



Via Email: comments@pcaobus.org

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

July 12, 2021

Re: PCAOB Rulemaking Docket Matter No. 048

Ladies and Gentlemen:

We appreciate the opportunity to comment on the proposed new PCAOB Rule 6100 “*Board Determinations Under the Holding Foreign Companies Accountable Act*”. The purpose of this new rule is to establish a framework for the PCAOB to make its determinations under the SEC’s HFCAA. The proposed rule would establish the manner of the PCAOB’s (“Board’s”) determinations; the factors the Board will evaluate and the documents and information it will consider when assessing whether a determination is warranted; the form, public availability, effective date, and duration of such determinations; and the process by which the Board can modify or vacate its determinations.

In this letter we provide responses to several of the PCAOBs specific questions. Further, we draw the Board’s attention to our related comment letter in response to the SEC’s request for comment re. “*File Number S7-03-21, Holding Foreign Companies Accountable Act Disclosure, Interim final rule.*” which also provides pertinent information to these issues.

Below we reproduce specific questions from the PCAOB request, Release No. 2021-001, in bold italics, followed by our responses. In our responses, we aim to provide details that emerged during our own analysis of data from registered audit firms (and their clients) that could be subject to the HFCAA requirements.

A.1 Determinations as to Registered Firms Headquartered in a Particular Foreign Jurisdiction

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

We believe that jurisdiction-wide determination, based on the location of signing audit firms’ headquarters is an appropriate starting point. However, the Board might need to provide more guidance in cases where an audit firm, with headquarters in a cooperative jurisdiction, signs the audit report of a client located in a non-cooperative jurisdiction, including cases where local

personal at the non-cooperative jurisdiction is substantially involved in audit tasks. For instance, an audit firm with headquarters in the U.S. signs an audit report of a client located in Mainland China and uses local resources from a Chinese affiliate (e.g., the Shanghai office).

Our review of issuers' risk factor disclosures in annual filings raises questions about the jurisdiction-wide determination approach. For example, Alibaba Group's [CIK: 0001577552] Form 20-F for fiscal year ended March 31, 2019 states:

In addition, auditors based outside of China are subject to similar restrictions under PRC law and CSRC directives in respect of audit work that is carried out in China that supports the audit opinions issued on financial statements of entities with substantial China operations. (*see Item 3*)

Therefore, if Alibaba retains KPMG U.S., it is unclear if the auditor could be legally able to allow the PCAOB to inspect the audit, if selected. This could result in U.S. audit firms (or other audit firms in cooperative jurisdictions) becoming non-compliant, so the jurisdiction-wide determination needs additional consideration and guidance.

Question b) Is it appropriate for the Board to look, in the first instance, at registered firms' required filings with the Board to determine where a firm is headquartered? If not, what information should the Board consider to determine where a firm is headquartered?

Registered firms' required filings (PCAOB Forms AP and 2/A) typically convey the most detailed, precise, and up to date information regarding the jurisdiction where signing audit firms' headquarters are located. However, we highlight two issues that could arise if the Board uses these filings as the sole basis for identifying the location of firm' headquarters.

- 1) We have identified several cases of omission or delay in the filing of Form AP.¹
- 2) We believe that an average investor, without access to database providers such as Audit Analytics, is likely to infer an auditor's jurisdiction based on the location printed under the signature of the audit report, filed along with issuers' 20-Fs and 10-Ks. While the auditor's signature in Form 20-F/10-K is identified with the signing branch's office city and country, the Form AP's information is directly provided by the audit firm.² However, there are cases where these locations differ (e.g., when audit firms in one country have branch offices in

¹ See for example Shanghai Perfect C.P.A Partnership (ID 3027), headquartered in China, has never appeared in the Form AP database (as of 2021/06/24), however lists MERCURY FINTECH HOLDING INC. [CIK: 0001527762] on the Item 4.1 of its Form 2 filed on 2021/5/12.

