

File No. PCAOB-2009-01  
Consists of 183 Pages

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

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Form 19b-4

Proposed Rule Change

By

Public Company Accounting Oversight Board

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

1. Text of the Proposed Rule

(a) Pursuant to the provisions of Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule (PCAOB Rule 4003(g)) concerning inspection frequency requirements applicable to certain inspections the Board is required to conduct. The proposed rule is attached as Exhibit A.

(b) The proposed rule will have a direct effect on existing PCAOB Rule 4003 by amending it to add a new provision. PCAOB Rule 4003 has been addressed in the following PCAOB filings in accordance with Rule 19b-4 under the Securities Exchange Act of 1934: PCAOB 2003-08, filed October 7, 2003; PCAOB-2006-03, filed December 20, 2006; PCAOB-2006-03 Amendment No. 1, filed May 31, 2007; PCAOB-2007-04, filed October 22, 2007; PCAOB-2008-04, filed June 17, 2008; and PCAOB-2008-06, filed December 9, 2008.

2. Procedures of the Board

(a) The Board approved Rule 4003(g) at a meeting on June 25, 2009. No other action by the Board is necessary for the filing of the proposed rule change.

(b) Questions regarding this rule filing may be directed to Michael Stevenson, Deputy General Counsel (202-207-9054; [stevensonm@pcaobus.org](mailto:stevensonm@pcaobus.org)).

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

(a) Purpose

The Act directs the Board to conduct a continuing program of inspections to assess registered public accounting firms' compliance with certain requirements. The

Act prescribes inspection frequency requirements but also authorizes the Board to adjust the frequency requirement by rule if the Board finds that such an adjustment is consistent with the purposes of the Act, the public interest, and the protection of investors. Inspection frequency requirements adopted by the Board are set out in PCAOB Rule 4003. The purpose of proposed Rule 4003(g) is to amend the inspection frequency requirement as it applies to certain inspections that the Board would, in the absence of Rule 4003(g), be required to conduct no later than 2009.

(b) Statutory Basis

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

4. Board's Statement on Burden on Competition

The Board does not believe that the proposed rule will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule imposes no burden beyond the burdens clearly imposed and contemplated by the Act.

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

The Board released the rule amendment for public comment on December 4, 2008. See Exhibit 2(a)(A). The Board received twenty-four written comment letters. See Exhibits 2(a)(B) and 2(a)(C).

The Board has carefully considered all comments it has received. The Board's responses to the comments it received are summarized in Exhibit 3 to this filing.

6. Extension of Time Period for Commission Action

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

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) of the Securities Exchange Act

Not applicable.

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

Not applicable.

9. Exhibits

Exhibit A – Text of Proposed Rule

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

Exhibit 2(a)(A) – PCAOB Release No. 2008-007 (December 4, 2008)

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

Exhibit 2(a)(C) – Comment Letters Received on Proposed Rules in PCAOB Release No. 2008-007

Exhibit 3 – PCAOB Release No. 2009-003 (June 25, 2009)

10. Signatures

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

Public Company Accounting Oversight Board

By:

  
J. Gordon Seymour  
General Counsel  
and Secretary

July 2, 2009

**Exhibit A – Text of Proposed Rule**

The Board is amending Section 4 of its rules by adding a new paragraph (g) to Rule 4003. The relevant portion of the rule, as amended, is set out below. Language added by this amendment is underlined. Other text that remains unchanged is indicated by " \* \* \* " in the text below.

RULES OF THE BOARD

\* \* \*

SECTION 4. INSPECTIONS

\* \* \*

Rule 4003. Frequency of Inspections

\* \* \*

(g) With respect to any foreign registered public accounting firm concerning which the preceding provisions of this Rule, other than paragraphs (a) and (f), would set a 2009 deadline for the first Board inspection and that is headquartered in a country in which no foreign registered public accounting firm that the Board inspected before 2009 is headquartered, such deadline is extended to 2012, provided, however, that from among the group of all such firms, the Board shall conduct some first inspections in each of the years from 2009 to 2012, scheduled according to such criteria as the Board shall publicly announce.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- ; File No. PCAOB-2009-01)

[Date]

Public Company Accounting Oversight Board; Notice of Filing of Proposed Amendment to Board Rules Relating to Inspections

Pursuant to Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), notice is hereby given that on July 2, 2009, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "SEC" or "Commission") the proposed rule changes described in Items I, II, and III below, which items have been prepared by the Board. The Commission is publishing this notice to solicit comments on the proposed rule from interested persons.

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

On June 25, 2009, the Board adopted an amendment to its rule relating to the frequency of inspections. The proposed amendment adds a new paragraph (g) to existing Rule 4003. The text of the proposed amendment is set out below. Language added by the amendment is underlined

Rule 4003. Frequency of Inspections

\* \* \*

(g) With respect to any foreign registered public accounting firm concerning which the preceding provisions of this Rule, other than paragraphs (a) and (f), would set a 2009 deadline for the first Board inspection and that is headquartered in a country in which no foreign registered public accounting firm that the Board inspected before 2009 is headquartered, such deadline is extended to 2012, provided, however, that from among the group of all such firms, the Board shall conduct some first inspections in each of the years from 2009 to 2012, scheduled according to such criteria as the Board shall publicly announce.

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

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

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

(a) Purpose

The Sarbanes-Oxley Act of 2002 directs the Board to conduct a continuing program of inspections to assess registered public accounting firms' compliance with certain requirements.<sup>1/</sup> The Act prescribes inspection frequency requirements but also authorizes the Board to adjust the frequency requirements by rule if the Board finds that an adjustment is consistent with the purposes of the Act, the public interest, and the protection of investors.<sup>2/</sup> Inspection frequency requirements adopted by the Board are set out in PCAOB Rule 4003, "Frequency of Inspections."

The Board began a regular cycle of inspections of U.S. firms in 2004 and has conducted 982 such inspections, including repeat inspections of several firms. Inspections of non-U.S. firms began in 2005, and the Board has inspected 140 non-U.S.

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<sup>1/</sup> See Section 104(a) of the Act.

<sup>2/</sup> See Section 104(b) of the Act.

firms. Those firms are located in 26 jurisdictions.<sup>3/</sup> There are, however, currently 68 non-U.S. firms that, by virtue of when they first issued audit reports after registering with the PCAOB, the Board is required to inspect for the first time by the end of 2009.<sup>4/</sup> For the reasons described below, the Board has adopted Rule 4003(g), which would affect the timing of a subset of those 68 inspections. Specifically, Rule 4003(g) will give the Board the ability to postpone, for up to three years, first inspections that the Board is currently required to conduct before the end of 2009 in jurisdictions where the Board conducted no inspections before 2009. The amendment does not affect inspection frequency requirements concerning any other first inspections, or concerning any second or later inspections, of firms that issue audit reports for issuers.<sup>5/</sup>

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<sup>3/</sup> The Board has inspected non-U.S. firms located in Argentina, Australia, Bermuda, Brazil, Canada, Chile, Colombia, Greece, Hong Kong, India, Indonesia, Ireland, Israel, Japan, Kazakhstan, Mexico, New Zealand, Norway, Panama, Peru, the Russian Federation, Singapore, South Africa, South Korea, Chinese-Taipei, and the United Kingdom.

<sup>4/</sup> This discussion does not include, or apply to, 21 non-U.S. firms whose first inspection deadline has been moved from 2008 to 2009 under Rule 4003(f).

<sup>5/</sup> Existing Rule 4003 effectively sets deadlines for the Board's inspections not only of firms that issue audit reports, but also of firms that play a substantial role in the preparation or furnishing of an audit report (as defined in PCAOB Rule 1001(p)(ii)). The Board has previously submitted for Commission approval amendments to Rules 4003(b) and 4003(d) that would eliminate from the Rule any frequency requirement or deadline for the Board to inspect a firm that plays a substantial role but does not issue an audit report. Unless and until the Commission approves such a rule change, however, the extension in proposed rule 4003(g) would (if approved by the Commission) apply to required 2009 PCAOB inspections of non-U.S. firms (in jurisdictions encompassed by the rule's terms) that have played a substantial role as well as to required 2009 inspections of non-U.S. firms that have issued audit reports.

The PCAOB has recognized since the outset of its inspection program that inspections of non-U.S. firms pose special issues.<sup>6/</sup> In its oversight of non-U.S. firms, the Board seeks, to the extent reasonably possible, to coordinate and cooperate with local authorities. Since 2003, when the PCAOB began operations, a number of jurisdictions have also developed their own auditor oversight authorities with inspection responsibilities or enhanced existing oversight systems.<sup>7/</sup> The Board believes that it is in the interests of the public and investors for the Board to develop efficient and effective cooperative arrangements with its non-U.S. counterparts.<sup>8/</sup> In jurisdictions that have their own inspection programs, this may include conducting joint inspections of firms that are subject to both regulators' authority.

Indeed, the Board has a specific framework for working cooperatively with its non-U.S. counterparts to conduct joint inspections and, to the extent deemed appropriate by the Board in any particular case, relying on inspection work performed by

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<sup>6/</sup> See Briefing Paper, Oversight of Non-U.S. Public Accounting Firms (October 28, 2003) (hereinafter "Oversight of Non-U.S. Firms"); Final Rules Relating to the Oversight of Non-U.S. Public Accounting Firms, PCAOB Release No. 2004-005 (June 9, 2004).

