered by Rule 3523 during the audit period but before the beginning of the professional engagement period. This aspect of the rule therefore effectively prevents a firm from accepting a new audit client if the firm, or an affiliate of the firm, provided tax services to such a person during the period covered by any financial statements to be audited or reviewed.

In preparing for implementation of the Board's tax services and independence rules, the Board decided to revisit the application of Rule 3523 to tax services provided during the audit period. As discussed above, on April 3, 2007, the Board issued a concept release to solicit comment about the possible effects on a firm's independence of providing tax services to a person covered by Rule 3523 during the portion of the audit period that precedes the beginning of the professional engagement period, and other practical consequences of applying the restrictions imposed by Rule 3523 to that portion of the audit period. After careful consideration of comments received in response to the concept release, the Board, on July 24, 2007, proposed to amend the rule to exclude the portion of the audit period that precedes the beginning of the professional engagement period.^{15/}

^{15/} See PCAOB Release No. 2007-008, which includes a discussion of the comments the Board received on the concept release.

The Board received 13 comments on the proposed amendment to Rule 3523. Almost all of the commenters supported the Board's recommendation to amend Rule 3523.^{16/} Many of these commenters reiterated their belief that the firm's independence would not be affected by the provision of tax services to a person in a FROR during the portion of the audit period that precedes the beginning of the professional engagement period. Commenters also reaffirmed their belief that, if Rule 3523 is not amended, it could adversely affect companies' ability to change auditors by limiting the companies' choice of auditors.

The Board has carefully considered these comments, as well as the comments on the concept release,^{17/} and determined to adopt the amendment to Rule 3523. The Board continues to believe that it is not necessary for the rule to

^{16/} Only one commenter on the proposed rule objected to the amendment of Rule 3523. This commenter's objection stemmed from the contention that the terms "professional engagement period" and "a person in a financial reporting role" were not defined. Definitions for "professional engagement period" and "financial reporting oversight role" are provided under Rules 3501(a)(iii)(2) and 3501(f)(i), respectively. The same commenter, while not specifically addressing the proposed amendment, also expressed concern with Rule 3523(a), which provides an exception for tax services to a person who is in a FROR only because he or she serves as a member of the Board of Directors, and, referring to the responsibilities of directors, recommended deleting this section in its entirety. This commenter also recommended that the Board eliminate Rule 3523(b), which provides an exception, under certain circumstances, for tax services to a person who is in a FROR only because of the person's relationship to an affiliate of the entity being audited. The Board does not believe that eliminating these exceptions is warranted.

^{17/} In response to the concept release, two commenters stated that Rule 3523 should not be amended to exclude the portion of the audit period that precedes the professional engagement period. These commenters believed that providing tax services to a person in a FROR during the audit period impairs independence, and suggested that audit firms may plan for a change of auditors sufficiently in advance to avoid or minimize any problems resulting from the application of the rule to the audit period.

restrict the provision of tax services during the portion of the audit period that precedes the professional engagement period. Rule 3523 relates to services provided to individuals and not the audit client that issues the financial statements subject to audit. Additionally, registered firms would remain responsible for considering the relevant facts and circumstances of a specific tax engagement and determining whether their independence is impaired under the SEC's general standard of auditor independence.^{18/}

One commenter objected to the discussion in the proposing release (and included here in the paragraph above) describing the firm's obligation to consider whether the firm's independence is impaired under the SEC's general standard of auditor independence. This commenter stated that the discussion sends a contradictory message by calling for firms to assess whether their independence is impaired despite the Board's conclusion that restrictions are unnecessary to preserve independence. The Board disagrees. As a result of the Board's amendment, firms will not be specifically prohibited by Rule 3523 from providing tax services to persons in a FROR during the portion of the audit period that precedes the professional engagement period. That does not mean, however, that such services are categorically permitted. Rather, as discussed in the proposing release, the amendment reflects the Board's belief that a more tailored approach, based on facts and circumstances and measured against the general standard of auditor independence, is preferable to a *per se* prohibition. Accordingly, as with any other service or relationship that is not specifically

^{18/} 17 C.F.R. § 210.2-01(b); see footnote 7.

prohibited by the independence rules, firms must determine whether the service or relationship impairs independence under the SEC's general standard of auditor independence.

Application of Rule 3523 to New Issuers

The Board proposed adding a note to Rule 3523 concerning the application of Rule 3523 in the context of an initial public offering in light of comments received on the concept release. The proposed note stated that, in the context of an initial public offering, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that a registered firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a firm's independence under Rule 3523. Commenters generally recommended that the Board adopt the note and encouraged the Board to consider expanding it to include other corporate life events, noting that corporate life events other than an initial public offering may also result in the need for an audit client's financial statements to be audited pursuant to the standards of the PCAOB for the first time.^{19/}

^{19/} Commenters suggested the following as examples of when an audit client's financial statements would, for the first time, need to be audited pursuant to the standards of the PCAOB – mergers, reverse mergers in which a privately-held entity merges with a public company and succeeds to the public company's reporting obligations under the Securities Exchange Act of 1934, issuance of publicly traded debt, issuance of partnership or other units, inclusion of a public company's securities in an employee benefit plan, decision by a foreign private issuer to list its securities in the United States, and companies that have greater than 500 U.S. shareholders and total assets exceeding \$10 million as of the latest fiscal year-end.

In response to these comments, the Board determined to revise the note to Rule 3523 to describe events, other than just initial public offerings, pursuant to which a company's financial statements must be audited in accordance with the standards of the PCAOB for the first time. Specifically, the Board replaced the words "[i]n the context of an initial public offering" with "[i]n an engagement for an audit client whose financial statements for the first time will be required to be audited pursuant to the standards of the PCAOB." This situation may occur when a company decides to conduct an initial public offering of its securities,^{20/} which would require the company to file, for the first time, a registration statement under the Securities Act of 1933. Additionally this situation may occur when a foreign private issuer decides to list its securities on a national securities exchange, which would require the company to register its securities, for the first time, under the Securities Exchange Act of 1934. In both cases, the company's audited financial statements would be required, for the first time, to be audited pursuant to the standards of the PCAOB.^{21/}

^{20/} The company may offer equity securities, debt securities, limited partnership interests, trust interests, or another type of securities in the initial public offering.

^{21/} The Board intends the note to Rule 3523 to describe all circumstances in which a company that was not an "issuer," as defined by the Act, becomes an issuer as a result of a corporate life event or otherwise. These circumstances include those in which a private company that was once an issuer becomes an issuer again. As long as the company was not required to have its financial statements audited pursuant to the standards of the PCAOB prior to being required to do so, the Board will consider the requirement to be a "first-time" requirement for purposes of the note.

The Board does not believe it is appropriate to list in the note the various corporate life events identified by commenters, such as mergers or acquisitions, reverse mergers or other similar transactions. The relevant factor is not the name given to a transaction or event but whether the transaction or event triggers the initial requirement for an audit pursuant to the standards of the PCAOB. For example, the surviving company in a merger or acquisition transaction may be an issuer that is already filing with the SEC financial statements required to be audited pursuant to the standards of the PCAOB. The Board did not intend the note to Rule 3523 to describe such a scenario.^{22/} By focusing on the need for a first-time audit pursuant to the standards of the PCAOB, the company and its auditors are better able to determine whether a proposed transaction or corporate life event is described by the note.

One commenter stated that, while it is easy to identify the date on which the initial engagement letter to perform an audit pursuant to the standards of the PCAOB is signed, it would be very difficult to apply the second prong of the note, which requires identification of the date that the auditor began procedures to perform an audit pursuant to the standards of the PCAOB, especially if the

^{22/} Another example is a private operating company becoming a reporting company through a reverse merger with a reporting shell company. In this scenario, even though the operating company assumes the reporting obligations of the former shell company, the surviving reporting company is the former shell company whose financial statements already were required to be audited pursuant to the standards of the PCAOB. Therefore, the note to Rule 3523 does not describe this situation.

registered firm audited the company's prior years' financial statements.^{23/} Another commenter similarly questioned whether this period begins when the auditor begins planning for the audit. The Board recognizes that, in certain circumstances, it may be difficult to identify when a continuing auditor began procedures pursuant to the standards of the PCAOB. An auditor begins procedures for purposes of Rule 3523 when he or she begins procedures, including required audit planning procedures, to update its earlier audits to conform them to the standards of the PCAOB or begins procedures on a new audit pursuant to those standards. This point in time will depend on the facts and circumstances of the particular engagement and corporate life event, rather than on any more specific triggering event that the Board could establish by rule.

Transition Periods

Rule 3523 prohibits the provision of tax services to covered persons once the professional engagement period begins. Some commenters on the concept release recommended that the Board amend Rule 3523 to allow a transition period after a company changes auditors so that the new auditor may complete any tax services in progress to any persons in FRORs affected by the issuer's

^{23/} The commenter noted that, when a company undertakes an initial public offering, it is required to include in the registration statement audited financial statements for its past three completed fiscal years. These financial statements may have previously been audited pursuant to generally accepted auditing standards ("GAAS"). The commenter was concerned that if the company does not retain a new auditor for its initial public offering, there may be a question as to whether the auditor should consider its audits of the prior years in assessing when it "began procedures" as provided under the note to Rule 3523. An auditor should not consider work already performed on previously completed GAAS audits for determining when the auditor "began procedures" because those audits were not performed pursuant to the standards of the PCAOB.

change of auditors.^{24/} Other commenters stated that tax services to persons in FRORs should, as is currently required, cease before the professional engagement period begins. The Board decided to seek further feedback on this topic in the proposing release. Specifically, the Board asked commenters to specify why they believed any transition period was necessary and how long any such transition period should be.^{25/}

The majority of commenters on this topic recommended that the Board provide for a 180-day transition period to allow an accounting firm to complete covered tax services once the professional engagement period begins. Most of these commenters stated that, since the Board has previously determined that a 180-day transition is appropriate when a person is hired or promoted into a FROR,^{26/} the Board should provide the same transition when an issuer changes its auditor. The commenters stated that, without a transition period, the person in a FROR could experience undue hardship because he or she may have to switch tax preparers in the middle of the personal tax services engagement. Additionally, some commenters stated that some accounting firms may not be able to terminate the in-process personal tax services engagements within a timeframe that would also allow them to submit their proposal for the new audit

^{24/} Rule 3523(c) provides a time-limited transition period for an auditor to complete in-progress tax services to a person that becomes a FROR at the audit client through a hiring, promotion, or other change in employment event. That transition period is unaffected by the proposed rules changes.

^{25/} See PCAOB Release 2007-008 (July 24, 2007), at 12.

^{26/} See Rule 3523(c).

engagement. Conversely, some commenters stated that they believed that the Board should not provide a transition period and that it is appropriate for the firm to cease the personal tax services before the professional engagement period begins or that a transition period should only be available on a case-by-case basis where cessation of services would cause significant hardship.^{27/}

After considering these comments, the Board does not believe that a transition period is necessary when a company changes its auditor and has determined not to amend Rule 3523 to include one. The Board adopted Rule 3523 because the provision of tax services to a person in a FROR after the accounting firm is hired as the auditor creates an unacceptable appearance that the firm lacks independence. While the Board believed a time-limited exception was warranted to accommodate persons who, through a hiring or promotion event, abruptly become covered by the rule, it does not believe that such a transition period is similarly necessary after an auditor change. In the former situation, the firm already is the issuer's auditor and has no control over whether or when the person is promoted or otherwise moved into a FROR. In contrast, the firm controls whether and when it begins a new engagement. The Board therefore believes that the firm is able to conclude, or transition to another

^{27/} Another commenter stated that Rule 3523 should be effective immediately for issuers with fiscal years ending on or after December 15, 2007, that all personal tax services in process should be allowed to continue until the filing of the applicable tax return, and that such services, along with the related fees, should be disclosed in the issuer's filings with the SEC and documented in the minutes of meetings of the audit committee.

provider, any tax services to persons in FRORs at a new audit client before beginning the engagement.^{28/}

Some commenters also encouraged the Board to consider providing a transition period for firms to complete tax services to persons who become covered by Rule 3523 as a result of a corporate life event, such as a merger, acquisition, or initial public offering. Commenters suggested that such corporate life events present conceptually similar transition issues to those related to the hiring or promotion of a person into a FROR and that Rule 3523(c) should therefore be expanded to accommodate them. Commenters also stated that the absence of transitional relief may cause unnecessary hardship for persons in FRORs whose tax return preparation work was well underway at the point of the initial public offering, merger, or acquisition.^{29/}

As discussed above, in the context of an initial public offering, the rule, as amended, makes clear that tax services provided to a person in a FROR do not impair independence as long as those tax services are concluded before the earlier of the date that the firm: (1) signed an initial engagement letter or other

^{28/} Nothing in Rule 3523 requires a firm to complete or terminate tax services to persons in FRORs at a potential audit client before submitting a proposal for a new audit engagement. Rather, the rule requires the accounting firm to complete or terminate those services by the beginning of the professional engagement period.

^{29/} The commenters further stated that, because persons in FRORs may receive tax services from a number of accounting firms, the application of the rule to the audit period may unreasonably restrict a company's ability to either continue or change auditors after a corporate life event. As discussed above, the Board has amended the rule to exclude the portion of the audit period that precedes the professional engagement period.

agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so. Auditors should have sufficient time before that date to conclude any tax services to persons that would be covered by the rule. Accordingly, the Board does not believe that the recommended transition period is necessary in the context of an initial public offering.

The Board also considered whether a transition period is necessary to allow a firm to conclude tax services to persons who become covered by the rule after a merger or acquisition. As discussed above, Rule 3523(c) already provides a transition period for a firm to conclude tax services to a person who was not in a FROR before a hiring, promotion, or other change in employment event. If a business combination results in a change of employer for a person in a FROR – from, for example, the acquired company to the acquiring company – the existing transition period in Rule 3523 would apply.^{30/} For example, if Company A acquires Company B, a person who was in a FROR at Company B would experience an "other change in employment event" if he or she became an employee of Company A in a FROR as a result of the acquisition. If such a person had been receiving tax services from Company A's registered public accounting firm pursuant to an engagement in process before the acquisition, the time-limited exception in Rule 3523(c) would apply.^{31/}

^{30/} See also *Staff Questions and Answers, Ethics and Independence Rules Concerning Independence, Tax Services and Contingent Fees* (April 3, 2007), Question and Answer No. 6, at 4-5.

^{31/} Id.

In the example above, persons in FRORs at Company A would not experience a change in employment event because they were employed by Company A both before and after the acquisition, and Rule 3523(c) would, therefore, not apply. If Company B's auditor became Company A's auditor after the acquisition (replacing Company A's auditor), Company B's auditor would have to conclude any tax services to persons in FRORs (and their immediate family members) at Company A before the start of the professional engagement period. The Board believes this is appropriate because, as discussed above, the Board does not believe that a transition period is necessary to allow a newly engaged auditor to conclude in-progress tax services to persons in FRORs at the new audit client. Accordingly, the Board has determined not to expand the existing transition period in Rule 3523(c).

Effective Date

Rule 3526 establishes new requirements for registered public accounting firms. The Board believes it is appropriate to allow a reasonable period of time for such firms to prepare internal policies and procedures and train their employees to ensure compliance with these new requirements. Accordingly, Rule 3526 will become effective, and ISB No. 1 and the related interpretations superseded, on the later of September 30, 2008, or 30 days after the date that the SEC approves the rule.

The amendment to Rule 3523 would have the effect of making permanent the Board's delay in implementing the rule as it applies to tax services provided during the period subject to audit but before the professional engagement period.

Accordingly, no transition period is necessary, and the amended rule will become effective immediately upon approval by the SEC.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Board consents, the Commission will:

- (a) by order approve such proposed rule change; or
- (b) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule is consistent with the requirements of Title I of the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule that are filed with the Commission, and all written communications relating to the proposed rule between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be

available for inspection and copying at the principal office of the PCAOB. All submissions should refer to File No. PCAOB-2008-03 and should be submitted within [] days.

By the Commission.

Secretary



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PROPOSED ETHICS AND INDEPENDENCE)	PCAOB Release No. 2007-008
RULE 3526, COMMUNICATION WITH AUDIT)	July 24, 2007
COMMITTEES CONCERNING INDEPENDENCE)	
)	PCAOB Rulemaking
PROPOSED AMENDMENT TO RULE 3523, TAX)	Docket Matter No. 017
SERVICES FOR PERSONS IN FINANCIAL)	
REPORTING OVERSIGHT ROLES)	
)	
IMPLEMENTATION SCHEDULE FOR RULE 3523)	
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)	

Summary: The Public Company Accounting Oversight Board ("PCAOB" or "Board") is proposing an ethics and independence rule, Rule 3526, *Communication with Audit Committees Concerning Independence*, that would supersede the Board's interim independence requirement, *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* ("ISB No. 1"), and two related interpretations. The Board is also proposing an amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*, and further adjusting the implementation schedule for Rule 3523 as it applies to tax services provided during the audit period. Specifically, Rule 3523 will not apply to tax services provided on or before April 30, 2008, when those services are provided during the audit period and are completed before the professional engagement period begins.

Public

Comment: Interested persons may submit written comments to the Board. Such comments should be sent to the Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, DC 20006-2803. Comments also may be submitted via e-mail to comments@pcaobus.org or through the Board's Web site at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 017 in the subject or reference line and should be received by the Board no later than 5:00 PM (EST) on September 7, 2007.



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Board

Contacts: Bella Rivshin, Associate Chief Auditor (202/207-9180; rivshinb@pcaobus.org), or Greg Scates, Deputy Chief Auditor (202/207-9114; scatesg@pcaobus.org).

* * *

I. Introduction

On July 26, 2005, the Public Company Accounting Oversight Board ("PCAOB" or "Board") adopted certain rules related to registered public accounting firms' provision of tax services to public company audit clients. As part of this rulemaking, the Board adopted Rule 3523, which provides that a registered firm, subject to certain exceptions, is not independent of an audit client if the firm, or an affiliate of the firm, provides tax services during the audit and professional engagement period to a person in, or an immediate family member of a person in, a financial reporting oversight role at an audit client. This rule was intended to address concerns related to auditor independence when auditors provide personal tax services to individuals who play a direct role in preparing the financial statements of public company audit clients. Rule 3523 was approved by the Securities and Exchange Commission ("SEC" or "Commission") on April 19, 2006.

On April 3, 2007, the Board issued a concept release to solicit comment about the possible effects on a firm's independence of providing tax services to a person covered by Rule 3523 during the portion of the audit period that precedes the beginning of the professional engagement period and other practical consequences of applying the restrictions imposed by Rule 3523 to that portion of the audit period.^{1/} The Board received 13 comment letters. Commenters included auditors, state certified public accountant societies, and one investor. The majority of the commenters recommended that the Board amend Rule 3523 to exclude the portion of the audit period that precedes the beginning of the professional engagement period.

After careful consideration of the comments received, the Board has decided to propose an amendment to Rule 3523 to exclude the portion of the audit period that precedes the beginning of the professional engagement period. However, as described below, in light of the comments received, the Board is also proposing a new independence rule that would require a registered public accounting firm to

^{1/} See PCAOB Release No. 2007-002 (April 3, 2007).



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communicate certain information as it relates to the firm's independence to the issuer's audit committee before accepting a new engagement pursuant to the standards of the PCAOB. The proposed rule would also require a registered public accounting firm to communicate certain information about its independence at least annually with respect to each of its issuer audit clients. The Board seeks comment on all aspects of these proposals.

Finally, on April 3, 2007, the Board also adjusted the implementation schedule for Rule 3523, as it applies to tax services provided during the period subject to audit but before the professional engagement period, so that the Board could revisit this aspect of the rule.^{2/} As described below, the Board is further adjusting the implementation schedule to allow sufficient time for consideration of comments received in response to this release.

II. Proposed Amendment to Rule 3523 to Exclude the Portion of the Audit Period That Precedes the Professional Engagement Period

Rule 3523 applies to registered firms in circumstances in which the firm, or an affiliate of the firm, provides or has provided tax services during the "audit and professional engagement period" to a person in, or an immediate family member of a person in, a financial reporting oversight role at an audit client. Consistent with the SEC's independence rules,^{3/} the phrase "audit and professional engagement period" is defined to include two discrete periods of time. The "audit period" is the period covered by any financial statements being audited or reviewed.^{4/} The "professional engagement period" is the period beginning when the firm either signs the initial engagement letter or begins audit procedures, whichever is earlier, and ends when either the company or the firm notifies the SEC that the company is no longer that firm's audit client.^{5/}

^{2/} See PCAOB Release No. 2007-002 (April 3, 2007), at 7. Specifically, the Board stated that Rule 3523 will not apply to tax services provided on or before July 31, 2007, when those services are provided during the audit period and are completed before the professional engagement period begins.

^{3/} 17 C.F.R. § 210.2-01(f)(5).

^{4/} Rule 3501(a)(iii)(1).

^{5/} Rule 3501(a)(iii)(2).



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In circumstances in which a registered firm has been the auditor for an audit client for more than a year, the "audit period" is a subset of the "professional engagement period." However, when a registered firm accepts a new audit client the audit period may cover a period of time before the commencement of the professional engagement period. In such circumstances, Rule 3523, as adopted, provides that the firm is not independent of its audit client if the firm, or an affiliate of the firm, provided tax services to a person covered by Rule 3523 during the audit period but before the professional engagement period. This aspect of the rule therefore effectively prevents a firm from accepting a new audit client when the firm, or an affiliate of the firm, provided tax services to such a person during the period covered by any financial statements to be audited or reviewed.

In preparing for implementation of the Board's tax services and independence rules, the Board decided to revisit the application of Rule 3523 to tax services provided during the audit period. On April 3, 2007, the Board issued a concept release to solicit comment about the possible effects on a firm's independence of providing tax services to a person covered by Rule 3523 during the portion of the audit period that precedes the beginning of the professional engagement period, and other practical consequences of applying the restrictions imposed by Rule 3523 to that portion of the audit period.

The Board received 13 comment letters on the concept release. Most commenters recommended amending Rule 3523 to exclude the portion of the audit period that precedes the professional engagement period. These commenters suggested that the accounting firm's independence would not be affected by the provision of tax services to a person in a financial reporting oversight role during the portion of the audit period that precedes the professional engagement period. Some of these commenters stated that a mutuality of interest does not exist during this time period because the accounting firm and the issuer do not have a professional audit client relationship at the time the tax services are provided to persons in financial reporting oversight roles.

All of these commenters also stated that if Rule 3523 is not amended to exclude the portion of the audit period that precedes the professional engagement period, it could adversely affect the company's ability to change auditors by limiting the company's choice of auditors. Commenters suggested that it is likely that persons in financial reporting oversight roles will use many different accounting firms for personal tax services and, therefore, finding an independent accounting firm to serve as a successor auditor could present a significant hardship for the issuer. According to one commenter, even when an issuer plans in advance to change auditors, Rule 3523, as



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currently adopted, could still create hardship for the issuer and the person in a financial reporting oversight role if the change is not planned sufficiently far in advance because many foreign tax compliance requirement dates for individuals do not follow the calendar-year cycle and also do not allow a mechanism for the extension of tax return filing deadlines.

Conversely, two of the commenters stated that Rule 3523 should not be amended to exclude the portion of the audit period that precedes the professional engagement period because they believe that providing tax services to a person in a financial reporting oversight role during the audit period impairs independence. These commenters also suggested that audit firms may plan for a change of auditors sufficiently in advance to avoid or minimize any problems resulting from the application of the rule to the audit period.

Additionally, a number of commenters recommended that even if the Board determines to exclude the portion of the audit period that precedes the professional engagement period from the scope of Rule 3523, the Board should allow a transition period for a new auditor to complete any tax services to persons in financial reporting oversight roles affected by the issuer's change of auditors in order to avoid any unnecessary hardship to such persons. Other commenters stated that tax services to persons in a financial reporting oversight role should cease before the professional engagement period begins.

After careful consideration, the Board is proposing an amendment to Rule 3523 to exclude the portion of the audit period that precedes the beginning of the professional engagement period. This would be accomplished by striking the words "audit and" from the current text of Rule 3523. The Board does not believe it is necessary to restrict the provision of tax services during the portion of the audit period that precedes the professional engagement period to preserve auditor independence. Unlike other SEC and PCAOB auditor independence rules that provide that firms are not independent if they or their affiliates have provided certain non-audit services to an audit client during the audit period,^{6/} Rule 3523 relates to services provided to

^{6/} For example, SEC auditor independence rules state that an accountant is not independent if the accountant provides, among other things, bookkeeping, management functions, or financial information system design and implementation services to an audit client at any point during the audit and professional engagement period. 17 C.F.R. § 210.2-01(c)(4). In addition, PCAOB Rule 3522, *Tax Transactions*,



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individuals and not the audit client that issues the financial statements subject to audit. Additionally, if the Board amends Rule 3523 as described, registered firms would remain responsible for considering the relevant facts and circumstances of a specific tax engagement and determining whether their independence is impaired under the SEC's general standard of independence.^{7/} The Board believes that this approach would allow for a more tailored application of the independence requirements to this area that would prohibit only those services that pose a risk, while allowing those that do not and avoid any unnecessary impediments to changing auditors.

In addition, in light of comments concerning the application of Rule 3523 in the context of an initial public offering, the Board is proposing to add a note to Rule 3523 that would state that in the context of an initial public offering, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.

Finally, the Board considered comments requesting that the Board amend Rule 3523 to include a transition period to complete covered tax services once the professional engagement period begins. At this time the Board is not convinced that such a transition period is necessary. The Board is interested in receiving additional comment, however, on the practical implications of not allowing for a transition period.^{8/}

prohibits the auditor from providing certain non-audit services to an audit client during the audit period as well as the professional engagement period.

^{7/} 17 C.F.R. § 210.2-01(b). The SEC's general standard on auditor independence treats an accountant as not independent if "the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant's engagement. In determining whether any accountant is independent, the Commission will consider all relevant circumstances, including all relationships between the accountant and the audit client, and not just those relating to reports filed with the Commission."

^{8/} The Board also considered comments requesting that the Board amend the rule to allow a transition period in various other circumstances, such as mergers and acquisitions, but has determined not to propose such amendments.



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III. Proposed Rule 3526, Communication with Audit Committees Concerning Independence

Although the concept release did not seek comment regarding audit committee communication, several commenters encouraged the Board to consider requiring additional communication between the auditor and the issuer's audit committee about matters that might bear on the auditor's independence if the Board decided to amend Rule 3523. These commenters suggested that such additional communication would assist the audit committee in assessing the auditor's independence. One commenter encouraged the Board to require the accounting firm to discuss with the audit committee all tax services provided to a person in a financial reporting oversight role during the portion of the audit period that precedes the professional engagement period, as well as any such services to be provided during the professional engagement period pursuant to the recommended transition provisions. This commenter also stated that these services should be considered by the accounting firm in conjunction with its communication under *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* ("ISB No.1"), which requires the auditor to disclose all relationships between the auditor and its related entities and the company and its related entities that may reasonably be thought to bear on the auditor's independence.^{9/} Another commenter stated that a determination of the impact of tax services to persons in a financial reporting oversight role should be left exclusively to the audit committee.

Under Section 301 of the Sarbanes-Oxley Act of 2002 ("the Act"), "[t]he audit committee of each issuer, in its capacity as a committee of the board of directors, shall be directly responsible for the appointment, compensation, and oversight of the work of any registered public accounting firm employed by that issuer...for the purpose of preparing or issuing an audit report or related work."^{10/} The Act, along with the SEC's related implementation rules, enhanced the required communication between the audit

^{9/} *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees.* ISB No. 1 is included in the Board's interim standards.

^{10/} The SEC has implemented this provision by adopting rules directing the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance with the audit committee requirements mandated by the Act.