² See for example the PCAOB's inspection report of MBP dated on Jan. 16th, 2020. The Form 2 of MBP shows the headquarter of the auditor is in New York, US., however the firm has branch offices in Beijing, Hangzhou, Shenzhen, Shanghai, Guangzhou, and Tianjin in China. It is these branches that appear on the MBP signatures on audit reports (e.g. SINOVAC BIOTECH LTD.'s 20-F for Dec. 31st, 2019 states "Marcum Bernstein & Pinchuck LLP, we have served as the Company's auditor since 2019, Beijing China, April 30, 2020".)



another country that do not operate as a separate legal entity). Our review of annual filings for fiscal years 2019 and 2020 revealed that 12 issuers had at least one of their audit reports signed by the auditor Marcum Bernstein & Pinchuk LLP [MBP, ID 5395].) MBP's signatures reveal the jurisdiction of MBP as China, but Form AP and Form 2 reveal the jurisdiction of MBP as the United States.³

We recommend the Board to: (1) ensure that information on Form 2 (e.g., audit firms' headquarters, and ITEM 4 "*Audit Reports Issued by the Firm for Issuers*") is completely incorporated into Form AP in a timely fashion. This measure would prevent situations where audit reports are already signed, and Form 2 is updated but not reflected in Form AP (see footnote #1); and, (2) provide additional guidance for investors to avoid confusion about a given audit firm's headquarters, for example, the Board could explicitly communicate to investors that the location disclosed under the auditor's signature may not be the location of the auditor's headquarters, and instead direct them to the "Auditor Search" function on PCAOB's official website.⁴

Moreover, we refer to our earlier comment letter to the SEC (S7-03-21), where we recommend the introduction of a structured XBRL tagging requirement pertaining to the auditor's name, branch office, and jurisdiction. This approach could alleviate several concerns and sources of discrepancies that one may observe across public data sources. We also recommended the SEC to include specific guidance to tag the auditor's name and location as listed on Form AP.

A2. Determinations as to a Particular Registered Firm in a Foreign Jurisdiction

Question d) Is it appropriate for the Board to look, in the first instance, at a registered firm's required filings with the Board to determine where the firm's offices are located? If not, what information should the Board consider to determine where a firm's offices are located?

We agree that it is appropriate to look at the registered firms' PCAOB filings to determine where their offices are located, but we recommend the Board to consider additional sources to validate this information, such as 20-Fs/10-Ks.

Question e) As noted in footnote 83, although the HFCAA refers to a "branch or office" of a registered firm, subparagraph (a)(2) of the proposed rule refers only to an "office". Is it appropriate to refer only to an "office" in subparagraph (a)(2)? If not, what distinction should the Board recognize between a "branch" and an "office" in this context?

Instead of "*branch or office*" we recommend that the Board refers to "*Issuing City*". Given that the Form AP database includes a field called "*Issuing City*" to refer to the branch or office that

³ This explicitly indicates a US auditor taking responsibility for the audit of Chinese companies. E.g., Deloitte Touché Tohmatsu's Form AP and Form 2 indicates jurisdiction in China, not the US.

⁴Auditor Search webpage: <https://pcaobus.org/resources/auditorsearch>

issued or signed the specific audit report. Employing this common terminology would allow the Board to avoid confusion between “branch” and “office” and ensure consistency.

A3. Timing of Board Determinations

Question 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)?

We believe that it is reasonable to rely on annual assessments, given the timing of audit reports. However, we raise several questions relating to events that may trigger jurisdictional changes that the Board should consider:

- 1) Are registered audit firms allowed to simply change their headquarters? If so, are there limitations on the frequency of these changes?
- 2) Are registered audit firms required to report to the Board any changes in their branch offices on a timely basis (e.g., additions or closures)?
- 3) Are audit firms required to report to the Board any mergers/acquisitions that may impact their office locations on a timely basis?

While we generally agree that the Board stipulate an annual approach, it seems prudent to require timely updates on the special report (Form 3) for any ongoing event(s) that could affect its jurisdiction determination.

D.2. Publication of Board Determinations

Question k) Are there any considerations the Board should take into account when determining where on the Board’s website to post copies of the Board’s reports to the Commission?

We recommend the Board to post copies of these reports on the PCAOB’s website, specifically in the section “*Audit Reports Issued by PCAOB-Registered Firms in Jurisdictions where Authorities Deny Access to Conduct Inspections*”.⁵

In addition, it may be useful to post both: (1) the report to the Commission, and (2) guidelines to investors, as per our recommendation in our response to *Question b)* above, together.