<sup>7/</sup> In 2006, for instance, the European Union enacted a directive requiring the creation of an effective system of public oversight for statutory auditors and audit firms within each Member State. See The Directive 2006/43/EC of the European Parliament and the Council (May 17, 2006) (the "Eighth Directive"). In addition, among others, Canada created the Canadian Public Accountability Board, and in Australia, the responsibilities of the Australian Securities and Investments Commission were expanded to include auditor oversight. In Asia, Japan established the Certified Public Accountants and Auditing Oversight Board, South Korea delegated responsibility for auditor oversight to its Financial Supervisory Service, and Singapore established the Accounting and Corporate Regulatory Authority.

<sup>8/</sup> See Oversight of Non-U.S. Firms at 2-3.

that counterpart.<sup>9/</sup> PCAOB Rule 4011 permits non-U.S. firms that are subject to Board inspection to formally request that the Board, in conducting its inspection, rely on a non-U.S. inspection to the extent deemed appropriate by the Board. If a Rule 4011 request is made, Rule 4012 provides that the Board will, at an appropriate time before each inspection of the firm, determine the degree, if any, to which the Board may rely on the non-U.S. inspection. Rule 4012 describes aspects of the non-U.S. system that the Board will evaluate in making that determination. Even where the Board does not work with a local regulator to conduct joint inspections, the Board communicates with its counterpart or other local authorities (such as securities regulators or other government agencies and ministries) regarding its inspections to be conducted in the jurisdiction.

In some jurisdictions, the PCAOB's ability to conduct inspections, either by itself or jointly with a local regulator, is complicated by the concerns of local authorities about potential legal obstacles and sovereignty issues. The Board seeks to work with the home-country authorities to try to resolve these and any other concerns.<sup>10/</sup>

The effort involved in attempting to resolve potential conflicts of law, or to evaluate a non-U.S. system in response to a Rule 4011 request, can be substantial. The effort typically involves negotiating the principles of an arrangement for cooperation consistent with the inspection obligations that the Act imposes on the Board. It also involves the Board gaining a detailed understanding of the other jurisdiction's auditor

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<sup>9/</sup> See PCAOB Rules 4011 and 4012; see also Oversight of Non-U.S. Firms at 2-3.

<sup>10/</sup> See Oversight of Non-U.S. Firms at 3.

oversight system in order for the Board to determine the degree of reliance it is willing to place on inspection work performed under that system in a particular inspection year.

Additional effort is involved in coordinating the scheduling of specific inspections. Where possible, the Board seeks to conduct inspections jointly with local authorities both to take advantage of potential efficiencies and to avoid imposing unnecessary regulatory burdens on firms. Like the PCAOB, several of these other authorities proceed according to inspection frequency requirements. While some of the Board's counterparts are established and have inspection programs, many have only recently begun inspections or are still building up their inspections resources. As a result, synchronizing the inspections schedules of these authorities and the PCAOB's requirements is sometimes difficult.

Notwithstanding these challenges, the Board has so far conducted 140 non-U.S. inspections. Moreover, 61 of those inspections, in six jurisdictions, have been conducted jointly with other auditor oversight authorities, while inspections in 20 jurisdictions have been conducted solely by the PCAOB.<sup>11/</sup>

As noted above, under existing Rule 4003, there are 68 non-U.S. firms that, by virtue of when they first issued audit reports after registering with the PCAOB, the Board is required to inspect for the first time by the end of 2009. Those firms are located in 36 jurisdictions, including several jurisdictions in which the Board has already conducted first inspections of other firms. Of those firms, 49 are located in 24 jurisdictions where the Board has not conducted any inspections to date. Most of those 24 jurisdictions

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<sup>11/</sup> Joint inspections have been conducted in Australia, Canada, South Korea, Norway, Singapore and the United Kingdom.

have or soon will have a local auditor oversight authority with which the Board would seek to work toward cooperative arrangements before conducting inspections.

Because of the steps involved in concluding such arrangements and to evaluate the local system, the Board has concerns about proceeding as if that work can be completed for all of the jurisdictions in which the PCAOB has not previously conducted inspections in time to conduct the required inspections by the end of 2009.

Accordingly, the Board is adopting a new paragraph (g) to Rule 4003 to allow the Board to postpone, for up to three years, the first inspection of any non-U.S. firm that the Board is currently required to conduct by the end of 2009 and that is in a jurisdiction where the Board has not conducted an inspection before 2009.

In determining the schedule for completion of the inspections subject to new paragraph (g), the Board will implement its proposal to sequence these 49 inspections such that certain minimum thresholds will be satisfied in each of the years from 2009 to 2012. The minimum thresholds relate to U.S. market capitalization of firms' issuer audit clients. The Board will begin by ranking the 49 firms according to the total U.S. market capitalization of a firm's foreign private issuer audit clients.<sup>12/</sup> Working from the top of the list (highest U.S. market capitalization total) down, the 49 firms will be distributed over 2009 to 2012 such that, at a minimum, the following criteria are satisfied:

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<sup>12/</sup> For purposes of the ranking described here, the Board will use the average monthly market capitalization on which each issuer's share of the Board's 2008 accounting support fee was based. Thus, the market capitalization figure used for the ranking does not include the value of any referred work performed by the firm.

- by the end of 2009, the Board will inspect firms whose combined issuer audit clients' U.S. market capitalization constitutes at least 35 percent of the aggregate U.S. market capitalization of the audit clients of all 49 firms;
- by the end of 2010, the Board will inspect firms whose combined issuer audit clients' U.S. market capitalization constitutes at least 90 percent of that aggregate;
- by the end of 2011, the Board will inspect firms whose combined issuer audit clients' U.S. market capitalization constitutes at least 99.9 percent of that aggregate; and
- the Board will inspect the remaining firms in 2012.<sup>13/</sup>

In addition to meeting those market capitalization thresholds, the Board also will satisfy certain criteria concerning the number of those 49 firms that will be inspected in each year. Specifically, the Board will conduct at least four of the 49 inspections in 2009, at least 11 more in 2010, and at least 14 more in 2011.<sup>14/</sup>

It is important to note that the distribution described above will not operate to prevent an inspection from occurring earlier than called for by the schedule. Any

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<sup>13/</sup> Under existing provisions of Rule 4003 that are not affected by this amendment, 2012 would also be the deadline for the Board to conduct the second inspection of those of the 49 firms whose first inspection occurs in 2009.

<sup>14/</sup> The issuer audit client U.S. market capitalization currently associated with a significant number of the 49 firms is relatively low, and even zero in a number of cases where firms appear to have stopped issuing audit reports for issuers. As a result, approximately 92% of the relevant issuer market capitalization is associated with 15 of the 49 firms.

inspection may be moved to an earlier year for a variety of reasons, such as the presence of risk factors (including risk factors relating to referred work<sup>15/</sup> that the firm performs on audits for which it is not the principal auditor), synchronization of schedules with a local regulator for purposes of a joint inspection, or simply the opportunity and the availability of resources to do an inspection earlier (including availability of inspectors with specialized industry knowledge and relevant language skills). In addition, the Board will at least annually review updated market capitalization data and consider whether there have been any changes that warrant moving a particular inspection forward to an earlier year.

Conversely, the Board does not intend to make changes that would move an inspection of one of these 49 firms to a later year than in the initial distribution except as the result of a development relating to the market capitalization of the firm's issuer clients. Specifically, if a firm's issuer audit client market capitalization drops significantly and the firm performs no significant amount of referred work on audits, its inspection might be delayed to a later year. In any event, the Board will not, for any reason, move one of these 49 inspections to a later year than in the initial distribution without publicly describing the change and the reason for it.

In the Board's view, this adjustment to the inspection frequency requirement is consistent with the purposes of the Act, the public interest, and the protection of investors. The Board believes that its approach to implementing Rules 4011 and 4012,

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<sup>15/</sup> Because the PCAOB is still in the process of gathering information about each firm's referred work, the 2009 inspections will not use referred work as a risk factor for purposes of scheduling.

developing cooperative arrangements, and conducting joint inspections with foreign regulators is enhancing the Board's efforts to carry out its inspection responsibilities. There is long-term value in accepting a limited delay in inspections to continue working toward cooperative arrangements where it appears reasonably possible to reach them. The Board also believes that the additional time to conduct certain inspections will have the added benefit of giving the Board more time to continue to enhance its inspection program, particularly in the areas of risk assessment and pre-inspection planning, and the Board intends to do so.

The Board recognizes that some non-U.S. firms may be reluctant to comply with PCAOB inspection demands because of a concern that doing so might violate local law or the sovereignty of their home country. The Board believes that the purposes of the Act, the public interest, and the protection of investors are better served, up to a point, by delaying some of the first inspections to work toward a cooperative resolution than by precipitating legal disputes involving conflicts between U.S. and non-U.S. law that could arise if the Board sought to enforce compliance with its preferred schedule without regard for the concerns of non-U.S. authorities.

