



CENTER FOR CAPITAL MARKETS  
COMPETITIVENESS

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August 31, 2015

Ms. Phoebe W. Brown  
Secretary  
Public Company Accounting Oversight Board  
1666 K Street, N.W.  
Washington, D.C. 20006-2803

**Re: PCAOB Supplemental Request for Comment: *Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form* (PCAOB Release No. 2015-004, June 30, 2015; PCAOB Rulemaking Docket Matter No. 029)**

Dear Ms. Brown:

The U.S. Chamber of Commerce<sup>1</sup> (the “Chamber”) created the Center for Capital Markets Competitiveness (“CCMC”) to promote a modern and effective regulatory structure for capital markets to fully function in a 21<sup>st</sup> century economy. The CCMC believes that businesses must have a strong system of internal controls, recognizes the vital role external audits play in capital formation, and supports efforts to improve audit effectiveness. Accordingly, the CCMC appreciates the opportunity to comment on the Public Company Accounting Oversight Board (“PCAOB”) Supplemental Request for Comment on *Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form* (“Supplemental Proposal”) and wishes to express serious concerns regarding the Supplemental Proposal.

The Supplemental Proposal represents the latest PCAOB release on these matters and the CCMC has commented on two prior proposals.<sup>2</sup> Our concerns

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<sup>1</sup> The Chamber is the world’s largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information.

<sup>2</sup> See CCMC letter dated March 10, 2014 on PCAOB Exposure Draft on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor’s Report of Certain Participants in the Audit* (PCAOB Release No. 2013-009, December 4, 2013; PCAOB Rulemaking Docket Matter No. 029) and CCMC letter dated January 9, 2012 on Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB*

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expressed in those two letters remain and we attach them with this letter as an appendix and request that they be made a part of the comment file for the Supplemental Proposal. The CCMC also has concerns that the Supplemental Proposal is not being put forth in a liability neutral fashion and that liability neutrality was not considered as part of the economic analysis. Finally, we also wish to raise the issue that comments are being solicited by the Securities and Exchange Commission (“SEC”) on audit committee disclosures and the CCMC requests that the PCAOB defer to the SEC on this matter.

Consistent with our prior comments, the CCMC does not support mandating disclosure of this information. The CCMC believes that any such disclosures should be voluntary and that U.S. regulators should let market forces sort out the consequences of any jurisdictional requirements to disclose this information.

The CCMC also reiterates that in the United States., the Sarbanes-Oxley Act of 2002 (“SOX”) created the PCAOB to regulate the accounting firms and individuals that audit public companies and reaffirmed the audit committee’s responsibility for oversight of the external audit. There is no need for mandating these disclosures when investors trust these structures and processes created by SOX on their behalf. In addition, mandating these disclosures will never put investors “in the shoes” of the PCAOB or audit committees. Nonetheless, such disclosures may result in investors and others unnecessarily second-guessing decisions of the PCAOB and audit committees—based on partial and incomplete information, which in turn undermines trust in regulatory and governance processes.

The PCAOB issued the Supplemental Proposal to solicit comment on an alternative mechanism for disclosing the name of the engagement partner and information about certain other participants in the audit—namely via a new PCAOB Form AP.<sup>3</sup> The CCMC appreciates that creating a new disclosure Form AP, instead of requiring disclosure in the auditor’s report, is intended to respond to concerns

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*Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011; PCAOB Rulemaking Docket Matter No. 029).

<sup>3</sup> The Supplemental Proposal indicates that the PCAOB is considering a basic filing deadline of 30 days after the date the auditor’s report is first included in a document filed with the SEC, with a shorter deadline of 10 days for initial public offerings (or within 10 days after the registration statement is publicly filed with the SEC for emerging growth companies (“EGCs”).

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raised by commenters, including the CCMC, that the PCAOB's proposed disclosures would create both legal and practical issues.

However, the Supplemental Proposal represents a response to such concerns only regarding disclosures in auditors' reports included or incorporated by reference into registration statements under the Securities Act of 1933—specifically in regards to liability under Section 11 and consents required under Section 7.<sup>4</sup> The Supplemental Proposal does not otherwise respond to litigation risks that would be created by the proposed disclosures, including under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

The CCMC reiterates that we strongly believe that liability neutrality represents a minimum threshold for these disclosures. The Supplemental Proposal states this PCAOB rulemaking process was undertaken in response to a recommendation of the U.S. Department of the Treasury's Advisory Committee on the Auditing Profession ("ACAP") that the PCAOB should consider mandating the engagement partner's signature on the audit report. However, as the CCMC has previously emphasized, this ACAP recommendation (regardless of form or placement of the name of the engagement partner) was premised on liability neutrality.

Further, the precondition of liability neutrality should also be part of an economic analysis. The CCMC has emphasized the importance of the PCAOB conducting substantive and robust economic analysis. Although consisting of 27 pages of qualitative discussion, the "Economic Considerations" section of the Supplemental Proposal does not address liability considerations at all.

