



February 15, 2011

**EXECUTIVE DIRECTOR**

Cynthia M. Fornelli

**GOVERNING BOARD**

Chairman

James S. Turley, Chairman and CEO  
Ernst & Young LLP

Vice Chair

Michele J. Hooper, President and CEO  
The Directors' Council

Vice Chair

Barry C. Melancon, President and CEO  
AICPA

Charles M. Allen, CEO  
Crowe Horwath LLP

Stephen Chipman, CEO and Executive Partner  
Grant Thornton LLP

Harvey J. Goldschmid, Dwight Professor of Law  
Columbia University

Robert E. Moritz, Chairman and Senior Partner  
PricewaterhouseCoopers LLP

Lynn S. Paine, Professor of Business  
Administration and Senior Associate Dean,  
Director of Faculty Development  
Harvard Business School

Barry Salzberg, CEO  
Deloitte LLP

Dave Scudder, Managing Partner  
McGladrey & Pullen, LLP

John B. Veihmeyer, U.S. Chairman and CEO  
KPMG LLP

Jack Weisbaum, CEO  
BDO USA, LLP

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

**Re: Request for Public Comment: *Proposed Temporary Rule for an Interim Program of Inspection Related to Audits of Brokers and Dealers*, PCAOB Rulemaking Docket Matter No. 32**

Dear Office of the Secretary:

The Center for Audit Quality (CAQ) is an autonomous public policy organization dedicated to enhancing investor confidence and public trust in the global capital markets. The CAQ fosters high quality performance by public company auditors, convenes and collaborates with other stakeholders to advance the discussion of critical issues requiring action and intervention, and advocates policies and standards that promote public company auditors' objectivity, effectiveness and responsiveness to dynamic market conditions. Based in Washington, D.C., the CAQ is affiliated with the American Institute of Certified Public Accountants (AICPA). The CAQ appreciates the opportunity to respond to the Public Company Accounting Oversight Board's (PCAOB or the Board) *Proposed Temporary Rule for an Interim Program of Inspection Related to Audits of Brokers and Dealers* (proposed temporary rule), as published in PCAOB Release No. 2010-008 dated December 14, 2010 (release). This letter represents the observations of the CAQ, but not necessarily the views of any specific firm, individual or CAQ Governing Board member.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) amended various provisions of the Sarbanes-Oxley Act of 2002 (the Act) by giving the Board oversight authority with respect to audits of brokers and dealers. These amendments provide the Board with oversight authority to promulgate standards, conduct inspections, and undertake investigations and disciplinary proceedings with respect to audits of brokers and dealers. Given the Dodd-Frank Act does not prescribe a specific program of inspections for registered public accounting firms that conduct audits of brokers and dealers, we believe the Board's approach of proposing a temporary rule for an interim program of inspection related to audits of brokers and dealers is an appropriate and reasonable approach. This will allow the Board to assess public accounting firms' current adherence to professional standards, the Act, and the U.S. Securities and Exchange Commission's (SEC or the Commission) rules, as well as inform the Board's decision about significant elements of a permanent inspection program. Although we support the Board's information gathering approach, we encourage the Board to focus a significant portion of its efforts on audits of brokers and

dealers that are considered to be of greater significance to investors and other users. For example, brokers and dealers that have possession and control of customer securities – or act as clearing, carrying or custodial brokers – are typically considered to be of greater significance to investors and other users than introducing brokers that accept customers’ orders but the orders are processed or “cleared” through another broker, known as a clearing broker.<sup>1</sup>

Further, the Board references “classes” of brokers and dealers a number of times throughout the release and the proposed temporary rule. Given there is no description or clear understanding of what constitutes such “classes,” we recommend that the Board specifically define what is meant by “classes” of brokers and dealers.

While we understand and support the Board’s intent is to inform its decisions in determining a permanent inspection program, we do, however, seek clarity on how the interim inspection program will be executed, as described below.

### ***PCAOB Progress Reports***

The CAQ commends the Board on its plan to at least every 12 months publish reports on the interim inspection program’s progress and significant observations that either may bear on the Board’s consideration of a permanent program or otherwise may be appropriate to protect the interests of investors or to further the public interest. We believe that such transparent reports will be helpful not only in informing the public as to the Board’s progress but also in improving audit quality. These reports will clarify the Board’s expectations for effective audits of brokers and dealers as well as focus registered public accounting firms on improving their work in areas where common deficiencies, if any, are identified. As the Board contemplates the structure and detail of these reports, we encourage the PCAOB to consider reporting its observations by different types of brokers and dealers whose audits were inspected during the interim inspection program. Including this level of detail in the Board’s progress reports will be informative to the public and investors in understanding how the Board ultimately determines the scope of the permanent inspection program. In addition, we believe this information will be helpful to the registered public accounting firms that perform such audits by enhancing their level of understanding of the Board’s expectations and observations with regard to engagements related to the different types of brokers and dealers. We understand the level of detail will have to be balanced with making certain that the registered public accounting firm and broker-dealer are not identified or could potentially be identified, but we believe such balance could be achieved.