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committee and the auditor by requiring the issuer's audit committee to pre-approve audit and non-audit services provided by the auditor.^{11/} However, the accounting firm does not have an existing requirement under SEC or PCAOB rules to provide information to the audit committee about the auditor's independence, including whether services are being provided to the issuer or any person in a financial reporting oversight role, in connection with *becoming* the issuer's auditor (i.e., *before* the person or firm becomes the issuer's auditor). While the ISB No. 1 communication is important, it typically occurs at the end of the audit when the financial statements are issued. As a result, it is not sufficient to ensure that appropriate information concerning the auditor's independence is communicated to the issuer's audit committee at the time that the audit committee is making the decision to retain the accounting firm as the issuer's auditor.

The Board believes that the accounting firm should discuss with the audit committee before accepting an initial engagement pursuant to the standards of the PCAOB any services the accounting firm has provided or is providing that may reasonably be thought to bear on independence. A requirement to communicate such information would provide the audit committee with information that may be important to its determination about whether to hire the firm as the company's auditor. Accordingly, the Board is proposing a new independence rule, Rule 3526, *Communication with Audit Committees Concerning Independence*.

The current requirement under ISB No. 1 requires the auditor to disclose to the audit committee, among other things, all relationships between the auditor and its related entities and the company and its related entities that, in the auditor's professional judgment, may reasonably be thought to bear on independence. Proposed Rule 3526 would build on that communication and require the registered public accounting firm, *prior to accepting an initial engagement* pursuant to the standards of the PCAOB, to –

1. describe, in writing, to the audit committee^{12/} of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm

^{11/} See Section 202 of the Act; 17 C.F.R. § 210.2-01(c)(7).

^{12/} Under Section 2(a)(3) of the Act, "[t]he term 'audit committee' means – (A) a committee (or equivalent body) established by and amongst the board of directors of an issuer for the purpose of overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer; and (B) if no



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and the potential audit client or persons in a financial reporting oversight role at the potential audit client that may reasonably be thought to bear on independence;

2. discuss with the audit committee of the issuer the potential effects of these relationships on the independence of the registered public accounting firm, should it be appointed the issuer's auditor; and
3. document the substance of its discussion with the audit committee of the issuer.

The registered public accounting firm would also be required on at least an annual basis after becoming the issuer's auditor to –

1. describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in a financial reporting oversight role at the audit client that may reasonably be thought to bear on independence;
2. discuss with the audit committee of the issuer the potential effects of these relationships on the independence of the registered public accounting firm;
3. affirm to the audit committee of the issuer, in writing, that the registered public accounting firm is independent in compliance with Rule 3520; and
4. document the substance of its discussion with the audit committee of the issuer.

The proposed rule would require disclosure of all relationships that may reasonably be thought to bear on independence whether those relationships existed during the period under audit or during earlier periods. In determining what relationships may reasonably be thought to bear on independence, the accounting firm would need to consider, in addition to whether the firm provided any specifically prohibited services or maintained any specifically prohibited relationships, the SEC's general standard on

such committee exists with respect to an issuer, the entire board of directors of the issuer." Accordingly, under the proposed rule, if an audit client does not have an audit committee, the auditor would be required to make the communications to the entire board of directors.



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auditor independence. Under that standard, an accountant is not independent if "the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant's engagement."^{13/} In considering this general standard, the SEC "looks in the first instance to whether a relationship or the provision of service: creates a mutual or conflicting interest between the accountant and the audit client; places the accountant in the position of auditing his or her own work; results in the accountant acting as management or an employee of the audit client; or places the accountant in a position of being an advocate for the audit client."^{14/}

Auditors would also need to consider AU sec. 220, *Independence*, in determining whether a particular relationship needs to be discussed with the audit committee. AU sec. 220 requires that "in all matters relating to the assignment, an independence in mental attitude is to be maintained by the auditor." AU sec. 220 notes that "[i]t is of utmost importance that the general public maintain confidence in the independence of independent auditors," and that public confidence in the auditor's independence "would be impaired by evidence that independence was actually lacking, and it might also be impaired by the existence of circumstances which reasonable people might believe likely to influence independence."

The proposed rule would require only those relationships that "may reasonably be thought to bear on independence" to be disclosed to the audit committee. This language is taken from ISB No. 1, and is consistent with the SEC's general standard on independence, which focuses on the perception of the "reasonable investor," and AU sec. 220, which focuses on the perceptions of "reasonable people." Unlike ISB No. 1, however, the proposed rule would not modify this basic reasonableness standard with the words "in the auditor's professional judgment." The Board believes that omitting these words will clarify the requirement by reminding auditors of the need to focus on the perceptions of reasonable third parties when making independence determinations. Auditors will, of course, need to apply professional judgment to determine what is reasonable under particular facts and circumstances.

^{13/} 17 C.F.R. § 210.2-01(b).

^{14/} 17 C.F.R. § 210.2-01, preliminary note.



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In addition, the proposed rule would describe the existing ISB No. 1 requirement to "discuss the auditor's independence with the audit committee" with more specificity. Specifically, the proposed rule would require the auditor to discuss with the audit committee of the issuer the potential effects of the relationships on the independence of the accounting firm. This articulation is intended to emphasize that the required communication should provide the audit committee with sufficient information to understand how a particular relationship might affect independence and to foster a robust discussion. The proposed rule would also add a new requirement for the firm to document the substance of its discussion with the audit committee.

Finally, if proposed Rule 3526 is adopted, it would supersede ISB No. 1 and two related interpretations – ISB Interpretation 00-1, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant*, and ISB Interpretation 00-2, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant, An Amendment of Interpretation 00-1*. The interpretations state that the responsibility to comply with ISB No. 1 rests with the primary auditor, but that the primary auditor should include in its report to the audit committee all relationships of its domestic and foreign associated firms that could reasonably bear on the independence of the primary auditor. Under these interpretations, if the primary auditor is relying on the work of secondary auditors not associated with the primary auditor's firm, the report of the primary auditor should either describe any such secondary auditors' relationships, or it should state that it does not do so. The proposed rule's treatment of secondary auditors would be similar to the treatment of secondary auditors under ISB No. 1 and the two interpretations. Specifically, secondary auditors would not need to comply with proposed Rule 3526, but the primary auditor would need to disclose to the audit committee any relationships of the firm's affiliates. Proposed Rule 3526 would not establish requirements relating to secondary auditors working on an audit that are not affiliated with the auditor of record.

The Board solicits comment on all aspects of these proposals, and in particular –

1. Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?
2. Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?
3. Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the



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audit committee? If so, what specific communications should the auditor be required to make to the audit committee?

4. To what extent if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?
5. Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why, and how long should the period be?
6. Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?

IV. Opportunity for Public Comment

The Board will seek comment for a 45-day period. Interested persons are encouraged to submit their views to the Board. Written comments should be sent to Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments also may be submitted by e-mail to comments@pcaobus.org or through the Board's Web site at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 017 in the subject or reference line and should be received by the Board no later than 5:00 PM (EST) on September 7, 2007.

The Board will carefully consider all comments received. Following the close of the comment period, the Board will determine whether to amend Rule 3523 and adopt a final rule on communication with audit committees concerning independence. Any rule amendment and final rule adopted will be submitted to the Securities and Exchange Commission for approval. Pursuant to Section 107 of the Act, proposed rules of the Board do not take effect unless approved by the Commission.

V. Adjustment of Implementation Schedule

Under the adjustment to the implementation schedule for Rule 3523 that the Board made on April 3, 2007, the Board will not apply Rule 3523 to tax services provided on or before July 31, 2007, when those services are provided during the audit period and are completed before the professional engagement period begins. The Board has determined to further adjust the implementation schedule for Rule 3523 to



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allow sufficient time for consideration of comments on this release. Specifically, the Board will not apply Rule 3523 to tax services provided on or before April 30, 2008, when those services are provided during the audit period and are completed before the professional engagement period begins.^{15/}

The PCAOB has filed this adjustment to the implementation schedule with the SEC as an immediately effective proposed rule change. The rule change became effective upon its filing with the SEC, thereby extending to April 30, 2008 the implementation date for this aspect of Rule 3523. The adjustment to the implementation schedule and related rule filing will not result in any textual changes to the Rules of the PCAOB.

* * *

On the 24 day of July, in the year 2007, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour
Secretary

July 24, 2007

^{15/} This will apply regardless of whether there is an engagement in process on July 31, 2007.



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APPENDIX 1 – Proposed Amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*

APPENDIX 2 – Proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*



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Appendix 1 – Proposed Amendment to Rule 3523

The relevant portion of the Rule, as amended, is set out below. Language deleted by this amendment is struck through. Language that is added is underlined.

RULES OF THE BOARD

* * *

SECTION 3. PROFESSIONAL STANDARDS

* * *

Part 5 – Ethics

* * *

Subpart I – Independence

* * *

Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles

A registered public accounting firm is not independent of its audit client if the firm, or any affiliate of the firm, during the ~~audit and~~ professional engagement period provides any tax service to a person in a financial reporting oversight role at the audit client, or an immediate family member of such person, unless –

(a) the person is in a financial reporting oversight role at the audit client only because he or she serves as a member of the board of directors or similar management or governing body of the audit client;

(b) the person is in a financial reporting oversight role at the audit client only because of the person's relationship to an affiliate of the entity being audited –

(1) whose financial statements are not material to the consolidated financial statements of the entity being audited; or



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(2) whose financial statements are audited by an auditor other than the firm or an associated person of the firm; or

(c) the person was not in a financial reporting oversight role at the audit client before a hiring, promotion, or other change in employment event and the tax services are –

(1) provided pursuant to an engagement in process before the hiring, promotion, or other change in employment event; and

(2) completed on or before 180 days after the hiring or promotion event.

Note: In the context of an initial public offering, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.



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Appendix 2 – Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence

RULES OF THE BOARD

* * *

SECTION 3. PROFESSIONAL STANDARDS

* * *

Part 5 – Ethics

* * *

Subpart I – Independence

* * *

Proposed Rule 3526. Communication with Audit Committees Concerning Independence

A registered public accounting firm must –

(a) prior to accepting an initial engagement pursuant to the standards of the PCAOB –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client or persons in a financial reporting oversight role at the potential audit client that may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (a)(1) on the independence of the registered public accounting firm, should it be appointed the issuer's auditor; and

(3) document the substance of its discussion with the audit committee of the issuer.



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(b) at least annually with respect to each of its issuer audit clients –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in a financial reporting oversight role at the audit client that may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (b)(1) on the independence of the registered public accounting firm;

(3) affirm to the audit committee of the issuer, in writing, that the registered public accounting firm is independent in compliance with Rule 3520; and

(4) document the substance of its discussion with the audit committee of the issuer.

**Exhibit 2(a)(B)****Alphabetical List of Comments**

American Bar Association, Linda L. Griggs, Chair of the Committee on Law & Accounting; Keith F. Higgins, Chair of the Committee on Federal Regulation of Securities

Audit Conduct, Catherine Allen

BDO Seidman, LLP

CalPERS, Russell Read, Chief Investment Officer

Center for Audit Quality, Cynthia M. Fornelli, Executive Director; Bruce P. Webb, Chair, AICPA Professional Ethics Executive Committee

Deloitte & Touche LLP

Dennis R. Beresford, Ernst & Young Executive Professor of Accounting, J. M. Tull School of Accounting, The University of Georgia

Ernst & Young LLP

Frank Gorrell

Grant Thornton LLP

KPMG LLP

National Association of State Boards of Accountancy, Wesley P. Johnson, Chair; David A. Costello, President & CEO

New York State Society of Certified Public Accountants

North Carolina State Board of Certified Public Accountant Examiners, Arthur M. Winstead, Jr., President

PricewaterhouseCoopers LLP

Texas Society of Certified Public Accountants, Sandra K. Johnigan, Chair,
Professional Standards Committee

ABA

AMERICAN BAR ASSOCIATION

**Defending Liberty
Pursuing Justice**

Section of Business Law

321 North Clark Street
Chicago, Illinois 60610
(312) 988-5588
FAX: (312) 988-5578
e-mail: businesslaw@abanet.org

September 19, 2007

via e-mail to:[**comments@pcaobus.org**](mailto:comments@pcaobus.org)

Public Company Accounting Oversight Board
Attention: Office of the Secretary
1666 K Street, N.W.
Washington, DC 20006-2803

**Re: PCAOB Rulemaking Docket Matter No. 017
Proposed Ethics and Independence Rule 3526, Communication with Audit
Committees Concerning Independence, etc.**

Ladies and Gentlemen:

This letter is submitted on behalf of the Committees on Federal Regulation of Securities and Law and Accounting (the “Committees”) of the Section of Business Law of the American Bar Association in response to the request for comments by the Public Company Accounting Oversight Board (the “Board”) in its July 24, 2007 proposal referenced above (the “Proposal”).

The comments expressed in this letter represent the views of the Committees only and have not been approved by the American Bar Association’s House of Delegates or Board of Governors and therefore do not represent the official position of the American Bar Association (the “ABA”). In addition, this letter does not represent the official position of the ABA Section of Business Law, nor does it necessarily reflect the views of all members of the Committees.

The Board proposes to adopt a new Rule 3526, which would, *inter alia*, 1) require a registered public accounting firm, prior to accepting an initial engagement, to provide written disclosures to the audit committee of the potential client of relationships that may reasonably be thought to bear on the independence of the registered accounting firm and to discuss the potential effects of these relationships on independence, and 2) require the registered public accounting

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firm to provide similar communications on an annual basis.¹ The new rule would supersede *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* (“ISB No. 1”), and two related interpretations.

The Committees generally support proposed Rule 3526. As the Board’s Release indicates, the proposed pre-engagement rule fills a gap in current ISB No. 1, which does not require a firm to provide disclosures to or engage in discussions with audit committees about independence prior to acceptance of the initial engagement.² Obviously, because independence is a prerequisite to a firm’s ability to render an audit report, it is a critical matter for the firm and the audit committee to consider before agreeing to an engagement. In light of that, we believe that accounting firms already communicate to audit committees about independence matters in connection with potential engagements of a registered public accounting firm. Therefore, the proposed rule for pre-engagement independence disclosures and discussions should not materially alter current practice. The requirement for annual disclosures and discussions largely codifies ISB No. 1.

We do wish to comment on one question posed by the Board in its release. The Board asks: “Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why, and how long should the period be?” The Committees believe that the Rule should contain a defined look-back period that would limit the relationships that would have to be disclosed to and discussed with the audit committee.

The purpose of the independence rules, of course, is to ensure that the accounting firm is independent with respect an audit report that it has been engaged to render. Independence could be affected by relationships that existed in periods prior to the current audit and engagement period. However, the further one goes back in time the less likely past relationships will be thought to bear on the current independence of the accounting firm. At the same time, the definitions of “accounting firm” and “audit client” in the SEC’s independence rules are broad. Therefore to identify all potential relationships could involve substantial effort by the accounting firm.³ At some point the effort required to develop the information about relationships in the

¹ The Board also proposes to amend Rule 3523, *Tax Services for Persons in Financial Oversight Roles*. The Committees believe that the proposed amendments are appropriate but otherwise do not comment on the proposed Rule 3523.

² ISB No. 1 does require communications with the audit committee prior to a company’s initial public offering.

³ See Regulation S-X, Rule 2-01(f)(1) (defining “accounting firm” to include “all of the organization’s departments, divisions, parents, subsidiaries and associated entities, including those located outside of the United States”); Rule 2-01(f)(4) (defining “audit client” to include “the entity whose financial statements or other information are being audited, reviewed or attested and any affiliates of the audit client,” subject to certain exceptions); Rule 2-01(f)(6) (defining “affiliate of the audit client” to include an entity that has control over, is controlled by or is under common control with, the audit client; an entity over which the

(cont’d)

September 19, 2007

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past and to discuss that information with the audit committee outweighs the value to the audit committee in being informed about such relationships. A specific look back can focus the accountants and the audit committee on those relationships that are most likely to be relevant to ascertaining whether the accounting firm is independent for purposes of the current audit.

Based on the foregoing, we believe that a look-back period of no longer than two years prior to the commencement of the audit period for which the accounting firm will be engaged should be sufficient to enable the accounting firm to identify relationships that should be communicated to the audit committee. Older relationships are unlikely, in our view, to raise issues that will bear on an assessment of the auditor's current independence.⁴

In addition to the foregoing, we suggest the following:

1. The Board should reconsider its proposal not to include the phrase "in the auditor's professional judgment," which presently appears in ISB 1, in the standard for determining what matters might reasonably be thought to bear on independence. We think it is reasonable and appropriate for audit committees to rely on the accounting firm's judgment as to what matters should be disclosed, and that it is not necessary to adopt an objective reasonableness standard for assessing whether the accountants have disclosed relevant matters.

2. The Board should consider modifying proposed Rule 3526(a)(1) and (b)(1) to provide that the relationships to be disclosed in writing are those that may be thought to bear on independence "as of the date of the writing." This would make it clear that the matters affecting independence would be assessed as of the date of the communication and do not have to include matters that might have affected independence in the past.

We appreciate the opportunity to provide these comments. Members of the Committees are available to discuss them should the Board or the staff so desire.

(cont'd)

audit client has "significant influence" unless the entity is not material to the audit client, or an entity which has significant influence over the audit client, unless the audit client is not material to that entity).

⁴ Our comments should in no way be construed as suggesting that accounting firms must perform more diligence about independence than they presently do or that they are required to look back for a longer time than they currently deem to be necessary.

September 19, 2007

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Respectfully submitted,

/s/ Linda L. Griggs

Linda L. Griggs, Chair of the Committee
on Law & Accounting

/s/ Keith F. Higgins

Keith F. Higgins, Chair of the
Committee on Federal Regulation of
Securities

Drafting Committee:

Peter Casey, Esq.

Matthew G. Medlin

Stephen Quinlivan, Esq.

Richard Rowe, Esq.

Thomas White, Esq.

cc. Public Company Accounting Oversight Board

Mark W. Olson, Chairman

Kayla J. Gillan, Member

Daniel L. Goelzer, Member

Bill Gradison, Member

Charles D. Niemeier

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September 7, 2007

Office of the Secretary
PCAOB
1666 K Street, NW
Washington, DC 20006-2803

Sent via Electronic Mail to: comments@pcaobus.org

Re: Proposed Rule 3526, *Communication with Audit Committees Concerning Independence, and Proposed Amendment of Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles* (Rulemaking Docket Matter No. 017)

To the Members and Staff of the PCAOB:

I offer the following comments on the above-cited proposals:

Proposed Rule 3526, Communication with Audit Committees Concerning Independence. I believe this rule, which expands upon Independence Standards Board (ISB) Standard No. 1 (an interim standard of the Board) will enhance communications between auditors and audit committees in the following ways:

- Requiring discussions about independence prior to accepting a new audit assignment would focus attention on an indispensable element of the relationship.
- The more explicit, structured requirements of rule 3526 would lend greater discipline to the independence assessment process and provide the audit committee better information on which to base its decisions.
- The more precise disclosure requirement, i.e., relationships between the firm (or any affiliates) and the audit client *or persons in financial reporting oversight roles*, would remind auditors that they should also consider relationships with persons in key financial roles.

Though the standard must be met before an initial audit engagement is accepted, on an ongoing basis the timing of these activities is not prescribed. Thus, it is possible that some accounting firms may have these critical discussions toward the end of the audit cycle. To promote maximum effectiveness, I suggest incorporating a timing element, (e.g., the planning stage of the audit), into rule 3526. This does not necessarily have to be a mandatory requirement. The rule could indicate, for example, that “firms should apply

rule 3526 as early in the audit process as practicable, preferably during the planning stage of the audit". This approach would allow firms that have good cause for applying the rule later in the audit process a means to remain compliant.

Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles. I support amending rule 3523 to apply to the professional engagement period *only* as this change is conceptually sound and will resolve difficulties experienced by issuers seeking a new auditor. I believe the change is conceptually sound because the simultaneous association (as both auditor and tax provider for the audit client's key executives), which causes the mutuality of interests is not present until the auditor is actually engaged or begins performing attest services, whichever comes first. Thus, if tax services are ceased prior to this period, independence is not affected.

That being said, I generally do not support an option allowing the completion of individual tax services once the professional engagement period has begun except on a very limited, case-by-case basis where cessation of the services to an individual would cause significant hardship and the services could be completed within a reasonable period. Such a case should be brought to the audit committee for review and approval and the accounting firm and the audit committee should agree on temporary safeguards to protect independence in fact and appearance. If independence may not be safeguarded, the services should be ceased prior to the professional engagement. For example, if the executive is the Chief Financial Officer (CFO) and the personal tax services would be provided to the CFO simultaneous with the audit, no safeguards would suffice to protect independence. However, if a case involved a different executive whose work could be segregated from the audit or temporarily performed by another individual while services to the executive were completed, this situation may be acceptable.

I appreciate the opportunity to comment on these issues.

Sincerely,



Catherine Allen, CPA
Audit Conduct



BDO Seidman, LLP
Accountants and Consultants

PCAOB 2008-03 Page Number 074
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New York, New York 10017-5001
Telephone: 212 885-8000
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September 7, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 2006

RE: PCAOB Rulemaking Docket Matter No. 017 – Proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence and Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles*, PCAOB Release No. 2007-008

Dear Board Members and Staff:

We are pleased to provide our comments on the above captioned matter. BDO Seidman, LLP is a member of BDO International, a global network of independent professional accounting firms in 95 countries worldwide. We welcome the opportunity to provide comments on key issues affecting the standards used to establish registered firms' independence. We endorse the PCAOB proposal to amend Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*, permitting the registered firm to provide such tax services during the audit period that precedes the beginning of the engagement, and adoption of Rule 3526, *Communication with Audit Committee Concerning Independence*.

Rule 3523

We believe that when tax services provided to restricted individuals in a financial reporting oversight role are completed before the firm's audit engagement begins, there is no mutuality of interests, or conflict, and their appearance is not a risk. The new provisions of Rule 3523 are appropriate, as the exceptions reduce the hardship upon the issuer and affected individuals. We believe that the PCAOB made a step forward in reviewing applicability of the rule by adding a carve out (via footnote) for Initial Public Offerings ("IPO").

However, we have the following comments to clarify and enhance the proposed amendment to the Rule:

We believe the Board should not only apply the exception of application of Rule 3523 for periods before the engagement period to initial public offerings, but also expand such exception to other corporate life events that cause existing clients to become first subject to SEC and PCAOB regulations, such as mergers, reverse mergers, companies with over 500 shareholders, and initial 11K filers. By limiting the exclusion to initial public offerings, other similarly affected entities face undue financial hardships by requiring a change in auditors and possible re-filings.

To ensure compliance with Treasury Department regulations, we wish to inform you that any tax advice that may be contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax-related penalties under the Internal Revenue Code or applicable state or local tax law provisions or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein.



We further recommend that the 180 day transition period not only apply as a result of employment status, but be expanded to include individuals at existing clients that first become subject to SEC and PCAOB requirements, as well as for situations involving new audit clients. Otherwise, these individuals would be confronted with undue hardship by having to seek new accountants. Individuals in these circumstances may be hampered because of inflexible filing deadlines imposed by foreign tax jurisdictions.

Rule 3526

While we generally support the Board's proposed Rule 3526, we think that audit firms and audit committees are already cognizant of and reactive to their responsibilities, which are prescribed in the independence rules, so we do not believe that adoption of Rule 3526 would have a significant effect on current practice. In adopting the final rule, we believe that the Board should leave to the discretion of the audit committee and the auditor the appropriate time period for communicating in detail relationships that may impact independence. If the Board does not agree with leaving the time period covered by these discussions to the judgment of the auditor and the audit committee, we suggest the covered period be limited to the number of years of audited financial statements in the initial filing after appointment of the auditor.

Regarding the Board's questions listed in the proposal, we note the following:

1. Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?

Although we believe that the present compliance with the Independence Standards Board ("ISB") Standard No.1 result in audit firms fulfilling their responsibilities as to communications with audit committees, we endorse the Board's action in proposing Rule 3526. Including the requirement for the auditor to detail any relationships to the client's audit committee at the onset of engagement enhances the accounting firm's, as well as the audit committee's commitment to independence. However, as noted above, we believe further clarification is needed regarding the period covered by such communications.

In addition, where unique circumstances prevent the required communications by the auditor at engagement for an existing client first subject to SEC and PCAOB requirements, there should be flexibility allowing the audit committee and the auditor to agree on alternate timing for such exchange. This would occur in situations where the existing client may initiate an IPO process, subsequent to the auditor beginning work on a current audit engagement.



2. Would proposed Rule 3526 assist audit committees in making a decision regarding appointment of a new auditor?

As discussed earlier, we believe that auditors and audit committees are already responsive to their independence responsibilities. However, we do support enhancements to communications as proposed by the Board's Rule 3526, which may not be specifically addressed in the ISB standard.

3. Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? If so, what specific communications should the auditor be required to make to the audit committee?

We do not believe additional matters need to be mandated under PCAOB Rule 3526. There are sufficient regulations and guidelines addressed by the SEC, stock exchanges and other regulatory authorities requiring specific information to be discussed with the client's audit committee. The audit committee is responsible for actively engaging in a dialogue with the auditors relating to the disclosure of any relationships or services that may reasonably be thought by the auditor to bear on independence and should take appropriate action, if necessary, to ensure the continued independence of the auditor.

4. To what extent if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?

We believe auditors and audit committees are already making the kinds of communications that would be required by proposed Rule 3526.

5. Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why, and how long should the period be?

Relationships existing prior to the auditor being engaged which may be a concern should be communicated to the audit committee, consistent with ISB No. 1. For the initial period of the engagement, we think the relevant period should be left to the judgment of the auditor and the audit committee, or, alternatively, should be limited to the period(s) covered by the initial filing subsequent to the engagement of the auditor. The proposal and release, as currently drafted, leaves it unclear as to the period that needs to be covered in this initial communication. Periods earlier than the periods covered by the filing should not have any bearing on the audit committee's decision to engage the auditor.

In addition, the auditor should not have to repeat prior communications, unless updates are necessary, and where it would be reasonable to believe there would be an impact on the auditor's independence.

Appropriate communications to new audit committee members, including matters affecting independence, should be the responsibility of the audit committee, not the auditor.



6. Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement begins? If so, why is such a transition period necessary? How long should any such transition period be?

Please see our response to these questions earlier in this letter, in our comments on the proposed changes to Rule 3523.

We appreciate the ability to comment on Release 2007-008. Should you have any questions, please contact Lawrence Shapiro, National Director of Independence at (212) 885- 8560.

Very truly yours,

A handwritten signature in black ink that reads "BDO Seidman, LLP". The "BDO" is written in a larger, bolder script, while "Seidman, LLP" is in a smaller, cursive script directly below it.

BDO Seidman, LLP



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September 7, 2007

J. Gordon Seymour
 Office of the Secretary
 Public Company Accounting Oversight Board
 1666 K Street N.W.
 Washington, D.C. 20006-2803

RE: Rulemaking Docket Matter No. 017 – (1) Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence, (2) Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles (3) Implementation Schedule for Rule 3523

Dear Mr. Seymour:

I am writing you on behalf of the California Public Employees' Retirement System (CalPERS). CalPERS is the largest US Public Pension Fund with total assets of \$247.7 billion and more than 1.5 million members. CalPERS appreciates the opportunity to offer comments to the Public Company Accounting Oversight Board (Board) regarding ethics and independence rules concerning communication with audit committees and the proposed amendments to Rule 3523 as it applies to tax services to individuals who play a direct role in preparing the financial statements of public company audit clients.

CalPERS unconditionally supports the Board's recommendation to expand communication between the auditor and the issuer's audit committee through proposed rule 3526, "Communication with Audit Committees Concerning independence." As solicited by the Board, CalPERS believes that the proposed Rule 3526 will assist:

1. registered firms and audit committees in fulfilling their respective obligations with respect to assessing the auditor's independence;
2. audit committees in making a decision on the appointment of a new auditor;
3. in requiring the registered accounting firm to communicate any additional matters on auditor independence that are determined to be significant through its own review and discussion and disclosure with the audit committee.

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We are in agreement that prior to acceptance of an engagement, the accounting firm should discuss with and provide written disclosures to the audit committee. These should include the following:

- all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client or persons in a financial reporting oversight role that may have a bearing on independence;
- the potential effects of these relationships on the independence in both appearance and fact of the registered public accounting firm;
- the substance of the registered accounting firm's discussion with the audit committee.