The Supplemental Proposal does not resolve other concerns discussed in our prior comments. While we do not restate these concerns, please consider them to be incorporated by reference in this letter.

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<sup>4</sup> Section 11 of the Securities Act of 1933 imposes liability on certain participants in a securities offering, including every accountant who, with his or her consent, has been named as having prepared or certified any part of the registration statement or any report used in connection with the registration statement. Section 7 of the Securities Act of 1933 requires that the consent of every accountant so named in a registration statement must be filed with the registration statement.

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Lastly, it is important to recognize that on July 1, 2015, the SEC voted to publish a Concept Release on *Audit Committee Disclosures* (“SEC Concept Release”). Among other matters, the SEC Concept Release solicits public comment on whether the SEC should require audit committees to disclose the name of the engagement partner and information about certain other participants in the audit.

While the CCMC does not support mandating disclosure of this information, as we have stated in our prior letters, the CCMC believes that any such disclosure is better suited for inclusion in a report by the audit committee in the proxy statement. Given the SEC has taken up considering the disclosure of this information, the CCMC urges the PCAOB to defer to the SEC on this matter.

Once again, the CCMC appreciates the opportunity to comment on the Supplemental Proposal. Thank you for your consideration and the CCMC stands ready to assist in these efforts.

Sincerely,

A handwritten signature in black ink, appearing to read 'TK' followed by a long horizontal flourish.

Tom Quadman



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TOM QUAADMAN  
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January 9, 2012

Mr. J. Gordon Seymour  
Secretary  
Public Company Accounting Oversight Board  
1666 K Street, N.W.  
Washington, DC 20006-2803

**Re: PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29)**

Dear Mr. Seymour:

The U.S. Chamber of Commerce (the “Chamber”) is the world’s largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness (“CCMC”) to promote a modern and effective regulatory structure for capital markets to fully function in a 21<sup>st</sup> century economy.

The CCMC believes that businesses must have a strong system of internal controls and recognizes the vital role external audits play in capital formation. The CCMC appreciates the opportunity to comment on the Public Company Accounting Oversight Board’s (“PCAOB”) Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (“the Proposal”).

The CCMC is concerned that the Proposal will undermine the foundation of the audit process impairing transparency and accountability. The CCMC believes that the Proposal in its current form will obfuscate essential responsibilities thereby harming accountability. Because of these concerns and the lack of any tangible

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demonstrated benefit, the CCMC believes that the Proposal should be reassessed through a public roundtable of all interested stakeholders and additional outreach such as field testing.

Rather than moving forward on this Proposal, the CCMC believes that the PCAOB should concentrate its efforts on updating its quality control standards that are long overdue for updating.

### **Discussion**

The Proposal would amend the PCAOB standards and rules to require registered public accounting firms to make two new disclosures in the audit report:

1. The name of the engagement partner for the most recent period's audit; and
2. Information on other independent public accounting firms and other persons that took part in the audit. In addition, the name of the engagement partner would also be required to be disclosed in Form 2 filed with the PCAOB for each audit report already required to be reported on the Form.

A foundational precept of independent audits is that the audit firm has ultimate responsibility for the audit report, while the opinion rendered represents the combined efforts of a team of individuals. Proposing disclosure requirements that could undermine and confuse this essential responsibility would impair transparency and accountability. It is also unclear what the objectives of the Proposal are, how the Proposal furthers the mission of the PCAOB, and what the consequences of the Proposal are in terms of its costs and benefits.

#### **1. Disclosing the Name of the Engagement Partner**

The proposal to disclose the name of the engagement partner for the most recent period's audit evolved from the PCAOB's *Concept Release on Requiring the Engagement Partner to Sign the Audit Report* issued on July 28, 2009. Among the concerns expressed by commenter's on that Concept Release was that

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partner signatures would suggest the engagement partner is responsible for the audit engagement and increase engagement partner legal liability.

The CCMC commends the PCAOB for responding to these concerns by not pursuing the original Concept Release. However, the CCMC believes that these fundamental concerns regarding the Concept Release hold equal weight with the current Proposal.

It is also problematic that the PCAOB continues to move in the direction of expecting engagement partners to somehow build their own individual reputations for audit quality, independent of their firm's reputation, undermining accountability in the audit process and harming investor protection.

In reality, the firm's quality control system, in accordance with the PCAOB's "interim" quality control standards, provides the foundation for the efficacy of the work performed on the engagement by the team of individuals in rendering the audit opinion. The CCMC believes that the PCAOB's quality control standards are long overdue for updating. Investors would likely be better served by the PCAOB focusing its efforts on updating these standards rather than diverting its time and resources on the Proposal.