### ***Conducting Inspections***

We note that proposed temporary Rule 4020T(a)(1), *Interim Inspection Program Related to Audits of Brokers and Dealers*, indicates that one of the purposes of the interim inspection program is to “assess the degree of compliance of registered public accounting firms and their associated persons with the Act, the Board’s rules, the Commission’s rules, and professional standards in connection with the performance of audits, issuance of audit reports, and *related matters involving brokers and dealers*.” We believe the Board should clarify what it means by “related matters” to enable registered public accounting firms to fully understand the Board’s expectations and execute against them.

In addition, we encourage the Board to elaborate on its expectations related to the voluntary cooperation of “certain” firms under the interim inspection program prior to the proposed temporary rules taking effect. Page 8 of the release states, “even before any such rule takes effect...the Board expects to be able to conduct relevant procedures with the voluntary cooperation of certain firms.” The Board should clarify what it means by “relevant procedures” during the voluntary period. For example, does the Board anticipate that inspection procedures performed during the voluntary period will include actual inspection of audits of brokers and

<sup>1</sup> As described in the PCAOB’s July 15, 2010 Standing Advisory Group Meeting Briefing Memo entitled, “Broker-Dealer Audit Considerations.” [http://pcaobus.org/News/Events/Documents/07152010\\_SAGMeeting/Broker\\_Dealer.pdf](http://pcaobus.org/News/Events/Documents/07152010_SAGMeeting/Broker_Dealer.pdf)

dealers or be limited to scoping procedures? In addition, we encourage the Board to elaborate on the timing of such procedures (e.g., inspection of 2010 broker-dealer audits will be conducted beginning in the second quarter of 2011, limited to inspections of broker-dealer audits with year-end dates after the enactment of the Dodd-Frank Act) and indicate which firms are expected to voluntarily cooperate (e.g., previously inspected firms or firms that have never been subjected to inspection).

### ***Firm-Specific Inspection Reports***

We have noted some inconsistencies between the release language and the proposed temporary rule amendments regarding firm-specific inspection reports and seek clarification regarding the process by which the Board will report inspection deficiencies in such reports. Specifically, during the course of the interim inspection program it is not sufficiently clear how inspection findings will be communicated to the firm, what opportunities the firm will have in responding to such findings, or the timing and extent to which interim inspection findings will be communicated in firm-specific reports. For example:

- 1) When inspection findings are communicated to the firm during the interim program, it is not clear if the findings will be communicated orally or in writing and what opportunities the firm will have to respond to such findings.

Page 9 of the release states that the Board will bring identified audit deficiencies “to the firm’s attention with the expectation that the firm will address the deficiencies and take steps to avoid future such deficiencies.” We are unclear how the Board intends to communicate those deficiencies throughout the interim inspection period or what the Board’s expectations are for the firms to respond to deficiencies noted. The proposed temporary rule amendments in the Appendix to the release do not discuss any procedures to allow a firm to respond to inspection findings during the interim inspection period. We recommend the Board clarify the process as to how the firm can expect to receive and address comments from the Board (i.e., whether comments from the Board are anticipated to be written or oral and the expectations by the PCAOB for firm responses thereto) during the interim inspection program.

- 2) It is not clear whether the Board intends to issue the public portion of a firm-specific report before the permanent rule takes effect and, if so, what opportunities the firm will have to respond to a draft inspection report before it is made public.

First, page 10 of the release states that the Board would issue firm-specific inspection reports that encompass procedures performed during the interim period but “would expect” to do so only after the permanent program takes effect. Further, footnote 21 in the release states that:

While the interim program is in place, a Board inspection of a firm that performs audit work for issuers and for brokers or dealers would include the full, regular inspection – including the firm-specific inspection report – of the firm’s issuer practice. Such an inspection could also include inspection procedures under the interim program with respect to the firm’s broker and dealer practice, but the Board would not expect to incorporate any evaluation of the firm’s broker and dealer practice into the public portion of a firm-specific report before the first inspection of the firm that occurs after a permanent program takes effect. Nothing in the temporary rule, however, would necessarily preclude the Board from issuing a firm-specific inspection report on, or including, inspection observations from the interim program before a permanent program takes effect.