⁵ <https://pcaobus.org/oversight/international/denied-access-to-inspections>



Question l) Apart from posting the Board’s reports to the Commission on the Board’s website, should the Board also indicate on a registered firm’s profile in the Board’s Registration, Annual, and Special Reporting System that the firm is subject to a Board determination under the HFCAA?

We believe the registered firm’s profile in the PCAOB’s website “*Auditor Search*” page is likely the most reliable (and direct) source for an average investor to look up detailed information for audit firms outside of issuers’ annual filings. Therefore, an indication in this system that the firm is subject to a Board determination, under the HFCAA, will likely be the most effective way to inform the public and can help reduce investors’ information processing costs.

Question n) Besides posting a copy of the Board’s report to the Commission on the Board’s website, should the Board notify stakeholders about Board determinations under the HFCAA by other means? If so, which stakeholders should receive such notice, and when and how should it be provided? Specifically, should registered firms that are subject to a Board determination receive notice of such determination, and if so, when and how should it be provided?

We believe that registered firms that are subject to a Board determination should receive notice of such determination at the same time as the Board submits the report to the Commission. However, this action depends on whether the Board will allow registered firms to appeal cases. If appeals are allowed, then the Board may want to consider granting a grace period between notifying the registered firms, and the submission to the Commission.

Question o) Should the Board continue its practice of publishing the Denied Access List on its website? If so, should any changes be made to the Denied Access List to avoid potential confusion with the Commission’s identification of covered issuers under the HFCAA or with the disclosures provided by covered issuers under the HFCAA and the Commission’s rules.

The current *Denied Access List* seems to be solely based on Form AP. However, as mentioned previously, there can be omission/delay cases in Form AP filings. The Board might want to assess the cost of frequently updating this list and litigation risks related to untimely updates.

In addition, if the Commission adopted the tagging suggestion (See our response to *Question b*) above) then an average investor can identify the jurisdiction of an audit firm using the tag, which would be consistent with the Board’s determination report. Therefore, there may be no longer be a need for the *Denied Access List*.

E. Effective Date, Duration, Modification and Vacatur of Board Determinations



Question 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?

We believe it reasonable for the Board's determinations to be effective on the date the Board issues its report to the Commission. However, as mentioned above, a grace period might need to be granted if the Board would like to open for appeals from registered audit firms.

Question 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 Commission to discharge their responsibilities under the HFCAA on a timely basis?

In providing comment to this question, we refer to our comments in earlier sections. In particular:

- a) In our responses to *Questions a) and b)*, regarding the timing of Board determinations, we recommend the Board to consider requiring timely updates on the special report (Form 3) from audit firms for any ongoing event(s) that could affect its jurisdiction determination. Therefore, the registered firms could file appeal cases/seek reconsideration/revaluation by the Board with respect to a Board determination at the same time. Effectively, this means that each year the Board reviews the determination status for audit firms based on the jurisdiction of their headquarters. For example, if a firm's status changes in a year, it can (and should) apply for reconsideration immediately if conditions triggering changes in its jurisdiction take place.
- b) In our response to *Question n)* above, we recommend the Board to consider granting a grace period between notifying the registered firms and submission to the Commission if they decided to provide registered firms with a mechanism to seek reconsideration/reassessment. For example, if the submission to Commission is Dec. 31st every year, the Board could publish a preliminary determination list (based on the most updated headquarter information on file) on its official website around Sept 30th, allowing a 90-day grace period for registered firms to explicitly seek for reassessment/reconsideration with reliable supporting documents.

Question r) Is subparagraph (h)(1)'s annual consideration of changed facts and circumstances clear and appropriate? Should the Board consider changes in facts and circumstances more or less frequently than annually (e.g., semi-annually or biennially)? Should the Board publicly report the outcome of this process whenever the Board decides that reassessment of a prior determination is not warranted or that a prior determination should not be modified or vacated?

If the Board decides on an annual evaluation, but requires timely reporting of special events, then the frequency seems appropriate.



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Further, we believe that the Board should publicly report the outcome of this process whenever it decides that reassessment of a prior determination is warranted, should not be modified, or is vacated. This could provide audit firms and issuers with more detailed guidance and transparent information on when one firm is deemed or not deemed to be “black” so that they could make informed decisions.

We hope you find our comments helpful. Please feel free to contact Professor Miguel Minutti-Meza (mminutti@bus.miami.edu) if you have any questions about this letter or our associated analysis.

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