In order to allow audit committees a robust foundation to determine the independence of the accounting firm, we recommend the proposed rule require the accountant to consider and provide written disclosures from a period of at least 3 years¹ prior to consideration.

We also agree that after becoming the issuer's auditor, the auditor should at a minimum annually discuss and provide written disclosure to the audit committee on the listed disclosures in the proposed rule 3526 along with the auditor affirming in writing that it is independent in compliance with Rule 3520. We support, as outlined in the SEC's general standard on auditor independence, that in determining what relationships may reasonably be thought to bear on independence, the auditor should additionally consider whether the firm provided any specifically prohibited services or maintained any specifically prohibited relationships. Consistent with the SEC's general standard on independence we agree the focus should be on the perception of the "reasonable investor" when making independence determinations.

We suggest the Board maintain a hard date of April 30, 2008 as the required application date with an earlier adoption recommendation. CalPERS does not believe the Board should provide a transition period in Rule 3523 allowing an accounting firm to complete covered tax services once the professional engagement begins specifically since Rule 3523 was amended to allow accounting firms to provide tax services during the audit period.

We recommend that audit committees provide better justification disclosure, through the proxy, when approving non-audit services performed by the auditor. Providing this type of transparency will permit investors a greater ability to evaluate audit committees' fiduciary performance for shareowners.

CalPERS is prepared to provide assistance to the PCAOB at its request. Please contact Dennis Johnson, Senior Portfolio Manager – Corporate Governance at (916) 795-2731 if there are questions or if we can be of further assistance. Again we thank the Board for its efforts and appreciate the opportunity to provide input from an institutional investor's perspective.

¹ 3 year look back periods are consistent with the New York Stock Exchange and Nasdaq 2006 on director independence standards. The Council of Institutional Investors 2006 director independence standards consist of a 5 year look back period. National Association of State Boards of Accountancy's (NASBA) comment letter to the PCAOB on this proposed rule also recommends a 3 year look back period.

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Page 3

Sincerely,



cc: Fred Buenrostro, Chief Executive Officer, CalPERS
Anne Stausboll, Chief Operating Investment Officer, CalPERS
Christy Wood, Senior Investment Officer, CalPERS
Peter Mixon, General Counsel, CalPERS
Dennis Johnson, Senior Portfolio Manager, CalPERS



September 11, 2007

Cynthia M. Fornelli, Executive Director

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Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, DC 20006-2803

RE: PCAOB Rulemaking Docket Matter No. 017 – Proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence and Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles*, PCAOB Release No. 2007-008

Dear Mr. Secretary:

The Center for Audit Quality (CAQ) is an autonomous public policy organization serving investors, public company auditors and the capital markets. The CAQ's mission is to foster confidence in the audit process and to aid investors and the markets by advancing constructive suggestions for change rooted in the profession's core values of integrity, objectivity, honesty and trust. Based in Washington, D.C., the CAQ is affiliated with the American Institute of Certified Public Accountants (AICPA). The CAQ consists of approximately 800 member firms that audit or are interested in auditing public companies.

We welcome the opportunity to share our views on Public Company Accounting Oversight Board (PCAOB or the Board) Release No. 2007-008. Due to the subject matter of the Release, the Center has received significant input from the AICPA Professional Ethics Executive Committee (PEEC) and accordingly, this letter is being issued jointly with PEEC.

General Comments and Recommendations with Respect to the Proposed Amendment to Rule 3523

The CAQ and PEEC support the PCAOB's proposed amendment to Rule 3523 to eliminate the prohibition against providing tax services to persons in a financial reporting oversight role during the portion of the "audit period" that precedes the "professional engagement period." We also support the PCAOB's proposed amendment to Rule 3523 to add the footnote explaining the application of Rule 3523 in the context of an initial public offering. These proposed changes are consistent with recommendations we made in our response to PCAOB Release No. 2007-002 and, in our view, do not diminish the effectiveness of the rule in maintaining auditor independence and investor confidence.

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Public Company Accounting Oversight Board

Office of the Secretary

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However the Board has not proposed two additional amendments to Rule 3523 that were included in our response to PCAOB Release No. 2007-002. Accordingly, we repeat the substance of those recommendations in the context of the proposed amendments:

1. The note the Board proposes to add to Rule 3523 explains the application of the rule in the context of an initial public offering, which is only one of several ways in which an audit client and its auditor can first become subject to the rule. For example, an audit client and its auditor can become subject to the PCAOB auditing and related professional practice standards through a reverse merger with an existing issuer, through acquisition by an existing issuer, or by exceeding the 500-shareholder threshold requiring the filing of a registration statement. We assume the Board intends that note to be applied in other circumstances where the audit client and the auditor first become subject to the rule; therefore, we recommend that the PCAOB expand the note to Rule 3523 to state, *"In the context of an initial public offering, reverse merger, or similar event that causes a registered public accounting firm to first become subject to the PCAOB's auditing and related professional practice standards with respect to an issuer, the provision of"*
2. We recommend that the 180-day transition period provided for the completion of tax services in process to persons hired or promoted into a financial reporting oversight role in Rule 3523 (c) be extended to persons in such a role at a new audit client or in situations such as those described above.

We believe, in the first instance, that failure to recognize situations similar to an initial public offering would result in significant hardship (including potential reaudits of all periods presented in the filing) to entities that first become subject to Securities and Exchange Commission (SEC) reporting requirements as a result of events (such as those described above) other than an initial public offering (an “other corporate life event”). We believe that a significant number of companies and their auditors first become subject to the SEC reporting requirements (and the PCAOB’s auditing and related professional practice standards) from other corporate life events. In substance, we believe that Rule 3523 should not be applied retroactively and should only apply from the point in time that the registered public accounting firm agrees to, or begins to, perform an audit in accordance with the standards of the PCAOB.

In the second instance, we believe the lack of a transition period for tax services in process for persons in a financial reporting oversight role at a new audit client or at an audit client that first becomes subject to the PCAOB’s auditing and related professional practice standards would place such persons in a position of hardship and severe disadvantage as compared to their counterparts who received a transition period upon adoption of the rule and as compared to persons hired or promoted into such positions for which the rule specifically grants a 180-day transition period. We believe 180 days is a reasonable period to complete services in process and effect a transition to a new service provider. Failure to grant a transition period in these circumstances would force any



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Office of the Secretary

September 11, 2007

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such persons currently using the audit firm for their personal tax services to switch service providers for tax services in process at the date of engagement of the auditor, almost certainly at significant cost and personal inconvenience.

We do not believe these additional changes would diminish the effectiveness of Rule 3523 in maintaining auditor independence and investor confidence.

General Comments and Recommendations with Respect to Proposed Rule 3526

In our comment letter on PCAOB Release No. 2007-002, we noted the requirements of Independence Standards Board Standard No. 1 and stated that, in our view, the requirements of that standard provided an excellent safeguard for preserving auditor independence. We are supportive of proposed Rule 3526 and offer the following general comments with respect to the proposed rule:

1. Although not explicitly stated in the proposed rule, PCAOB Release No. 2007-008 states, “The proposed rule would require disclosure of all relationships that may reasonably be thought to bear on independence whether those relationships existed during the period under audit or during earlier periods.” This statement implies that the communication and discussion between the registered public accounting firm and the audit committee of the issuer should potentially include communication and discussion of relationships that existed in periods prior to the beginning of the audit and professional engagement period or that had been communicated, discussed and resolved in prior years. We believe that the Board should not specify the period that should be covered and allow auditors and audit committees to agree on the relevant criteria for reporting such relationships. We address this matter in further detail in our response to Question #5 below.
2. The proposed rule would remove the phrase “in the auditor’s professional judgment” from the requirement to describe, in writing, relationships that may reasonably be thought to bear on independence. PCAOB Release No. 2007-008 acknowledges, however, “Auditors will, of course, need to apply professional judgment to determine what is reasonable under particular facts and circumstances.” We do not object to the deletion of this phrase provided the final release contains a similar acknowledgment that the auditor must apply professional judgment in determining which matters are required to be communicated to the audit committee.
3. While we agree with the Board that requiring the communication and discussion with the audit committee prior to the engagement of the auditor only makes sense and we support it in the case of a new audit client, we are concerned that, in certain other circumstances, imposing that requirement may unnecessarily delay the filing of an initial public offering or the closing of a transaction. Under Independence Standards Board Standard No. 1, an auditor may begin work (for example on an existing audit client that decides to file a



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registration statement for an initial public offering) based upon an initial review of relationships between the firm and the audit client. The firm would then simultaneously initiate the more comprehensive review of such relationships that would be necessary to support the required communications (which would have to occur prior to the filing of any report with the SEC). If the proposed rule is adopted, registered firms could not begin work until the comprehensive review was completed, which could delay the filing of the registration statement by anywhere from a few days to a few weeks. As the Board knows, time is often of the essence when a company decides to file an initial public offering or initiate a transaction.

Comments and Recommendations with Respect to Matters for which Comments were Specifically Solicited

1. Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?

We are supportive of proposed Rule 3526 and believe that Independence Standards Board Standard No. 1 already requires accounting firms to make the kinds of communications that would be required by proposed Rule 3526. Accordingly, the purpose of the proposed rule appears to be to (a) expand the communications to include relationships between the auditor and persons in a financial reporting oversight role at the audit client; (b) require the communications prior to engagement of the auditor; (c) remove the phrase “in the auditor’s professional judgment” as a modifier to the phrase “relationships that may reasonably be thought to bear on independence”; and (d) require the audit firm to document the substance of its independence discussions with the audit committee.

We have addressed specific implementation and transition issues in our general comments on the proposed rule and responses to certain questions included in the Release.

2. Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?

We believe that audit committees should possess knowledge of the relationships contemplated by Rule 3526 prior to appointing their auditor. We believe that auditors are currently identifying all such relationships as part of the proposal process for a new audit client and auditors and audit committees are currently discussing and resolving such matters prior to the appointment of the auditor. Accordingly, we do not believe the rule would significantly change practice.



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- 3. Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? If so, what specific communications should the auditor be required to make to the audit committee?**

No, we believe audit committees and auditors are currently working together to identify any additional information regarding auditor independence that should be communicated and discussed based on the unique facts and circumstances of the company.

- 4. To what extent if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?**

See response to questions 1 and 2 above.

- 5. Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why and how long should the period be?**

The relationships that are deemed to potentially impair an audit firm's independence are generally limited to those that existed during the audit and professional engagement period. Accordingly, the initial communication should cover all relationships that existed during the audit and professional engagement period, which in the case of an initial public offering or reverse merger, could cover several years. Relationships that existed prior to the beginning of the audit and professional engagement period may be relevant to the extent those relationships have continuing implications during the audit and professional engagement period or limit the auditor's ability to audit adjustments to financial statements of prior periods. As a general rule, relationships that existed prior to the beginning of the earliest audited period included in the audit client's current SEC filings would not be relevant.

We believe that the rule need not specify the period to be covered during the initial communication and that subsequent annual communications should be limited generally to relationships that existed subsequent to the most recent annual (or, initial in the case of the first annual) communication. We believe that guidance of this nature is best set forth in the discussion contained within the rule release rather than within the rule itself.

- 6. Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?**



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When the Board adopted Rule 3523 it provided for an approximately 180-day transition period for engagements in process at the date of adoption. In addition, the Rule provides for a 180-day transition period for engagements in process at the date of a hiring or promotion event.

Presumably, these transition periods were provided in order to allow persons in a financial reporting oversight role that had a pre-existing professional service relationship with the audit firm a reasonable period of time to complete work in process and engage another service provider for future services. In order to avoid imposing a hardship (transitioning services in process to another firm at significant cost and personal inconvenience), we believe these same transition periods should be afforded to persons in a financial reporting oversight role at a new audit client or an existing audit client that first becomes subject to the PCAOB's auditing and related professional practice standards. We also point out that persons subject to the rule live in various jurisdictions with varying tax filing dates and that, in the case of entities that first become subject to the rule, all such persons may not even have been identified at the time of the occurrence of the event that gives rise to the application of the rule.

We appreciate the opportunity to comment on PCAOB Release No. 2007-008 and would welcome the opportunity to respond to any questions you may have regarding any of our comments and recommendations.

Sincerely,

A handwritten signature in black ink that appears to read "Cynthia M. Fornelli".

Cynthia M. Fornelli

Executive Director

Center for Audit Quality

A handwritten signature in black ink that appears to read "Bruce P. Webb".

Bruce P. Webb

Chair, AICPA Professional Ethics Executive Committee

cc: Mark W. Olson, Chairman

Kayla J. Gillan, Member

Daniel L. Goelzer, Member

Willis D. Gradison, Member

Charles D. Niemeier, Member

Thomas Ray, Chief Auditor and Director of Professional Standards



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September 7, 2007

Public Company Accounting Oversight Board
 Office of the Secretary
 Attn: J. Gordon Seymour
 1666 K Street, N.W.
 Washington, D.C. 20006-2803

Re: **PCAOB Rulemaking Docket Matter No. 017**

Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence
Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles

Dear Mr. Seymour:

Deloitte & Touche LLP is pleased to respond to the request for comments from the Public Company Accounting Oversight Board (“PCAOB” or the “Board”) on its *Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence* (“proposed Rule 3526”) and *Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles* (“proposed Amendment to Rule 3523”), PCAOB Release No. 2007-008, PCAOB Rulemaking Docket Matter No. 017 (July 24, 2007) (the “Release”).¹

We strongly support the goals of the Sarbanes-Oxley Act of 2002 (the “Act”) and the efforts of the Board to achieve those goals through rulemaking. Recognizing that the Board faced difficult and sensitive judgments in drafting proposed Rule 3526 and the proposed Amendment to Rule 3523, we believe the Board’s efforts in that regard represent a thoughtful approach to furthering the goals of the Act. Accordingly, we strongly support the Board’s proposal and its solicitation of comments as set forth in the Release.

With that support in mind, we offer the comments and recommendations herein. These comments and recommendations are aimed at achieving the effective and efficient implementation of, and compliance with, proposed Rule 3526 and the proposed Amendment to Rule 3523. We believe that all of the parties affected (e.g., issuers, audit committees and auditors) must have both a clear understanding of the scope of proposed Rule 3526 and the proposed Amendment to Rule 3523 and the ability to effectively apply them. When the scope

¹ http://www.pcaob.org/rules/docket_017/2007-07-23_release_2007-008.pdf

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or application of a rule is unclear, affected parties will likely find it necessary to seek frequent guidance regarding application of the rule on a case-by-case basis directly from the staff of the Board. This would place additional burden on audit committee members, do little to benefit investors and place an unnecessary burden on the already limited resources of the Board. For these reasons, our comments and recommendations are primarily aimed at enhancing compliance and addressing application issues in today's complex global business environment. We will also respond to specific questions posed by the Board in the Release.

In providing our comments, we have chosen to follow the order of the specific questions posed by the Board in the Release. Accordingly, the order of our comments in no way reflects the importance we place on proposed Rule 3526 and the proposed Amendment to Rule 3523.

1) Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?

The Act, the Securities Exchange Commission ("SEC" or the "Commission") and the Board have all emphasized the importance of audit committee oversight of auditor independence. As the Board indicates in its Release, Rule 3526, as proposed, is built upon the Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees* ("ISB No. 1"),² and adds a new requirement that such communications should take place not only annually, but also prior to accepting an initial engagement pursuant to the standards of the PCAOB. While we support proposed Rule 3526 and believe that the proposed rule would assist registered firms and audit committees in fulfilling their respective obligations to investors with respect to auditor independence, we believe specific clarifications should be made by the Board in adopting its final rule as discussed below.

Proposed Rule 3526 requires that all relationships that "may reasonably be thought to bear on independence" must be disclosed to the audit committee of the issuer. However, as noted in the Release, "unlike ISB No. 1 ... the proposed [Rule 3526] would not modify this basic reasonableness standard with the words "in the auditor's professional judgment." The Board expressed its belief in the Release that omitting these words will clarify the requirement by "reminding auditors of the need to focus on the perceptions of reasonable third parties when making independence determinations."

As discussed in more detail below, we believe that the omission of the specific words "in the auditor's professional judgment" departs from and is inconsistent with the Board's recent focus on the importance of the use of auditor judgment and its efforts to amend its auditing standards and other rules to ensure a greater emphasis on the auditor's judgment. We also believe that the omission of the words "in the auditor's professional judgment" is not necessary, and that such a change in proposed Rule 3526 would create unnecessary confusion for audit committees and investors.

² http://www.pcaob.org/Standards/Interim_Standards/Independence_Standards/ISB1.pdf

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The Importance of Professional Judgment

As noted above, we believe that, by omitting the words “in the auditor’s professional judgment”, the Board departs from its existing audit standards and creates inconsistency among proposed Rule 3526 and those standards and other rules. Such a departure sends mixed messages to audit committees, investors and auditors working to implement revised standards and rules.

In the Board’s most recent standard-setting effort, PCAOB Audit Standard No. 5, *An Audit of Internal Control Over Financial Reporting That is Integrated with an Audit of Financial Statements*,³ the Board and its staff have diligently gone through a deliberate process of revising AS No. 2 to clearly and expressly permit the auditor to use professional judgment. Proposing to remove these words from an existing PCAOB rule is inconsistent with the Board’s focus on encouraging the use of auditor judgment.

In addition to AS No. 5, there are many examples in standards promulgated by the PCAOB demonstrating that the use of auditor judgment is encouraged. For example, the Board’s Auditing Standards No. 3, *Audit Documentation*⁴ states:

“A18. Auditors exercise **professional judgment** in nearly every aspect of planning, performing, and reporting on an audit. Auditors also exercise **professional judgment** in the documentation of an audit and other engagements...” (Emphasis added.)

Even the Board’s Release indicates that in applying proposed Rule 3526:

“Auditors will, of course, **need to apply professional judgment** to determine what is reasonable under particular facts and circumstances.”⁵ (Emphasis added.)

We believe the use of auditor judgment should continue to be emphasized in Rule 3526 not only to maintain the PCAOB’s consistent message, but also to avoid confusion for audit committees, investors and auditors as to whether the standard for these communications to the audit committee have changed.

The Meaning of Professional Judgment

In a letter to the Securities Exchange Commission Practice Section (“SECPS”) of the American Institute of Certified Public Accountants (“AICPA”), then ISB Chairman William Allen clarified the use of the auditor’s professional judgment under ISB No. 1. He stated:

³ http://www.pcaob.org/Rules/Rules_of_the_Board/Auditing_Standard_5.pdf

⁴ http://www.pcaob.org/Rules/Rules_of_the_Board/Auditing_Standard_3.pdf

⁵ http://www.pcaob.org/rules/docket_017/2007-07-23_release_2007-008.pdf

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“[I]n asking itself whether a fact or relationship is material in this setting the auditor may not rely on its professional judgment that such fact or relationship does not constitute an impairment of independence. Rather the auditor is to ask, in its informed good faith view, whether the members of the audit committee who represent reasonable investors, would regard the fact in question as bearing upon the board's judgment of auditor independence.”⁶

The Commission's independence rules adopted Chairman Allen's interpretation stating:

“We believe that Chairman Allen's interpretation is appropriate.”⁷

Therefore, we believe that the language in ISB No. 1, as it currently exists, already encompasses the need for the auditor to consider the viewpoint of reasonable investors. Changing the language would serve only to create confusion as audit committees, investors and auditors strive to understand whether the standard with respect to these communications has changed.

Accordingly, we recommend that the Board clarify proposed Rule 3526 through the following revisions:

“(a)(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client or persons in a financial reporting oversight role at the potential audit client that in the auditor's professional judgment may reasonably be thought to bear on independence; ...

(b)(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in a financial reporting oversight role at the audit client that in the auditor's professional judgment may reasonably be thought to bear on independence;...

(b)(3) affirm to the audit committee of the issuer, in writing, that the registered public accounting firm, in its professional judgment, is independent in compliance with Rule 3520;...”

Based on discussions set forth above, we believe that our recommended revisions to proposed Rule 3526 would assist in effective and efficient implementation of the rule.

⁶ Letter from William T. Allen, Chairman, ISB, to Michael A. Conway, Chairman, Executive Committee, SECPS (Feb. 8, 1999).

⁷ <http://www.sec.gov/rules/final/33-7919.htm>, footnote 168

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- 2) *Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?*

We believe that the Board's proposal provides an opportunity to enhance the audit committee's understanding of all relationships that, in the auditor's professional judgment, may reasonably be thought to bear on independence. The opportunity to discuss potential impacts of those relationships on the independence of the registered public accounting firm permits the audit committee of the issuer to initiate open and interactive dialogues on potential independence issues, challenge the analysis of the registered public accounting firm, request additional information, evaluate all relevant and available facts and circumstances to determine whether any such relationship would, pursuant to the Board's and the SEC's independence rules, adversely impact independence should the registered public accounting firm be appointed the issuer's independent auditor, and ultimately make a decision as to whether the registered public accounting firm should be appointed as the issuer's independent auditor.

Additionally, we believe that where difficult decisions regarding the appointment of a new auditor must be made by the audit committee of the issuer, the independence communications should serve to enable the audit committees, in their professional judgment, to analyze the facts and circumstances and to conclude, based on such facts and circumstances, whether a registered public accounting firm could accept an audit engagement without independence conflicts. Accordingly, we believe that proposed Rule 3526 would assist audit committees in exercising their judgment in making the appropriate decision regarding the appointment of a new auditor.

- 3) *Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? If so, what specific communications should the auditor be required to make to the audit committee?*

As noted above, we believe that proposed Rule 3526 should limit required communications with the audit committee of the issuer to relationships that, in the auditor's professional judgment, may reasonably be thought to bear on independence. We also believe that such communications would be sufficient to assist registered public accounting firms and audit committees in fulfilling their respective obligations to investors with respect to auditor independence and to assist audit committees in making a decision regarding the appointment of a new auditor. Accordingly, we do not believe proposed Rule 3526 should require a registered public accounting firm to communicate additional matters on auditor independence to the audit committee of the issuer, unless such additional communications are specifically requested by the audit committee of the issuer. However, we also believe that proposed Rule 3526 should be modified to make it clear that such communications may be based on the auditor's professional judgment, as previously explained, and may exclude communications regarding tax services provided to persons in a financial reporting oversight role or to trusts or other entities controlled by such persons, as discussed further below.

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If the proposed amendment to Rule 3523 to allow tax services to persons in a financial reporting oversight role at the issuer during the portion of the “audit period” that precedes the beginning of the “professional engagement period” is adopted, such services will, absent additional transition rules, have to be terminated prior to “an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB” being signed by the new auditor. Accordingly, we question the need to include a discussion of such services within the scope of Rule 3526, in that compliance with amended Rule 3523 would appear to adequately address any independence concerns involving tax services provided to persons in a financial reporting oversight role.

Accordingly, we respectfully request that the Board exclude tax services to persons in a financial reporting oversight role from the required communications under proposed Rule 3526. Such a change could be effected by striking out “or persons in a financial reporting oversight role at the potential audit client” from proposed Rule 3526(a)(1) and (b)(1) as follows:

“(a)(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client ~~or persons in a financial reporting oversight role at the potential audit client that in the auditor’s professional judgment~~ may reasonably be thought to bear on independence; ...”

(b)(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client ~~or persons in a financial reporting oversight role at the audit client that in the auditor’s professional judgment~~ may reasonably be thought to bear on independence;...”

If the Board continues to believe that tax services previously provided to persons in a financial reporting oversight role need to be included in the scope of proposed Rule 3526, it is unclear whether tax services provided to trusts or other entities controlled by persons in a financial reporting oversight role at the issuer would need to be discussed with the audit committee of the issuer. Rule 3523 specifically excludes “entities controlled by persons in a financial reporting oversight role, such as trusts and investment partnerships”⁸ from its scope. Since entities controlled by persons in a financial reporting oversight role are outside the scope of Rule 3523, we believe that proposed Rule 3526 should, at a minimum, be clarified to specifically exclude services to trusts or other entities controlled by persons in a financial reporting oversight role at the issuer from its scope.

- 4) *To what extent if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?*

With respect to existing audit clients, proposed Rule 3526(b) requires that a registered public accounting firm communicate annually with the audit committee of its audit client concerning

⁸ <http://www.sec.gov/rules/pcaob/34-53427.pdf>

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independence, and document the substance of such communications. ISB No. 1 already requires the auditor to make these communications to the audit committee. In practice, it is our understanding that registered public accounting firms appropriately follow ISB No. 1 by discussing with and disclosing in writing to the audit committee of the audit client all relationships between the registered public accounting firm and the audit client that, in the auditor's professional judgment, may reasonably be thought to bear on independence, confirming in the communication that, in its professional judgment, the auditor is independent of the audit client. Additionally, since registered public accounting firms generally include the issued ISB No. 1 communication as part of their audit working papers, the additional documentation requirement pursuant to proposed Rule 3526(b)(4) is followed in practice.

With respect to potential audit clients, it is our understanding that, in practice, registered public accounting firms generally, informally or sometimes in writing, communicate to the audit committee all relationships that, in the auditor's professional judgment, may reasonably be thought to bear on independence. Such communications generally occur near the final stage of the auditor selection process when the registered public accounting firm, being the only candidate remaining in the proposal process, has taken all necessary measures to analyze and cure its independence with respect to the potential audit client. The registered public accounting firm would describe potential independence issues identified based on its professional judgment, the potential impacts on independence, and actions that the registered public accounting firm has taken, and will undertake to ensure its independence should the registered public accounting firm be appointed as the independent auditor. In instances when a registered public accounting firm is not independent of the issuer, the firm would have notified the audit committee of the issuer that it could not serve as the independent auditor of the issuer due to independence conflicts and withdrawn during the early stages of the proposal process.

Accordingly, it is our understanding that to a large extent, accounting firms are already making the kinds of communications that would be required by proposed Rule 3526. However, although the current communications are similar, due to the language in proposed Rule 3526, we believe the Board should revise and clarify its proposal as indicated herein.

- 5) *Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why, and how long should the period be?*

With respect to independence communications to prospective audit clients, we note that the Commission's independence rules require that a registered public accounting firm maintain its independence with respect to its issuer audit clients during both the "audit period" (the period covered by any financial statements being audited or reviewed) and (ii) the "professional engagement period" (the period of the engagement to audit or review the audit client's financial statements or to prepare a report filed with the Commission).⁹

⁹ <http://www.sec.gov/rules/final/33-7919.htm>

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Consistent with the Commission's independence rules, we believe the length of the period to be covered by proposed Rule 3526(a) should be determined by the years of issuer financial statements to be audited by the registered independent public accounting firm and included in a filing with the Commission. For example, if a registered public accounting firm is proposing to audit the issuer's financial statements for the year ending December 31, 2007, it should only be required to communicate to the audit committee of the issuer, all relationships, which in its professional judgment may reasonably be thought to bear on independence, that existed from the earlier of 1) the date an engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB is signed; 2) the date the auditor begins audit procedures pursuant to that engagement letter; or 3) January 1, 2007. An audit committee should not be required to, but should have the flexibility to, based on the exercise of its judgment, ask for additional information that would facilitate its evaluation of the auditor's independence.

Accordingly, we ask that the Board only require communication of matters that existed or that would continue to exist in the audit and professional engagement period and permit audit committees with the flexibility to request additional information based on their judgment.

With respect to continuing communications, we believe it should not be necessary for the registered public accounting firm to continue to disclose matters that have previously been disclosed to the audit committee of the issuer audit client. As noted above, registered public accounting firms already provide ISB No. 1 communications to the audit committees of their issuer audit clients. These communications are typically documented in the meeting minutes of the audit committee and should be in the audit committee's records. In view of these prior disclosures, auditors generally provide only an update of the previous ISB No. 1 communication to cover new items that may have occurred since the issuance of the last ISB No. 1 communication. In situations where there has been significant turnover in the audit committee of the issuer, we would expect the new audit committee members to be focused on independence matters prospectively, and believe that the minutes of the audit committee meetings should provide information sufficient to inform new audit committee members of the audit committee's prior conclusions with respect to independence matters.