#### *a. Legal Liability*

The potential for the disclosure of the name of the audit partner to increase engagement partner legal liability was recognized by Board Member Dan Goelzer in his Statement on the Proposal and his comments at the PCAOB's open Board meeting on October 22, 2011. The duties and relationships established by federal securities laws, Securities Exchange Act Rule 10b-5 and Securities Act Section 11 are the basis of those concerns. The June 2011 decision of the U.S. Supreme Court in *Janus Capital Group, Inc.*<sup>1</sup> has added to the uncertainty over legal liability under Rule 10b-5 in the context of this Proposal. In addition, it remains to be seen whether the Securities and Exchange Commission ("SEC") would require issuers to file not only the consent of the accounting firm that prepared the audit report but also a separate

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<sup>1</sup> See *Janus Capital Group, Inc. v. First Derivative Traders*, 131 S.Ct. 2296 (2011).

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consent of the engagement partner whose name is disclosed in the audit report.<sup>2</sup> If this requirement unfolds, this would subject the partner, along with the accounting firm, to potential Section 11 liability. Further, the CCMC understands liability issues could potentially extend to disclosure of the name of the engagement partner in PCAOB Form 2.

Given these legal uncertainties, the CCMC believes it would be premature of the PCAOB to proceed with this Proposal. The Board needs to fully understand the liability implications and have persuasive evidence that disclosure of the name of the engagement partner would be liability neutral. Neutrality is consistent with the recommendation of the Advisory Committee on the Auditing Profession (“ACAP”) that was the genesis for the Proposal.<sup>3</sup> The ACAP recommendation was premised on the condition that the requirement not impose on the engagement partner “any duties, obligations or liability that are greater than the duties, obligations and liability imposed on such person as a member of an auditing firm.”<sup>4</sup>

### ***b. Objectives***

The Proposal reiterates that the objectives from the Concept Release on partner signature—namely transparency and accountability—continue to be the objectives for disclosing the name of the engagement partner in the audit report and on PCAOB Form 2. Unfortunately, these objectives lack clarity in the context of this Proposal.

While the Proposal articulates the “means” of disclosing more information, it fails to state the “ends” it seeks to achieve. The Proposal fails to articulate the problem that needs to be addressed and how disclosing the name of the engagement partner will enhance financial reporting for investors.

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<sup>2</sup> If this scenario was to unfold, it is unclear if an issue of consent would be created for others participating in the audit.

<sup>3</sup> ACAP recommended that the PCAOB “undertake a standard-setting initiative to consider mandating the engagement partners’ signature on the auditor’s report (*Final Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury*, (2008), VII: 19, VII: 20).

<sup>4</sup> *Ibid* at VII: 20. The ACAP Report also noted that this language is similar to safe harbor language the SEC promulgated in its rulemaking pursuant to The Sarbanes-Oxley Act of 2002 (“SOX”) for audit committee financial experts.



Such an articulation is important as the Proposal simply provides conjectures for some of which the Board seeks comments on. For example, the Board asks whether the additional transparency could promote auditor independence by discouraging audit clients from inappropriately pressuring the firm to remove an engagement partner sooner than is required under the partner rotation requirements in SOX and SEC rules<sup>5</sup>. Yet, there are many substantive reasons for changes in engagement partners. And, without additional information disclosed about the reason for a change in the engagement partner an “inappropriate” partner change could not be discerned from a change in the name alone.

At the November 2011 meeting of the PCAOB’s Standing Advisory Group (“SAG”), PCAOB staff emphasized that no such additional disclosure regarding a change in engagement partners is proposed or planned. Indeed, current disclosure requirements on auditor change reside within the SEC’s jurisdiction and strongly suggest that any rulemaking along these lines would be better left to the SEC.

In the Proposal, accountability is described in terms of the original Concept Release with the added proviso that disclosure may make partners feel more accountable for the quality of the work and, therefore: “Disclosing the name of the engagement partner may be one means of promoting better performance”<sup>6</sup>. Not all agree with that statement and at the November 2011 SAG meeting; one SAG member took strong issue with this notion.

Reinforcing the speculative and likely illusory nature of any such improvements, the PCAOB has provided no evidence related to how this Proposal might improve audit quality. This is important because audit quality is the PCAOB’s mission. As Dan Goelzer stated at the PCAOB’s open Board meeting on October 11, 2011: “Unless engagement partner disclosure can be directly linked to improving audit quality, or to promoting understanding of the financial statement audit or of the Board’s inspection program, the issue would seem to fall in the SEC’s bailiwick.”<sup>7</sup>

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<sup>5</sup> PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29), Page 9.

<sup>6</sup> *Ibid.*

<sup>7</sup> See “Statement on Proposed Amendments to Improve Transparency Through Disclosure of Engagement Partner and Certain Other Participants in Audits” at the October 11, 2011 PCAOB Open Board Meeting by Daniel L. Goelzer, Board Member.

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### *c. Improving Audit Quality*

Evidence linking the Proposal with improvements to audit quality is a necessary condition for PCAOB rulemaking and for SEC approval of such rulemaking. The absence of any such evidence is likewise troublesome because the PCAOB considers collecting such evidence through its inspection process as one of its unique strengths. For example, the PCAOB's Strategic Plan for 2011-2015 (the "Strategic Plan") states: "We possess unique data and analysis related to audits based on eight years of inspections and enforcement experience, as well as a sophisticated research and analysis function".<sup>8</sup> Yet, there is no PCAOB data or analysis in evidence to support this Proposal and the Proposal makes no reference to the PCAOB having either collected or analyzed any relevant data.

