

Via E-Mail

June 24, 2021

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

Re: PCAOB Rulemaking Docket Matter No. 048

Dear Madam Secretary:

I am writing of behalf of the Council of Institutional Investors (CII) in response to The Public Company Accounting Oversight Board (PCAOB or Board) proposed “new rule, PCAOB Rule 6100, *Board Determinations Under the Holding Foreign Companies Accountable Act*” (HFCAA) (Proposed Rule).¹

CII is a nonprofit, nonpartisan association of United States (U.S.) public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of approximately \$4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families, including public pension funds with more than 15 million participants – true “Main Street” investors through their pension funds. Our associate members include non-U.S. asset owners with about \$4 trillion in assets, and a range of asset managers with more than \$40 trillion in assets under management.²

As the leading voice for effective corporate governance and strong shareholder rights, CII believes that accurate and reliable audited financial statements are critical to investors in making informed decisions, and vital to the overall well-being of our capital markets.³ For far too long, more than 13 years, there has been a gap in the PCAOB’s ability to inspect and investigate

¹ PCAOB Rule 6100, Board Determinations Under the Holding Foreign Companies Accountable Act, PCAOB Rulemaking Docket Matter No. 048, PCAOB Rel. No. 2021-001 at 1 (May 13, 2021), https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/rulemaking/docket048/2021-001-hfcaa-proposing-release.pdf?sfvrsn=dad8edcf_6.

² For more information about the Council of Institutional Investors (“CII”), including its board and members, please visit CII’s website at <http://www.cii.org>.

³ CII, Policies on Other Issues, Independence of Accounting and Auditing Standard Setters (updated Mar. 1, 2017), http://www.cii.org/policies_other_issues#indep_acct_audit_standards.

completely auditing firms located in China.⁴ We believe the PCAOB's inability to inspect those firms has been to the detriment of long-term investors.⁵

More specifically, CII has long believed that for the protection of investors, all firms performing audits of issuers listed on U.S. exchanges should be subject to PCAOB inspections and investigations, without impediments from foreign authorities such as exist in China.⁶ Investors should be able to rely on the financial statements of issuers traded in the United States, regardless of where the issuers' audits take place.⁷ We generally supported the HFCAA because it will finally close the gap by requiring the PCAOB and the U.S. Securities and Exchange Commission (Commission) to take actions consistent with their responsibilities under the federal securities laws to protect investors.⁸

⁴ See, e.g., Soyoung Ho, Trump Administration Seeks to Delist U.S.-Listed Chinese Companies for Blocking Audit Inspections, Thomson Reuters Tax & Acct. (Aug. 10, 2020), <https://tax.thomsonreuters.com/news/trump-administration-seeks-to-delist-u-s-listed-chinese-companies-for-blocking-audit-inspections/> (“the PCAOB has not been able to get Chinese authorities to agree to a joint inspection program despite over 13 years of off-and-on negotiations”).

⁵ See, e.g., Final Rule Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspection of Non-U.S. Firms, PCAOB Rulemaking Docket Matter No. 027, PCAOB Rel. No. 2009-003 at 8-9 (June 25, 2009), https://pcaob-assets.azureedge.net/pcaob-dev/docs/default-source/rulemaking/docket_027/2009-06-25_release_no_2009-003.pdf?sfvrsn=61e7cb9b_0 (“The Board believes that it is not in the interests of investors or the public to exempt non-U.S. firms from the Act's inspection requirement given that the Board has previously determined not to exempt non-U.S. firms from the Act's registration requirements and given that an inspection is the Board's primary tool of oversight.”).

⁶ See, e.g., Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to Office of the Secretary, PCAOB at 6 (Sept. 6, 2018), https://www.cii.org/files/issues_and_advocacy/correspondence/2018/September%206.%202018%20PCAOB%20Strategic%20Plan.pdf (“We are particularly concerned about PCAOB-registered firms located in China for at least four reasons: (1) since 2010 the PCAOB has actively sought without success inspections of China-based audit firms and the mainland affiliates of the Big Four accountancies - Deloitte, KPMG, PricewaterhouseCoopers and EY; (2) many of the China-based audit firms do significant work on audits of major U.S. companies doing business in China; (3) the recent surge in the number of Chinese companies listed on U.S. stock exchanges; and (4) most of the Chinese companies listed on U.S. stock exchanges in recent years have a variable interest entity structure that is highly complex and might include risks that some investors and auditors may not fully understand or appreciate.”); see also CII, Buyer Beware: Chinese Companies and the VIE Structure (Dec. 2017), https://www.cii.org/files/publications/misc/12_07_17%20Chinese%20Companies%20and%20the%20VIE%20Structure.pdf (describing the frequency and risks of Chinese companies with variable interest entity structures).