The Board does not intend, however, to make any further adjustments to the inspection frequency requirements applicable to firms whose first inspection was due no later than 2009. While the Board will continue to work toward cooperation and coordination with authorities in the relevant jurisdictions, the Board will make inspection demands on the firms early enough in the year in which they are scheduled for

inspection according to the above described sequencing to allow the Board to conduct the inspections during that year.<sup>16/</sup>

(b) Statutory Basis

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

B. Board's Statement on Burden on Competition

The Board does not believe that the proposed rule will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule imposes no burden beyond the burdens clearly imposed and contemplated by the Act.

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

The Board released the proposed rule amendment for public comment in Release No. 2008-007 (December 4, 2008). A copy of Release No. 2008-007 and the comment letters received in response to the PCAOB's request for comment are available on the PCAOB's Web site at [www.pcaobus.org/Rules/Docket\\_027](http://www.pcaobus.org/Rules/Docket_027). The Board

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<sup>16/</sup> Apart from the proposed rule amendment, the Board has implemented certain practices to provide additional transparency with regard to the Board's international inspections program. These practices include (1) making a public announcement, near the beginning of each year until 2012, identifying all non-U.S. jurisdictions in which there are firms that the Board will inspect that year, (2) maintaining a public list of all registered firms that have not yet had their first Board inspection even though more than four years have passed since the end of the calendar year in which they first issued an audit report while registered with the Board, and (3) making biannual public announcements of the Board's progress toward meeting the thresholds described above with respect to the number of firms to be inspected and the aggregate market capitalization of firm clients. The Board also maintains on its Web site a list of all jurisdictions in which there are registered firms that the Board has inspected. Additional details concerning these practices are provided in PCAOB Release No. 2009-003, available on the Board's Web site at [www.pcaobus.org/Rules/Docket\\_027](http://www.pcaobus.org/Rules/Docket_027).

received twenty-four written comment letters. The Board has carefully considered the comment letters, as discussed below.

Several commenters suggested that the Board exercise its authority under Section 106 of the Act to exempt firms that cannot cooperate with PCAOB inspections due to legal conflicts or sovereignty-based opposition from their local governments. 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.<sup>17/</sup>

The Board also received several comment letters addressing the length of the proposed extension for certain firms with 2009 deadlines. Some comment letters expressed concern about the inspection delay of up to three years but ultimately expressed qualified support for the Board's decision. These comments urged the Board to permit no further delays and to proceed as described above by sequencing the inspection of firms subject to the extension based on certain thresholds relating to the U.S. market capitalization of firms' issuer audit clients. Some comments also suggested that the Board should utilize the additional time provided by the proposed extension to enhance its international inspections program, particularly in the areas of risk assessment and pre-inspection planning.

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<sup>17/</sup> When it first became operational, the Board considered whether to exempt non-U.S. firms from registration with the Board. The Board determined that exempting non-U.S. firms would not protect the interests of investors or further the public interest given that registration is the predicate to all of the Board's other oversight programs. See Registration System for Public Accounting Firms, PCAOB Release No. 2003-007 (May 6, 2003) at 13.

Other comment letters supported the Board's decision to extend the inspection deadlines, but some qualified their support by noting that three years may not be enough time to overcome the legal conflicts and sovereignty concerns in all relevant jurisdictions. Several comments expressed support for the Board's plan to sequence the deferred inspections in time based on the U.S. market capitalization of the firms' clients, but some also noted that this plan did not adequately take into account the varying degree of legal conflicts present in the different jurisdictions and might have the effect of requiring early on during the three year period the inspection of firms in jurisdictions with legal obstacles that cannot be overcome quickly.

As explained above, the Board believes that an extension of up to three years for the relevant firms is the appropriate course. Distributing the affected firms across three years strikes the proper balance between avoiding unnecessary delays in the inspection of registered firms and allowing reasonable time for the Board to continue its efforts to reach cooperative arrangements with the relevant home-country regulators. The Board believes that any longer or further extension would not be in the interests of investors or the public.

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

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

(A) by order approve such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule is consistent with the requirements of Title I of the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule that are filed with the Commission, and all written communications relating to the proposed rule between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the PCAOB. All submissions should refer to File No. PCAOB-2009-01 and should be submitted within [ ] days.

By the Commission.

Secretary





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December 4, 2008  
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## RELEASE

Board Contacts: Rhonda Schnare, Director of International Affairs (202-207-9167; schnarer@pcaobus.org).

### Overview

In this release, the Board is addressing and seeking public comment on a group of interconnected issues that relate to the Board's responsibility to conduct inspections of registered firms, including registered non-U.S. firms, and the corresponding obligation of firms to cooperate with Board inspections. Part I of the release deals with amendments to the Board's rule that implements the provisions of the Sarbanes-Oxley Act of 2002 ("the Act") governing the minimum frequency with which the Board must conduct inspections. The Board is adopting a final rule amending the inspection frequency requirement as it applies to the first inspection of certain non-U.S. firms that would otherwise be required before the end of 2008. The Board is also seeking comment on a proposed rule that would amend the inspection frequency requirement as it applies to a specific group of other non-U.S. first inspections that are currently required to be conducted no later than 2009.

Part II of the release discusses registered firms' obligations to cooperate with Board inspections. The Board invites comment on that discussion, which includes a description of possible Board action in the event non-U.S. firms decline to provide information requested by the Board because of a concern that providing the information may violate their local law.

### I. Rule Amendments Concerning the Timing of Certain Inspections

#### A. Background

Under the Act and PCAOB Rules, it is unlawful for any public accounting firm to prepare or issue an audit report with respect to any issuer or play a substantial role in the preparation or furnishing of any such audit report without being registered with the PCAOB.<sup>1/</sup> For non-U.S. firms, this registration requirement took effect on July 19, 2004.

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<sup>1/</sup> See Sections 102(a) and 106 of the Act and PCAOB Rule 2100. For these purposes, the term "issuer" is defined by Section 2(a)(7) of the Act and generally encompasses entities that have issued securities that are registered under Section 12 of the Securities Exchange Act of 1934, or that otherwise have certain reporting obligations to the Securities and Exchange Commission ("Commission"), or that have filed registration statements with the Commission that have not yet become effective.



## RELEASE

The Act directs the Board to conduct a continuing program of inspections to assess registered public accounting firms' compliance with certain requirements.<sup>2/</sup> With respect to each registered firm that regularly provides audit reports for 100 or fewer issuers, the Act requires the Board to conduct an inspection at least once every three years.<sup>3/</sup> The Act authorizes the Board to adjust that inspection frequency requirement by rule if the Board finds that a different inspection schedule is consistent with the purposes of the Act, the public interest, and the protection of investors.<sup>4/</sup>

Inspection frequency requirements adopted by the Board are set out in PCAOB Rule 4003, "Frequency of Inspections."<sup>5/</sup> Under Rule 4003, when a firm issues an audit report while registered,<sup>6/</sup> the Board must conduct an inspection of that firm within a certain number of calendar years following the year of the audit report.<sup>7/</sup>

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<sup>2/</sup> See Section 104(a) of the Act.

<sup>3/</sup> See Section 104(b)(1)(B) of the Act.

<sup>4/</sup> See Section 104(b)(2) of the Act.

<sup>5/</sup> Registered non-U.S. firms are subject to the Act and the Board's rules "in the same manner and to the same extent as" registered U.S. firms (see Section 106(a) of the Act), including the requirement to cooperate in periodic PCAOB inspections.

<sup>6/</sup> Section 2(a)(4) of the Act defines "audit report" to mean, in essence, an audit report with respect to the financial statements of an "issuer," and that is how the term is used in this release.

<sup>7/</sup> In general, if a firm issues audit reports for 100 or fewer issuers in a calendar year, Rule 4003(b) requires that the Board inspect the firm within the following three calendar years. Rule 4003(d), however, provides that the first such inspection of firms that registered in 2003 or 2004 is not required sooner than the fourth calendar year (after the first calendar year in which the firm, while registered, issues an audit report). This release focuses on firms that become subject to Board inspection by virtue of issuing an audit report, but Rules 4003(b) and (d) also describe inspection frequency requirements for firms that play a substantial role in the preparation or furnishing of an audit report (as defined in PCAOB Rule 1001(p)(ii)) but do not issue an audit report. The Board has adopted and submitted for Commission approval amendments that would eliminate the requirement that the Board regularly inspect such firms.



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The Board began a regular cycle of inspections of U.S. firms in 2004 and has conducted 911 such inspections, including repeat inspections of several firms. Inspections of non-U.S. firms began in 2005, and the Board has inspected 123 non-U.S. firms<sup>8/</sup> located in 24 jurisdictions.<sup>9/</sup> Under Rule 4003's current inspection frequency requirements, there are 134 additional non-U.S. firms in 42 jurisdictions that, by virtue of their having issued audit reports, the Board is currently required to inspect but has not yet inspected.<sup>10/</sup> Those 134 pending "first inspections" of non-U.S. firms (with deadlines ranging from 2008 to 2012 under the existing rule) are in addition to pending second, and later, inspections of non-U.S. firms that the Board has already inspected once.