Paradoxically, the objective for the disclosure of the name of the engagement partner, particularly the Form 2 disclosures, appears to be to facilitate analysis *by others*, not for the benefit of the PCAOB. For example, the Proposal states the purpose of the Form 2 disclosures is to compile this information in one place that could be easily accessed<sup>9</sup>. This implies that meaningful analysis of this data is possible and useful, which in reality is problematic given the complex nature of audit quality. This also ignores the facts that a thorough analysis of any such data requires such data to be considered in conjunction with information that may not be available or relevant to investors.<sup>10</sup>

Finally, it is worth noting that the PCAOB has not yet developed audit quality indicators—another ACAP recommendation. It would seem that the development of such indicators should occur in advance of any rulemaking on disclosing the name of the engagement partner as, at least implicitly, the Proposal is suggesting that the name of the engagement partner is somehow a quality indicator.

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<sup>8</sup> See Public Company Accounting Oversight Board Strategic Plan: *Improving the Relevance and Quality of the Audit for the Protection and Benefit of Investors 2011-2015* (November 30, 2011), Page 8.

<sup>9</sup> PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29), Page 17.

<sup>10</sup> Additionally, the Proposal fails to take into account that various actors aggregate a variety of data from SEC filings that they find relevant.

#### ***d. Other Costs and Benefits***

An additional motivation for disclosing the name of the engagement partner appears to be to provide useful information for audit committees. For example, the Proposal reiterates a point made in the Concept Release that “providing financial statement users, audit committees, and others with the name of the engagement partner might provide them the opportunity to evaluate, to a degree, an engagement partner’s experience and track record. If so, audit committees might increasingly seek out engagement partners who are viewed as performing consistently high quality audits, and the resulting competition could lead to an improvement in audit quality”<sup>11</sup>. However, this rationale cannot serve as a basis for rulemaking as audit committees already have access to this information and would need to use it in conjunction with a variety of other information, both public and private, for assessing quality on their audits.

As expressed in previous letters to the PCAOB,<sup>12</sup> the CCMC continues to be concerned that this Proposal provides yet another illustration of the PCAOB’s skepticism regarding the role of audit committees and that this and other PCAOB proposals may actually interfere with the prerogatives, discretion and duties of audit committees. For example, with this Proposal, the PCAOB seems to be expecting investors to second guess the work of audit committees based on “one” data point – the name of the engagement partner.

## **2. Disclosing Information on Others Participating in the Audit**

Somewhat ironically the Proposal combines a disclosure focused on one individual with a requirement to disclose more information about others participating in the engagement not employed by the auditor. The Proposal calls for disclosure, with limited exceptions, of other participants in the audit for whose audit the auditor takes responsibility or whose audit procedures the auditor supervises. The Proposal

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<sup>11</sup> Ibid, Page 6.

<sup>12</sup> For example, see the September 14, 2011 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on the *Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements* (PCAOB Release No. 2011-003, June 21, 2011, Rulemaking Docket Matter No. 34) and the October 20, 2011 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on the *Concept Release on Auditor Independence and Audit Firm Rotation* (PCAOB Release No. 2011-006, August 15, 2011, PCAOB Rulemaking Docket Matter No. 37).

would require the auditor to disclose in the audit report, the names, location, and percentage of hours attributable to the other participants for those whose participation is 3% or greater of total hours. Disclosures would also be required when the auditor divides responsibility with another independent public accounting firm.

The Proposal suggests that these disclosures would “enable investors and other users of the audit report to determine whether a disclosed independent public accounting firm is registered with the Board and has been subject to PCAOB inspection, and whether a disclosed independent public accounting firm or another person has had any publicly available disciplinary history with the Board or other regulators”<sup>13</sup>. However, this is information that the audit committee has access to and can consider in exercising its oversight responsibilities. Further, the auditor either takes responsibility for the work of others or divides responsibility. In the case of the later, current disclosures to investors do not appear wanting for assessing audit quality and the applicability of PCAOB inspection information.

Essentially the “new” information proposed to be disclosed involves work for which the auditor assumes responsibility. As such, the proposed disclosures are likely to only cause confusion over who has responsibility for the audit. The CCMC notes that avoiding such confusion is an important objective of current auditing standards. This suggests that investors would be better served with more targeted disclosures founded on some meaningful objective.

The potential for confusion is exacerbated by the low threshold for disclosure of 3% being proposed. The basis for this threshold is unclear as the Proposal provides no meaningful rationale for it. Further, a 3% threshold is much lower and in marked contrast to the 20% threshold already incorporated in PCAOB rules to determine others performing a substantial role in audits and thus subject to PCAOB registration and inspection. So, why should investors be interested in what the PCAOB is not?

Further, there is no indication that the PCAOB has field-tested the 3% threshold to determine the relevance of the information to be disclosed. For example,

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<sup>13</sup> PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29), Page 20.