⁷ See, e.g., Rebekah Goshorn Jurata, Board Member, PCAOB, Statement on the PCAOB's Proposing Release for Rule 6100, Board Determinations Under the Holding Foreign Companies Accountable Act (May 13, 2021), <https://pcaobus.org/news-events/speeches/speech-detail/statement-on-the-pcaob-s-proposing-release-for-rule-6100-board-determinations-under-the-holding-foreign-companies-accountable-act> (“Investors should be able to rely on the financial statements of issuers traded in the United States, regardless of where the issuers' audits take place.”).

⁸ See, e.g., Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors to The Honorable Carolyn B. Maloney, Chair, Subcommittee on Investor Protection, Entrepreneurship, and Capital Markets Committee on Financial Services, United States House of Representatives et al. 6 (June 18, 2019), [https://www.cii.org/files/issues_and_advocacy/correspondence/2019/June%2018%202019%20Letter%20to%20Subcommittee%20on%20Investor%20Protection%20Entrepreneurship%20and%20Capital%20Markets%20\(finalF\).pdf](https://www.cii.org/files/issues_and_advocacy/correspondence/2019/June%2018%202019%20Letter%20to%20Subcommittee%20on%20Investor%20Protection%20Entrepreneurship%20and%20Capital%20Markets%20(finalF).pdf) (“We acknowledge that there are a number of possible alternative actions the SEC, the PCAOB, the stock exchanges, or Congress could potentially take to address, at least in part, the investor protection and general oversight issues that exist for U.S. Chinese listed companies [and] [i]n our view, the provisions of the . . . Act are not an unreasonable response, particularly in light of the apparent increasing size, scope, and significance of those issues.”).

CII generally supports the Proposed Rule. We agree that the Proposed Rule is not expressly required because the HFCAA is largely self-executing.⁹ However, we also agree that the Proposed Rule is appropriate because it can promote transparency and consistency regarding the PCAOB determination of whether it is unable to inspect or investigate completely registered public accounting firms located in foreign jurisdictions because of a position taken by one or more authorities in that jurisdiction.¹⁰ And we offer the following comments in response to select questions identified in the Proposed Rule:

- a. Is it appropriate to limit jurisdiction-wide determinations to registered firms headquartered in the jurisdiction? If not, what should be the scope of jurisdiction-wide determinations under the proposed rule?¹¹

CII generally agrees with the Board that “a jurisdiction-wide approach to its determinations under the HFCAA is consistent with the structure of the statute.”¹² We also agree that “[w]hen the obstacles to completing inspections and investigations are not specific to individual registered firms, but instead reflect threshold or general positions taken by a foreign authority, the Board . . . should be able to address those obstacles on a jurisdiction-wide basis in a consistent manner and in a single determination.”¹³ We also agree that “investors and the public interest would be best served by making a jurisdiction-wide determination under the HFCAA, even if the foreign jurisdiction’s law (or interpretation or application of that law) affects the Board’s ability to inspect or investigate only certain types of audit engagements.”¹⁴

- f. Is this approach to the timing of Board determinations appropriate? Should the Board take a different approach to the timing of its determinations? Should the Board consider changes in facts and circumstances more or less frequently than annually (e.g., semi-annually or biennially)?¹⁵

CII generally believes the approach to the timing of Board determinations is appropriate. We, however, also believe the approach should be sufficiently flexible to ensure that the Board determinations do not conflict with the language and intent of the HFCAA which we believe

⁹ See PCAOB Rule 6100, Board Determinations Under the Holding Foreign Companies Accountable Act, PCAOB Rulemaking Docket Matter No. 048, PCAOB Rel. No. 2021-001 at 17 (“the HFCAA does not expressly require the Board to adopt a rule governing the determinations it makes under the statute”); Holding Foreign Companies Accountable Act, Pub. L. No. 116-222, § 104(i)(3)(A) (Dec. 18, 2020), *available at* <https://www.congress.gov/116/plaws/publ222/PLAW-116publ222.pdf> (“if the Commission determines that a covered issuer has 3 consecutive non-inspection years, the Commission shall prohibit the securities of the covered issuer from being traded”).

¹⁰ See PCAOB Rule 6100, Board Determinations Under the Holding Foreign Companies Accountable Act, PCAOB Rulemaking Docket Matter No. 048, PCAOB Rel. No. 2021-001 at 17 (“Although the HFCAA does not expressly require the Board to adopt a rule governing the determinations it makes under the statute, the Board believes that such a rule will inform investors, registered firms, issuers, audit committees, foreign authorities, and the public at large as to how the Board will perform its functions under the statute [and] . . . a Board rule will promote consistency in the Board’s processes regarding determinations under the HFCAA.”).

¹¹ *Id.* at 23.

¹² *Id.* at 18.

¹³ *Id.*

¹⁴ *Id.* at 21.