This release discusses rule amendments that would affect a portion of those 134 pending first inspections. Specifically, these amendments would affect 21 of the 52 first inspections that existing Rule 4003 requires the Board to conduct no later than 2008,<sup>11/</sup> and 50 of the 70 first inspections that the rule requires the Board to conduct no later than 2009. Nothing in this release affects inspection frequency requirements

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<sup>8/</sup> The Board has issued reports on 799 of the 1,034 inspections conducted to date, including reports on 42 of the 123 non-U.S. inspections. Reports on the other inspections are in process.

<sup>9/</sup> The Board has inspected non-U.S. firms located in Argentina, Australia, Bermuda, Brazil, Canada, Chile, Colombia, Greece, Hong Kong, India, Indonesia, Ireland, Israel, Japan, Kazakhstan, Mexico, New Zealand, Panama, Peru, Singapore, South Africa, South Korea, Taiwan R.O.C., and the United Kingdom.

<sup>10/</sup> Those 134 firms are located in Argentina, Australia, Austria, Belgium, Canada, Cayman Islands, China, Cyprus, the Czech Republic, Denmark, Finland, France, Germany, Greece, Hong Kong, Hungary, India, Indonesia, Ireland, Israel, Italy, Japan, Kazakhstan, Luxembourg, Malaysia, Netherlands, New Zealand, Norway, Papua New Guinea, Philippines, Poland, Portugal, the Russian Federation, Singapore, South Korea, Spain, Sweden, Switzerland, Turkey, the United Arab Emirates, the United Kingdom, and Venezuela.

<sup>11/</sup> Thirty-one of those required 52 first inspections have been, or will be, conducted in 2008. In addition, the Board has conducted 16 other first inspections of non-U.S. firms in 2008 even though the deadline for the Board's inspection of those firms is not until a later year.



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concerning any other first inspections or concerning any second, or later, inspections of a firm.

The Board is adopting an amendment to Rule 4003 that will give the Board the ability to postpone, for up to one year (*i.e.*, to the end of 2009), first inspections of the remaining non-U.S. firms that the Board is currently required to conduct before the end of 2008. The Board is also proposing, and seeking comment on, an amendment that will give the Board the ability to postpone, for up to three years, first inspections that the Board is currently required to conduct before the end of 2009 in jurisdictions where the Board has conducted no inspections before 2009.

### B. Conducting Inspections of Non-U.S. Firms

The PCAOB has recognized since the outset of its inspection program that inspections of non-U.S. firms pose special issues.<sup>12/</sup> In its oversight of non-U.S. firms, the Board seeks, to the extent reasonably possible, to coordinate and cooperate with local authorities. Since 2003, when the PCAOB began operations, a number of jurisdictions have also developed their own auditor oversight authorities with inspection responsibilities or enhanced existing oversight systems.<sup>13/</sup> The Board has a specific framework for working cooperatively with its non-U.S. counterparts to conduct joint inspections and, to the extent deemed appropriate by the Board in any particular case,

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<sup>12/</sup> See Briefing Paper, Oversight of Non-U.S. Public Accounting Firms (October 28, 2003); Final Rules Relating to the Oversight of Non-U.S. Public Accounting Firms, PCAOB Release No. 2004-005 (June 9, 2004) (hereinafter "Oversight of Non-U.S. Firms").

<sup>13/</sup> In 2006, for instance, the European Union enacted a directive requiring the creation of an effective system of public oversight for statutory auditors and audit firms within each Member State. See The Directive 2006/43/EC of the European Parliament and the Council (May 17, 2006) (the "Eighth Directive"). In addition, among others, Canada created the Canadian Public Accountability Board, and in Australia, the responsibilities of the Australian Securities and Investments Commission were expanded to include auditor oversight. In Asia, Japan created the Certified Public Accountants and Auditing Oversight Board, South Korea gave responsibility for auditor oversight to its Financial Supervisory Service, and Singapore created the Accounting and Corporate Regulatory Authority.



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relying on inspection work performed by that counterpart.<sup>14/</sup> The Board has previously expressed the view that it is in the interests of the public and investors for the Board to develop efficient and effective cooperative arrangements with its non-U.S. counterparts.<sup>15/</sup> In jurisdictions that have their own inspection programs, this may include conducting joint inspections of firms that are subject to both regulators' authority. Even where the Board does not work with a local regulator to conduct joint inspections, the Board communicates with its counterpart or other local authorities (such as securities regulators or other government agencies and ministries) regarding its inspections to be conducted in the jurisdiction.

In some jurisdictions, the PCAOB's ability to conduct inspections, either by itself or jointly with a local regulator, is complicated by the need to address with local authorities potential legal obstacles and sovereignty concerns. The Board seeks to work with the home-country authorities to try to resolve potential conflicts of laws.<sup>16/</sup>

In addition, PCAOB Rule 4011 permits non-U.S. firms that are subject to Board inspection to formally request that the Board, in conducting its inspection, rely on a non-U.S. inspection to the extent deemed appropriate by the Board. If a Rule 4011 request is made, Rule 4012 provides that the Board will, at an appropriate time before each inspection of the firm, determine the degree, if any, to which the Board may rely on the non-U.S. inspection. Rule 4012 describes aspects of the non-U.S. system that the Board will evaluate in making that determination.

Where the need arises to try to resolve potential conflicts of law, or to evaluate a non-U.S. system in response to a Rule 4011 request, the effort can be substantial. The effort typically involves negotiating the principles of an arrangement for cooperation consistent with the inspection obligations that the Act imposes on the Board. It also involves the Board gaining a detailed understanding of the other jurisdiction's auditor oversight system in order for the Board to determine the degree of reliance it is willing to place on inspection work performed under that system in a particular inspection year. Additional effort is involved in coordinating the scheduling of specific inspections.

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<sup>14/</sup> See PCAOB Rules 4011 and 4012; see also Oversight of Non-U.S. Firms at 2-3.

<sup>15/</sup> See Oversight of Non-U.S. Firms at 2-3.

<sup>16/</sup> See Oversight of Non-U.S. Firms at 3.



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Where possible, the Board seeks to conduct inspections jointly with local authorities both to take advantage of potential efficiencies and to avoid imposing unnecessary regulatory burdens on the firm. Like the PCAOB, several of these other authorities proceed according to inspection frequency requirements. While some of the Board's counterparts are established and have inspection programs, many are new organizations still building up their inspections resources. As a result, synchronizing the inspections schedules of these authorities and the PCAOB's requirements may sometimes require one-time scheduling adjustments by the PCAOB and/or the other authority.

Notwithstanding these challenges, the Board has so far conducted 123 non-U.S. inspections. Moreover, 57 of those inspections, in five jurisdictions, have been conducted jointly with other auditor oversight authorities, while 66 have been conducted solely by the PCAOB.

### C. Extension of the Deadline for Certain 2008 Inspections

There are 52 non-U.S. firms in 22 jurisdictions that, by virtue of when they first issued audit reports while registered, the current inspection frequency rule requires the Board to inspect for the first time by the end of 2008. In 13 of those jurisdictions,<sup>17/</sup> the PCAOB expects to have conducted 31 of those inspections by the end of 2008.<sup>18/</sup> Eighteen other first inspections of non-U.S. firms that are currently required by the end of 2008, however, face challenges to being conducted in 2008.<sup>19/</sup> Those inspections involve firms in nine jurisdictions, several of which have newly established auditor oversight entities that have just recently started their own inspections programs. In some of those nine jurisdictions, the auditor oversight authority's 2008 inspections

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<sup>17/</sup> Those jurisdictions are Australia, Canada, Greece, Hong Kong, India, Ireland, Israel, Japan, Norway, the Russian Federation, Singapore, South Africa, and the United Kingdom.

<sup>18/</sup> This is in addition to first inspections of 16 other non-U.S. firms that the Board will conduct by the end of 2008 even though the deadline for the Board to conduct those inspections is in later years.

<sup>19/</sup> Three other required 2008 non-U.S. inspections appear unlikely to be conducted in 2008 for reasons other than those described here, as discussed in footnote 21 below.



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schedules did not include some or any of the firms the PCAOB is required to inspect in 2008. In still other jurisdictions, local authorities have raised sovereignty concerns or potential legal conflicts, and efforts to resolve those issues are incomplete.

The Board has made an effort to resolve issues with authorities in the nine jurisdictions in time to conduct these inspections in 2008.<sup>20/</sup> The Board remains hopeful that ongoing discussions with these authorities will result in the resolution of outstanding issues. It is now apparent, however, that this will not occur in time to conduct those inspections this year. Accordingly, the choice the Board now faces is whether to (1) postpone these inspections while continuing discussions on the outstanding issues or (2) proceed with inspections by making inspection demands on the individual firms over the objection of local authorities, including in circumstances where local authorities take the position that a firm's cooperation in a Board inspection would violate local law.