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the Proposal contains no useful illustrations based on real-world data. The absence of these data to inform stakeholders about the implications of the Proposal is surprising, given the PCAOB has access to the necessary data through its inspection process and, as previously noted, the PCAOB emphasizes this in its Strategic Plan as strength of the organization.<sup>14</sup>

### Conclusion

The CCMC appreciates the opportunity to comment on the Proposal. However, the CCMC believes that the Proposal will disseminate information that is non-material, lacks relevance that could undermine the fundamental foundations of the audit function hampering the ability of investors to make informed decisions. Without a clear articulation of the problems to be solved and the benefits of the proposal, the CCMC does not believe that the proposal should move forward.

Furthermore, based on the statements and comments by Board members at the October 11, 2011 open Board meeting, it appears that the majority of Board members strongly support enacting the Proposal raising potential due process questions. The CCMC hopes that the PCAOB will take the concerns expressed in this letter under consideration when deliberating on the Proposal.

Thank you for your consideration and the CCMC stands ready to discuss these concerns in further detail.

Sincerely,  


Tom Quadman

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<sup>14</sup> While the CCMC does not believe that it is in the best interests of financial reporting to move forward on this proposal, one alternative the PCAOB may wish to consider is that the Form 2 would be a more useful location for such disclosures, as the determination of information in SEC filings is more appropriately maintained within the SEC's jurisdiction, Form 2 disclosures would not lengthen issuer and broker-dealer filings with tangential information, and Form 2 disclosures would not be subject to the estimation of hours necessitated by the short time constraints for SEC filings. In addition, disclosure in Form 2, instead of the audit report, might help mitigate potential liability issues and confusion over auditor responsibility, as previously discussed.



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March 10, 2014

Ms. Phoebe W. Brown  
Secretary  
Public Company Accounting Oversight Board  
1666 K Street, NW  
Washington, D.C. 20006

**Re: PCAOB Exposure Draft on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor's Report of Certain Participants in the Audit* (PCAOB Release No. 2013-009, December 4, 2013; PCAOB Rulemaking Docket Matter No. 029)**

Dear Ms. Brown:

The U.S. Chamber of Commerce (the "Chamber") is the world's largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21<sup>st</sup> century economy. The CCMC believes that businesses must have a strong system of internal controls and recognizes the vital role external audits play in capital formation. The CCMC supports efforts to improve audit effectiveness and appreciates the opportunity to comment on the Public Company Accounting Oversight Board ("PCAOB") Exposure Draft on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor's Report of Certain Participants in the Audit* ("the Proposal").

The CCMC has serious concerns that the PCAOB has not met the minimum thresholds needed to move forward on the Proposal, namely the failure to

demonstrate how the Proposal will provide investors with decision useful information and what investor interests are being addressed. While the CCMC applauds the PCAOB for establishing the Center for Economic Analysis, the Proposal's cost-benefit analysis is insufficient as it fails to provide stakeholders with an analysis to comment on, nor is any analysis provided to meet the statutory requirements as to why Emerging Growth Companies ("EGCs") should be subject to the Proposal if adopted. Finally, the issues raised in our January 9, 2012 comment letter to the Proposal's predecessor ("2012 letter") remain unaddressed. Accordingly, we have attached the 2012 letter as an appendix to this letter and ask that it also be considered a part of the record.

Our concerns are discussed in more detail below.

## I. Background

The Proposal would require disclosure in the auditor's report of the following:

- The name of the engagement partner;
- The names, locations, and extent of participation of other independent public accounting firms that took part in the audit; and
- The locations and extent of participation of other persons not employed by the auditor, whether an individual or a company, ("other participants") that took part in the audit.

The Proposal represents the latest PCAOB release on these matters. In July 2009, the PCAOB issued a Concept Release on *Requiring the Engagement Partner to Sign the Audit Report*. In October 2011, the PCAOB proposed a rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2*. The CCMC provided comments on the proposed rulemaking.<sup>1</sup>

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<sup>1</sup> See the January 9, 2012 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29).

## II. Naming the Engagement Partner

While the Proposal calls for audit firms to disclose the name of the engagement partner in the auditor's report, it does not provide a meaningful rationale for why this should be done. The Proposal states that this information "*could* be valuable to investors in making investment decisions as well as if they are asked to vote to ratify the company's choice of registered firm as its auditor" (emphasis added).<sup>2</sup> However, there is a marked failure to show how this change in disclosure will benefit investors and the arguments in support of the Proposal, including those related to audit quality, are superficial.<sup>3</sup>

The Proposal states the "means" of more disclosure but fails to demonstrate the "ends" it seeks to achieve. The Proposal does not articulate the problem that will be resolved through the adoption of the Proposal, or how the Proposal is the best option to solve the undefined problem. Moreover, the Proposal fails to show how investor needs will be enhanced through the naming of the engagement partner.