- 6) *Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?*

We believe the proposed Amendment to Rule 3523 addresses certain transition issues and we support the proposed modifications. However, we believe further clarification and guidance is needed to fully address other transition matters that will arise. Below we describe the additional matters that we believe should be addressed by the Board, including the need, in certain instances, for a transition period to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins.

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The note addressing initial public offerings (“IPOs”) as provided by the proposed Amendment to Rule 3523 states:

“Note: In the context of an initial public offering, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.”¹⁰

We understand that the Board intends to consistently apply the term “professional engagement period” as defined in the Commission’s independence rules. In doing so, it is easy to identify the “date that the firm signed an initial engagement letter to perform an audit pursuant to the standards of the PCAOB,” however, we believe that it will be very difficult to apply the second prong of the requirement set forth in the note which reads “the earlier of the date that the firm … (2) began procedures to do so.”

For example, assume that a registered public accounting firm has been the independent auditor of a private company for several years. In 2007, the company decided to undertake an IPO and has determined that it needs to include its December 31, 2004, 2005 and 2006 financial statements in the filing with the Commission. The registered public accounting firm completed its audit procedures on the company’s December 31, 2004, 2005 and 2006 financial statements pursuant to Generally Accepted Auditing Standards (“GAAS”) and the standards of the AICPA and has issued its audit opinions on such financial statements. Company management and the audit committee prefer that the registered public accounting firm continue to serve as its independent auditor through and after the IPO.

In this IPO scenario, some may question whether the date that the registered public accounting firm “began procedures” would precede the “date that the firm signed an initial engagement letter to perform an audit pursuant to the standards of the PCAOB,” presumably sometime in 2007. We believe that such a reading of the note could effectively contradict the changes contemplated by the proposed Amendment to Rule 3523.

To address this issue, and consistent with our previous comments submitted to the Commission¹¹ and the Board,¹² we continue to believe that additional clarification and a transition period are necessary to ensure that the proposed Amendment to Rule 3523 permits companies to navigate independence issues that arise from the application of the rule as a result of corporate “life events.” Similar to an IPO, mergers and acquisitions, employment events, and other corporate “life events” are driven by the ever-changing business environment which usually does not allow for advanced planning for auditor changes. This hardship is further compounded because Rule 3523 prohibits tax services to persons in a financial reporting and oversight role at most of the affiliates of the audit client. Therefore,

¹⁰ http://www.pcaob.org/rules/docket_017/2007-07-23_release_2007-008.pdf

¹¹ See Letter from Deloitte & Touche LLP to the PCAOB dated April 3, 2006.

¹² See Letter from Deloitte & Touche LLP to the PCAOB dated May 18, 2007.

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failure to modify the proposed Amendment to Rule 3523 to address other corporate “life events” could impose an undue hardship on an issuer and its investors by requiring an unscheduled auditor change while potentially limiting the field of registered public accounting firms that could serve as the independent auditor for the issuer.

We also note that independence related transition issues resulting from IPOs or other corporate “life events” are conceptually similar to the transition issue related to the hiring or promoting of a person to a financial reporting oversight role. In such situations, the Board adopted a transition period to address commenters’ concerns that Rule 3523 could impose an undue hardship on persons who become subject to the rule because they are hired or promoted into a financial reporting oversight role at an audit client. The Board stated:

“Specifically, the Board has determined to add a new exception to the rule that applies to a person who was not in a financial reporting oversight role at the audit client before a hiring, promotion, or other change in employment event, when the tax services are both: (1) provided pursuant to an engagement that was in process before the hiring, promotion, or other change in employment event; and (2) completed on or before 180 days after the hiring or promotion event.”¹³

This 180-day transition provision provided in Rule 3523 recognizes the appropriate balance between maintaining auditor independence, the protection of investors and the hardship of immediately discontinuing tax services provided to individuals in financial reporting oversight roles, and acknowledges that such services can be continued for a limited period of time during the audit and/or the professional engagement period without impairing independence. We believe the proposed Amendment to Rule 3523 should extend the PCAOB’s 180-day transition policy to registrants and persons that first become subject to Rule 3523 due to corporate “life events” such as IPOs, mergers and acquisitions, and other scenarios that may require an entity to re-evaluate the independence of its auditor under Rule 3523.

If the Board decides to adopt a transition period, we believe that the period should begin no earlier than with the filing of an IPO or the occurrence of the corporate “life event” because until such time, the transaction or event could be abandoned and if so, Rule 3523 would not apply. Transactions such as IPOs and mergers are often delayed or abandoned due to various business and market considerations. Accordingly, mandating that executives change tax advisors before a transaction closes has the real potential for imposing burdens that may ultimately prove to be unnecessary.

Accordingly, we recommend that the Board adopt the following transition rule:

“Providing tax services to a person covered by Rule 3523 will not impair the independence of an audit firm if the tax services are: (1) performed pursuant to an

¹³ Rule 3523(c), PCAOB; Notice of Filing of Proposed Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees; Notices; 71 Fed. Reg. 12722 (Mar. 7, 2006) (citations omitted).

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engagement that is in process before the company or person becomes subject to Rule 3523; and (2) completed in accordance with the guidance and under the oversight of the audit committee on or before 180 days after the occurrence of the event that subjects the company or person to Rule 3523, provided that such services are appropriately approved by the audit committee and the audit firm precludes personnel providing such tax services from being members of the audit team.”

If such a transition rule is not adopted, we recommend that the Board clarify the IPO note provided by the proposed Amendment to Rule 3523 through the following revisions:

“Note: In the context of an initial public offering, or merger, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures ~~to do so~~ pursuant to that engagement letter, does not impair a registered public accounting firm's independence under Rule 3523.”

Conclusion

We support the efforts of the Board to further the goals of the Act, and believe that the Board’s request for comments regarding proposed Rule 3526 and the proposed Amendment to Rule 3523 demonstrates a thoughtful approach to furthering those goals. We also firmly believe that to be effective, all of the parties affected by proposed Rule 3526 and the proposed Amendment to Rule 3523 must have both a clear understanding of the scope of the rules and the ability to effectively apply them. Accordingly, we respectfully request that the recommendations provided herein, which help to achieve the goal of effective and efficient implementation, be adopted.

We appreciate your consideration of the recommendations and views set forth herein, and look forward to working with the Board to achieve clarity in any final rules. We would welcome the opportunity to further discuss these matters with the Board and the staff. If you have any questions or would like to discuss these matters, please contact Robert Kueppers at (212) 492-4241 or Roger Page at (202) 879-5630.

Sincerely,

/s/ Deloitte & Touche LLP

cc: Mark W. Olson, Chairman
 Kayla J. Gillan, Member
 Daniel L. Goelzer, Member
 Bill Gradison, Member
 Charles D. Niemeier, Member
 Tom Ray, Chief Auditor and Director of Professional Standards

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Chairman Christopher Cox, Securities and Exchange Commission
Commissioner Paul Atkins
Commissioner Roel Campos
Commissioner Annette Nazareth
Commissioner Kathleen Casey
Conrad Hewitt, Chief Accountant
Zoe-Vonna Palmrose, Deputy Chief Accountant for Professional Practice

Dennis R. Beresford
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July 31, 2007

Office of the Secretary
PCAOB
1666 K Street, N.W.
Washington, DC 20006-2803

Rulemaking Docket No. 017

Board Members:

I write to comment on your Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence. I am now or formerly have been chairman of the audit committee of five large, publicly held companies and my comments are influenced by those experiences. But these comments are personal and should not be ascribed to any of those companies.

I support the general thrust of the proposed additions to PCAOB literature with respect to independence communications with auditors. If nothing else, it will be less confusing to audit committees and others to eliminate references to the now extinct Independence Standards Board. Having all of the authoritative literature relating to auditing and independence in one place is a positive move. However, I have a few suggestions that I think would improve a final Rule 3526.

General Approach to the Independence Determination

While audit committees need to be assured of independent auditors' independence, that doesn't mean they should be expected to know all of the detailed SEC, PCAOB, and AICPA rules and then weigh whether particular

circumstances do or do not affect independence. Thus, I question whether it is necessary and appropriate for a registered public accounting firm to both (1) describe all relationships that may reasonably bear on independence and (2) discuss the potential effects of those relationships on independence. Instead, it should be sufficient for the accounting firm to affirm its independence to the audit committee based on existing standards rather than, in effect, requiring the audit committee to somehow evaluate how the firm has applied those standards. With respect to the audit as a whole, the audit committee relies on the fact that the accounting firm has performed the audit “in conformance with the standards of the Public Company Accounting Standards Board,” so why should audit committee members have to accept more responsibilities with respect to independence? To do so would be somewhat like an accounting firm asking an audit committee to review and judge whether appropriate audit procedures have been selected among various procedures that could have been used.

Therefore, I suggest the proposed rule should be simplified by deleting both subpoints (1) and (2) of points (a) and (b). The onus should be on the accounting firm to determine all possible independence issues and resolve them to its satisfaction, and that is accomplished through subpoint (3). In potentially problematic circumstances, the accounting firm should check with the SEC or PCAOB but further discussing these with the audit committee provides no additional value in my view.

Other Comments

The proposal would remove the reference in ISB No. 1 to “in the auditor’s professional judgment” with respect to the need to discuss matters relating to independence. However, without a specific reference to the matters covered in footnotes 13 and 14 of the proposal, those reading the actual rule might be left to wonder how “may reasonably be thought to bear on independence” should be applied (thought by whom?). Therefore, I suggest adding the substance of footnotes 13 and 14 to the actual rule. Of course, this would be relevant only if the PCAOB chooses not to accept my larger point above.

The timing of the annual affirmation to the audit committee ought to be specified in the final rule. While the audit committee should be able to assume that the accounting firm is independent at all times during a particular year under audit, I feel that there are two critical times for the affirmation. First would be at the time of the engagement letter and second

would be near the end of the audit, similar to the timing of the company's letter of representations.

Please let me know if you have any questions about these comments.

Sincerely,

Dennis R. Beresford



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September 7, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street NW
Washington, D.C. 20006

Re: Rulemaking Docket Matter No. 17

Mr. J. Gordon Seymour:

Ernst & Young LLP (EY) is pleased to comment on the *Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence, the Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles and the Implementation Schedule for Rule 3523* as requested in PCAOB Release No. 2007-008 dated July 24, 2007 (Release).

The Release proposes an amendment to Rule 3523, as originally adopted by the PCAOB in July of 2005, as well as an explanatory Note concerning the implementation of the Rule when a company undertakes its initial registration (IPO) of its securities with the Securities and Exchange Commission (SEC). The Release announces a further adjustment of the implementation schedule for Rule 3523 to allow for comment on these proposals.

The Release also proposes a new independence rule, Rule 3526, *Communication with Audit Committees Concerning Independence*. This proposal expands on the current requirements of Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees ("ISB No. 1"), and two related interpretations, ISB Interpretation 00-1 and ISB Interpretation 00-2, which were adopted by the PCAOB as interim independence standards.

The Release requests comments on all aspects of the proposals and, in particular, comments with regard to six specific questions.

We support the PCAOB's efforts to continue to provide and enhance guidance on the PCAOB Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees (the Rules) and matters surrounding implementation, particularly, those aspects of the Rules that may impact, unnecessarily, a registrant's choices when seeking to make a change in the registered firm conducting its audit. We have previously submitted comments and provided views to the Staffs of both the PCAOB and SEC on the Rules and EY's understanding and implementation processes surrounding these Rules.

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Additionally, we support the PCAOB's efforts to continue to encourage communication between auditors and audit committees concerning matters that might reasonably bear on the auditor's independence. We believe the proposal regarding communication to the audit committee associated with an accounting firm's initial engagement pursuant to the standards of the PCAOB will provide the audit committee with important, timely and relevant information in order for the audit committee to make an informed decision in selecting an accounting firm as the issuer's auditor.

Our comment letter herein responds to the requests and includes additional information as we considered necessary to explain our views.

1. Comments Regarding Proposed Amendments to Rule 3523

EY previously responded to and commented on the PCAOB *Concept Release Concerning Rule 3523* (Concept Release) which was issued by the PCAOB on April 3, 2007. In our comment letter on the Concept Release, dated May 18, 2007 (a copy of which is attached to this letter for your convenience), we indicated our support for a potential amendment to Rule 3523 to eliminate the words "audit and" from the first sentence of the Rule. Accordingly, we support the PCAOB proposal which incorporates this change. We believe that this change is a positive one for the reasons set forth in our comment letter of May 18, 2007; namely it potentially provides companies more flexibility and choice when desiring to change auditors. We agree with the comments made during the Board's open meeting on July 24, 2007 that this proposed change can remove an obstacle to selecting the best firm to meet a company's needs without any compromise to the basic issues surrounding independence. Based on the analysis outlined in our prior letter, we believe that providing a tax service to an individual during the audit period but prior to the start of the professional engagement period poses less of a threat to independence than other services to the corporate entity might pose during the same period.

We did not comment on the matter of specific relief in the event of an IPO in our May 18, 2007 comment letter, but we note that other commenters did offer views on this important issue. We have commented on this specific aspect of Rule 3523 in previous comment letters and in meetings with the PCAOB Staff. We support the Board's decision to add a Note to Rule 3523 clarifying the application of that Rule with respect to periods prior to the engagement of the registered independent accounting firm to perform an audit in accordance with PCAOB standards. We believe that this proposed change creates more certainty with respect to what services rendered to a privately held audit client are permissible and do not impair independence if that company determines in the future to undertake a registration under the US securities laws. We believe that this Note is consistent with the goal of making the PCAOB rules no broader than necessary to accomplish their desired result while remaining cognizant of the general principle that requires companies and their auditors to avoid circumstances that could reasonably be thought to impair independence. The PCAOB's proposed change aids by removing a potential issue which could pose an unnecessary barrier to registration under the US securities laws.

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Without this change, privately held companies that undertake an IPO would find that routine tax services rendered to individuals in Financial Reporting Oversight Roles (FROR) by the company's existing auditors created independence violations under PCAOB rules, even though the company had no involvement in such engagements and, indeed, such services complied with the applicable auditor independence standards at the time they were provided.

With respect to the amendment to Rule 3523 and the Note we suggest the PCAOB consider broadening the Note to include other transactions that have the same potential impact as an IPO, namely reverse mergers and similar transactions.

The Release indicates the Board is interested in commenter's views concerning transition periods. In the Board's open meeting, a concern was raised that the transition period could extend beyond the completion of the initial audit engagement. We have addressed these matters below in our response to the Board's specific question concerning Rule 3523.

2. Comments Regarding Proposed Rule 3526

The Release notes a gap in the existing requirements under ISB No. 1 and the SEC and PCAOB rules for communications between the issuer's audit committee and an accounting firm concerning independence matters prior to the firm becoming the issuer's auditor. ISB No. 1 requires communication to the issuer's audit committee regarding all relationships between the auditor and its related entities and the company and its related entities that, in the auditor's professional judgment, may reasonably be thought to bear on the auditor's independence prior to the company's initial filing and at least annually thereafter. These communications are made for initial registrants before the initial filing date and cover all periods included in a registration statement for the initial public offering of securities. ISB No. 1 does not specify a timetable for providing annual written and oral communication about independence matters; however, the SEC rules on communication with audit committees require that all other material communications with management be communicated to audit committees prior to the filing of the audit report with the SEC.

Although ISB No. 1 does not specifically address communication on independence matters during the period an audit committee is evaluating and making its decision to initially retain an accounting firm as the issuer's auditor, existing SEC and PCAOB pre-approval rules require that the audit committee pre-approve all current and proposed services prior to or simultaneously with engaging an accounting firm as the issuer's auditor. In our experience, communication currently takes place between EY and an issuer's audit committee prior to accepting an initial engagement pursuant to the standards of the PCAOB, whether that engagement is a new client acceptance or an initial public offering of an existing private audit client of EY. This communication may not be the same in content, timing or manner of documentation in each instance, but EY is cognizant of the need to identify and address potential independence issues at

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the earliest feasible date and to comply with applicable professional standards in the circumstances.

We concur with the Board's observation that there may be a gap in the communication of relevant information about an accounting firm's independence when the audit committee is considering multiple firms in making its decision to retain a new accounting firm as the issuer's auditor. While an audit committee may request, or an accounting firm may offer, relevant information about the firm's independence for consideration in making the decision, there may be differences in the form and content of the communication from the involved accounting firms. We believe providing relevant information to the audit committee about the accounting firm's independence will aid the audit committee in its decision making process when considering a change in auditor. In the case of an existing issuer considering a change in auditors, this earlier communication may offer additional independence information to the audit committee, in a reasonable timeframe, which would assist in its determination about whether to retain the firm as the company's auditor. However, in the proposed rule there is no specified time period over which an accounting firm should consider the relationships that might reasonably be thought to bear on independence with respect to a prospective new audit client. We believe that a time period should be specified and that the period should appropriately include the current period and the expected "audit and professional engagement period" bearing in mind that, in certain circumstances, other prior relationships may need to be considered. An auditor must consider the reasonable investor standard and its independence "in appearance" in the given circumstances. Using the current period and the expected "audit and professional engagement period" would take into account the specific circumstances, for example, if a given audit committee believed that it wanted the auditor to consider past relationships in the event of the need for re-audits of prior years for various reasons.

However, we believe Rule 3526, as currently proposed, could cause an undue burden on private companies pursuing IPOs if such communication is required prior to the acceptance of the engagement to assist an existing private audit client with its initial registration. Generally, in our experience, for an existing private audit client, the assessment under the SEC and PCAOB independence rules occurs simultaneously with the performance of the engagement to assist the company in preparing for its IPO. The independence assessment, particularly for multinational companies, may require significant time to complete. If a requirement existed for the independence assessment to be completed before any work could be commenced by the existing auditor related to the IPO, this might put the company at a disadvantage by causing a delay in the timing of its filing. We believe this work can proceed simultaneously and that the current timing of the required communication under ISB No. 1 in the case of an IPO is sufficient to allow the audit committee to properly assess the auditor's independence prior to the company's initial filing.

Currently under ISB No. 1, certain information is required to be reported to the audit committee if in the "*auditor's professional judgment*" it may reasonably be thought to bear on

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independence. In making that determination, the auditor is currently required to consider not only relationships that are specifically proscribed by the SEC and PCAOB rules, but also the general standard of auditor independence and four fundamental principles set forth in the Preliminary Note to Rule 2-01 of Regulation S-X. Although the Board's stated intention for omitting these words is to "clarify the requirement by reminding auditors of the need to focus on the perceptions of reasonable third parties when making independence determinations," we believe the removal of this language may serve to confuse, rather than clarify, the requirement. Since the Board believes that the auditor will still "need to apply professional judgment to determine what is reasonable under particular facts and circumstances," consideration should be given to retaining the "auditor's professional judgment" language and making reference to the SEC general standard and four principles of auditor independence in the adopting release or the proposed rule.

Subject to the recommendation to maintain the standard of "*auditor's professional judgment*", we support the proposal's requirement for the auditor to (i) annually provide details in writing to the audit committee, (ii) have discussions with the audit committee, and (iii) document the substance of the discussions with the audit committee.

3. Responses to Specific Questions

The Release seeks responses to six specific questions. We have addressed these below.

A. Question 1

Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?

We believe the communication requirements under the proposed rule will likely assist the audit committee in fulfilling its obligations with respect to auditor independence, particularly when contemplating a change in auditor. However, it is unclear how the proposed rule would enhance compliance with the auditor independence requirements by registered firms. EY has policies, processes, and procedures in place, which are annual, periodic or event driven (e.g., IPO, new client acceptance, business combinations, change in control) to help ensure auditor independence during the applicable audit and professional engagement period. As a result, we do not believe that the differences between the proposed rule and the existing requirements under ISB No. 1 and the SEC and PCAOB rules would enhance EY's ability to fulfill its obligations with respect to auditor independence.

Under the proposed Rule 3526, an auditor would be required to communicate "*prior to accepting an initial engagement pursuant to the standards of the PCAOB*." Currently

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this communication occurs, as required by ISB No. 1, prior to a company's initial filing and at least annually thereafter. While services must be pre-approved prior to engaging an accounting firm as the issuer's auditor, there is no existing requirement to specifically communicate information on certain other relationships to the issuer's audit committee at the time it is making a decision regarding a change in auditor. The proposed rule would not change the firm's obligation to ensure that it is independent during the audit and professional engagement period prior to accepting a new audit client. However, since auditor independence is a mutual responsibility, the proposed rule may assist the audit committee with fulfilling its obligations with respect to auditor independence when considering a change in auditor.

As noted above, the timing of the required communication for private companies contemplating an IPO should be reconsidered as the acceleration of the timing of the communication from that which is currently required under ISB No. 1 may interfere with a company's ability to complete its IPO within its desired timeframe.

B. Question 2

Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?

We believe that requiring communication of certain information, similar to that required annually under ISB No. 1, prior to becoming an existing issuer's auditor will aid the audit committee in its decision making process. The proposed rule should serve to improve the consistency of information being received by audit committees from all accounting firms under consideration for selection. Consistency in the communication received by the audit committees would offer a comparative look at the accounting firms and their respective independence matters, understanding that the same types of relationships were considered and principles were applied, and that appropriate professional judgment was employed. The additional information and consistency of such information would help facilitate the audit committee's assessment regarding a firm's independence and decision about whether to retain an accounting firm as the issuer's auditor. The proposed requirements would serve to augment the discussions between the audit committee and the accounting firm(s) involved in the proposal process.

C. Question 3

Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? If so, what communications should the auditor be required to make to the audit committee?

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Open and transparent communication is an important part of the relationship between the auditor and the audit committee. It helps to ensure that both parties have the information necessary to fulfill their shared responsibility as it relates to independence. We believe the information concerning independence currently required to be communicated under ISB No. 1, enhanced by the change in the timing of the required communication for a change in auditor of an existing issuer under proposed Rule 3526, would be sufficient for the audit committee to fulfill its obligations with respect to auditor independence. We do not believe that additional information is necessary to accomplish the Board's objective and, in fact, could unnecessarily overburden the audit committee. The communication should disclose information that is useful and relevant to a particular company's audit committee and we would continue to encourage audit committees to request additional information to fulfill the specific needs of that audit committee or issuer.

D. Question 4

To what extent, if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?

Registered accounting firms are required by ISB No. 1 to communicate relevant information related to the firm's independence to the audit committees of its issuer audit clients. In our experience, discussions between the audit committee and EY generally occur in connection with IPOs, changes in auditors to EY, at least annually for EY issuer audit clients, and with respect to significant transactions in which an issuer audit client engages (for example with respect to an acquisition). We communicate to audit committees those financial, employment, and business relationships, and services and fee arrangements during the audit and professional engagement period that, in our professional judgment, may reasonably be thought to bear on independence, taking into consideration the particular facts and circumstances and available guidance from the SEC and PCAOB. In addition, accounting firms are required to communicate information on the scope of proposed services and fee arrangements sufficient for the audit committee to make its own determination regarding the permissibility of such service and fee arrangement, pursuant to SEC and PCAOB pre-approval rules including PCAOB Rules 3524 and 3525 which cover specific pre-approval requirements for certain non-audit services.

EY's communications with audit committees are not limited to the required formal communications but also generally consist of frequent informal dialogue and discussion with the audit committee about independence related matters. These informal communications, which may be initiated either by us or the audit committee, assist both parties in fulfilling their mutual responsibility for auditor independence.

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Accounting firms may not, necessarily, be communicating the same information as required under ISB No. 1 to audit committees prior to being engaged as the auditor of an issuer unless requested by the issuer's audit committee. EY's current policy is to assess such relationships and evaluate whether we are independent under the applicable SEC and PCAOB rules for the anticipated audit and professional engagement period(s) and communicate our findings to the audit committee prior to accepting an issuer as a new audit client or prior to the filing of an initial registration statement under the SEC rules for an existing private audit client.

E. Question 5

Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why and how long should the period be?

Information regarding certain relationships is used by the audit committee to assess an auditor's independence during the expected audit and professional engagement period, as defined by the SEC. The initial communication under proposed Rule 3526(a) should require the disclosure and discussion of information for the timeframe that is of relevance to the audit committee. We believe that prior to filing an initial registration or making a decision to retain a new accounting firm, the relevant relationships are those that exist currently, or will continue to exist, during the expected audit and professional engagement period. Since the relationships that may potentially bear on an accounting firm's independence are generally limited to those that exist during the audit and professional engagement period, requiring identification and communication of relationships existing prior to this period would cause an unnecessary burden on the accounting firm to identify and communicate these matters, and on the audit committee to consider such information, bearing in mind that the accounting firm was not subject to the auditor independence rules with respect to this company at that prior time. We recognize that in certain instances an issuer may request that the accounting firm provide relevant information about a longer period; such would be the case if the audit committee needed to have information about the firm's ability to potentially audit restated financial statements for prior years for various reasons.

Once an independence matter is communicated to the audit committee in writing, we do not believe it is necessary to repeat the communication of this matter unless the matter continues to exist in a future audit period or is an on-going matter. We recognize that audit committee members may change from time to time; however, the continuing or prior audit committee members may inform the new members of the matters that they believe have a bearing on auditor independence on a going forward basis.

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Although certain services rendered by an accounting firm prior to the start of the audit and professional engagement period may continue to have an effect on the issuer's financial statements, such services would not impair the successor auditor's independence and should not be required to be communicated under proposed Rule 3526. Examples of services that may have a continuing impact on future periods include appraisals, valuations, Section 404 related procedures, and financial information systems design and implementation. If the results of those services were subject to audit by the predecessor auditor, we believe that disclosure of such services would not be warranted since the services would have no bearing on the independence of the potential successor auditor. Comments made by Michael W. Husich, Associate Chief Accountant, Office of the Chief Accountant, in a speech on December 11, 2006 at the AICPA National Conference on Current SEC and PCAOB Developments and a recent FAQ issued by the Staff of the SEC on August 6, 2007 on prohibited and non-audit services, support the thinking that such services would not need to be disclosed in the initial communication since the successor auditor's independence would not be impaired.

F. Question 6

Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?

Current PCAOB Rule 3523(c) contains a transition rule which addresses the appropriate time period for a registered accounting firm to complete or otherwise terminate tax services provided to a person who becomes an FROR due to a "change in employment event". That transition period is 180 days, provided the work was being performed pursuant to a previously existing engagement on which work of substance has been performed. A previously existing engagement implies an engagement in progress as opposed to an existing client relationship where there is no current work being performed. We believe that a transition period is appropriate for purposes of Rule 3523 for engagements in process at the time of initial engagement to perform an audit in accordance with the standards of the PCAOB. This transition period should cover not only the new auditor situation and the IPO situation contemplated by the Note to Rule 3523, but also other events that may result in the initial application of the Rule, such as a subsidiary previously deemed immaterial becoming material or a new equity-based transaction occurring which causes the company being audited to become subject to the provisions of Rule 3523. The application of a transition period would be beneficial to both audit clients and FRORs who could find their compliance with all relevant tax requirements threatened by the current and proposed PCAOB Rules.

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The Board has already identified 180 days as an appropriate transition period for services rendered pursuant to change in employment events. This time period could allow tax services to be provided to an FROR during the period when audit services are being provided to the issuer. Thus, the Board has already evaluated the independence risk concerning tax services provided to persons in an FROR role and concluded that reasonable transition periods are an important aspect of the Rule. If a company were to hire a new CFO, the existing auditor would be permitted under the current Rule to continue to provide service to that individual for 180 days. To provide a shorter or different period for new audit engagements or initial public offerings would serve to add an unnecessary complexity and inconsistency to the PCAOB Rules. Therefore, we support a consistent transition period for all situations where one is needed and we believe that the situations contemplated by the Board's proposed amendments to Rule 3523 are situations where a transition period is needed.