Neither option is ideal. While the Board sees value in cooperation and joint inspections, that value must be balanced against the statutory presumption that PCAOB-registered firms will be subject to timely PCAOB inspections in order to protect the interests of investors in U.S. markets. On balance, in light of the status of the ongoing discussions with authorities in the nine jurisdictions described above, the Board believes that a rule amendment allowing the Board to postpone those inspections for up to one year is the appropriate course. For that reason, the Board is adopting a new paragraph (f) to Rule 4003, allowing the Board to postpone for up to one year the first inspection of any non-U.S. firm that the Board is otherwise required to conduct by the end of 2008. The Board is adopting Rule 4003(f) as a final rule to take effect upon Commission approval.<sup>21/</sup>

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<sup>20/</sup> In two of these jurisdictions, the Board was able to arrange for and conduct some joint inspections in 2008, but, due to scheduling conflicts, could not conduct joint inspections of all firms with 2008 deadlines.

<sup>21/</sup> In addition to postponing the 18 required 2008 inspections discussed above, the Board would use Rule 4003(f) to postpone three other required 2008 inspections that now appear unlikely to be conducted in 2008 for a different reason than that discussed above. In October 2007, after soliciting public comment, the Board adopted and requested Commission approval of an amendment to Rule 4003 that would give the Board discretion not to conduct any otherwise required inspection of a firm if, after the firm issued the audit report that triggered the inspection requirement, the firm went two consecutive years without issuing an audit report. The three firms in question fall into that category. The proposed amendment remains pending before the



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In the Board's view, this adjustment to the inspection frequency requirement is consistent with the purposes of the Act, the public interest, and the protection of investors. The Board believes that its approach to implementing Rules 4011 and 4012, developing cooperative arrangements, and conducting joint inspections with foreign regulators is enhancing the Board's efforts to carry out its inspection responsibilities. There is long-term value in accepting a limited delay in inspections to continue working toward cooperative arrangements where it appears reasonably possible to reach them. The Board recognizes that some non-U.S. firms may be reluctant to comply with PCAOB inspection demands because of a concern that doing so might violate local law. Up to a point, the purposes of the Act, the public interest, and the protection of investors are better served by delaying a first inspection to work toward a cooperative resolution than by precipitating legal disputes involving conflicts between U.S. and non-U.S. law that could arise if the Board sought to enforce compliance with its preferred schedule without regard for the concerns of non-U.S. authorities.

The Board does not intend, however, to make any further adjustments to the inspection frequency requirements applicable to firms whose first inspection was due no later than 2008. While the Board will continue to work toward cooperation and coordination with authorities in those jurisdictions, the Board will make inspection demands on the firms early enough in 2009 to allow the Board to conduct the inspections during 2009.<sup>22/</sup> As noted above, the Board is aware of the possibility that, in the absence of resolution of cross-border legal and other issues, a PCAOB-registered firm might in some cases be reluctant to comply with a PCAOB inspection demand because of a concern that doing so might violate local law. Issues related to that possibility are discussed in Part II of this release.

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Commission, and in the event it is not approved this year, the Board would need to postpone the inspections of these three firms pursuant to the amendment described here.

<sup>22/</sup> Nothing in this release is inconsistent with the Board's willingness to place reliance on a non-U.S. inspection consistent with Rules 4011 and 4012, or suggests any position on the nature of the inspection process in circumstances in which the Board relies on a non-U.S. inspection to the maximum extent that would be consistent with the Board's responsibilities under the Act.



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### D. Proposed Extension of the Deadline for Some 2009 Inspections

Under existing Rule 4003, there are 70 non-U.S. firms that, by virtue of when they first issued audit reports while registered, the Board is required to inspect for the first time by the end of 2009.<sup>23/</sup> Those firms are located in 37 jurisdictions, including several jurisdictions in which the Board has already conducted first inspections of other firms. Of those firms, 50 are located in 24 jurisdictions where the Board will not have conducted any inspections by the end of 2008. Many of those 24 jurisdictions have or soon may have a local auditor oversight authority with which the Board would seek to work toward cooperative arrangements before conducting inspections, but has not yet begun to do so. Because of the steps involved in concluding such arrangements and to evaluate the local system, the Board has concerns about proceeding as if that work can be completed for all of the jurisdictions in which the PCAOB has not previously conducted inspections in time to conduct the required inspections in 2009.

In part, the Board views the challenge before it as how to reasonably allocate that jurisdiction-level work over time without unduly delaying inspections of firms whose audit work has the broadest impact on U.S. investors. As a starting point, a reasonable, and perhaps the most readily measurable, indicator of the impact of a firm's audit work on U.S. investors is the total U.S. market capitalization of the firm's issuer audit clients.<sup>24/</sup> The Board believes that the most practical approach to the jurisdiction-level work is to allow three years beyond 2009 to perform that work. At the same time, the Board intends, within that framework, to have inspected by no later than 2010, firms whose issuer audit clients account for more than 90 percent of the aggregate U.S. market capitalization of the issuer audit clients of all 50 firms.

Accordingly, the Board is proposing a new paragraph (g) to Rule 4003. Proposed Rule 4003(g) would allow the Board to postpone, for up to three years, the first inspection of any non-U.S. firm that the Board is currently required to conduct by

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<sup>23/</sup> This is in addition to at least 16 non-U.S. firms that the PCAOB will inspect for the second time in 2009.

<sup>24/</sup> The U.S. market capitalization of a firm's issuer audit clients is not the only relevant measure of the impact on U.S. markets of a firm's audit work. For example, even a firm that has no issuer audit clients could have an impact on U.S. markets by virtue of referred work that the firm performs on audits for which it is not the principal auditor.



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the end of 2009 and that is in a jurisdiction where the Board has not conducted an inspection before 2009. The Board believes that this approach will provide appropriate time for the Board reasonably to pursue cooperative arrangements and evaluate the relevant systems in response to Rule 4011 requests. The Board will, however, conduct first inspections in some number of these jurisdictions in each of the years from 2009 to 2012.

The proposed adjustment should not be understood as a reprieve that allows all affected firms to view 2012 as their deadline for PCAOB inspections. The Board intends to set a schedule of inspections for the period 2009 to 2012, as described below, for the 50 affected firms. The Board will work toward cooperation and coordination with the relevant local authorities, but the Board will not delay making inspection demands on the selected firms early enough in the year chosen by the Board to allow the Board to conduct the inspections in that year.

In determining the schedule, the Board intends to sequence these 50 inspections such that certain minimum thresholds would be satisfied in each of the years from 2009 to 2012. The minimum thresholds would relate to U.S. market capitalization of firms' issuer audit clients. The Board would begin by ranking the 50 firms according to the total U.S. market capitalization of a firm's issuer audit clients.<sup>25/</sup> Working from the top of the list (highest U.S. market capitalization total) down, the Board would distribute the inspection of the 50 firms over 2009 to 2012 such that, at a minimum, the following criteria would be satisfied:

- by the end of 2009, the Board would inspect firms whose combined audit clients' U.S. market capitalization constitutes at least 35 percent of the aggregate U.S. market capitalization of the audit clients of all 50 firms;
- by the end of 2010, the Board would inspect firms whose combined audit clients' U.S. market capitalization constitutes at least 90 percent of that aggregate;

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<sup>25/</sup> For purposes of the ranking described here, the Board would use the average monthly market capitalization on which each issuer's share of the Board's 2008 accounting support fee was based.



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- by the end of 2011, the Board would inspect firms whose combined audit clients' U.S. market capitalization constitutes at least 99.9 percent of that aggregate; and
- the Board would inspect the remaining firms in 2012.<sup>26/</sup>

Along with meeting those market capitalization thresholds, the Board would also satisfy certain criteria concerning the number of those 50 firms that would be inspected in each year. Specifically, the Board would conduct at least four of the 50 inspections in 2009, at least 11 more in 2010, and at least 14 more in 2011.<sup>27/</sup>

The distribution described above, however, would not operate to prevent an inspection from occurring earlier than called for by the schedule.<sup>28/</sup> Any inspection may be moved to an earlier year for a variety of reasons, such as the presence of risk factors (including risk factors relating to referred work that the firm performs on audits for which it is not the principal auditor), synchronization of schedules with a local regulator for purposes of a joint inspection, or simply the opportunity to do an inspection earlier and the availability of resources to do so (including availability of inspectors with specialized industry knowledge and relevant language skills). In addition, the Board will at least annually review updated market capitalization data and consider whether there have been any changes that warrant moving a particular inspection forward to an earlier

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<sup>26/</sup> Under existing provisions of Rule 4003 that the Board does not propose to change, 2012 would also be the deadline for the Board to conduct the second inspection of those of the 50 firms whose first inspection occurs in 2009.

<sup>27/</sup> The issuer audit client U.S. market capitalization currently associated with a significant number of the 50 firms is relatively low, and even zero in a number of cases where firms appear to have stopped issuing audit reports for issuers. As a result, a substantial portion of the relevant issuer market capitalization is associated with a relatively small number of the 50 firms.

<sup>28/</sup> If the Board should fail to make an inspection demand on any firm included in the inspection schedule in a particular year, the Board would publicly describe that fact and the reasons.



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year.<sup>29/</sup> The Board encourages commenters to address whether there are other factors that should be treated as a reason to consider moving an inspection to an earlier year.