### a. Audit Quality

As we expressed in the 2012 letter, regardless of their nature and size, audits are performed by a team of individuals. In reality, the audit firm's quality control system, in accordance with the PCAOB's "interim" quality control standards, provides the foundation for the efficacy of the work performed on audits. The CCMC continues to believe that investors would be better served by the PCAOB focusing its efforts on updating its quality control standards rather than naming the engagement partner.

The Proposal states that the PCAOB has noticed through its inspection process variation in the quality of audits performed. While the inspections process can and should be a useful tool in setting priorities for the PCAOB, the justification for the Proposal falls short. The Proposal states that, while many factors contribute to this variation, the role of the engagement partner is an important factor to

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<sup>2</sup> See page 3 of the Proposal.

<sup>3</sup> Setting aside the conceptual flaws with the Proposal, from a practical standpoint, the CCMC notes that naming the engagement partner in the auditor's report is retrospective and does not necessarily disclose to investors the identity of the engagement partner for the *upcoming* period that applies to the shareholder vote on ratification of the audit firm.



consider.<sup>4</sup> Unfortunately, this is not a compelling argument for this Proposal. If a variation of audit quality is found because of a variety of factors, either that combination of factors must be addressed in a policy response, or a clear and demonstrable showing must be made of how naming the engagement partner is the over-riding cause of such a variation.

The Proposal does not make either case.

Naming the engagement partner does not enable investors or other third-parties to even begin to approach “stepping into the shoes” of the PCAOB or audit committee. Indeed, third-parties may instead get an incorrect view of the role of the engagement partner related to audit quality based on the information available from the name of the engagement partner. Investors are better served by relying on the regulatory and governance processes rather than trying to second guess these processes based on a disclosure of the name of the engagement partner.

Reinforcing this point, the CCMC notes that another current PCAOB initiative focuses on developing audit quality indicators (“AQIs”). The PCAOB staff Discussion Paper for the May 15-16, 2013 meeting of the Standing Advisory Group (“SAG”) describes this initiative. The definition of audit quality in the Discussion Paper includes “meeting investors’ needs for independent and reliable audits.”<sup>5</sup> In this regard, the SAG Discussion Paper provides 40 different AQIs involving operational inputs (13), the audit process (15), and audit results (12). The name of the engagement partner is not among these 40 AQIs. Thus, the PCAOB’s own initiative on audit quality does not recognize the relevance of disclosing the name of the engagement partner to investors.

## **b. Legal Liability**

The Proposal calls for placing the disclosure of the name of the engagement partner in the auditor’s report. In the 2012 letter, the CCMC expressed concern that disclosing the name of the partner could increase engagement partner legal liability. Disclosure in the auditor’s report is a major contributor to the liability increase.

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<sup>4</sup> See page 6 of the Proposal.

<sup>5</sup> See pages 3 and 4 of the Discussion Paper on AQIs for the May 15-16, 2013 SAG meeting.

The CCMC appreciates that the Proposal contains a section on liability considerations, including under Section 11 of the Securities Act and Section 10(b) and Rule 10b-5 of the Exchange Act.<sup>6</sup> As explained in the Proposal, Section 11 of the Securities Act imposes liability for material misstatements or omissions in a registration statement, subject to a due diligence defense, on “every accountant ... who has with his consent been named as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement ... which purports to have been prepared or certified by him.”<sup>7</sup>

In turn, Section 7 of the Securities Act requires issuers to file with the Securities and Exchange Commission (“SEC”) the consent of any accountant who is named as having prepared or certified any part of the registration statement or any valuation or report included in the registration statement. The Proposal recognizes that engagement partners (and participating accounting firms) named in the auditor’s report would have to consent to the inclusion of their names in such reports filed with the SEC, or included by reference in another document filed under the Securities Act with the SEC.<sup>8</sup>

As to Section 11 liability, the Proposal acknowledges litigation-related costs would increase, but conjectures that these costs should “not be substantial.”<sup>9</sup> As to liability under Section 10(b) of the Exchange Act, the Proposal acknowledges concerns similar to those we expressed in our letter of January 9, 2012 and states that the Board “cannot conclude with certainty whether its approach might increase liability.”<sup>10</sup>

The CCMC continues to strongly believe that “liability neutral” represents a minimum threshold for proceeding with any initiative that would involve disclosing the name of the engagement partner. The CCMC urges the PCAOB to recognize this important pre-condition as anything other than liability neutral standards will ultimately harm investors. Such a precondition should also be a part of an economic

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<sup>6</sup> See pages 20-26 of the Proposal.

<sup>7</sup> See page 21 of the Proposal.

<sup>8</sup> See pages 21-22 of the Proposal.

<sup>9</sup> See page 23 of the Proposal.

<sup>10</sup> See page 25 of the Proposal.

analysis.<sup>11</sup> Economic analysis should be used to determine if a proposed standard or revision to a standard is liability neutral and if not what the costs to investors and businesses will be.

**c. Placement of Disclosures**

While the CCMC does not support a requirement to disclose the name of the engagement partner, we would also like to comment on the Proposal in regards to the placement of any such disclosure. If any such requirement ensues from this initiative, disclosures should not be in the audit report. Rather than being part of the auditor's report, any such disclosure seems better suited for inclusion in a report by the audit committee in the proxy statement.