Companies are increasingly global in scope and the definition of FROR could include employees around the world. At the time a firm would be engaged as auditor, it would be possible for that firm to have several tax services engagements in process to FRORs in different countries of the world. Different tax regimes exist with many different filing dates. The accounting firm and the company should be aware of the relationships that exist as of the date of the appointment, but some of those engagements may not be able to be terminated without considerable cost or inconvenience to the FROR. While the start of the professional engagement period can be managed to a certain degree by the timing of the signing of the engagement letter or the initiation of audit procedures, this does not offer sufficient flexibility to address practical situations. Further, a delay in the start of the professional engagement period in order to terminate various personal tax services would possibly create a situation where the new accounting firm has less time to become familiar with the company's books and records prior to issuing its first report or completing a quarterly review. In the United States, a personal tax return is due 3 ½ months after the beginning of the year. Upon request, the tax return due date can be extended for an additional 6 months. Thus, the process of preparing a tax return for a client in the US can span 9 ½ months. In other parts of the world, the due dates for personal tax returns are not consistent with April 15, and, in many jurisdictions, extensions of the filing deadline are not permitted. Thus, the requirement of a "hard stop" on the date of the appointment as auditors could cause hardship and lead to situations where registered public accounting firms and audit committees are forced to deal with such matters which do not compromise the basic issues surrounding auditor independence.

Forcing tax service provider changes within a short time period can have an impact on the FROR who potentially could be facing two significant issues:

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- The need to complete the existing tax engagement and ensure he or she complies with the relevant tax laws to timely file the associated returns.
- The need to find a new qualified tax service provider.

The combination of these two activities can be difficult for an FROR if sufficient time is not available especially since the time available to resolve these issues is not within the control of the FROR.

The same timing and global issues regarding the audit client discussed above may force the FROR to turn to another provider prior to the completion of a tax engagement. Switching to a new tax service provider prior to the completion of an existing tax engagement can create duplicate time, effort and costs to the FROR. Additional time should be allowed to complete work in progress to alleviate a significant portion of this duplication of time, effort and cost. The application of a transition period similar to the one currently provided within Rule 3523(c)(2) would allow sufficient time for the completion of work in progress without adding any additional risk than is currently had with a change in employment status.

In addition to the time, effort and cost to the FROR, there is the additional risk that the FROR may find it difficult to immediately find a qualified replacement for tax services provided by the current audit firm. Without a sufficient transition period, the FROR may be faced with the need to rush with the identification of competent replacements, review such choices, and then make a selection of the most appropriate replacement. Furthermore, in many global assignments, the choices available to the FROR may be limited due to independence or other reasons relevant to the issuer.

Undoubtedly, there is a need to transition to a new tax service provider in these situations. The question is whether the FROR should be faced with the difficult task of doing this within a very limited time period when he or she also has pressing needs to have an existing tax engagement completed. The added complexity of choosing an appropriate replacement provider warrants the need for a transition period. There needs to be sufficient time to ensure that a complete and accurate assessment can be completed before a decision as to the new tax service provider is made. The risk of additional time, effort, cost and the potential of choosing an inappropriate tax service provider due to time constraints out of the FROR's control outweighs any small risks involved by providing a transition period similar to what is provided within current Rule 3523(c)(2).

The Board's proposals encompassed in Rule 3526 would offer the accounting firm and the audit committee an opportunity to assess the permitted tax services rendered to FRORs and to determine if limitations on those services during the transition period are warranted. For instance, the audit committee might decide that the tax services could be

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limited to tax return preparation only as opposed to tax planning. Alternatively, the audit committee might decide to require a shorter time period for transition.

We encourage the PCAOB to consider a broad application of a transition period to include other situations in which a company or an individual first becomes subject to Rule 3523. Merger and acquisition transactions during the year may cause similar challenges to those described above for individuals who are FRORs at companies involved in the transactions. Such transactions may be more problematic than a change in auditor situation, in which it may be possible to delay the start of the engagement period, because a transaction date may not be flexible due to financing or other business reasons. In addition, FRORs at a subsidiary that becomes material to the consolidated financial statements for the first time during the year may not be aware they are subject to the Rule until after year end. Without a transition period for these types of situations, the potential exists for many inadvertent violations of Rule 3523, even though such situations may have no more of an effect on auditor independence than services provided during a change in employment event.

We recognize in certain very rare instances tax services that have been provided to individuals in an FROR role in the audit period may have an impact on the financial statements of the audit client. Such rare circumstances could be where the tax services include advice on transactions where there may be a mutuality of interest or conflicting positions between the tax treatment of the individual and that of the employer. This could be the situation in an IPO environment where the auditor could be advising the FRORs about personal tax matters and where the tax effect to the FRORs and shareholders is impacted by decisions the company makes. We believe these circumstances, if they exist, would warrant more consideration and evaluation from an independence perspective but we believe that the assessment should be based on the existence of the service or the relationship, and made jointly by the independent accounting firm and the audit committee. This assessment could conclude as to an appropriate transition period for the services within the period allowed by the PCAOB.

Conclusion

For the reasons cited above, Ernst & Young LLP strongly supports the proposal to amend Rule 3523 to strike the words “audit and” from the current text of Rule 3523. We also support the addition of the proposed Note concerning initial public offerings to Rule 3523 with the additional recommendation that the Board consider transactions and events which are equivalent to IPOs. We believe this is a reasoned approach and one that does not fundamentally impact independence.



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We also urge the Board to consider a modification to add a transition period to the Rule. We support a Board clarification that treats an “initial engagement to perform an audit pursuant to the standards of the PCAOB, similar to that of a “change in employment event” as that term is defined in Rule 3523(c). This clarification would allow for the time limited exception to the rule to come to bear. We believe this change would improve standardization of the Rule provisions within Rule 3523(c) while maintaining the overall protection originally intended by the Rule. Given the rationale previously stated, we believe a standard transition period is more appropriate than multiple Rules to address different situations. The potential impact on independence is not different and a similar approach simplifies the application of the Rule in otherwise complex situations.

We also fully support the Board’s efforts to encourage communication regarding independence matters between the accounting firm and the audit committee. We support the intent of proposed Rule 3526 to require appropriate information concerning the accounting firm’s independence to be communicated to the issuer’s audit committee at the time that the audit committee is making the decision to retain the accounting firm as the issuer’s auditor. We request the Board reconsider the timing requirements of the proposed Rule which could apply in the event of an IPO, including clarifying the requirements so that a company’s decision to register shares is not unduly delayed while an audit firm evaluates its independence under the rules of the PCAOB, and that the Board consider specifying the time period of the consideration in an initial appointment circumstance to be the current period and the expected audit and professional engagement period. This would take into account, depending on the specific circumstances and the audit committee’s interests and expectations, that this could include multiple periods including some in the past in the event of the possible need for re-audits for a variety of reasons.

We would be pleased to provide the Board with additional information on these matters and our views as addressed by this letter.

Respectfully submitted,

A handwritten signature in black ink that reads "Ernst & Young LLP". The signature is written in a cursive style with a large, flowing 'E' and 'Y'.

Attachment

Attachment

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May 18, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street N.W.
Washington, D.C. 20006-2803

Re: Rulemaking Docket Matter No. 17

Mr. J. Gordon Seymour:

Ernst & Young LLP (EY) is pleased to comment on the *Concept Release Concerning Scope of Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles, Implementation Schedule for Rule 3523* as requested in PCAOB Release No. 2007-002 dated April 3, 2007. We support the PCAOB's efforts to provide and enhance guidance on the PCAOB Ethics and Independence Rules Concerning Independence, Tax Services, and Contingent Fees (the Rules) and matters surrounding implementation, particularly those aspects of the Rules that may unnecessarily impact registrant's choices when seeking to make a change in the registered firm conducting its audit. We have previously submitted comments and provided views to the Staffs of both the PCAOB and SEC on the Rules and our Firm's understanding and implementation processes surrounding these Rules.

The Concept Release indicates the Board is interested in views on whether the distinction that Rule 3523 relates to services provided to individuals and not to the audit client directly has a bearing on the nature and the extent of any independence concerns that may exist with respect to tax services provided during the audit period to persons covered by Rule 3523. The Concept Release seeks responses to two specific questions.

We have addressed these matters below:

1. Question 1

To what extent, if any, is a firm's independence affected when the firm, or an affiliate of the firm, has provided tax services to a person covered by Rule 3523 during the portion of the audit period that precedes the professional engagement period?

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As the Board notes, under currently existing Rule 3523, if a registered firm provides tax services during the audit period, but before the commencement of the professional engagement period, this is an impairment of independence and this violation cannot be remedied by the registered firm's ceasing to provide the tax services before accepting the engagement. Accordingly, in this circumstance, the registered firm may not become the auditor to the company. This is consistent with the SEC's auditor independence rules regarding proscribed services—i.e. that an accountant is not independent if prohibited services are provided during the audit and professional engagement period. However, a recent speech by Mr. Michael Husich, Associate Chief Accountant, Office of the Chief Accountant, provides important new thinking on this point. Mr. Husich states that in instances of potential auditor change, this occurrence will not operate to deem an accountant not independent when certain services are provided in the audit period, but prior to being appointed the auditor, so long as such services:

- relate solely to the prior period which is audited by a predecessor auditor
- will not be subject to audit procedures by the successor auditor, and
- are not management functions.¹

With respect to the tax services contemplated by Rule 3523, the criteria above can, in most instances, be easily applied leading to enhanced consistency with the recent views of the Staff as expressed in Mr. Husich's speech. If tax services have been provided to individuals in financial reporting oversight roles (FROR) during the audit period, but prior to being appointed the auditor, applying the above criteria addresses the potential of an independence threat based on the principles of independence as found in the Preliminary Note to Regulation S-X, Rule 2-01 (b) which states.

¹ Speech by Mr. Michael Husich, December 11, 2006 at the AICPA National Conference on Current SEC and PCAOB Developments. "I have a few comments concerning three matters, for which additional guidance is being considered. First, five of the prohibited services delineated in Rule 2-01(c) (4) (bookkeeping, financial information system design and implementation, appraisal or valuation services, actuarial services, and internal audit outsourcing services) have an exception condition, "unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the client's financial statements", also known as the "not subject to audit" provision. **The staff's position is that a successor auditor's independence would not be impaired if the successor auditor provided prohibited non-audit services in the current audit period and these services (i) relate solely to the prior period which is audited by a predecessor auditor, (ii) will not be subject to audit procedures by the successor auditor, and (iii) are not management functions."** (emphasis added)

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"In considering this standard, the Commission looks in the first instance to whether a relationship or the provision of a service: creates a mutual or conflicting interest between the accountant and the audit client; places the accountant in the position of auditing his or her own work; results in the accountant acting as management or an employee of the audit client; or places the accountant in a position of being an advocate for the audit client."

While the services contemplated by Rule 3523 do not necessarily have the safeguard of being subject to the audit procedures of the predecessor auditor, they are not services provided to the audit client but, rather, to individuals who serve in FROR roles at the audit client. Indeed, it would be rare that the results of tax services provided to an individual in an FROR role would impact the financial statements at all. The fact that these services are provided to the individual and not to the audit client act to counter any mutuality of interest.

We believe the Board's concept release has recognized the significant and compelling difference between services provided to an individual who is in an FROR role and services provided directly to the audit client. The Board has already, in part, differentiated these services, as Rule 3523 has a time limited exception in Rule 3523(c) which permits continuation of a tax services engagement to a person who becomes subject to Rule 3523 due to certain changes in the individual's employment (employment events). This time limited exception already recognizes that tax services provided to an individual in an FROR role can be continued during an audit period without immediately impairing independence. We concur that services rendered to an individual in an FROR role, prior to an auditor appointment, are fundamentally different from services provided directly to an audit client. It is our view that if the Board determined to amend Rule 3523 to only encompass the "professional engagement period" as opposed to the "audit and professional engagement period" such change will not raise any new or additional independence considerations surrounding personal tax services to individuals in an FROR role. We find this consistent with the direction of Mr. Husich's speech cited above and we find that direction an appropriate balance between the importance of an auditor's independence and the ability of registrants to have adequate choices in auditor selection and not be impeded in such choices by services that do not fundamentally affect auditor independence as they were commenced and, in many cases delivered, prior to being considered to be the auditor.

We recognize in certain rare instances tax services that have been provided to individuals in an FROR role in the audit period may have an impact on the financial statements of the audit client. Such rare circumstances could be where

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the tax services include advice on transactions where there may be a mutuality of interest or conflicting positions between the tax treatment for the individual and that of the employer. Should such rare circumstances arise, they could create a situation where tax services to an individual in an FROR role create the potential for an independence concern. This situation was noted in comments of the Internal Revenue Service, the Securities and Exchange Commission and the PCAOB in February 2005 concerning the transactions entered into by certain taxpayers concerning executive stock options². We believe these circumstances are rare following both the reforms of the Sarbanes-Oxley Act, the PCAOB's rulemaking and operational changes incorporated into the tax practices of many accounting firms. We believe these circumstances, if they exist, would warrant more consideration and evaluation from an independence perspective prior to client acceptance but believe that the assessment should be based on the existence of the service or the relationship, not the time frame in which the service was rendered and are adequately provided for in existing literature and guidance.

2. Question 2

What effect, if any, would application of Rule 3523 to the audit period have on a company's ability to make scheduled or unscheduled changes in auditors? Could any such effect be minimized or managed through advanced planning or otherwise?

This question in the Concept Release focuses on a company's ability to make scheduled or unscheduled changes in its auditors based on the application of Rule 3523 to the audit period. An auditor change may occur relatively quickly and often under a high degree of confidentiality. This can occur in transaction driven situations and other circumstances. In other instances, the decision to consider an auditor change is made well in advance. Where possible, advance planning would minimize an effect of Rule 3523. However, advance planning is not always possible. Further, for confidentiality reasons, not all individuals in an FROR role may be informed of a company's possible evaluation of changes in its auditor.

We believe application of Rule 3523 to the audit period would serve to limit a company's potential choices among auditors. We believe this is not in the best interests of shareholders and other participants in the capital markets. Approximately 70% of the Fortune 1000 companies report their financial results on a calendar year basis. For such companies, the audit period begins January 1

² IR 2005-17 February 22, 2005 Settlement Offer Extended for Executive Stock Option Scheme and comments of the PCAOB and SEC.

and continues to December 31. Any plan to consider a change in auditor initiated after January 1 exposes the company to have fewer potential firms that can perform the audit due to the application of Rule 3523 to the audit period. In addition, considering the tax filing deadline in the United States, the selection process may coincide with and overlap with April 15th - the initial deadline for U.S. personal income tax returns. It is likely that an auditor selection process which started March 1 would find that several firms would not be independent due to tax services provided to individuals in an FROR role for a period after January 1 of that year.

The above example only addresses the potential impact of the audit period beginning prior to the professional engagement period for U.S. tax compliance services in calendar year audit situations. Further conflicts will also be created when dealing with various foreign tax compliance filing requirement dates for individuals in FROR roles and/or audit clients with other than calendar year ends. As an example, in many foreign jurisdictions, there is no mechanism for the extension of tax return filing deadlines. Therefore, an announced auditor change could potentially place an individual in an FROR role in a position of considerable hardship to file a tax return on a timely basis. Absent an appropriate transition rule, the individual in an FROR role may be forced, under extreme time constraints and at a significant cost, to identify a new service provider.

We believe the hardship imposed on companies by the current provisions of Rule 3523 exist whether the auditor change is scheduled or unscheduled. Unscheduled changes often occur in a tight timeframe and provide many other issues beyond tax services to individuals in FROR roles. In the case of scheduled changes, the additional time may simplify the issue, but, often, does not. There may be more than one potential audit firm (especially in global organizations) providing tax services to individuals in FROR roles at the time of commencement of an evaluation of auditors. Even with advance planning, it is possible that confidentiality concerns may create difficulties in determining whether a potential audit firm is providing services to individuals in an FROR role. The definition of who is an FROR covers a range of individuals at both the parent company and its material subsidiaries and affiliates around the world. Should an auditor have to communicate to an individual tax service client that independence concerns relating to a possible auditor change make it impossible for the audit firm to provide the individual with tax service, that auditing firm could find itself in a position of violating a request for confidentiality during the proposal process. Again, this would be an example of putting a potential audit firm and the company in an impractical position.



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Given that companies often use multiple non-audit service providers, continued application of the provisions of Rule 3523 could lead to circumstances where not only is the company restricted in its choice of audit providers but individuals in FROR roles are restricted in their choice of tax service providers. Without this revision, it is possible that companies would adopt a policy of restricting individuals in FROR roles from using the tax services of certain audit firms. This creates a lack of choice for these individuals and quite possibly denies them access to the specialized tax services they may require.

Conclusion

For the reasons cited above Ernst & Young would strongly support if the Board determined to amend Rule 3523 to strike the words “audit and” from the current text of Rule 3523 (as identified in footnote 9 of the Concept Release). We believe this is a reasoned approach and one that does not fundamentally impact independence.

We also urge the Board to consider a further but related modification. We support a Board clarification that treats a change in auditor in a manner similar to that of a “change in employment event” as that term is defined in Rule 3523 (c). This clarification would allow the time limited exception to the rule to come to bear. We believe this change would improve standardization of the Rule provisions within Rule 3523 (c) while maintaining the overall protection originally intended by the Rule. Given the rationale previously stated, we believe a standard transition period is more appropriate than multiple rules to address different situations. The potential impact on independence is not different and a similar approach simplifies the application of the Rule in otherwise complex situations.

We would be pleased to provide the Board with additional information on the matters and our views as addressed by this letter.

Respectfully submitted,

A handwritten signature in black ink that reads "Ernst & Young LLP". The signature is written in a cursive style with a large, flowing 'E' and 'Y'.

July 27, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street N.W.
Washington, D.C. 20006-2803

Re: PCAOB Rulemaking Docket Matter No. 17
Proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*; Proposed Amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*; and Implementation Schedule for Rule 3523
July 24, 2007

Dear Board Members,

I am submitting my comments to you regarding the above referenced Rulemaking Docket Matter. These are my personal comments and do not necessarily reflect those of my employer. You specifically asked respondents to answer six (6) questions regarding Proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*. I begin with comments on the Proposed Amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*.

Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles

In the very first paragraph I find concern with two seemingly undefined items. How do we define “the professional engagement period”? The Board indicates that if a registered public accounting firm starts an attestation engagement on Day 1, no tax services may be performed until the report is issued. Suppose the report is issued on Day 185. It is conceivable that the person for whom the return is prepared may extend their filing date, which may be Day 205. A subsequent extension may bring the actual filing to Day 300. Even though the actual filing apparently occurs outside the time of “the professional engagement period,” one could reasonably believe that the tax services were contemplated during the performance time of the attestation engagement.

This also leaves the question of the commencement date. Does the Board intend to begin “the professional engagement period” with fieldwork; or is it when the engagement manager begins to review files, staffing requirements, budgets, and scheduling needs with the issuer? Is it when the issuer’s audit committee signs the engagement letter, or when the proposal is submitted to the audit committee?

Furthermore, a definition of “a person in a financial reporting role” is needed. How far down the corporate chain does this go? Could it include anyone with the authority to approve a general ledger journal entry? The Board hints at this in subsection (b)(1), yet we may run into another issue of defining materiality. For example, Issuer Corporation’s (“Issuer”) registered accounting

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firm (“the Firm”) determines that materiality is \$50,000,000 on the consolidated financial statements. Issuer has 100 locations. No location could reach the threshold on a net income basis, but five locations have gross revenues in excess of \$500,000,000 – ten times materiality. Given that “a person in a financial reporting oversight” role may receive a bonus based upon location performance, even a non-material journal entry could move the location from missing the goal to reaching the goal. Therefore, I recommend (b)(1) be struck and (b)(2) be merged into a single section (b).

I strongly disagree with section (a). The board of directors has too much responsibility to ignore their role in financial reporting oversight. I recommend that paragraph (a) be struck in its entirety.

Section (c) and its sub-paragraphs and note appear to be reasonable.

Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence

- 1. Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?**

I believe that Rule 3526 moves in that direction. I have some suggestions below in my answer to Item 3 and after my response to Item 6.

- 2. Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?**

This rule ought to achieve that goal.

- 3. Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? Is so, what specific communications should the auditor be required to make to the audit committee?**

Here is the first of my more detailed suggestions for the Board. The Rule begins:

A registered public accounting firm must –

- (a) in its prior to accepting an initial engagement proposal to the issuer's audit committee pursuant to the standards of the PCAOB ...**

This will require all firms bidding on the issuer's professional engagement to assess independence before being awarded the engagement. Then further down:

- (a)(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (a)(1) on the independence of the registered public accounting firm, should it be appointed or retained as the issuer's auditor ...**

I believe the three added words guide us towards what the Board intends and describes in section (b). See my recommendations after my response to Item 6.

4. To what extent, if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?

I am not aware of the communication between my company's audit committee and our registered public accounting firm.

5. Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why, and how long should the period be?

I do not believe there ought to be any limit on when a relationship first existed. To illustrate this, I will use the Firm and Issuer from my discussion of Rule 3523 above.

Suppose Issuer hired a controller, who at the time of the interview was employed by the Firm. At that time several years ago, Issuer was contemplating going public and wanted to hire someone with SEC experience. Issuer has been reporting for a few years engaging another registered public accounting firm, and the audit committee has opted to put the audit engagement out to bid. While it may stand to reason that all parties concerned know that the controller (who may have been promoted in the intervening years) once worked for the Firm, it ought to be clearly acknowledged. This ensures that all members of the audit committee are aware of the past relationship.

It may actually work to the benefit of the Firm and Issuer to have this past relationship. Since the Board placed a premium on prior knowledge to guide external auditors in planning and performing their audits (new Auditing Standard No. 5), this "prior knowledge" of the Firm's methods may assist Issuer in producing documentation with more ease. In addition, Issuer will have a deeper appreciation of what the Firm needs to perform their procedures.

Ensuring that this information is openly discussed is important if there is ever a problem with the audit. One can assume that a lawyer will bring that past relationship into court.

6. Should the Board provide a transition period in Rule 3526 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?

Given the time frame for approval, I recommend that this Rule be effective immediately for issuers with fiscal years ending on or after December 15, 2007. Tax work ought to be complete for 2006. For those issuers whose most recent fiscal year end is between January 1, 2007 and December 14, 2007, who have engaged a registered external accounting firm (either initial professional engagement or retaining the prior year's firm)

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the transition period ought to be through the filing of the tax return, including proper extensions. However, I also recommend that the tax work be fully disclosed in appropriate filings, including fees for such services, and clearly documented in audit committee meeting minutes.

I also recommend the following changes and additions to Rule 3526.

(b) at least annually with respect to each of its issuer audit clients –

~~(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in a financial reporting oversight role at the audit client that may reasonably be thought to bear on independence;~~

~~(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (b)(1) on the independence of the registered public accounting firm;~~

~~(3)(1) affirm to the audit committee of the issuer, in writing, that the registered public accounting firm is independent in compliance with Rule 3520; and~~

~~(4)(2) document the substance of its discussion with the audit committee of the issuer.~~

(c) as soon as the registered public accounting firm becomes aware of a potential impairment due to a previously unknown or new relationship –

~~(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in a financial reporting oversight role at the audit client that may reasonably be thought to bear on independence;~~

~~(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (c)(1) on the independence of the registered public accounting firm;~~

~~(3) affirm to the audit committee of the issuer, in writing, that the registered public accounting firm is independent in compliance with Rule 3520; or~~

~~(4) describe to the audit committee of the issuer, in writing, that the registered public accounting firm's independence is impaired under Rule 3520 and must resign; and~~

~~(5) document the substance of its discussion with the audit committee of the issuer.~~

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I believe that these changes protect all parties – issuers, auditors, and investors. It appears that Rule 3526 as presented presumes independence is not (could one say, “never”) impaired by these relationships. It is important that we understand that independence may be impaired. We also want to recognize that independence is in fact and appearance. (See Securities and Exchange Commission pamphlet at <http://www.sec.gov/info/accountants/audit042707.htm> for further discussion.) Independence may be impaired merely in appearance to an investor, and this ought to be enough to give the audit committee and registered public accounting firm pause.

If the registered public accounting firm does need to resign, we ought to have time to put the engagement out to bid as soon as possible. While section (b) states that the registered public accounting firm will affirm its independence “at least annually”, the Board may wish to guide the firms when this affirmation is needed. I recommend that it occurs before substantial planning procedures commence. Many audit committees may meet with their auditors to discuss the prior year’s engagement period and discuss how the upcoming engagement can be smoother. This is an excellent opportunity for this affirmation. Some may argue that this affirmation of independence occurs by default when the registered public accounting firm issues its report. I suggest that the Board not take this approach.

Thank you for your efforts and attention to this matter.

Respectfully submitted,
Frank Gorrell, MSA, CPA
Frank Gorrell, MSA, CPA

Accountants and Business Advisors

September 14, 2007

Office of the Secretary
 Public Company Accounting Oversight Board
 1666 K Street, NW
 Washington, DC 20006-2803

Re: PCAOB Rulemaking Document Matter No. 017 – Proposed Ethics and Independence Rule 3526,
Communication with Audit Committees Concerning Independence, and Proposed Amendment to
 Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles* (PCAOB Release No.
 2007-008)

Dear Board Members and Staff,

As a leading public accounting, tax, and business advisory firm, Grant Thornton LLP (“Grant Thornton”) appreciates the opportunity to provide comments on key questions and issues affecting the criteria used to establish registered public accounting firms’ independence. We welcome the opportunity to share our views on the Public Company Accounting Oversight Board’s (“Board” or “PCAOB”) Proposed Ethics and Independence Rule 3526 (“Proposed Rule 3526”), *Communication with Audit Committees Concerning Independence*, Proposed Amendment to Rule 3523 (“Proposed Rule 3523 Amendment”), *Tax Services for Persons in Financial Reporting Oversight Roles*, and the Board’s related questions in PCAOB Release No. 2007-008.

Grant Thornton LLP is the U.S. member firm of Grant Thornton International, a global organization of member firms in over 100 countries. The views and comments expressed in this letter represent those of Grant Thornton LLP and do not constitute the views of Grant Thornton International or any of the other Grant Thornton International member firms.

Grant Thornton strongly supports the Board’s commitment to strengthen the ethics and independence of registered public accounting firms that audit issuers’ financial statements. Grant Thornton believes that robust ethics and independence standards are integral to investor confidence in the integrity of the audited financial statements.

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Proposed Rule 3526

Grant Thornton LLP is generally supportive of Proposed Rule 3526. Historically, Grant Thornton has supported the recommendations of the Blue Ribbon Commission and the independence rules and interpretations of the Independence Standards Board, and the U.S. Securities and Exchange Commission (“SEC” or the “Commission”) independence rules (Section G of the January 2003 final rule, *Strengthening the Commission’s Requirements Regarding Auditor Independence*), which encourage robust, periodic communication between an issuer’s audit committee and the independent accounting firm. Proposed Rule 3526 would require documentation of the substance of discussions between an independent accounting firm and the issuer’s audit committee. It would supersede *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* (“ISB 1”), and ISB 1’s two related interpretations.

Grant Thornton understands that Proposed Rule 3526 would require a registered public accounting firm (“registered firm”) to provide the audit committee of a prospective or current issuer audit client (the “issuer audit committee”) with the following:

- Written disclosures of relationships that may reasonably be thought to bear on the independence of the registered firm and its affiliated firms and discussions of the potential effects of these relationships on the registered firm’s independence before the firm’s acceptance of an initial engagement
- Similar written communications on an annual basis thereafter, including an independence affirmation that the registered firm is independent pursuant to PCAOB Rule 3520

We believe that the written communications and discussions between the registered firm that is the auditor of record and the issuer audit committee emphasizes the importance of independence, in fact and in appearance, as a critical component of audit quality. The discussions provide an opportunity to augment the identified independence threats and safeguards that may reasonably be thought to bear on the registered firm’s independence. However, we would request that the Board consider our comments on the following topics before final approval of Proposed Rule 3526:

- Consistency of Proposed Rule 3526 with existing SEC independence rules
- Definition of “affiliates of the firm”
- Recognition of legal impediments to Rule 3523 disclosures
- Audit period pertaining to initial and subsequent written communications
- Additional guidance for issuers without audit committees
- Multiple issuers with the same audit committee, such as entities within the same investment company complex

Consistency with the SEC's January 2003 final independence rule

As required by the Sarbanes Oxley Act of 2002 (the "Act"), Section G of the SEC's January 2003 final independence rules includes detailed requirements on auditor communications with audit committees, including an independence requirement. We believe that the Board's independence communications requirement should be consistent with Section G since it represents the SEC's codification of the Act.