If the proposed rule is adopted, the Board would, no later than January of each year from 2009 to 2012, and after providing advance notice to the authorities in the relevant jurisdictions, publicly announce all of the non-U.S. jurisdictions in which there are firms whose inspection the Board will conduct in that year (including, but not limited to, jurisdictions relevant to the 50 inspections discussed above). Once that announcement was made, the Board would conduct inspections that year in each of those jurisdictions unless the Board made a subsequent public announcement explaining why that had changed with respect to a particular jurisdiction.<sup>30/</sup>

For the same reasons as described above in connection with the adoption of Rule 4003(f), the Board believes that proposed Rule 4003(g) would be consistent with the purposes of the Act, the public interest, and the protection of investors. The Board invites commenters to address that issue.

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<sup>29/</sup> The Board does not intend to make changes that would move an inspection of one of these 50 firms to a later year than in the initial distribution except as the result of a development relating to factors described in the text. For example, if a firm's issuer audit client market capitalization drops significantly and the firm performs no significant amount of referred work on audits, its inspection might be delayed to a later year. In any event, the Board would not, for any reason, move one of these 50 inspections to a later year than in the initial distribution without publicly describing the change and the reason for it.

<sup>30/</sup> Even apart from whether the Board eventually adopts the proposed rule, the Board will announce in January 2009 non-U.S. jurisdictions in which the Board will conduct inspections in 2009. While the Board may later add jurisdictions to its 2009 plan (as could occur for various reasons, including if the Board does not adopt the deadline extension proposed in Rule 4003(g)), the Board will conduct 2009 inspections in at least the announced jurisdictions unless the Board makes a subsequent public announcement explaining why that had changed with respect to a particular jurisdiction. The Board also intends to maintain on its web site an up-to-date list of those jurisdictions in which there are registered firms that the Board has inspected. The current list of those jurisdictions is provided in footnote 9 above.



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### E. Transparency Concerning Delayed Inspections

The Act and the Board's inspection frequency rule give rise to an expectation among investors, and the public generally, that the Board will inspect certain firms within a specific timeframe. Under existing Board rules, the Board must conduct the first inspection of most registered firms that issue audit reports no later than the fourth calendar year after the firm first issues an audit report while registered (and at least every third year thereafter).<sup>31/</sup> Because of the postponement of certain 2008 non-U.S. inspections, the end of 2008 will mark the first time in which first inspections of any firms that issue audit reports will not have been conducted within that timeframe. The Board is also proposing, as discussed in Part I.D., that some inspections now due no later than the end of 2009 be postponed.

The Board recognizes that investors may have an interest in the identity of firms that have not been inspected within the timeframe that investors could reasonably have expected an inspection to occur. Accordingly, the Board is considering maintaining on its web site an up-to-date list of all registered firms that have not yet had their first Board inspection even though more than four years have passed since the end of the calendar year in which they first issued an audit report while registered with the Board.<sup>32/</sup> Inclusion on the list would not be an indication that a firm has not cooperated with the Board or is at fault in any way, nor would the list be intended as a substitute for action the Board might take in the event that a firm did fail to cooperate. The list would be intended only to provide public transparency related to delayed inspections.

No rulemaking is required in order for the Board to maintain this public list. Nevertheless, the Board invites comment on this proposed practice.

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<sup>31/</sup> See PCAOB Rules 4003(b) and 4003(d); see also Amendments to Board Rules Relating to Inspections, PCAOB Release No. 2006-008 (December 19, 2006).

<sup>32/</sup> The name of any firm on the list would link to that firm's registration application on Form 1 and to any annual or special reports the firm may have filed on Form 2 or Form 3.



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### II. Registered Firms' Obligations

The Board intends to continue its efforts to develop cooperative relationships with its foreign counterparts. As discussed in Part I, however, in light of its statutory obligation, the Board will need to make inspection demands on non-U.S. firms even in circumstances where the sovereignty concerns or legal objections of local authorities have not been overcome. The Board recognizes that, in those circumstances, some non-U.S. firms may be reluctant to comply with PCAOB inspection demands because of a concern that doing so may violate local law. The Board cannot, however, let the prospect of such refusals dictate delays in the Board's efforts to conduct inspections.

Firms must register with the Board in order to engage in certain professional activity directly related to, and affecting, U.S. financial markets, and all registered firms are subject to the Act and the rules of the Board irrespective of their location.<sup>33/</sup> A registered firm is subject to various requirements and conditions, including PCAOB Rule 4006's requirement to cooperate in an inspection. In addition, as reflected in Section 102(b)(3) of the Act, a firm's compliance with Board requests for information is a condition of the continuing effectiveness of the firm's registration with the Board.<sup>34/</sup>

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<sup>33/</sup> See Section 106(a)(1) of the Act.

<sup>34/</sup> Section 102(b)(3) requires that a firm's registration application include a statement that the firm consents to cooperate in and comply with Board requests for information and that the firm understands and agrees that such cooperation and compliance is a condition to the continuing effectiveness of the firm's registration with the Board. Some non-U.S. firms, invoking PCAOB Rule 2105, declined to include such statements in their applications on the ground that, because of the possibility that the Board might someday request information that local law would restrict the firm from providing, the firm could not represent in advance that it would comply with every request that the Board might make. As long as certain criteria are satisfied, PCAOB Rule 2105 allows a firm's registration application to be considered complete, for purposes of registering the firm, even in the absence of the consent to cooperate. The absence from the application of the broad consent to cooperate, however, does not absolve a firm of the underlying obligation to cooperate if and when the Board seeks information, a point that the Board conveys in writing to any such firm when notifying the firm that its application is approved. See also Oversight of Non-U.S. Firms at A2-15 – A2-19.



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A registered firm's failure or refusal to provide requested information is a violation of Rule 4006 and is inconsistent with the condition reflected in Section 102(b)(3). The Board could impose disciplinary sanctions in any case where a violation of Rule 4006 is established.<sup>35/</sup> There are, of course, a range of disciplinary and remedial sanctions available to the Board, including revocation of a firm's registration. Conceivably, however, there might be circumstances in which the Board initially addresses a Rule 4006 violation with sanctions short of revocation. For example, the Board could restrict a firm from accepting any new issuer audit clients, or performing referred work on the audit of any issuer for which it has not previously performed referred work, until the firm cooperates in an inspection. But even if the specific facts seemed to make that sanction appropriate initially, the Board would be unlikely to allow that situation to continue indefinitely without another inspection request being made and, in the event of noncooperation, more serious sanctions being imposed.

The Board's consideration of any actual noncooperation case will be based on the facts of the case. The Board must, however, take into account the importance of the inspection process to the oversight regime established by the Act. Moreover, the Board must be sensitive to the legislative premise reflected in Section 102(b)(3) – that firms that cannot or will not cooperate with Board requests for information should not be registered. At the same time, the Board recognizes that a refusal to provide information based on non-U.S. legal restrictions or the sovereignty concerns of local authorities implicates considerations not present in other noncooperation circumstances. The Board invites public comment generally on whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006.

Apart from the sanctions the Board would impose on a firm after a Rule 4006 violation is established, the Board is also considering whether there are possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information. One example that the Board has begun to consider would involve requiring a principal auditor to make certain public disclosures as part of, or in connection with, each audit report it issues for an issuer, including, among other possibilities:

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<sup>35/</sup> The Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection.



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- If the principal auditor has failed to provide information in response to an inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns, the principal auditor would need to disclose that fact as part of, or in connection with, its audit report.
- In each case, the principal auditor would need to make a representation about whether the principal auditor used the work of any registered firm that has declined to provide information or documents in response to a Board inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns. The principal auditor would have an obligation to make this inquiry to any registered firm whose work the principal auditor uses, regardless of whether that work constituted a "substantial role" as defined in PCAOB Rule 1001(p)(ii). The principal auditor would also have to retain documentation of the inquiry and response.
- If the principal auditor uses the work of any such firm and assumes responsibility for that work (under AU § 543.04), the principal auditor would have to disclose (a) the identity of the firm, (b) the nature of the work performed by the firm, (c) any steps the principal auditor took to assure itself concerning the firm's and the relevant individuals' familiarity with relevant professional standards, ability to perform the work adequately, and the adequate performance of the work, (d) any other procedures on which the principal auditor relies to monitor or assess the firm's performance of audit procedures in the audits of issuers, and (e) a brief summary of any information available to the principal auditor about deficiencies in the firm's performance of any such procedures in the two-year period preceding the date of the audit report.
- If the principal auditor used the work of any such firm and makes reference to the audit of the other auditor (under AU 543.06), the principal auditor would have to disclose, in addition to the division of responsibility described in AU 543.07, the identity of the firm and the other information described in the preceding sentence.

The Board invites comment on the potential benefits and drawbacks of a rule along the lines described above. The Board also invites comment more generally on



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other possible rulemaking approaches relating to those issues that might provide useful disclosure to investors or otherwise be in the public interest.