In addition, we note the Board has stated in the release that inspection observations will constitute a “foundational portion” of the first inspection and firm-specific inspection report only after the permanent program takes effect in order to make “consistent and meaningful evaluations of the types of quality control issues that going forward, firms need to address in their practices.” [Emphasis added.] We agree

with such an approach, because the professional standards and the Commission's rules regarding brokers and dealers are anticipated to be amended and/or replaced over the three-year interim inspection period and firms' quality control systems likewise will be evolving in response to changed standards and rules.

Based on these discussions in the release, our expectation is that, until the permanent rule takes effect, the Board will not be commenting on a firm's broker and dealer practice's inspection results in the public portion of inspection reports of firms currently subject to inspection and will not be issuing public inspection reports on firms that audit brokers and dealers and currently are not subject to inspection. We recommend the Board clearly state so in the final temporary rule.

On the other hand, if the Board intends to publicly issue firm-specific broker and dealer inspection results prior to the permanent rule taking effect, it is not clear if the firm will have an opportunity to respond before an inspection report is made public. Would the Board follow the same procedures as are currently required by Section 4, *Inspections* of the PCAOB's rules? We note that footnote 10 of the release states that "[a]mong other things...the confidentiality provisions of Sections 104(g)(2) and 105(b)(5) of the Act will apply, as will the provisions for a firm to review and respond to a *draft inspection report*." Although there is a reference to a draft inspection report in the release, the Board has not included Rule 4007, *Procedures Concerning Draft Inspection Reports* as applicable to the interim inspection program under proposed temporary Rule 4020T. Further, the proposed temporary rule amendments in the Appendix to the release do not discuss any provisions for issuance of a draft inspection report or procedures to allow a firm to respond to a draft inspection report during the interim inspection program.

- 3) It is not clear what interim inspection observations the Board intends to include in the initial firm-specific reports released after a permanent program takes effect.

We note that the Board expects to issue firm-specific inspection reports after rules for a permanent program take effect. As stated above, the Board has explained that inspection observations noted throughout the interim inspection period will constitute a "foundational portion" of the first inspection and firm-specific inspection report issued after the permanent program takes effect. The PCAOB expects that this process will result in "consistent and meaningful evaluations of the types of quality control issues that going forward, firms need to address in their practices."<sup>2</sup> Although we expect that the Board would only include observations noted during the interim inspection period that would have an impact on a firm going forward, the release does not address what specifically the Board intends to include in the initial firm-specific inspection report. For example, it is not clear as to whether potential deficiencies included in a firm-specific report will be cumulative in nature – that is, whether inspection comments will be cumulative over the course of the three years of the interim inspection program.

Because there could be a significant time lag between the date of interim inspection(s) and the date of the initial report issuance under the permanent program - a period of time during which there likely will be changes in standards and rules and changes in firms' quality controls and procedures, we believe there is a risk that the initial firm-inspection reports under the permanent program could be based on outdated information that would be inappropriate, and particularly so if reported to the public. As such, we urge the Board to reconsider whether it is helpful to include findings from the interim program in the first firm-specific reports under the permanent program.

Lastly, in order to avoid possible confusion, we recommend the Board describe in the final temporary inspection rule (as opposed to only being discussed in the release accompanying the final temporary rule) the process for the PCAOB to communicate findings and audit firms to respond to such findings as well as the

---

<sup>2</sup> Page 10 of the Release

protocol for including findings from the interim program in a firm-specific inspection report issued after the permanent program takes effect.

\*\*\*\*

The CAQ appreciates the opportunity to comment on the proposed temporary rule and would welcome the opportunity to respond to any questions you may have regarding any of the comments and recommendations included in this letter.

Sincerely,



Cynthia M. Fornelli  
Executive Director  
Center for Audit Quality

cc: PCAOB  
James R. Doty, Chairman  
Lewis H. Ferguson, Member  
Daniel L. Goelzer, Member  
Jay D. Hanson, Member  
Steven B. Harris, Member  
George Diacont, Director, Division of Registration and Inspections

SEC  
Chairman Mary L. Schapiro  
Commissioner Luis A. Aguilar  
Commissioner Kathleen L. Casey  
Commissioner Troy A. Paredes  
Commissioner Elisse B. Walter  
James L. Kroeker, Chief Accountant  
Brian T. Croteau, Deputy Chief Accountant