Specifically, we believe that the guidance in Section G pertaining to investment companies and entities within the same investment company complex with respect to the timing of required communications, including the independence letter, modernizes the requirements imposed by ISB 1 and its related interpretations. Further, for initial registrations by an entity within the same investment company complex or control group, we believe that the Section G requirements for communications with the investment company complex's audit committee—that is, 90 days before the initial filing—should be sufficient to comply with Proposed Rule 3526.

Definition of affiliates of the firm

Proposed Rule 3526 requires communication of all relationships between the "registered public accounting firm or any affiliates of the firm." In its interim or final rules, the Board has not defined "affiliates of the firm." Grant Thornton encourages the Board to adopt a definition consistent with the SEC's term "associated entities" (FRR 602.01.H.2). Alternatively, we request that the Board either specifically define the term through reference to PCAOB standards or rules or, similar to the European Union, adopt criteria for identifying network firms.

Potential legal impediments for disclosure of personal income tax information

The Internal Revenue Code and state tax provisions specifically prohibit disclosure of personal income tax information by tax preparers without the specific consent of the clients. Furthermore, many foreign jurisdictions exercise more stringent legal prohibitions on disclosure of personal information due to strict data privacy laws and regulations. However, if a Grant Thornton International member firm has a legal impediment to providing requested information to Grant Thornton LLP, we may not be able to provide full disclosure to a prospective issuer client's audit committee. Additionally, we anticipate that all non-US registered accounting firms will have to obtain a legal opinion on their ability to make such disclosures when the firms subsequently update their PCAOB registration.

Due to the significant preparer penalties imposed on violations of taxpayer confidential information or privacy statutes, we believe that the Board needs to specifically address these legal impediments before adoption of this requirement. Therefore, we ask the Board to consult with its own legal and international counsel on how best to structure the requirement to disclose confidential information related to income tax services provided to an individual in a financial reporting oversight role (FROR) or the individual's family members.

Audit period in the initial written communications and in the annual updates

Grant Thornton recommends that the initial written communication include only the audit period(s) in which independence will be required if the prospective auditing firm is named as the issuer's auditor of record. The successor auditor is required to be independent of the audit periods for which the auditor renders its reports, through the period of the engagement, and, in subsequent periods when the auditor-client relationship has ceased, the period of the updates to the auditor's report. The predecessor auditor must be independent at the date(s) of its reports and the registrant will ask the predecessor auditor to consent to the inclusion of its report or reports in the filing. The successor auditor does not take responsibility for any of the registrant's fiscal years or periods unless the successor subsequently audits that period.

In normal circumstances, the successor auditor and the audit committee need not be concerned about the successor auditor's independence in prior periods. In the event of a restatement or a reaudit, the successor auditor will undertake a thorough independence analysis of the prior period(s) to assess whether the successor could audit the period(s). Therefore, we believe that there may be little benefit gained from requiring the auditing firm to disclose all independence matters affecting any year that independence is not required.

Further, the checks for independence conflicts require substantial effort by both company management and the auditing firm. Due to the complexity of the SEC's definition of an "affiliate of the audit client" (Rule 2-01(f)(4)), an independence analysis of all affiliates would be a time-consuming process. For example, if a portfolio company of a large private equity group is an issuer due to publicly traded debt securities, the registered firm must undertake an analysis not only of the portfolio company and its direct affiliates, but also of the other portfolio companies and their affiliates controlled by the same private equity group. This would trigger multiple layers of inquiry and analyses that would result in disclosure that has no bearing on the audit committee's requirements under The Act or Section D of the SEC's January 2003 independence rules.

Fundamentally, we believe that the underlying principle in Proposed Rule 3526 should be enhancement of the communications and dialogue between the prospective or current auditor of record and the audit committee. As a result, we recommend that the written communications and discussions address independence threats and related safeguards that either arise during the audit period or, if the matters arose in prior periods, are of continuing importance to the audit committee. In other words, all independence concerns that may reasonably be thought to bear on the auditor's independence in the current period should be addressed.

Grant Thornton understands that the independent directors on an audit committee may periodically change. However, we believe that before agreeing to become an independent director and serving on the audit committee, the prospective audit committee member should undertake its own due diligence by reading the audit committee charter, the disclosures in the proxy statements or other filings pertaining to auditor independence, the committee's minutes, and previously issued written communications by the auditor of record. As clearly delineated in the Act, the audit committee members have certain responsibilities related to maintaining the auditor's independence. Therefore, we categorically reject that the auditor of record has a responsibility to perform the due diligence for a prospective audit committee member or an audit committee member who forgoes its duties.

While an audit committee or the auditor of record may elect to include prior periods or independence matters that no longer pertain to the current audit, Grant Thornton does not support inclusion of matters that are no longer pertinent to the audit committee's assessment of the registered firm's independence. Therefore, we believe that limiting the relevant audit period or periods to those in which the auditor is engaged in providing services, as well as limiting independence matters to issues that fall under PCAOB standards, best achieves Proposed Rule 3526's underlying principle.

Issuers without audit committees

We also encourage the Board to provide guidance for situations in which an issuer audit client does not have an audit committee. Under the ISB 1 standards, the independence disclosures would default to the issuer audit client's governing board or body. We believe that many entities initiating an initial public offering may not have an audit committee or an independent board member who could serve on the audit committee when it initially files with the Commission. Further, other entities also may lack audit committees, such as certain employee benefit plans that file on Form 11-K, certain foreign private issuers, limited partnerships with publicly traded units, or unit investment trusts.

Additionally, the SEC rules requires a registered firm to apply the PCAOB standards if it is a secondary auditor or if its auditor's report for a nonissuer is included in an issuer's filing with the Commission. For example, the SEC requires application of PCAOB standards for the audit of a nonpublic entity that is a significant investee of a registrant and for reports on an asset-backed securities servicer or subservicer. Frequently, a secondary firm may be a non-US accounting firm auditing certain international operations and, depending on whether the firm "plays a substantial role" in the audit, it may or may not render an auditor's report in filing with the Commission. In these cases, the principal or primary auditor frequently asks the secondary auditor for independence affirmations and for information for its ISB 1 communications to the issuer, but the secondary auditor may not have the opportunity to review the primary auditor's ISB 1 communication or to be a party to the independence discussions with the issuer's audit committees. Because we believe that these communications are largely beyond the secondary auditor's control, we request consideration of an exemption for secondary auditors from Proposed Rule 3526's requirements for communication with the issuer's audit committee.

Multiple issuers with the same audit committee

Many mutual funds, unit investment trusts, limited partnerships, or other similar entities that are in the same investment company complex may not have separate audit committees or governing boards. Frequently, the registered firm's engagement includes the audit of the initial deposit or a start-up mutual fund. For these types of entities, written communications to the audit committee or its equivalent have conformed to the requirements of Section G of the SEC's January 2003 final independence rules. We believe that initial communications within the 90 day period permitted by Section G for an investment company complex substantially meets the spirit and intent of Proposed Rule 3526's requirement for written communications and discussions to occur before the period of the engagement begins.

PCAOB questions and Grant Thornton comments**1. Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?**

The requirement to have a registered firm disclose and discuss independence matters that may reasonably be thought to bear on the auditor's independence will assist an issuer audit committee fulfill its responsibilities before engaging a new auditor. However, we believe that Proposed Rule 3526 largely codifies existing practice for registered firms. As a practical matter, before a registered firm agrees to be appointed as the auditor of record, it generally analyzes all identified relationships in the current audit period and in prior audit periods that are thought to have a bearing on the firm and its affiliated firms' independence.

In our experience, an issuer audit committee generally requires issuer management to undertake similar due diligence. Further, consistent with the requirements of Section 202 of the Sarbanes-Oxley Act and Section D of the SEC's January 2003 final independence rules, an issuer audit committee invariably evaluates a prospective auditor's independence as one of its primary qualifications. Neither the newly appointed registered firm nor an issuer audit committee wants to negatively affect investor confidence with the resignation of a newly appointed auditor due to independence issues that were not fully vetted before the change was announced.

Because Proposed Rule 3526 corresponds closely to ISB 1 and its interpretations' requirements to update an auditor's identification of independence threats and safeguards and the auditor's conclusions thereon at least annually, we believe that the proposed rule does not create any substantive changes in current practice for registered firms or issuer audit committees.

2. Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?

As discussed above, audit committees adhere to Section D of the SEC's January 2003 final independence rules, the audit committee charter, and/or exchange guidelines in the performance of their duties. In our experience, an issuer audit committee generally requests that both company management and all of the proposing registered firms conduct thorough, global independence fact gathering and analysis before a new auditor is appointed. Registered firms and issuer audit committees currently discuss and resolve any identified independence matters before the new auditor's appointment. Therefore, we do not believe that Proposed Rule 3526 will greatly enhance current practice.

3. Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? If so, what specific communications should the auditor be required to make to the audit committee?

In addition to matters that may reasonably be thought to bear on independence, Proposed Rule 3526 would require the registered firm to disclose whether it or any associated firm had performed tax services, prior to the beginning of the audit period, for an FROR or the FROR's immediate family member. As previously discussed, Grant Thornton requests that the PCAOB consider the numerous legal impediments that exist in the US and internationally that could impact a registered firm's ability to meet this requirement. We ask that the Board consult its US and international tax counsel before finalizing this requirement.

4. To what extent, if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?

We believe that registered firms already comply with the disclosure requirements of Section G of the Commission's January 2003 final independence rule, including the independence letter specified in section 3. We also believe that these communications, except for the disclosure of tax services to an FROR or its immediate family members, between the prospective auditors and the audit committee represent common practice.

5. Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why and how long should the period be?

As discussed above, the initial communication should be limited to the relationships that existed during the prospective client's audit period or periods in which the auditor initially renders its report. For example, for an existing registrant, Grant Thornton believes that the period of interest to the audit committee is the period in which the registered firm is engaged to perform the audit or audits under PCAOB standards, which is generally the current fiscal period. For an entity undergoing initial registration with the Commission, the auditor would include all periods included in the auditor's report in the auditor's initial communication to the audit committee or its equivalent.

However, if independence threats are ongoing, such as permitted services or relationships, then the auditor should continue to include these matters in written communications and in discussions until the auditor concludes that these matters are no longer pertinent. The auditor needs to provide sufficient information for the audit committee to make its own assessment of auditor independence.

At some point, the effort required to develop the information about relationships in the past and to discuss that information with the audit committee outweighs the value of such information to the audit committee. A clear limitation on the scope of both diligence that the firm must perform and matters that the audit committee must consider will make the process more efficient. It will also help accountants and audit committees to focus on relationships that are most likely to be relevant in ascertaining whether the accounting firm is independent for purposes of the current audit.

Proposed Rule 3523 Amendment

Grant Thornton strongly supports the Proposed Rule 3523 Amendment. As we discussed in our May 17, 2007 comment letter on the questions posed in PCAOB Release No. 2007-002, Grant Thornton strongly supports eliminating the prohibition against providing tax services to an FROR or its immediate family members in the client's fiscal period before the engagement begins. We believe that the elimination of this prohibition will greatly enhance an audit committee's ability to select a new independent auditor.

If the tax services to the FROR or its immediate family members are completed or terminated before the professional engagement period begins, we believe that there is no ongoing mutuality of interest or continuing association. For a US FROR, we believe that a mutuality of interest may possibly exist if tax positions recommended by the registered firm do not meet either the PCAOB's or US Internal Revenue Service's "more likely than not" criteria. In evaluating its independence with respect to the issuer, its officers, directors, and substantial shareholders, the registered firm now generally assesses the tax consulting and compliance services provided to an FROR or its immediate family members to evaluate whether an ongoing mutuality of interest exists.

Grant Thornton also strongly endorses the Board's stated intention to provide a footnote to explain the application of Rule 3523 in the context of an initial public offering ("IPO"). We concur with the Board's conclusion that Rule 3523 should not apply before the earlier of when the registered firm signs an initial engagement letter to perform an audit pursuant to PCAOB standards or begins audit or interim review procedures.

We would request that the Board consider other circumstances in which an entity becomes an issuer. For example, a registration may arise from the

- Issuance of publicly traded debt
- Issuance of partnership or other units
- Reverse merger in which a nonpublic entity succeeds to the public registration
- Inclusion of a public sponsor's securities in an employee benefit plan and a determination by SEC counsel that a Form 11-K filing is required
- Decision by a foreign private issuer to file with the Commission
- Exceeding 500 shareholders coupled with the entity's total assets exceeding \$10 million as of the latest fiscal year end

PCAOB questions and Grant Thornton comments

6. **Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?**

The Board has solicited additional comment on the practical implications of not providing a transition period for a registered firm to complete tax services after the professional engagement period begins. We believe that an initial transition period should be permitted to ensure consistency with Rule 3523's current 180-day transition period. Since a transition period is permitted if an individual becomes an FROR or if a corporate event occurs, we do not see any substantial difference between these situations and the appearance of a mutuality of interest when a registered firm is initially engaged as the auditor of record.

The FROR bears the most significant hardship for terminating tax services since it must find another tax return preparer to meet its filing deadlines. The registered firm providing the service to the FROR may suffer damage to its reputation if it terminates the FROR's tax services because it believes the FROR may have difficulty meeting filing deadlines. We believe that requiring a registered firm to terminate services when such termination may cause potential harm or jeopardy to a tax client generally runs counter to the accountant's professional ethics and value systems.

Grant Thornton

Further, the audit committee (assuming there are no legal impediments to the Proposed Rule 3526 disclosure) is placed in an equally untenable position. The issuer audit committee may need to select a registered firm that is not its first choice or engage a firm that will have to resign from any tax services engagement with an FROR before the engagement period begins. If there is no ongoing mutuality of interest created by providing the tax services and such services are terminated within 180 days of the start of the engagement, we believe that the audit committee should be able to exercise its responsibilities under the Act and Section D of the January 2003 independence rules without additional constraints.

In addition, Rule 3523 requires that the registered firm terminate or conclude tax services to any FROR or its immediate family members at any of the issuer's material subsidiaries. The determination of whether a subsidiary is a material affiliate is in itself an audit procedure. Additionally, due to changes in operations, business strategy, or growth, different subsidiaries may become more significant during a given audit period. Also, certain locations may be subject to audit procedures due to periodic rotation of various locations for the integrated audit procedures. If an entity became a significant subsidiary or is subject to audit procedures during the audit period, the issuer and the auditor need sufficient time to terminate previously permitted tax services to an FROR or its immediate family members at that entity.

The ability of a US registered firm and a non-US registered firm to terminate or extend the deadline for a tax filing may differ greatly. While a US-registered firm may terminate its tax services engagement or obtain an extension for filing tax returns, non-US firms may face significant legal impediments in terminating services or obtaining extensions of filing due dates. We believe that a 180-day transition period would alleviate many of the legal impediments and other issues faced by non-US firms in complying with Rule 3523.

Finally, Grant Thornton does not see any theoretical difference between the permitted 180-day transition period permitted for a new FROR or another corporate event and the change in auditors. If no mutuality of interest is assumed for the permitted transition period, then no mutuality of interest should be presumed for the finalization of tax services from the date that the period of the engagement commences.

* * * * *

We would be pleased to discuss our comments with you. If you have any questions, please contact Karin French, Assistant National Managing Partner of Professional Standards, at 703-847-7533.

Very truly yours,

Grant Thornton LLP

Grant Thornton LLP



KPMG LLP
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September 6, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

**PCAOB Rulemaking Docket Matter No. 017:
Proposed Ethics and Independence Rule 3526; Proposed Amendment to
Rule 3523 and Implementation Schedule for Rule 3523**

Dear Mr. Secretary:

KPMG LLP appreciates this opportunity to comment on the Public Company Accounting Oversight Board's (PCAOB or Board) Release No. 2007-008 that includes the following Appendices (collectively, the Proposals):

- Proposed Amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*
- Proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*

As further explained in this letter, we generally support:

- The Proposed Amendment to Rule 3523 to exclude the portion of the audit period that precedes the beginning of the professional engagement period from the scope of the Rule; and
- Proposed Rule 3526 on communication of independence matters with audit committees.

We believe the rationale for the Proposals, as expressed in the Release accompanying the Proposals, is well reasoned and practicable. We provide two recommendations for the Board's consideration in adopting the final rules.



Proposed Amendment to Rule 3523

We believe that Rule 3523 should be amended further to include a transition period to allow registered firms to complete any in-process services subject to Rule 3523. The transition period should be 180 days from the date that the professional engagement period begins. The decision to permit completion of the services within the transition period should be approved by the audit committee. A transition period is necessary and appropriate for the following reasons:

- Without a transition period, it is likely that one or more registered firms will determine that they cannot comply with Rule 3523 within the timeframe permitted. This would have the effect of reducing an audit committee's choices of registered accounting firms and could ultimately have a negative impact on the public interest; and
- Rule 3523 already provides a 180 day transition period for covered tax services to employees of an audit client who are promoted to a financial reporting oversight role. This exception recognizes the practical considerations and unnecessary hardships to individuals associated with quickly terminating in-process engagements and the minimal threat to independence associated with allowing completion of those services within a brief transition period. Providing a similar transition period for individuals in financial reporting oversight roles at new audit clients seems reasonable and would result in a consistent application of the rule for similar situations.

Proposed Rule 3526

With respect to proposed Rule 3526(a), it is our current practice to discuss with audit committees of both prospective audit clients and existing audit clients where we are being engaged to perform an audit pursuant to PCAOB standards for the first time (e.g., an initial public offering) the relationships that exist or existed that may reasonably be thought to bear on independence. We support the formalization of this process in Rule 3526.

With respect to the scope of the initial communication required under proposed Rule 3526(a), we believe that the proposed Rule appropriately defines the method for identifying matters that should be communicated to audit committees. Establishing a specific period in the proposed Rule could result in a “one size fits all” approach that could result in the arbitrary exclusion of certain relationships. To promote the disclosure of all relationships reasonably thought to bear on independence, we believe that Rule 3526(a) should not place limits on the periods that registered firms should consider when evaluating matters to be communicated to audit committees.

KPMG

We would like to take this opportunity to formally recognize the efforts of the PCAOB and its staff in development of the Proposals. We welcome the opportunity to participate in strengthening auditor independence and serving the public interest.

We would be pleased to clarify any comments or answer any questions about our comments. Please call or write David Winetroub at (212) 909-5552 or dawinetroub@kpmg.com.

Very truly yours,

KPMG LLP



August 27, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

Via e-mail to: **comments@pcaobus.org**

Re: PCAOB Release No. 2007-008 July 24, 2007:
PCAOB Rulemaking Docket Matter No. 17

To the Members of the Board:

We appreciate the opportunity to offer comments to the Public Company Accounting Oversight Board (Board) on the Proposed Ethics and Independence Rule 3526, Communicating with Audit Committees Concerning Independence, Proposed Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles and Implementation Schedule for Rule 3523 (Proposal). The National Association of State Boards of Accountancy's (NASBA) goal is to increase the effectiveness of State Boards of Accountancy. In furtherance of that objective, our Regulatory Response Committee (Committee) offers the following comments on the Proposal.

The Board is proposing to amend Rule 3523 to exclude the portion of the audit period that precedes the professional engagement period from the scope of Rule 3523. The Committee believes that an enterprise should have the widest possible selection of registered public accounting firms (registered firms) if and when the enterprise decides to change auditors. The Committee also believes that independence of the registered firm selected will not be impaired if the Board adopts its proposal to amend Rule 3523. The Committee supports the Board's proposal.

The Board is also considering whether or not to allow for a transition period in Rule 3523 to accompany the proposed amendment. A transition period would permit a registered firm to conclude tax services to a person in a financial reporting role for the client -- or an immediate family member of such a person -- for a period of time after the initial acceptance of a professional engagement. If a transition period is provided in the rule, we recommend that it state no further services could be undertaken during the transition period.

A transition period will keep open the number of registered firms that an enterprise can choose from if and when it changes auditors. Although in most circumstances an enterprise will have sufficient time to schedule a change to another auditor, there are situations where the present auditor may have to be replaced on short notice. One example would be the commencement of certain litigation between the registered firm

PCAOB
August 27, 2007
Page 2 of 3

and the auditor. Another example would be where the present auditor has become the auditor of a competitor and the enterprise does not want to use the auditor that its competitor uses. The quarterly and yearly reporting requirements of the enterprise may not allow for a long period of time to choose another auditor. The Committee believes that a transition period for a reasonable period of time should be permitted.

Rule 3523 has a provision for a 180-day transition period when a person in a non-financial reporting oversight role takes on such a role because of hiring, promotion or other change in employment. The Committee believes that the same 180-day period be allowed for a transition period when a registered firm is first engaged. Such a period should provide sufficient time to allow the registered firm and any affiliated firm to conclude the otherwise prohibited tax service engagements. The Committee believes that the public interest is served by a transition period because it allows for the largest pool possible of registered firms that could be chosen as auditors. Also, the Committee believes that public perception of independence will not be affected because the period will be in harmony with an existing transition period.

The Board is proposing Rule 3526 that would expand the communications between a registered firm and its client's audit committee. The Committee supports the disclosures proposed. Although audit committees can ask for any information that they want prior to retaining a registered firm, a rule that requires the proposed initial disclosures will provide a good starting point for discussion of services previously rendered to the prospective client that should be considered by an audit committee. The audit committee can always ask for more information. The Committee also supports the proposal for ongoing disclosures.

Additionally, the Committee agrees with the position of the Board that the basic reasonableness standard proposed not be modified with the words "in the auditor's professional judgment."

The period to be covered for disclosures prior to engagement should be long enough to give the audit committee a good idea of services previously performed. The Committee believes that disclosures to an audit committee prior to initial engagement should cover a period of three years. That information should still be readily available from the records of the registered firm.

Some of the proposed disclosures may require a registered firm to obtain consent from an individual before confidential services rendered to the individual are disclosed to the prospective enterprise client. Although the responsibility to obtain such consent rests with the registered firm, the Committee believes that it would be helpful if the final release by the Board includes a comment that appropriate consents should be obtained prior to disclosure of confidential information and accepting an engagement.

PCAOB
August 27, 2007
Page 3 of 3

We hope these comments will assist the Board in its work.

Very truly yours,

Sincerely,



Wesley P. Johnson, CPA
NASBA Chair



David A. Costello, CPA
NASBA President & CEO



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September 7, 2007

Public Company Accounting Oversight Board
Office of the Secretary
1666 K Street, N.W.
Washington, DC 20006-2803

By e-mail: comments@pcaobus.org

Re: Proposed Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence

**PCAOB Release No. 2007-008
PCAOB Rulemaking Docket Matter No. 017**

The New York State Society of Certified Public Accountants, representing 30,000 CPAs in public practice, industry, government and education, welcomes the opportunity to comment on the proposed rule referenced above.

The NYSSCPA's Auditing Standards and Procedures Committee deliberated the proposed rule and drafted the attached comments. If you would like additional discussion with us, please contact Robert W. Berliner, the Chair of the Auditing Standards and Procedures Committee, at (212) 503-8853, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,

David A. Lifson
President

Attachment



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COMMENTS ON PCAOB PROPOSED RULE 3526

Communication with Audit Committees Concerning Independence

PCAOB Release No. 2007-008

PCAOB Rulemaking Docket Matter No. 017

September 7, 2007

Principal Drafters

**Robert W. Berliner
Anna Zubets**

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NYSSCPA Staff

Ernest J. Markezin

NYSSCPA COMMENTS ON PCAOB PROPOSED RULE 3526**Proposed Ethics and Independence Rule 3526,
Communication with Audit Committees Concerning Independence****GENERAL COMMENTS**

We agree with the proposed rule as it relates to independence communications during the engagement period. We also agree that the registered public accounting firm should be required to provide information about its independence to the audit committee before being engaged as the company's auditor. However, we recommend that the registered public accounting firm should be required to confirm its independence in writing to the audit committee prior to accepting an initial engagement as well as annually during the engagement period.

We recognize that, prior to performing an audit of the financial statements of the issuer, the auditor cannot be expected to be aware of all relationships that may reasonably bear on its independence. Therefore, the auditor's letter to the audit committee should state that, based on the information provided to it by the issuer, it believes that it would be independent of the issuer if it were engaged as auditor. This information would assist the audit committee in making its choice of auditor.

MATTERS ON WHICH SPECIFIC COMMENTS WERE REQUESTED**1. Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor's independence?**

Yes, the proposed independence communication requirements would help registered firms and audit committees in fulfilling their respective obligations.

2. Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?

Yes, the proposed initial communication would help the audit committee in selecting the issuer's auditor.

3. Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee?

As discussed in the general section above, we recommend that prior to accepting an audit engagement, a registered public accounting firm should provide an audit committee with a letter confirming its independence. The letter should communicate that, based on the information provided by the issuer, the firm believes that it would be independent of the issuer if it became its auditor.

4. To what extent if any, are accounting firms already making the kinds of communications that would be required by proposed Rule 3526?

The Committee does not have sufficient information to respond to this question.

5. Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why, and how long should the period be?

The initial communication should apply, at a minimum, to those relationships that existed during the audit period. Further, the rule should require the accounting firm to consider communicating any relationships that existed prior to the audit period if a reasonable third party may perceive such relationships as bearing on the auditor's independence.



North Carolina State Board of Certified Public Accountant Examiners

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August 20, 2007

Office of the Secretary
 PCAOB
 1666 K Street, N.W.
 Washington, D.C. 20006-2803

Re: PCAOB Rule Making Docket Matter No. 017

To Whom It May Concern:

The North Carolina State Board of CPA Examiners (the Board) has reviewed the PCAOB's proposed amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles* and the proposed ethics and independence rule, Rule 3526, *Communication with Audit Committees Concerning Independence*.

The Board agrees with the amendment to Rule 3523 to exclude the portion of the audit period that precedes the professional engagement period to determine the possible effects on a firm's independence of providing tax services to a person covered by Rule 3523.

The Board also agrees with the content of the proposed new independence Rule 3526 and the requirement to disclose all relationships that may reasonably be thought to bear on independence, whether those relationships existed during the period under audit or during earlier periods.

The Board is very appreciative of the PCAOB's efforts to improve the auditing standards related to independence that will certainly have a positive impact on the reliability of work performed by CPAs.

Sincerely,

A handwritten signature in black ink, appearing to read "Arthur M. Winstead".

Arthur M. Winstead, Jr., CPA
 President



September 7, 2007

Public Company Accounting Oversight Board
 Office of the Secretary PCAOB
 1666 K Street, N.W.
 Washington, DC 20006-2803

PricewaterhouseCoopers LLP
 101 Hudson Street
 Jersey City NJ 07302
 Telephone (201) 521 3000
 Facsimile (201) 521 3333

Re: PCAOB Rulemaking Docket Matter No. 017 - Proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*; Proposed Amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*; Implementation Schedule for Rule 3523

To the Members of the Board:

PricewaterhouseCoopers LLP ("PwC") appreciates the opportunity to provide comments on the Public Company Accounting Oversight Board's (the "Board") proposed Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence* ("Rule 3526") and proposed amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles* ("Rule 3523").

We support the proposed amendment to Rule 3523, but believe that the rule should be further modified so that the transition period applies to all individuals in a financial reporting oversight role (FROR) regardless of when they become subject to the rule. Likewise, we agree with the Board's proposed new Rule 3526, but believe that it could be enhanced as detailed in our comments below.

Amendments to Rule 3523

Application of Rule 3523 during the professional engagement period

If amended as proposed, Rule 3523 would apply to the professional engagement period in new audit client acceptance situations. We fully support this proposal since it maintains a level of auditor independence commensurate with the principal goal of investor protection and does so without imposing unnecessary burdens that could limit a registrant's choice of auditors. (This is discussed at greater length in our comment letter of May 18, 2007, regarding the Board's concept release concerning the scope of Rule 3523).