¹⁵ *Id.* at 26.

requires the prohibition of company securities from being traded on a U.S. national securities exchange or an ‘over-the-counter’ market by 2024 if the company has had three consecutive non-inspection years.¹⁶

- h. To determine whether the Board can “inspect or investigate completely” under the HFCAA, the proposed rule provides that the Board will look to three factors. Are the three factors identified in paragraph (b) of the proposed rule appropriate, and sufficiently clear? Is there any additional guidance or clarity the Board should provide with respect to those factors? Are there other factors the Board should consider using to determine whether it can inspect or investigate completely?¹⁷

CII generally believes that the Board should consider clarifying the second factor by inserting the word “timely” before the word “access.”¹⁸ In our view, the Board cannot inspect or investigate completely if its access to documents or information is not timely.¹⁹

- p. Is it appropriate to have Board determinations become effective on the date the Board issues its report to the Commission? If not, when should Board determinations take effect?

CII generally believes that it is appropriate to have the Board determinations become effective on the date the Board issues its report to the Commission. See our response to question f.

- q. Should the proposed rule provide registered firms with a mechanism to provide relevant information to, or to seek reconsideration or reevaluation by, the Board with respect to a Board determination? If so, when should such a process be available, what procedures should it entail, and how could it be administered so as not to interfere with the ability of the Board and the Commission to discharge their responsibilities under the HFCAA on a timely basis?

¹⁶ See Richard Vernon Smith & Jinsong Zhang, Orrick, Herrington & Sutcliffe LLP, *The Holding Foreign Companies Accountable Act Is Signed Into Law*, JDSUPRA (Jan. 22, 2021), <https://www.jdsupra.com/legalnews/the-holding-foreign-companies-5211670/> (“If the SEC determines that a public company has three consecutive ‘noninspection years,’ beginning in 2021, the SEC would prohibit the company’s securities from being traded on a U.S. national securities exchange or an ‘over-the-counter’ market subject to SEC regulations.”); Holding Foreign Companies Accountable Act, Pub. L. No. 116-222, § 104(i)(3)(A) (“if the Commission determines that a covered issuer has 3 consecutive non-inspection years, the Commission shall prohibit the securities of the covered issuer from being traded”); *cf.* President’s Working Group on Financial Markets: Report on Protecting United States Investors from Significant Risks from Chinese Companies (July 24, 2020), <https://home.treasury.gov/system/files/136/PWG-Report-on-Protecting-United-States-Investors-from-Significant-Risks-from-Chinese-Companies.pdf> (recommending “the new listing standards could provide for a transition period until January 1, 2022 for currently listed companies from NCJs to come into compliance [and] [t]he new listing standards would apply immediately to new company listings once the necessary rulemakings and/or standard-setting are effective”).

¹⁷ PCAOB Rule 6100, Board Determinations Under the Holding Foreign Companies Accountable Act, PCAOB Rulemaking Docket Matter No. 048, PCAOB Rel. No. 2021-001 at 27-28.

¹⁸ *Id.* at 43.

¹⁹ See, e.g., Corrected Order on the Basis of Offers of Settlement of Certain Respondents Implementing Settlement, Exchange Act Rel. No. 74,217, Accounting and Auditing Enforcement No. 3,627 at 22 (Feb. 6, 2015), <https://www.sec.gov/litigation/admin/2015/34-74217.pdf> (public accounting firms based in the People’s Republic of China agreeing to specific required time periods for production of information to the United States Securities and Exchange Commission).

CII generally believes that the proposed rule should provide a mechanism for the registered firm to provide relevant information. But we think any mechanism should not be permitted to delay the ability of the Board or Commission to discharge their responsibilities under the HFCAA on a timely basis. See our response to question f.

- u. Does the Board’s analysis of the potential economic impacts of the proposed rule adequately address the benefits and costs of the proposed rule?

We agree with the Board that the potential economic impact of the Proposed Rule includes that it would benefit investors because it “would inform investors . . . as to how the Board will perform its functions under the HFCAA [and] [t]he improved transparency and reduced regulatory uncertainty might help market participants make more efficient investment decisions and, hence, enhance capital formation [and] . . . [i]t will also assist the Commission in its consistent implementation of the HFCAA and achieving the statute’s intended objectives.”²⁰ In addition, we note that “achieving the statute’s intended objective” includes, as discussed in our response to question f., the prohibition of company securities from being traded on a U.S. national securities exchange or an ‘over-the-counter’ market by 2024 if the company has had three consecutive non-inspection years.

- v. Is the Board’s existing exemption authority adequate, or should the proposed rule include a process that would enable the Board to grant exceptions from a jurisdiction-wide determination? If the latter, what factors should the Board take into account when considering exceptions, and how could an exception process be structured and implemented to address the concerns identified above?

CII generally believes the Board’s existing exemption authority is adequate. We agree with the Board that “[a]llowing firms to seek exceptions could effectively transform the Board’s jurisdiction-wide approach to a firm-by-firm approach that consumes substantial Board resources and fails to protect investors.”²¹

Thank you for consideration of our views. If we can answer any questions or provide additional information, please do not hesitate to contact me.

Sincerely,



Jeffrey P. Mahoney
General Counsel

²⁰ PCAOB Rule 6100, Board Determinations Under the Holding Foreign Companies Accountable Act, PCAOB Rulemaking Docket Matter No. 048, PCAOB Rel. No. 2021-001 at 37.

²¹ *Id.* at 41.