### III. Opportunity for Public Comment

Interested persons may submit written comments on proposed Rule 4003(g) (extending the deadline for the Board to conduct first inspections of non-U.S. firms otherwise required by 2009), on the disclosure point discussed in Part I.E., and on the issues discussed in Part II by sending them to the Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, DC 2006. Comments also may be submitted by e-mail to [comments@pcaobus.org](mailto:comments@pcaobus.org). All comments should refer to PCAOB Rulemaking Docket Matter No. 027 in the subject or reference line and should be received by the Board no later than 5:00 p.m. (EST) on February 2, 2009.

\* \* \*

On the fourth day of December, in the year 2008, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour

J. Gordon Seymour  
Secretary

December 4, 2008

APPENDICES –

Amendment to PCAOB Rule 4003  
Proposed Amendment to PCAOB Rule 4003



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### Appendix A – Amendments to Rule 4003

The Board is amending Section 4 of its rules by amending Rule 4003. The relevant portion of the rule, as amended, is set out below. Language added by the amendments is shown in bold italics. Other text in Section 4, including notes to the Rules, remains unchanged and is indicated by " \* \* \* " in the text below.

#### RULES OF THE BOARD

\* \* \*

#### SECTION 4. INSPECTIONS

\* \* \*

##### Rule 4003. Frequency of Inspections

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***(f) With respect to any foreign registered public accounting firm concerning which the preceding provisions of this Rule would set a 2008 deadline for the first Board inspection, such deadline is extended to 2009.***



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### Appendix B – Proposed Amendments to Rule 4003

The Board proposes to amend Section 4 of its rules by amending Rule 4003. The relevant portion of the rules, as amended, is set out below. Language added by the proposed amendments is shown in bold italics. Other text in Section 4, including notes to the Rules, would remain unchanged and is indicated by " \* \* \* " in the text below.

#### RULES OF THE BOARD

\* \* \*

#### SECTION 4. INSPECTIONS

\* \* \*

##### Rule 4003. Frequency of Inspections

\* \* \*

*(g) With respect to any foreign registered public accounting firm concerning which the preceding provisions of this Rule, other than paragraphs (a) and (f), would set a 2009 deadline for the first Board inspection and that is headquartered in a country in which no foreign registered public accounting firm that the Board inspected before 2009 is headquartered, such deadline is extended to 2012, provided, however, that from among the group of all such firms, the Board shall conduct some first inspections in each of the years from 2009 to 2012, scheduled according to such criteria as the Board shall publicly announce.*

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

BDO International, Noel Clehane, Global Head of Regulatory & Public Policy Affairs

CalPERS, Mary Hartman Morris, Investment Officer

Joseph V. Carcello, Ernst & Young Professor, Director of Research - Corporate Governance Center, University of Tennessee

Certified Public Accountants and Auditing Oversight Board of Japan, Nobuyuki Kinoshita, Secretary General; Financial Services Agency of Japan, Junichi Maruyama, Deputy Commissioner for International Affairs

China Securities Regulatory Commission, Tong Daochi, Director General, Department of International Affairs

Jack Ciesielski

Compagnie Nationale des Commissaires aux Comptes, Vincent Baillot, President

Consumer Federation of America, Barbara Roper, Director of Investor Protection

Council of Institutional Investors, Jeff Mahoney, General Counsel

Danish Commerce and Companies Agency, Peter Kroglund Jensen, Chief Special Advisor

Deloitte Touche Tohmatsu

Ernst & Young LLP

Federation of European Accountants, Hans van Damme, President

Grant Thornton International, Kenneth C. Sharp, Global Leader – Assurance Service

Hong Kong Institute of Certified Public Accountants, Chris Joy, Executive Director
Institut der Wirtschaftsprüfer in Deutschland e.V., Klaus-Peter Feld, Executive Officer
KPMG International
Mazars Risk Management & Audit Quality, Jean-Luc Barlet
Netherlands Authority for the Financial Markets, Prof. dr. S.J. Maijoor, Managing Director
PricewaterhouseCoopers LLP
Swiss Federal Audit Oversight Authority, Frank Schneider, Director
The Auditing Board of the Central Chamber of Commerce, Aatto Prihti, Chairman
The European Commission
UK Professional Oversight Board, Paul George, Director



February 2, 2009

*By email to;*  
Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, NW  
Washington, DC 20006-2803

**PCAOB Rulemaking Docket Matter No. 027**

**Rule Amendments concerning the timing of certain inspections of non-U.S. Firms, and other issues relating to inspections of non-U.S. Firms -- PCAOB Release No. 2008-007**

Dear Sir,

BDO International welcomes the opportunity to comment on the Public Company Accounting Oversight Board's (hereafter the PCAOB or the Board) Release No 2008-007. BDO International is a worldwide network of independent public accounting firms ("BDO Member Firms"), each of which is a separate legal entity serving international clients, including U.S. public companies. The network is coordinated by BDO Global Coordination B.V. located in Brussels, Belgium.

BDO International believes that investors and the securities markets benefit through coordination and cooperation among national regulators. In an increasingly global economy, we have seen only too starkly how transactions and events impacting businesses can transcend national borders. As a consequence we firmly believe that convergence of professional standards (including oversight norms) and coordination of regulatory efforts is imperative.

We make our submission on the PCAOB Release in that context and draw attention also to the related submission made by BDO International in March 2008 on PCAOB Release No. 2007-011 (Guidance Regarding Implementation of PCAOB Rule 4012).

### **General remarks**

We fully support the Board's efforts to establish cooperative relationships with non-U.S. oversight authorities and believe that these efforts will be a key step in moving towards a system of mutual recognition, in which a foreign country's oversight authority accepts the results of an inspection performed by the domestic country's (home country) oversight authority, as being sufficient to satisfy its own inspection requirements.

There will undoubtedly be many challenges to achieving such a an outcome, but we believe that establishing cooperative relationships with non-U.S. oversight authorities will further the Board's goals of protecting investors, ensuring effective and efficient oversight of audit firms, improving audit quality, and helping to preserve the public trust in the auditing profession.

We generally support the extension of the Board's inspection schedules, but would encourage additional flexibility in setting the revised extension deadlines for reasons set out below.

We do not support the Board's proposal to publish a list of audit firms not yet inspected, without a means of ensuring that non-US audit firms included on the list are not stigmatised or otherwise disadvantaged. We also believe that such a proposal could give rise to confusion among investors and have the potential unintended consequence of reflecting poorly on the oversight authority in the jurisdiction of any non-US firms so listed.

We have serious concerns about the proposal under consideration that would require public disclosure in the principal auditor's audit report, or elsewhere, of information regarding a non-US firm's refusal to provide information because of legal restrictions or sovereignty concerns and the principal auditor's procedures to gain comfort as to the adequacy of the work performed by the non-US firm. It is our belief that the disclosures under consideration would be confusing to investors, would be disproportionate to other elements of the audit, and would seem to further precipitate non-US legal and sovereignty issues by indirectly requiring disclosure of internal and external inspection results of non-US firms. We believe that the existing protocol involving PCAOB inspections of US firms already provides sufficient comfort to the inspection staff in the areas covered by much of the contemplated disclosures.

Lastly, we are concerned with the Board's reiteration that a non-US firm would be in violation of Rule 4006 for a failure to provide information to the Board where such failure arises as a result of a legal impediment present in the non-U.S. firm's home country law. Such situations arise as a result of a conflict of law and should be addressed and resolved by inter-governmental or inter-regulator contact, rather than by forcing non-US audit firms to choose which law they wish to violate. Such a situation is untenable and arguably will set back cooperative relationships with the oversight authorities in the jurisdictions whose laws give rise to the situations in question.

Our more specific comments are as follows:

### **1. Timing of certain inspections**

We note that the Board has adopted and submitted for SEC approval, amendments that would eliminate the requirement that the Board regularly inspect firms that play a substantial role in the preparation or furnishing of an audit report but do not issue an audit report. We support such amendments based on the principle of reducing unnecessary regulatory burdens.

We are mindful that the Sarbanes-Oxley Act and the PCAOB Rules place certain responsibilities on the Board in relation to conducting a continuing programme of inspections of registered public accounting firms. Nonetheless we believe that delays in completing inspections can be justified where the delay serves investors' long-term interests of establishing cooperative arrangements that facilitate inspections of non-U.S. firms. Accordingly, we agree with the Board's proposed amendment to Rule 4003 regarding postponing first inspections of the remaining non-US audit firms which the Board is currently required to conduct before end of 2008.

We are concerned, however, that the extension by one year will not be sufficient to allow the Board and the non-U.S. oversight authorities to address existing impediments to the Board's inspections. It may not be practicable, within the extended timeframe allowed, to resolve those impediments and conduct inspections in those countries covered by this one-year extension. We suggest therefore, that the Board should not rule out further adjustments to the inspection-frequency requirements applicable to firms whose first inspection was due by the end of 2008, where such further extension would facilitate cooperation with non-US oversight authorities.

We also support the Board's proposal to amend its rules giving it the ability to postpone for up to three years, inspections that the Board is currently required to conduct before the end of 2009, in jurisdictions where the Board has conducted no inspections before 2009. As the underlying objective giving rise to extensions of the "2008 inspections" is the same as that justifying the extensions of the "2009 inspections", we would see a justification for seeking a similar extension period or flexibility for the "2008 inspections". As indicated above, we demur as to whether one year extensions for inspections that should have taken place by 2008, will prove to be an adequate extension period .