We also agree with the Board that, as stated in the eighth paragraph of Part II of the Release, it is unnecessary to restrict the provision of tax services during the portion of the audit period that precedes the professional engagement period in order to preserve auditor independence. The Board's rationale for this conclusion follows that sentence, which we agree with as well. To ensure that the strength of this conclusion is not diluted, if the



Board decides to include this paragraph in the release accompanying the final rule, we recommend that the last two sentences in that paragraph be deleted. Those sentences send a contradictory message by calling for firms to assess whether their independence is impaired despite the Board's conclusion that restrictions are unnecessary to preserve independence. We believe the Board's conclusions on these matters are sufficient to stand on their own and any language accompanying such conclusions that introduces confusion or sends mixed messages should be avoided. As a practical matter, we expect that firms will be alert to unique circumstances that deserve analysis. Accordingly, it is unnecessary to include language in the Release that attempts to capture those situations with a broad-brush approach that risks confusing readers and dilutes the Board's message.

Broadening the circumstances in which the 180-day transition period should apply

In its previous consideration of Rule 3523, the Board concluded that it was appropriate to provide a 180-day transition period to ensure that individuals in a FROR are not subjected to undue hardship because they are hired or promoted into a FROR (including other change in employment events) at an audit client when the tax services they receive are both: (1) provided pursuant to an engagement that was in process before the hiring, promotion, or other change in employment event; and (2) completed on or before 180 days after the hiring or promotion event.

The practice of granting such a transition period, concurrent with the adoption of a newly promulgated independence standard, is a well-established and generally accepted practice. A prominent example includes the transitional provisions granted under the Securities and Exchange Commission's November 2000 final rule release, *Revision of the Commission's Auditor Independence Requirements*, which contains transition periods relating to certain financial interests and all the employment provisions. Such allowances represent an equitable approach that balances the threats to independence with undue hardship considerations. We support this approach and believe that the Board should extend the existing transitional provisions of Rule 3523 to include individuals in FRORs who become subject to the rule by virtue of a merger or acquisition, an IPO or new audit appointments as the same principle of avoiding undue hardship on individuals in FRORs previously embraced by the Board is equally applicable to such events and, therefore, should be subject to consistent treatment.

In these circumstances, absent equitable allowances for transition, where the prospective auditor had previously been engaged to prepare the personal tax return of an individual in a FROR, it is necessary to attempt to complete the assignment prior to the effective date of the merger or acquisition or, in the case of an IPO or new audit appointment, the earlier of signing the engagement letter or commencing audit procedures. The completion of outstanding tax work, however, may present considerable difficulties in practice, given the wide range of compulsory tax return filing dates, which vary from



country to country.¹ In addition, many jurisdictions do not have facilities to request extensions to filing, as noted in the comment described on page 5 of the Release.

The absence of transitional relief may cause unnecessary hardship for individuals in FRORs whose tax return preparation work was well underway at the point of the IPO, merger or acquisition or new audit appointment. Individuals in FRORs may be left with uncompleted returns, requiring them to seek a new provider to finish the return. This has cost implications for the individual in a FROR (or their employer, if the employer has agreed to bear the cost of the return preparation) and compliance implications with the attendant risk of incurring penalties and interest for late filing. Most, if not all, foreign jurisdictions attribute full responsibility for timely filing to the taxpayer concerned rather than the preparer.

As the Board has already concluded that it is possible to balance the threats to independence while avoiding undue hardship for individuals in FRORs, we believe it appropriate to adopt a consistent approach that allows transition periods for IPOs, mergers or acquisitions, and new audit client acceptance situations. Recognizing that there may be other situations where a transition period would be appropriate (e.g., a reverse merger with an existing registrant), and that it is unreasonable to expect the Board to envision all such situations, we believe that it would be appropriate for the Board to also provide audit committees with some degree of flexibility in utilizing, as may be appropriate in the circumstances, the 180-day transition period in other comparable situations relating to tax services provided to individuals in FRORs.

Proposed Rule 3526

Initial communication with the audit committee

We support the Board's newly proposed Rule 3526, which would supersede the Independence Standards Board's Standard No. 1, *Communications with Audit Committees*, and its related interpretations. We believe that the proposed requirement to undertake independence discussions with the audit committee *prior* to engagement serves to emphasize the critical importance of auditor independence through transparent discussions undertaken at the outset of the professional engagement. The timing of such communications will provide a level of prominence to auditor independence and heightened awareness that will assist both audit committees and the auditors they retain in fulfilling their respective obligations.

Period to be covered by the initial communication

¹ Examples of non-US filing deadlines include: UK – January 31st, South Africa – February 28th, Japan – March 15th, Russia – April 30th, Germany – May 31st, and Australia – October 31st.



The Board has requested comments about the period to which the initial communication should relate. As defined within the Board's current rules, existing independence requirements apply to the "audit and professional engagement period". This long-standing, widely-known, and generally accepted principle is based on the understanding that the period during which the "reasonable investor" would expect the auditor to maintain independence with respect to the audit client includes the period covered by the financial statements on which the auditor reports (the audit period), as well as the period during which the auditor has been engaged to perform the audit (the professional engagement period). As such, we believe that, if appointment occurs during the audit period, the initial communication should cover relationships that exist or existed during the period covered by the audit that are thought to bear on the auditor's independence.

Sometimes an auditor is asked to propose on the audit of a future period e.g., respond by September 1, 2007 to a request for proposal with respect to the audit period beginning on January 1, 2008 (this is in contrast to the timing contemplated in the preceding paragraph). We suggest that for purposes of the initial communication in this circumstance, the auditor (1) make the audit committee aware of any relationships that exist at the time of the proposal and are subject to the required proposed communication; (2) discuss how these relationships bear on auditor independence; and (3) discuss any actions required.

Disclosures relating to individuals in FRORs

With regard to the proposed disclosure requirement relating to individuals in a FROR, we suggest that the Board provide an exemption in circumstances where applicable legal restrictions (such as privacy and confidentiality regulations) impede an auditor's ability to fully comply with this disclosure requirement.

We would be pleased to discuss our comments and to answer any questions that the PCAOB staff or the Board may have. Please contact Joseph Marucci (201-521-4470) regarding our submission.

Sincerely,

A handwritten signature in black ink, appearing to read "Joseph Marucci".

PricewaterhouseCoopers LLP



August 27, 2007

Office of the Secretary
Public Company Accounting Oversight Board
1666 K Street, N. W.
Washington, D. C. 20006-2803

RE: PCAOB Rulemaking Docket Matter No. 017

To Whom It May Concern:

One of the expressed goals of the Texas Society of Certified Public Accountants (TSCPA) is to speak on behalf of its members when such action is in the best interest of its members and serves the cause of Certified Public Accountants in Texas, as well as the public interest. The views expressed herein are written on behalf of the Professional Standards Committee (PSC) of the TSCPA. The committee has been authorized by the TSCPA Board of Directors to submit comments on matters of interest to the committee membership. The views expressed in this letter have not been approved by the TSCPA Board of Directors or Executive Board and, therefore, should not be construed as representing the views or policy of the TSCPA. We appreciate the opportunity to provide input into your deliberations on the above-referenced Exposure Draft (ED).

In general, the members of the PSC are in agreement with the direction of the proposed standard. We have addressed each of the six questions presented in the ED and provide the following comments related thereto for your consideration.

Question 1: Would proposed Rule 3526 assist registered firms and audit committees in fulfilling their respective obligations with respect to auditor independence?

We believe that a significant tax engagement performed by a public accounting firm for key members of an entity's financial oversight group prior to being engaged to perform attestation services for the entity would, in most instances, have minimal impact on the independence of the public accounting firm. We do believe that a consideration of such prior tax work should be made by the entity's audit committee in evaluating any impact on the public accounting firm's independence. It is the responsibility of the audit committee to make the final decision regarding any independence problems that such prior relationships might impose.

Question 2: Would proposed Rule 3526 assist audit committees in making a decision regarding the appointment of a new auditor?

We consider the proposed Rule to be of assistance to the audit committee in its deliberations regarding the appointment of a new auditor. However, the audit committee needs to decide on the extent of the prior relationships between members of the entity's financial oversight group and the proposed new audit firm that it needs to consider. The audit committee is responsible for making an informed decision on the independence of any new audit firm it wishes to consider. Thus, the audit committee should solicit the proposed new auditor to disclose the prior or current tax engagements with the entity that it considers to be relevant to its decision regarding the firm's independence.

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Question 3: Should proposed Rule 3526 require the registered public accounting firm to communicate any additional matters on auditor independence to the audit committee? If so, what specific communications should the auditor be required to make to the audit committee?

We believe the significant issue regarding auditor independence as described in the ED is the performance of tax work for key members of the entity's financial oversight group. To expand the ED to include "additional matters on independence" would result in a need for expanded guidance that would do little to enhance the proposed rule. The performance of tax work for key members of the entity's financial oversight group is the critical issue regarding independence and should be the primary focus of the ED.

Question 4: To what extent, if any, are accounting firms already making the kinds of communications that would be required by the proposed Rule 3526?

Based on the personal experience of PSC members, we believe every effort is made to disclose any and all relationships between the accounting firm personnel and key members of the entity's financial oversight group. In most instances, we believe this disclosure also extends to family members of the financial oversight group. Public accounting firms, in our opinion, appear to be well aware of the responsibility they have to disclose any activities that might impact their independence with respect to new attest clients.

Question 5: Should the initial communication required under proposed Rule 3526(a) be limited to relationships that existed during a particular period? If so, why, and how long should the period be?

We do not believe there should be a limiting time frame regarding the relationships that existed between the public accounting firm and the prospective audit client. We feel the audit committee should be charged with the responsibility of determining the relevant time frame within which it considers an event could impact the auditor's independence. The decision is being made by the audit committee members and only they know what time frame is relevant for their consideration.

Question 6: Should the Board provide a transition period in Rule 3523 to allow a registered public accounting firm to complete covered tax services once the professional engagement period begins? If so, why is such a transition period necessary? How long should any such transition period be?

We believe the registered public accounting firm should be allowed time to complete a pending tax engagement up to the time the firm begins its year-end audit work. We feel work on the tax engagement can be continued, if necessary, during the time the firm is performing interim audit work. However, once the year-end audit work commences there should be no additional time spent on the tax engagement. Thus, if the tax engagement cannot be completed prior to the initiation of year-end audit work, the tax engagement should be terminated and the client should seek the assistance of another accounting firm to complete the tax engagement.

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We appreciate the opportunity to provide input into the standard setting process.

Sincerely,

A handwritten signature in black ink, appearing to read "Sandra K. Johnigan".

Sandra K. Johnigan, CPA, CFE
Chair, Professional Standards Committee
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ETHICS AND INDEPENDENCE RULE 3526, COMMUNICATION WITH AUDIT COMMITTEES CONCERNING INDEPENDENCE))))	PCAOB Release No. 2008-003
AMENDMENT TO INTERIM INDEPENDENCE STANDARDS)))	April 22, 2008)
AMENDMENT TO RULE 3523, TAX SERVICES FOR PERSONS IN FINANCIAL REPORTING OVERSIGHT ROLES))))	PCAOB Rulemaking Docket Matter No. 017
IMPLEMENTATION SCHEDULE FOR RULE 3523)))))

Summary: The Public Company Accounting Oversight Board ("PCAOB" or "Board") is adopting an ethics and independence rule, Rule 3526, *Communication with Audit Committees Concerning Independence*, that will supersede the Board's interim independence requirement, *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* ("ISB No. 1"), and two related interpretations. The Board is also adopting an amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*, and further adjusting the implementation schedule for Rule 3523 as it applies to tax services provided during the audit period. Specifically, amended Rule 3523 will not prohibit tax services provided during the portion of the audit period that precedes the beginning of the professional engagement period. In order to maintain the status quo while the SEC considers this amendment, the Board has further delayed the implementation of the prohibition against pre-engagement period tax services to persons in financial reporting oversight roles in existing Rule 3523 until December 31, 2008. The amendment to Rule 3523 will become effective immediately upon approval by the SEC, and Rule 3526 will become effective on the later of September 30, 2008, or 30 days after the date the SEC approves the rule.



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* * *

I. Introduction

On July 26, 2005, the Public Company Accounting Oversight Board ("PCAOB" or "Board") adopted certain rules related to registered public accounting firms' provision of tax services to public company audit clients. As part of this rulemaking, the Board adopted Rule 3523, which provides that a registered firm, subject to certain exceptions, is not independent of an audit client if the firm, or an affiliate of the firm, provides tax services during the audit and professional engagement period to a person in, or an immediate family member of a person in, a financial reporting oversight role ("FROR") at an audit client. Rule 3523 was intended to address concerns related to auditor independence when auditors provide personal tax services to individuals who play a direct role in preparing the financial statements of public company audit clients. Rule 3523 was approved by the Securities and Exchange Commission ("SEC" or "Commission") on April 19, 2006.

On April 3, 2007, the Board issued a concept release to solicit comment about the possible effects on a registered firm's independence of providing tax services to a person covered by Rule 3523 during the portion of the audit period that precedes the beginning of the professional engagement period and other practical consequences of applying the restrictions imposed by Rule 3523 to that portion of the audit period.^{1/} With a few exceptions, commenters on that release recommended that the Board amend Rule 3523 to exclude that portion of the audit period.

^{1/} See PCAOB Release No. 2007-002 (April 3, 2007). Because the Board has adjusted the implementation schedule for Rule 3523, the rule has not prohibited the provision of tax services to persons in FRORs during the portion of the audit period that precedes the beginning of the professional engagement period.



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After considering the comments received, on July 24, 2007, the Board proposed to amend Rule 3523 as described in the concept release.^{2/} At the same time, the Board also proposed Rule 3526, *Communication with Audit Committees Concerning Independence*, a new ethics and independence rule that would supersede *Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees* ("ISB No. 1"), and two related interpretations, and require a registered public accounting firm to communicate certain information related to the firm's independence to the issuer's audit committee.

The Board received 16 comment letters on the proposed rules. Overall, the commenters were supportive of proposed Rule 3526 and the proposed amendment to Rule 3523. Commenters generally agreed that proposed Rule 3526 would enhance communication between the auditor and the audit committee and recommended that the Board adopt the rule. Commenters also reiterated that they believed that an auditor's independence would not be impaired by the provision of tax services to a person in a FROR during the portion of the audit period that precedes the beginning of the professional engagement period, and that the Board should adopt the proposed amendment to Rule 3523. Commenters also suggested certain modifications to the proposed rules.

The Board is adopting proposed Rule 3526 and the proposed amendment to Rule 3523 with some modifications in response to comments. This release describes key aspects of the amendment and new rule, comments received, and changes incorporated in the final rules. Additionally, as described below, the Board is further adjusting the implementation schedule for Rule 3523, as it applies to tax services provided to persons in FRORs during the period subject to audit but before the professional engagement period begins, to allow sufficient time for the SEC to consider whether to approve the amendment to the rule.

II. Rule 3526. Communication with Audit Committees Concerning Independence

Under Section 301 of the Sarbanes-Oxley Act of 2002 ("the Act"), "[t]he audit committee of each issuer, in its capacity as a committee of the board of directors, shall be directly responsible for the appointment, compensation, and oversight of the work of any registered public accounting firm employed by that issuer...for the purpose of

^{2/} See PCAOB Release No. 2007-008 (July 24, 2007).



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preparing or issuing an audit report or related work....^{3/} PCAOB interim independence standards require the auditor to provide certain information to the audit committee about independence that could assist the audit committee in fulfilling these oversight responsibilities. Specifically, ISB No. 1 requires, among other things, firms to disclose at least annually to the audit committee all relationships between the auditor and its related entities and the company and its related entities that, in the auditor's professional judgment, may reasonably be thought to bear on the auditor's independence. ISB No. 1 does not, however, require the firm to provide information to the audit committee about the firm's independence in connection with *becoming* the issuer's auditor (*i.e.*, before the person or firm becomes the issuer's auditor).

As discussed in the proposing release, the Board proposed Rule 3526 because it believed that the accounting firm should discuss with the audit committee before accepting an initial engagement pursuant to the standards of the PCAOB any relationships the accounting firm has with the issuer that may reasonably be thought to bear on its independence. The proposed rule was intended to build on the communication requirements in ISB No. 1 and provide the audit committee with information – including information about the firm's relationships with persons in FRORs at the company – that may be important to its determination about whether to hire the firm as the company's auditor. The Board also proposed to include in the rule a new requirement for the firm to document the substance of its discussion with the audit committee.

All commenters were generally in favor of the Board adopting the proposed rule, and, as discussed more fully below, some recommended modifications. Commenters stated that Rule 3526 would assist audit committees in fulfilling their responsibilities and would aid them in their decision-making process. After carefully considering the comments, the Board is adopting Rule 3526 with one modification, as described below. If approved by the SEC, Rule 3526 will supersede ISB No. 1 and two related interpretations.^{4/}

^{3/} The SEC has implemented this provision by adopting rules directing the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance with the audit committee requirements mandated by the Act.

^{4/} ISB Interpretation 00-1, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant*, and ISB Interpretation



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A. Scope of the Required Communication

The Board proposed in Rule 3526(a) to require the registered firm, prior to accepting an initial engagement pursuant to the standards of the PCAOB, to describe in writing to the audit committee^{5/} all relationships between the accounting firm or any

00-2, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant, An Amendment of Interpretation 00-1*. The interpretations state that the responsibility to comply with ISB No. 1 rests solely with the primary auditor, but that the primary auditor should include in its report to the audit committee all of its relationships and those of its domestic and foreign associated firms that could reasonably bear on the independence of the primary auditor. Under these interpretations, if the primary auditor is relying on the work of secondary auditors not associated with the primary auditor's firm, the report of the primary auditor should either describe any such secondary auditors' relationships, or it should state that it does not do so. The treatment of secondary auditors under Rule 3526 will be similar to the treatment of secondary auditors under ISB No. 1 and the two interpretations. Secondary auditors will not need to comply with Rule 3526, but the primary auditor will need to disclose to the audit committee any relationships of the firm's affiliates that could reasonably be thought to bear on the independence of the primary auditor. As under ISB No. 1 and the related interpretations, the scope of any communications about secondary auditors under Rule 3526 should be clear to the audit committee. Accordingly, the Board expects the primary auditor's report to either include any covered relationships of any secondary auditors not affiliated with the firm or state that it does not do so. One commenter recommended that the Board consider providing an exemption for secondary auditors. Because the rule does not require communications by secondary auditors, an exemption is not necessary.

^{5/} One commenter recommended the Board provide guidance in situations in which an issuer does not have an audit committee. Under Section 2(a)(3) of the Act, "[t]he term 'audit committee' means – (A) a committee (or equivalent body) established by and amongst the board of directors of an issuer for the purpose of overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer; and (B) if no such committee exists with respect to an issuer, the entire board of directors of the issuer." Accordingly, under Rule 3526, if an audit client does not have an audit committee, the auditor would be required to make the communications to the entire board of directors.



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affiliates of the firm^{6/} and the potential audit client or persons in FRORs at the potential audit client that may reasonably be thought to bear on independence. The Board also proposed to require the firm to discuss with the audit committee the potential effects of those relationships on the firm's independence. In Rule 3526(b), the Board proposed to require a registered firm on at least an annual basis after becoming the issuer's auditor to provide the same information described above and also affirm to the audit committee of the issuer, in writing, that the firm is independent in compliance with Rule 3520, *Auditor Independence*.^{7/} As described in the proposing release, the Board intended for these communications to provide the audit committee with sufficient information to understand how a particular relationship might affect independence and to foster a robust discussion between the firm and the audit committee.

Commenters generally believed that the scope of the required communications was appropriate. Several commenters noted that, to a large extent, firms are already making the kinds of communications that would be required by proposed Rule 3526. One commenter acknowledged, however, that existing communications between the firm and a potential new audit client do not include the disclosure of tax services to a person in a FROR or his or her immediate family member. Additionally, some registered firms noted that communications regarding the auditor's independence currently vary in content and timing and may, in some instances, occur only orally.

Most commenters did not believe that it was necessary for the Board to expand the scope of the required communication to include any additional matters. One

Additionally, one commenter recommended that audit committees provide better disclosure, through the proxy, when approving non-audit services performed by the auditor. The commenter stated that providing this type of transparency will permit investors a greater ability to evaluate audit committee's fiduciary performance of shareholders. The Board does not have statutory authority to require disclosure by audit committees.

^{6/} One commenter recommended that the Board adopt a definition of affiliate of the firm. This term is already defined in Rule 3501.

^{7/} Rule 3520 states that a registered public accounting firm and its associated persons must be independent of the firm's audit client throughout the audit and professional engagement period.



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commenter, however, recommended requiring the firm to confirm its independence in writing to the audit committee prior to accepting an initial engagement. Another commenter recommended revising Rule 3526(a) to require the firm to make the communications in its initial proposal to the company's audit committee.

As discussed above, the Board proposed to require firms to affirm their independence annually but did not propose a similar requirement that would apply before the firm is initially engaged as the company's auditor. Rule 3526(a) requires registered firms to make certain communications about relationships that may reasonably be thought to bear on independence before accepting an initial engagement pursuant to the standards of the PCAOB. Rather than prescribing a particular time before that point when the communications must occur, however, the rule allows registered firms and audit committees the flexibility to make that determination. The Board understands that, in some cases, firms need time before a new engagement begins to resolve any matters that could impair their independence. If a firm were required to affirm its independence prior to accepting a new engagement, it would need to wait until it has resolved any independence issues to make the required communications. These communications are intended to assist the audit committee in fulfilling its responsibility to hire the auditor – their usefulness for that purpose may diminish if they are left until immediately before the engagement begins. Accordingly, the Board does not believe a requirement for auditors to affirm that they are independent before accepting a new engagement is appropriate.

Other commenters recommended certain exclusions from the scope of the required communications. For example, one commenter asserted that the auditor cannot be expected to know about all relationships that may reasonably be thought to bear on its independence, and recommended that the written communication to the audit committee state that the auditor's assessment is based on information provided to the auditor by the issuer. The Board does not believe that allowing auditors to include such a limitation in the communication would be appropriate. Complying with the Board's independence requirements is the responsibility of the auditor.^{8/} To fulfill this

^{8/} Another commenter suggested that the audit committee should be able to rely on the firm to determine and resolve any independence issues, and that a requirement for the auditor to discuss these matters with the audit committee would increase the responsibilities of the audit committee with respect to independence. This commenter recommended that the Board not adopt these requirements. As discussed above, the rule is intended to provide audit committees with information to assist them



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responsibility, as well as their related responsibility under the SEC's independence rules, auditors need to ascertain what relationships with the issuer and persons in FRORs at the issuer may reasonably be thought to bear on their independence. Moreover, some of the information the auditor must assess in order to assure its independence and that may need to be communicated under Rule 3526 – such as the firm's or its associated persons' financial interests in the audit client – can be more readily obtained by the auditor than its audit client.

Another commenter recommended that the Board exclude tax services to a person in a FROR from the required communications because the commenter believed that compliance with Rule 3523, as amended, should adequately address any independence concerns regarding such services. As discussed in the proposing release, Rule 3526 is intended to require disclosure of not only whether the firm provided any specifically prohibited services or maintained any specifically prohibited relationships, but also whether any of the firm's relationships or services may reasonably be thought to bear on independence under the SEC's general standard of auditor independence^{9/} and AU sec. 220, *Independence*.^{10/} Because auditors will need

in carrying out their responsibilities to oversee the audit engagement, but auditors remain responsible for complying with the independence requirements. Nothing in the rule adds to, or otherwise modifies, the responsibilities of the audit committee.

^{9/} 17 C.F.R. § 210.2-01(b). Under that standard, an accountant is not independent if "the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant's engagement." In considering this general standard, the SEC "looks in the first instance to whether a relationship or the provision of service: creates a mutual or conflicting interest between the accountant and the audit client; places the accountant in the position of auditing his or her own work; results in the accountant acting as management or an employee of the audit client; or places the accountant in a position of being an advocate for the audit client." 17 C.F.R. § 210.2-01, preliminary note.

^{10/} AU sec. 220, *Independence*, requires that "[i]n all matters relating to the assignment, an independence in mental attitude is to be maintained by the auditor..." AU sec. 220 notes that "[i]t is of utmost importance to the profession that the general public maintain confidence in the independence of independent auditors" and that public confidence in the auditor's independence "would be impaired by evidence that



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to consider the relevant facts and circumstances in order to make such a determination, the Board does not believe that *per se* exemptions are appropriate.

Some commenters suggested that, in certain circumstances, firms would be restricted in the information they could provide to the audit committee about relationships with persons in FRORs due to legal limitations imposed by confidentiality and privacy laws. Specifically, one commenter was concerned that the auditor would not be able to disclose to the audit committee information about tax services rendered to a person in a FROR prior to obtaining a consent from that person. Another commenter recommended that the Board address the need for obtaining such a consent in its final release, while another recommended that the Board provide an exemption in circumstances where applicable legal restrictions impede an auditor's ability to comply fully with the disclosure requirement.

Under ISB No. 1, auditors have been required to disclose to the audit committee relationships with the company and its related entities and to discuss the auditor's independence with the audit committee. Accordingly, the required communications could include discussion of tax or other services provided to an entity or person other than the company itself. The Board understands that firms are subject to certain confidentiality requirements in the tax context^{11/} and that other restrictions could arise outside of that context, depending on the facts and circumstances that a particular relationship presents. The Board is not, however, aware that firms have encountered difficulty in communicating with audit committees, as required by ISB No. 1 or any other professional practice standard, as a result of such privacy requirements.

As described above, Rule 3526 is a general requirement that, like ISB No. 1, requires disclosure of certain relationships that may be relevant to the audit committee's oversight of the engagement. It does not set forth a list of relationships that must always

independence was actually lacking, and it might also be impaired by the existence of circumstances which reasonable people might believe likely to influence independence."

^{11/} See 26 U.S.C. § 7216; 26 C.F.R. § 301.7216-3 (prohibiting disclosure or use of tax return information without written consent of taxpayer that meets specified requirements); 26 C.F.R. § 301.7216-1 (defining "tax return information" to mean "any information, including, but not limited to a taxpayer's name, address, or identifying number, which is furnished in any form or manner for, or in connection with, the preparation of a tax return of the taxpayer").



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be disclosed or mandate specific information that must be communicated when disclosure is required. Rather, Rule 3526 allows firms significant flexibility to determine how to comply with the requirements to describe a covered relationship and discuss the potential effects of that relationship on the firm's independence. Accordingly, while the Board will monitor the application of the rule in this regard, it does not believe that the recommended exception is necessary or appropriate at this time.

The Board also received several comments on its proposal not to include the words "in the auditor's professional judgment" in the rule's description of the scope of the required communications. ISB No. 1 requires disclosure of certain relationships that "in the auditor's professional judgment may reasonably be thought to bear on independence." In the proposing release, the Board explained that it believed that omitting the reference to the auditor's professional judgment would clarify the requirement by reminding auditors of the need to focus on the perceptions of reasonable third parties when making independence determinations.

Some commenters supported the proposed exclusion of the words "in the auditor's professional judgment" from Rule 3526. Other commenters, however, believed that the absence of the reference to judgment could confuse, rather than clarify, the requirement and noted that it is reasonable and appropriate for audit committees to rely on the accounting firm's judgment as to what matters should be disclosed. One of these commenters contended that this aspect of the Board's proposal is inconsistent with the Board's recent focus on the importance of the use of auditor judgment. Conversely, one commenter did not object to the absence of a reference to judgment, provided that the adopting release contain an acknowledgement that the auditor must apply judgment in determining which matters are required to be communicated to the audit committee.^{12/}

As the Board explained in the proposing release, auditors will need to apply judgment to determine whether a relationship may reasonably be thought to bear on independence. After considering commenters' views, the Board continues to believe that adding specific reference to the auditor's professional judgment is unnecessary and inappropriate in this instance. While the Board agrees that auditors must exercise sound

^{12/} Additionally, one commenter recommended including the reference to judgment and also referring to the SEC's general standard of auditor independence and the preliminary note to the SEC's independence rules in the proposed rule or the adopting release. Footnote 9 of this release refers to the general standard and the preliminary note.