Importantly, the PCAOB could have circumvented some of the Section 11 liability concerns previously discussed by not proposing the name of the engagement partner (and other participants involved in the audit) be disclosed in the auditor's report. An alternative mode of naming the engagement partner would be a disclosure on the PCAOB's website through the use of Form 2.

In this regard, it is worth recalling that the PCAOB's October 2011 Proposed Rulemaking would have required disclosure of the name of the engagement partner in both the audit report and PCAOB Form 2. Instead of focusing the initiative on disclosures in Form 2, the current Proposal would require the disclosure only in the audit report. Apparently this focus was premised on arguments that disclosures in the audit report on the SEC's website would be more timely and accessible for investors. However, these arguments are not at all compelling.

It is unclear as to why a posting on both the SEC's and PCAOB's websites would not be the preferable route of disclosure. If the decision to make this disclosure on the SEC website alone is because the PCAOB's website is not "user friendly", that is a problem that can be fixed by the PCAOB. It cannot be used as a rationale to impose costs on all stakeholders. Moreover, according to the PCAOB's Strategic Plan and statements by Board members at the PCAOB's November 25,

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<sup>11</sup> Liability neutrality is not a new concept; it was also included in the *Final Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury* (2008), VII: 19-20.

2013 open meeting on the PCAOB budget,<sup>12</sup> the PCAOB already has an initiative underway to leverage its technology, improve the “usability” of its website, and enhance communication to public constituencies. Thus, this technology “impediment” seems fixable in the near term; and, it is under the purview of the PCAOB to do so.

Further, the notion that investors would have all necessary information in-hand with disclosure of the name of the engagement partner in the audit report is flawed. Setting aside that the name of the engagement partner is unlikely to provide any actionable information for investors, there is no information content in the name of the engagement partner per se. Indeed, it is unclear how the disclosure of a name, which on its face will be of no utility to an investor, will help the reasonable investor make an investment decision. Indeed, the PCAOB acknowledges in the Proposal that this disclosure would have to be considered in combination with other information.<sup>13</sup>

It appears that the PCAOB envisions some of this other information would come from the SEC’s website, but it would also involve information on the PCAOB’s existing website as well. In addition, according to the Proposal, much of this other information would have to be obtained (and only available over time) from academic research and databases developed by third-parties.<sup>14</sup> Thus, the argument that the name of the engagement partner needs to be included in the audit report in order for investors to have all necessary information readily available in one place falls apart in practice.

Not disclosing the name of the engagement partner (and other participants in the audit) in the auditor’s report would likewise avoid the complex and costly administrative nightmare that would be imposed on audit firms and issuers from needing to obtain Section 7 consents from engagement partners (and other participating accounting firms) so that issuers could file required consents with the SEC. The Proposal fails to recognize the multiple difficulties that would arise in trying to obtain such consents. These difficulties would likely hinder the ability of issuers to make timely filings with the SEC, thereby harming investors.

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<sup>12</sup> For example, see *PCAOB Strategic Plan: Improving the Quality of the Audit for the Protection and Benefit of Investors 2013-2017* (November 26, 2013), pages 16-17.

<sup>13</sup> See page 11 of the Proposal.

<sup>14</sup> See, for example, pages 12-13 of the Proposal.

As just one example of the difficulties that could arise from needing Section 7 consents, assume that an engagement partner is rotated off an audit because of the Sarbanes-Oxley Act of 2002 (“SOX”) mandatory partner rotation requirement and the SEC’s rules implementing this requirement. Also assume that the partner’s initial consent needs to be reissued. On one hand, the partner would need to do additional work in order to allow the reissuance of the consent.<sup>15</sup> On the other hand, the partner would be precluded from doing any additional work because it would cause the audit firm to be in violation of the SEC’s independence rules. Moreover, this example assumes the partner would be willing and able to reissue the consent and does not consider the need to address the myriad of circumstances when this would not be the case.

The Proposal appears to set up a dynamic whereby PCAOB requirements would force the SEC to waive its requirements (as a matter of policy) for audit partners (and other participants in audits) to reissue their consents in a broad array of circumstances in order to make our markets function efficiently.

All things considered, the arguments in the Proposal for disclosing the name of the engagement partner (and other participants in the audit) in the audit report are simply not convincing. The proposed placement of the disclosures significantly increases the costs of the Proposal, including legal and administrative costs, for no substantive benefit. The CCMC strongly urges that the PCAOB reconsider the Proposal in this regard.

### **III. Other Participants in the Audit**

In addition to disclosing the name of the engagement partner, the Proposal would also require that the audit report disclose the names, locations, and extent of participation of other independent public accounting firms that took part in the audit and the locations and extent of participation of other persons not employed by the auditor. The proposed threshold for these disclosures is any public accounting firm or other participant performing 5% or more of the total hours in the most recent period’s audit. This threshold is designed to demonstrate if an accounting firm plays a substantial role in the audit. The current threshold is 20%.

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<sup>15</sup> Our discussion sets aside any considerations related to determining the nature of and standards for this work.

While the CCMC appreciates that the Proposal does raise the threshold from the 2011 proposal of 3% to 5%, we believe that the Proposal does not provide a compelling case for why the current 20% threshold should not be used instead.

As expressed in our 2012 letter, we do not believe that it is in the best interests of financial reporting to move forward on these matters. And, as previously discussed in this letter, we continue to be concerned that any such disclosures do not belong in the auditor's report.

#### **IV. Cost Benefit Analysis**

The Proposal recognizes that the Jumpstart Our Business Startups Act ("JOBS Act") now makes economic analysis a necessary pre-condition for applying new PCAOB auditing standards and rules to an audit of any emerging growth company ("EGC"). Specifically, Section 103(a) (3) of SOX as amended by Section 104 of JOBS Act requires that rules adopted by the Board after the date of enactment of JOBS Act shall not apply to an audit of any EGC, unless the SEC determines that the application of such additional requirements is necessary or appropriate in the public interest, after considering the protection of investors and whether the action will promote efficiency, competition, and capital formation. The Proposal recommends that EGCs follow the requirements if adopted.

At the outset, we commend the PCAOB for establishing the Center for Economic Analysis to help fulfill the statutory requirements of the JOBS Act. The CCMC has been a strong advocate of economic analysis as a means of using empirical evidence to guide smart regulation and standard setting.<sup>16</sup>

However, in our view, the economic analysis provided with the Proposal fails to provide commenters with any information to comment on and fails to delineate the costs or benefits to EGCs if they are to follow the requirements of the Proposal. Indeed there is no analysis to provide an articulation of the benefits or of the costs to

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<sup>16</sup> For example, see the December 9, 2013 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on Proposed Auditing Standards on *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion; the Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report; and Related Amendments to PCAOB Standards* (PCAOB Release No. 2013-005, August 13, 2013 and PCAOB Rulemaking Docket Matter No. 34).

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EGCs. This not only calls into question the ability of the Proposal to meet the economic analysis requirements needed for the Proposal to be approved through the SEC's rulemaking process, it also raises questions regarding the level of the PCAOB's commitment to economic analysis.

A review of some academic studies of companies in jurisdictions that do not have similar legal, regulatory, governance, market, and cultural environments and structures with the United States does not pass muster as an economic analysis. The Proposal contains no analysis or articulation of the direct costs to issuers, the direct costs to auditors, possible liability costs to issuers, possible impacts on stock price, possible impacts on returns to investors, potential discussion of benefits, if any public companies in the United States voluntarily disclose the name of the engagement partners and the costs and benefits comparing those companies to similarly situated companies. This is by no means an exhaustive list, but it is the type of analysis that accompanies proposed regulations when required by law. As such an analysis is required by the JOBS Act and as this Proposal must go through the SEC rulemaking process which will require an analysis of the impacts on competition and capital formation a more thorough study subject to public comment is necessary to move forward in applying the Proposal to EGCs.

The CCMC notes that the PCAOB's Strategic Plan for 2013-2017 states the PCAOB has developed "internal" guidance on economic analysis.<sup>17</sup> The CCMC strongly urges the PCAOB to release its internal guidance on economic analysis for public comment so that stakeholders can be informed of the PCAOB's understanding of the role of economic analysis and how it can be used. Such public commentary can create a useful dialogue on the issue that all sides can benefit from. The merits of the PCAOB's analysis of costs and benefits in any particular proposal cannot be evaluated without understanding the essentials of the guidance being applied by the PCAOB for economic analysis.

The CCMC is very disappointed with the level of economic analysis provided in the Proposal and believes that it cannot pass the requirements of the JOBS Act and other statutory provisions that must be met for the Proposal to be approved and

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<sup>17</sup> For example, see page 13 of the PCAOB *Strategic Plan: Improving the Quality of the Audit for the Protection and Benefit of Investors 2013-2017* (November 26, 2013).

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become operational. Economic analysis, with a thorough weighing of the costs and benefits, can and should be used as a means of using empirical evidence to develop smart regulations. That goal has not been met.

## **V. Conclusion**

Once again, the CCMC appreciates the opportunity to comment on the Proposal. However, the CCMC has serious concerns that the Proposal in its current form is flawed.

The Proposal fails to demonstrate how naming an engagement partner will improve audit quality, will provide investors with decision-useful information, and what investor interests are being addressed. Additionally, the cost-benefit analysis is insufficient as it fails to provide stakeholders with an analysis to comment on, nor is any analysis provided to meet the statutory requirement that must be fulfilled for the Proposal to be applied to EGCs. Indeed, we are concerned about the commitment of the PCAOB to a robust economic analysis as envisioned by the bipartisan JOBS Act.

Thank you for your consideration and the CCMC stands ready to assist in these efforts.

Sincerely,

A handwritten signature in black ink, appearing to read 'T. Quadman', with a long, sweeping horizontal stroke extending to the right.

Tom Quadman