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judgment in carrying out their responsibilities, it does not believe that specific reference to judgment in this rule is necessary to encourage auditors to do so. Judgment is called for in applying any reasonableness standard to particular facts and circumstances, and Rule 3526 is no different. Determining what relationships may reasonably be thought to bear on independence requires consideration of how a third party – not the auditor – would view the relationship, which is consistent with the SEC's general standard of auditor independence and AU sec. 220. A reference to "in the auditor's professional judgment" could suggest otherwise, however, and therefore could discourage the necessary analysis. Accordingly, the Board has determined not to add the phrase to Rule 3526.

B. Time Period Covered by Rule 3526(a)

In the proposing release, the Board solicited comment on whether the initial communication in Rule 3526(a) should be limited to relationships that existed during a particular period, and, if so, how long that period should be. Commenters provided a wide variety of recommendations in this area. Some commenters stated that the initial communication should not be limited to relationships that existed during a particular period. Some of these commenters noted that establishing a specific period could result in arbitrary exclusion of certain relationships and recommended that the audit committee and auditor be responsible for determining the relevant time frame.

Other commenters recommended that the time period be limited to the audit and professional engagement period because, according to these commenters, the relevant relationships are those that exist currently or will continue to exist. One of these commenters stated that requiring communication of relationships that existed prior to this period would cause an unnecessary burden on the firm to identify and communicate these matters and on the audit committee to consider such information, because the firm was not subject to the auditor independence rules with respect to the audit client before the beginning of the audit and professional engagement period. One commenter recommended that the required time period should, at a minimum, be the audit period and that the rule should require auditors to consider communicating relationships that existed before that time. Finally, one commenter recommended that the time period should be no longer than two years prior to the commencement of the audit period, and two commenters recommended that the proposed rule should cover a time period of at least three years.



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After considering these comments, the Board has determined that the initial communication required by Rule 3526(a) should not be limited to relationships that existed during a particular time period. While the Board agrees that a relationship that existed during the audit and professional engagement period may be more likely to bear on independence than a relationship that ended substantially before that time, it does not believe that the passage of time is the only factor relevant to a determination of whether a relationship may reasonably be thought to bear on independence. The nature of the relationship must also be considered. For example, if the firm customized and implemented the company's financial reporting system, that relationship, depending on the circumstances, might reasonably be thought to bear on independence even if the engagement to design the system was concluded before the beginning of the audit and professional engagement period. Determining whether a particular relationship is covered by Rule 3526(a) will, therefore, depend on the relevant facts and circumstances.

The Board is making one modification to the rule in response to a comment recommending that Rule 3526 make clear that the relationships required to be disclosed are those that may reasonably be thought to bear on independence as of the date of the communication. Because the relevant relationships are those that continue to bear on independence at the time of the communication, the Board has modified the rule by adding the words "as of the date of the communication" where appropriate. This clarification should help firms distinguish relationships that are covered by the rule from those that are not.

This modification should also clarify that, if a relationship may reasonably be thought to bear on independence as of the date of the communication, it must be disclosed regardless of whether it was disclosed in a prior year. Some commenters suggested that auditors should not be required to repeat a previously made disclosure. The Board believes that an earlier disclosure may reduce the amount of information that needs to be disclosed, but it does not obviate the need for disclosure altogether. If the nature of the relationship and the potential effects of the relationship on independence remain substantially unchanged, a reference to the earlier disclosure will generally be sufficient when disclosure is required. Moreover, as discussed above, after some amount of time, the length of which depends on the nature of the relationship, a relationship may no longer reasonably be thought to bear on independence and, therefore, would no longer need to be disclosed.



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C. Timing of the Communications

As discussed above, the Board proposed Rule 3526(a) because it believed that auditors should communicate relevant information about independence before becoming the issuer's auditor. A few commenters expressed concern that the proposed rule could cause undue burden on private companies pursuing an initial public offering if the communication were required before the auditor accepts an engagement to assist an existing private company client in going public. According to commenters, a requirement to complete the independence assessment before the auditor could commence work related to the initial public offering might disadvantage the audit client by causing delay. One commenter stated that auditors generally begin work on the initial public offering based upon an initial review of relationships between the accounting firm and the company and complete their independence assessment before the company's registration statement is filed. This commenter suggested that the Board reconsider the required timing of the communications in the context of an initial public offering.

After considering these comments, the Board has determined that relieving a firm whose private company audit client is pursuing an initial public offering from compliance with Rule 3526 is not necessary or appropriate. As discussed above, the rule is intended to provide audit committees with the information they need to effectively oversee the audit engagement. When a private company undertakes an initial public offering, it must, for the first time, have its financial statements audited by an auditor that is independent within the meaning of the rules of the SEC and PCAOB. Among other decisions an audit committee must make is whether to engage its existing auditor for the initial public offering or whether to retain a new auditor for that purpose. In this context, the Board believes that the communication about an existing auditor's independence – which is relevant to the existing auditor's ability to continue as the company's auditor through, and after, the initial public offering – should not be delayed until just before the registration statement is filed. Moreover, the Board believes that this evaluation will not cause an unnecessary burden because the private company is already a client of the accounting firm and therefore should already be aware of most of the relationships that would need to be communicated.

The Board also received comment on the timing of the annual communication requirement that the Board proposed in Rule 3526(b). Like ISB No. 1, proposed Rule 3526 did not specify when during the year the firm would be required to make the



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annual communication.^{13/} One commenter recommended that the Board specify in Rule 3526(b) when the annual communication should take place to make sure that these critical discussions do not take place at the end of the audit engagement. The commenter recommended that the proposed rule be changed to state that firms should apply Rule 3526 as early in the audit process as practicable, preferably during the planning stage of the audit. One commenter recommended that the communication occur before substantial planning procedures commence, while another recommended that the annual communication should take place at the time the engagement letter is signed and then again near the end of the audit. Finally, one commenter recommended adding a section to Rule 3526 requiring an auditor to update the communications when he or she becomes aware of a covered, previously unknown or new relationship.

After considering these comments, the Board does not believe it is appropriate to mandate specifically when the Rule 3526(b) annual communication take place. In most cases, the communications will be more useful if they take place near the beginning of the audit process. However, by not prescribing the timing of the communication, Rule 3526(b) will allow the auditor and audit committee to determine the timing that is most appropriate in the circumstances of the particular engagement. Similarly, the Board does not believe that it is necessary for the rule to explicitly address how a firm should correct an incomplete communication.

III. Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles

A. Amendment to Rule 3523 to Exclude the Portion of the Audit Period That Precedes the Professional Engagement Period

Rule 3523, as adopted by the Board, prohibits a registered public accounting firm, or an affiliate of the firm, from providing tax services during the "audit and professional engagement period" to a person in, or an immediate family member of a person in, a FROR at the audit client. Consistent with the SEC's independence rules,^{14/} the phrase "audit and professional engagement period" is defined to include two discrete periods of time. The "audit period" is the period covered by any financial

^{13/} The Board understands that, under ISB No. 1, the communication typically occurs at the end of the audit when the financial statements are issued.

^{14/} 17 C.F.R. § 210.2-01(f)(5).



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statements being audited or reviewed.^{15/} The "professional engagement period" is the period beginning when the firm either signs the initial engagement letter or begins audit procedures, whichever is earlier, and ends when either the company or the firm notifies the SEC that the company is no longer that firm's audit client.^{16/}

In circumstances in which a registered firm has been the auditor for an audit client for more than a year, the "audit period" is a subset of the "professional engagement period." However, when a registered firm accepts a new audit client, the audit period may cover a period of time before the commencement of the professional engagement period. In such circumstances, Rule 3523, as adopted, provides that the firm is not independent of its audit client if the firm, or an affiliate of the firm, provided tax services to a person covered by Rule 3523 during the audit period but before the beginning of the professional engagement period. This aspect of the rule therefore effectively prevents a firm from accepting a new audit client if the firm, or an affiliate of the firm, provided tax services to such a person during the period covered by any financial statements to be audited or reviewed.

In preparing for implementation of the Board's tax services and independence rules, the Board decided to revisit the application of Rule 3523 to tax services provided during the audit period. As discussed above, on April 3, 2007, the Board issued a concept release to solicit comment about the possible effects on a firm's independence of providing tax services to a person covered by Rule 3523 during the portion of the audit period that precedes the beginning of the professional engagement period, and other practical consequences of applying the restrictions imposed by Rule 3523 to that portion of the audit period. After careful consideration of comments received in response to the concept release, the Board, on July 24, 2007, proposed to amend the rule to exclude the portion of the audit period that precedes the beginning of the professional engagement period.^{17/}

^{15/} Rule 3501(a)(iii)(1).

^{16/} Rule 3501(a)(iii)(2).

^{17/} See PCAOB Release No. 2007-008, which includes a discussion of the comments the Board received on the concept release.



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The Board received 13 comments on the proposed amendment to Rule 3523. Almost all of the commenters supported the Board's recommendation to amend Rule 3523.^{18/} Many of these commenters reiterated their belief that the firm's independence would not be affected by the provision of tax services to a person in a FROR during the portion of the audit period that precedes the beginning of the professional engagement period. Commenters also reaffirmed their belief that, if Rule 3523 is not amended, it could adversely affect companies' ability to change auditors by limiting the companies' choice of auditors.

The Board has carefully considered these comments, as well as the comments on the concept release,^{19/} and determined to adopt the amendment to Rule 3523. The Board continues to believe that it is not necessary for the rule to restrict the provision of tax services during the portion of the audit period that precedes the professional engagement period. Rule 3523 relates to services provided to individuals and not the

^{18/} Only one commenter on the proposed rule objected to the amendment of Rule 3523. This commenter's objection stemmed from the contention that the terms "professional engagement period" and "a person in a financial reporting role" were not defined. Definitions for "professional engagement period" and "financial reporting oversight role" are provided under Rules 3501(a)(iii)(2) and 3501(f)(i), respectively. The same commenter, while not specifically addressing the proposed amendment, also expressed concern with Rule 3523(a), which provides an exception for tax services to a person who is in a FROR only because he or she serves as a member of the Board of Directors, and, referring to the responsibilities of directors, recommended deleting this section in its entirety. This commenter also recommended that the Board eliminate Rule 3523(b), which provides an exception, under certain circumstances, for tax services to a person who is in a FROR only because of the person's relationship to an affiliate of the entity being audited. The Board does not believe that eliminating these exceptions is warranted.

^{19/} In response to the concept release, two commenters stated that Rule 3523 should not be amended to exclude the portion of the audit period that precedes the professional engagement period. These commenters believed that providing tax services to a person in a FROR during the audit period impairs independence, and suggested that audit firms may plan for a change of auditors sufficiently in advance to avoid or minimize any problems resulting from the application of the rule to the audit period.



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audit client that issues the financial statements subject to audit. Additionally, registered firms would remain responsible for considering the relevant facts and circumstances of a specific tax engagement and determining whether their independence is impaired under the SEC's general standard of auditor independence.^{20/}

One commenter objected to the discussion in the proposing release (and included here in the paragraph above) describing the firm's obligation to consider whether the firm's independence is impaired under the SEC's general standard of auditor independence. This commenter stated that the discussion sends a contradictory message by calling for firms to assess whether their independence is impaired despite the Board's conclusion that restrictions are unnecessary to preserve independence. The Board disagrees. As a result of the Board's amendment, firms will not be specifically prohibited by Rule 3523 from providing tax services to persons in a FROR during the portion of the audit period that precedes the professional engagement period. That does not mean, however, that such services are categorically permitted. Rather, as discussed in the proposing release, the amendment reflects the Board's belief that a more tailored approach, based on facts and circumstances and measured against the general standard of auditor independence, is preferable to a *per se* prohibition. Accordingly, as with any other service or relationship that is not specifically prohibited by the independence rules, firms must determine whether the service or relationship impairs independence under the SEC's general standard of auditor independence.

B. Application of Rule 3523 to New Issuers

The Board proposed adding a note to Rule 3523 concerning the application of Rule 3523 in the context of an initial public offering in light of comments received on the concept release. The proposed note stated that, in the context of an initial public offering, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that a registered firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a firm's independence under Rule 3523. Commenters generally recommended that the Board adopt the note and encouraged the Board to consider expanding it to include other corporate life events, noting that corporate life events other than an initial public offering may also result in the need for

^{20/} 17 C.F.R. § 210.2-01(b); see footnote 9.



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an audit client's financial statements to be audited pursuant to the standards of the PCAOB for the first time.^{21/}

In response to these comments, the Board determined to revise the note to Rule 3523 to describe events, other than just initial public offerings, pursuant to which a company's financial statements must be audited in accordance with the standards of the PCAOB for the first time. Specifically, the Board replaced the words "[i]n the context of an initial public offering" with "[i]n an engagement for an audit client whose financial statements for the first time will be required to be audited pursuant to the standards of the PCAOB." This situation may occur when a company decides to conduct an initial public offering of its securities,^{22/} which would require the company to file, for the first time, a registration statement under the Securities Act of 1933. Additionally this situation may occur when a foreign private issuer decides to list its securities on a national securities exchange, which would require the company to register its securities, for the first time, under the Securities Exchange Act of 1934. In both cases, the company's audited financial statements would be required, for the first time, to be audited pursuant to the standards of the PCAOB.^{23/}

^{21/} Commenters suggested the following as examples of when an audit client's financial statements would, for the first time, need to be audited pursuant to the standards of the PCAOB – mergers, reverse mergers in which a privately-held entity merges with a public company and succeeds to the public company's reporting obligations under the Securities Exchange Act of 1934, issuance of publicly traded debt, issuance of partnership or other units, inclusion of a public company's securities in an employee benefit plan, decision by a foreign private issuer to list its securities in the United States, and companies that have greater than 500 U.S. shareholders and total assets exceeding \$10 million as of the latest fiscal year-end.

^{22/} The company may offer equity securities, debt securities, limited partnership interests, trust interests, or another type of securities in the initial public offering.

^{23/} The Board intends the note to Rule 3523 to describe all circumstances in which a company that was not an "issuer," as defined by the Act, becomes an issuer as a result of a corporate life event or otherwise. These circumstances include those in which a private company that was once an issuer becomes an issuer again. As long as the company was not required to have its financial statements audited pursuant to the



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The Board does not believe it is appropriate to list in the note the various corporate life events identified by commenters, such as mergers or acquisitions, reverse mergers or other similar transactions. The relevant factor is not the name given to a transaction or event but whether the transaction or event triggers the initial requirement for an audit pursuant to the standards of the PCAOB. For example, the surviving company in a merger or acquisition transaction may be an issuer that is already filing with the SEC financial statements required to be audited pursuant to the standards of the PCAOB. The Board did not intend the note to Rule 3523 to describe such a scenario.²⁴ By focusing on the need for a first-time audit pursuant to the standards of the PCAOB, the company and its auditors are better able to determine whether a proposed transaction or corporate life event is described by the note.

One commenter stated that, while it is easy to identify the date on which the initial engagement letter to perform an audit pursuant to the standards of the PCAOB is signed, it would be very difficult to apply the second prong of the note, which requires identification of the date that the auditor began procedures to perform an audit pursuant to the standards of the PCAOB, especially if the registered firm audited the company's prior years' financial statements.²⁵ Another commenter similarly questioned whether

standards of the PCAOB prior to being required to do so, the Board will consider the requirement to be a "first-time" requirement for purposes of the note.

²⁴/ Another example is a private operating company becoming a reporting company through a reverse merger with a reporting shell company. In this scenario, even though the operating company assumes the reporting obligations of the former shell company, the surviving reporting company is the former shell company whose financial statements already were required to be audited pursuant to the standards of the PCAOB. Therefore, the note to Rule 3523 does not describe this situation.

²⁵/ The commenter noted that, when a company undertakes an initial public offering, it is required to include in the registration statement audited financial statements for its past three completed fiscal years. These financial statements may have previously been audited pursuant to generally accepted auditing standards ("GAAS"). The commenter was concerned that if the company does not retain a new auditor for its initial public offering, there may be a question as to whether the auditor should consider its audits of the prior years in assessing when it "began procedures" as provided under the note to Rule 3523. An auditor should not consider work already performed on previously completed GAAS audits for determining when the auditor



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this period begins when the auditor begins planning for the audit. The Board recognizes that, in certain circumstances, it may be difficult to identify when a continuing auditor began procedures pursuant to the standards of the PCAOB. An auditor begins procedures for purposes of Rule 3523 when he or she begins procedures, including required audit planning procedures, to update its earlier audits to conform them to the standards of the PCAOB or begins procedures on a new audit pursuant to those standards. This point in time will depend on the facts and circumstances of the particular engagement and corporate life event, rather than on any more specific triggering event that the Board could establish by rule.

C. Transition Periods

Rule 3523 prohibits the provision of tax services to covered persons once the professional engagement period begins. Some commenters on the concept release recommended that the Board amend Rule 3523 to allow a transition period after a company changes auditors so that the new auditor may complete any tax services in progress to any persons in FRORs affected by the issuer's change of auditors.^{26/} Other commenters stated that tax services to persons in FRORs should, as is currently required, cease before the professional engagement period begins. The Board decided to seek further feedback on this topic in the proposing release. Specifically, the Board asked commenters to specify why they believed any transition period was necessary and how long any such transition period should be.^{27/}

The majority of commenters on this topic recommended that the Board provide for a 180-day transition period to allow an accounting firm to complete covered tax services once the professional engagement period begins. Most of these commenters stated that, since the Board has previously determined that a 180-day transition is

"began procedures" because those audits were not performed pursuant to the standards of the PCAOB.

^{26/} Rule 3523(c) provides a time-limited transition period for an auditor to complete in-progress tax services to a person that becomes a FROR at the audit client through a hiring, promotion, or other change in employment event. That transition period is unaffected by this release.

^{27/} See PCAOB Release 2007-008 (July 24, 2007), at 12.



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appropriate when a person is hired or promoted into a FROR,^{28/} the Board should provide the same transition when an issuer changes its auditor. The commenters stated that, without a transition period, the person in a FROR could experience undue hardship because he or she may have to switch tax preparers in the middle of the personal tax services engagement. Additionally, some commenters stated that some accounting firms may not be able to terminate the in-process personal tax services engagements within a timeframe that would also allow them to submit their proposal for the new audit engagement. Conversely, some commenters stated that they believed that the Board should not provide a transition period and that it is appropriate for the firm to cease the personal tax services before the professional engagement period begins or that a transition period should only be available on a case-by-case basis where cessation of services would cause significant hardship.^{29/}

After considering these comments, the Board does not believe that a transition period is necessary when a company changes its auditor and has determined not to amend Rule 3523 to include one. The Board adopted Rule 3523 because the provision of tax services to a person in a FROR after the accounting firm is hired as the auditor creates an unacceptable appearance that the firm lacks independence. While the Board believed a time-limited exception was warranted to accommodate persons who, through a hiring or promotion event, abruptly become covered by the rule, it does not believe that such a transition period is similarly necessary after an auditor change. In the former situation, the firm already is the issuer's auditor and has no control over whether or when the person is promoted or otherwise moved into a FROR. In contrast, the firm controls whether and when it begins a new engagement. The Board therefore believes that the firm is able to conclude, or transition to another provider, any tax services to persons in FRORs at a new audit client before beginning the engagement.^{30/}

^{28/} See Rule 3523(c).

^{29/} Another commenter stated that Rule 3523 should be effective immediately for issuers with fiscal years ending on or after December 15, 2007, that all personal tax services in process should be allowed to continue until the filing of the applicable tax return, and that such services, along with the related fees, should be disclosed in the issuer's filings with the SEC and documented in the minutes of meetings of the audit committee.

^{30/} Nothing in Rule 3523 requires a firm to complete or terminate tax services to persons in FRORs at a potential audit client before submitting a proposal for a new



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Some commenters also encouraged the Board to consider providing a transition period for firms to complete tax services to persons who become covered by Rule 3523 as a result of a corporate life event, such as a merger, acquisition, or initial public offering. Commenters suggested that such corporate life events present conceptually similar transition issues to those related to the hiring or promotion of a person into a FROR and that Rule 3523(c) should therefore be expanded to accommodate them. Commenters also stated that the absence of transitional relief may cause unnecessary hardship for persons in FRORs whose tax return preparation work was well underway at the point of the initial public offering, merger, or acquisition.^{31/}

As discussed above, in the context of an initial public offering, the rule, as amended, makes clear that tax services provided to a person in a FROR do not impair independence as long as those tax services are concluded before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so. Auditors should have sufficient time before that date to conclude any tax services to persons that would be covered by the rule. Accordingly, the Board does not believe that the recommended transition period is necessary in the context of an initial public offering.

The Board also considered whether a transition period is necessary to allow a firm to conclude tax services to persons who become covered by the rule after a merger or acquisition. As discussed above, Rule 3523(c) already provides a transition period for a firm to conclude tax services to a person who was not in a FROR before a hiring, promotion, or other change in employment event. If a business combination results in a change of employer for a person in a FROR – from, for example, the acquired company

audit engagement. Rather, the rule requires the accounting firm to complete or terminate those services by the beginning of the professional engagement period.

^{31/} The commenters further stated that, because persons in FRORs may receive tax services from a number of accounting firms, the application of the rule to the audit period may unreasonably restrict a company's ability to either continue or change auditors after a corporate life event. As discussed above, the Board has amended the rule to exclude the portion of the audit period that precedes the professional engagement period.



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to the acquiring company – the existing transition period in Rule 3523 would apply.^{32/} For example, if Company A acquires Company B, a person who was in a FROR at Company B would experience an "other change in employment event" if he or she became an employee of Company A in a FROR as a result of the acquisition. If such a person had been receiving tax services from Company A's registered public accounting firm pursuant to an engagement in process before the acquisition, the time-limited exception in Rule 3523(c) would apply.^{33/}

In the example above, persons in FRORs at Company A would not experience a change in employment event because they were employed by Company A both before and after the acquisition, and Rule 3523(c) would, therefore, not apply. If Company B's auditor became Company A's auditor after the acquisition (replacing Company A's auditor), Company B's auditor would have to conclude any tax services to persons in FRORs (and their immediate family members) at Company A before the start of the professional engagement period. The Board believes this is appropriate because, as discussed above, the Board does not believe that a transition period is necessary to allow a newly engaged auditor to conclude in-progress tax services to persons in FRORs at the new audit client. Accordingly, the Board has determined not to expand the existing transition period in Rule 3523(c).

IV. Effective Date and Adjustment of Implementation Schedule

Rule 3526 establishes new requirements for registered public accounting firms. The Board believes it is appropriate to allow a reasonable period of time for such firms to prepare internal policies and procedures and train their employees to ensure compliance with these new requirements. Accordingly, Rule 3526 will become effective, and ISB No. 1 and the related interpretations superseded, on the later of September 30, 2008, or 30 days after the date that the SEC approves the rule.

The amendment to Rule 3523 would have the effect of making permanent the Board's delay in implementing the rule as it applies to tax services provided during the

^{32/} See also *Staff Questions and Answers, Ethics and Independence Rules Concerning Independence, Tax Services and Contingent Fees* (April 3, 2007), Question and Answer No. 6, at 4-5.

^{33/} Id.



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period subject to audit but before the professional engagement period. Accordingly, no transition period is necessary, and the amended rule will become effective immediately upon approval by the SEC. The Board has also determined to further adjust the implementation schedule for Rule 3523 to allow sufficient time for the SEC to consider whether to approve the amendment to Rule 3523.^{34/} Specifically, the Board will not apply Rule 3523 to tax services provided on or before December 31, 2008, when those services are provided during the audit period and are completed before the professional engagement period begins.^{35/} The Board has filed this adjustment to the implementation schedule with the SEC as an immediately effective proposed rule change. The rule change became effective upon its filing with the SEC, thereby extending to December 31, 2008 the implementation date for this aspect of Rule 3523.

* * *

On the 22nd day of April, in the year 2008, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour
 Secretary

April 22, 2008

^{34/} Under the adjustment to the implementation schedule for Rule 3523 that the Board made on July 24, 2007, the Board will not apply Rule 3523 to tax services provided on or before April 30, 2008, when those services are provided during the audit period and are completed before the professional engagement period begins.

^{35/} This will apply regardless of whether there is an engagement in process on April 30, 2008.



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APPENDIX 1 – Amendment to Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles*

APPENDIX 2 – Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence*

APPENDIX 3 – Amendment to the PCAOB Interim Independence Standards



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Appendix 1 – Amendment to Rule 3523, Tax Services for Persons in Financial Reporting Oversight Roles

The relevant portion of the Rule, as amended, is set out below. Language deleted by this amendment is struck through. Language that is added is underlined.

RULES OF THE BOARD

* * *

SECTION 3. PROFESSIONAL STANDARDS

* * *

Part 5 – Ethics

* * *

Subpart I – Independence

* * *

Rule 3523. Tax Services for Persons in Financial Reporting Oversight Roles

A registered public accounting firm is not independent of its audit client if the firm, or any affiliate of the firm, during the audit and professional engagement period provides any tax service to a person in a financial reporting oversight role at the audit client, or an immediate family member of such person, unless –

(a) the person is in a financial reporting oversight role at the audit client only because he or she serves as a member of the board of directors or similar management or governing body of the audit client;

(b) the person is in a financial reporting oversight role at the audit client only because of the person's relationship to an affiliate of the entity being audited –



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(1) whose financial statements are not material to the consolidated financial statements of the entity being audited; or

(2) whose financial statements are audited by an auditor other than the firm or an associated person of the firm; or

(c) the person was not in a financial reporting oversight role at the audit client before a hiring, promotion, or other change in employment event and the tax services are –

(1) provided pursuant to an engagement in process before the hiring, promotion, or other change in employment event; and

(2) completed on or before 180 days after the hiring or promotion event.

Note: In an engagement for an audit client whose financial statements for the first time will be required to be audited pursuant to the standards of the PCAOB, the provision of tax services to a person covered by Rule 3523 before the earlier of the date that the firm: (1) signed an initial engagement letter or other agreement to perform an audit pursuant to the standards of the PCAOB, or (2) began procedures to do so, does not impair a registered public accounting firm's independence under Rule 3523.



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Appendix 2 – Ethics and Independence Rule 3526, Communication with Audit Committees Concerning Independence

RULES OF THE BOARD

* * *

SECTION 3. PROFESSIONAL STANDARDS

* * *

Part 5 – Ethics

* * *

Subpart I – Independence

* * *

Rule 3526. Communication with Audit Committees Concerning Independence

A registered public accounting firm must –

(a) prior to accepting an initial engagement pursuant to the standards of the PCAOB –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client or persons in financial reporting oversight roles at the potential audit client that, as of the date of the communication, may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (a)(1) on the independence of the registered public accounting firm, should it be appointed the issuer's auditor; and



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(3) document the substance of its discussion with the audit committee of the issuer.

(b) at least annually with respect to each of its issuer audit clients –

(1) describe, in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the audit client or persons in financial reporting oversight roles at the audit client that, as of the date of the communication, may reasonably be thought to bear on independence;

(2) discuss with the audit committee of the issuer the potential effects of the relationships described in subsection (b)(1) on the independence of the registered public accounting firm;

(3) affirm to the audit committee of the issuer, in writing, that, as of the date of the communication, the registered public accounting firm is independent in compliance with Rule 3520; and

(4) document the substance of its discussion with the audit committee of the issuer.



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Appendix 3 – Amendment to PCAOB Interim Independence Standards

Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees* ("ISB Standard No. 1"), ISB Interpretation 00-1, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant*, and ISB Interpretation 00-2, *The Applicability of ISB Standard No. 1 When "Secondary Auditors" Are Involved in the Audit of a Registrant, An Amendment of Interpretation 00-1*, are superseded by Rule 3526.