Whilst supportive of the Board's proposals above, we encourage the Board to continue its efforts on to finalise cooperative arrangements with all relevant non-U.S. oversight authorities.

## **2. Basis for prioritising the timing of inspections in 2009-2012**

The Board indicates in the Release that in determining the schedule, it intends to "sequence ..... inspections such that certain minimum thresholds would be satisfied in each of the years from 2009 to 2012. The minimum thresholds would relate to U.S. market capitalisation of firms' issuer-audit clients."

Whilst we agree that use of U.S. market capitalisation is a reasonable *starting point* for prioritising inspections, we believe that the Board's approach as set out, without consideration of other relevant factors-- particularly legal and sovereignty impediments-- could result in premature inspection deadlines that could hinder concluding cooperative agreements with non-US oversight authorities and could be counterproductive.

In our opinion, other factors that should be taken into account would include the nature of existing impediments to securing cooperative working arrangements, the extent to which inspections are currently conducted by the oversight authority in that country, or other difficulties encountered in conducting inspections in the non-U.S. country.

The Board already assesses the oversight regimes of non-U.S. countries under its Rule 4012. Accordingly, audit firms located in countries where the oversight authority is strong, independent, transparent, and already conducting effective inspections, may merit a lower inspection priority than

those firms located in countries where the oversight authority is not yet fully developed. We endorse risk-based approaches of this nature and encourage a move towards *full mutual reliance* of home country inspections in appropriate circumstances.

As we stated in our submission on the proposal relating to Rule 4012 Release (Question 5):

*“We are of the view that the PCAOB should extend the meaning of full reliance to eliminate the need for joint inspections or the observation of portions of the inspection process. Any variations of this are in effect, versions of “partial reliance” and not indicative of mutual trust or unconditional professional recognition of the capabilities of the non-US Oversight Body”*

### **3. Transparency concerning delayed inspections**

The Board has indicated that it is considering “maintaining on its web site an up-to-date list of all registered firms that have not yet had their first Board inspection even though more than four years have passed since the end of the calendar year in which they first issued an audit report while registered with the Board.” The Board also indicates that “inclusion on the list would not be an indication that a firm has not cooperated with the Board or is at fault in any way....”

We have the following concerns about any such listing:

- The fact that a firm has not been the subject of a PCAOB inspection and is included on this list could be wrongly interpreted as meaning that the public can take no comfort as to the audit quality of that firm. This is unfair to the non-US firm, given that the scheduling of the Board’s inspections of a non-U.S. firm is outside the control of that firm as are many of the legal and other impediments that may have prevented a satisfactory (or any) inspection from taking place.
- It is unclear as to whether any caveats or explanations to be provided would neutralise the possible conclusions that might be drawn by third parties as a result of a non-U.S. firm being included on the list.

- Finally, we believe that issuers could be impacted negatively by their auditor being identified on the list, as a result of doubts forming in investors' minds about the quality of the issuer's audit where the auditor has not been inspected by the Board. As the issuer does not have the ability to control the timing of a Board inspection or in any way affect the legal or other impediments that may have resulted in its auditor not having been inspected, such an action on the Board's part may have adverse unintended consequences.

In any event, we believe that such a list is unnecessary. The PCAOB website already lists the names of all firms that have been inspected including non-U.S. firms. It would be a simple matter of adding a note to that list, explaining the Board's inspection schedule as contemplated by this Release and that certain firms have been inspected, but their reports have not yet been finalised.

#### **4. Refusal to provide information by non-US firms due to non-US legal impediments or sovereignty concerns**

We are concerned by the Board's viewpoint in relation to the unwillingness or inability of non-US firm to provide information requested by PCAOB inspectors, where there are legal or sovereignty impediments.

The Release recognises in several places (pages 6, 8, and 9 in particular) that such impediments exist and that attempts to try to resolve the resulting conflicts can require a substantial effort. Nevertheless, the Release appears to start from the premise that a non-U.S. firm's failure or refusal to provide requested information constitutes a violation of Rule 4006 even in situations where the inability to comply is attributable to a legal restriction.

Whilst the Release indicates that the Board's consideration of any actual non-cooperation will be based on the facts of the case, footnote 35 on page 16 of the Release clearly states that "*the Board does not view non-US legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding .....for failing or refusing to provide information requested in an inspection*"

We recognise that the Board's ability to fulfill its mandate literally, may be compromised when it is unable to obtain access to audit working papers or other information that it has requested in connection with its inspections. However, we believe that the Board's view on this issue is unworkable as it

will place non-U.S. firms in an impossible position as a consequence of what is essentially a conflict of laws.

Where a firm declines to provide the information sought to the Board's inspectors, that firm then risks being deemed to have violated the Board's rules with the various consequences and lines of censure available to the Board, up to and including revocation of registration.

On the other hand, if a firm provides the information to the Board's inspectors in apparent violation of its home country's laws, it will be exposed to home country discipline, which could also include revocation of the firm's licence and in certain countries, personal criminal law sanctions.

Furthermore, there are jurisdictions where violations of law or professional discipline rules in a foreign jurisdiction must be reported to the domestic oversight body, leading to a circular punishment scenario. It is highly undesirable to place a non-US firm in such a position and we strongly urge the Board to reconsider its actions in this regard.

Ultimately, the conflict of laws is a matter for resolution between sovereign powers and/or the oversight authorities involved. We would also suggest that the prospects for establishing sustainable cooperation with non-U.S. oversight authorities may be damaged if a non-U.S. firm's ability to comply fully with its home country laws is compromised by compliance with the Board's requirements. In the long term, this would be more injurious to the public interest and investor needs than the more immediate "non-compliance" by the non-US firm if it led to deregistration by non-US auditors, thus exacerbating the audit firm concentration concern and conceivably denying an issuer the right to appoint an appropriate auditor in its home country if all other domestic audit firms arrived at the same conclusion.

##### **5. Public Disclosure under Consideration by the PCAOB**

We appreciate the Board's concern about addressing aspects of the problem created by refusal of a non-U.S. firm to provide information on the basis of home country legal or sovereignty issues. However, the example of public disclosures that the Board has begun to consider is not, in our view, an appropriate solution.

We do not perceive there to be a benefit to disclosure to financial statement users of the fact that the principal auditor has failed to provide information in response to an inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns. In those instances, the PCAOB inspection staff would likely have achieved an appropriate degree of comfort through other means (including perhaps cooperation with the home country regulator), so disclosure of the fact under consideration would not seem to be useful information. Furthermore, such disclosure might be detrimental to establishing cooperative arrangements with non-U.S. oversight authorities.

If the various disclosures under consideration were included in the auditor's report, they would likely be confusing to investors. Audit reports are intended to fulfill a specific purpose in conveying the broad scope of the auditor's examination of the financial statements and, if required, the issuer's internal controls over financial reporting. Inclusion of specific procedures employed by the primary auditor in overseeing the work of the non-U.S. registered auditor, as well as the fact, based on inquiry, that the non-U.S. auditor declined to provide information in response to a Board inspection demand, would tend to obfuscate the focus of the report. This would pose particular problems if there were a proliferation of information resulting from the need to provide it regardless of whether the non-U.S. auditor played a "substantial role" in the audit and would be further exacerbated if there were a large number of non-U.S. auditors involved in the audits of the subsidiaries of a consolidated group that declined to provide information to the Board because of legal or sovereignty restrictions. Even if the Board were to adopt disclosures contemplated by the example, it should do so only with respect to non-U.S. auditors whose work constituted a "substantial role" on the engagement. Any level below that would appear not to be meaningful under any circumstances.

We also do not agree with the public disclosure of the information in the example even if it were not part of the audit report. An audit of financial statements and, where required, of internal controls over financial reporting, encompasses a vast array of procedures in many areas. Public disclosure of these procedures is not required and we perceive no demands for such disclosure by financial statement users. In contrast, the details set forth in the Release would place disproportionate emphasis on the importance of the procedures performed by the principal auditor to monitor the performance of the work of the non-U.S. auditor.

We are also concerned about the part of the example disclosure with respect to “(d) any other procedures on which the principal auditor relies to monitor or assess the firm’s performance of audit procedures in the audits of issuers, and (e) a brief summary of any information available to the principal auditor about deficiencies in the firm’s performance of any such procedures in the two-year period preceding the date of the audit report”. This disclosure seems to require public disclosure of the results of a non-U.S. firm’s internal inspection or domestic regulatory inspection if that information is available in any form to the principal auditor. If that is what is intended by this provision, we believe it would precipitate sovereignty issues and, therefore, should not be considered by the Board at this time.

In addition, we are concerned that the representation by the principal auditor that the non-U.S. firm declined to provide information or documents on the basis of legal or sovereignty issues might be construed as the principal auditor taking responsibility for the validity of the non-U.S. firm’s basis for declining to provide such information or documents. Accordingly, any such representation should clearly indicate that the principal auditor is not assuming such responsibility.

Whilst we do not support the public disclosures being considered in the Release, we believe there is already an effective means for the PCAOB to gain comfort as to the work performed by non-U.S. registered firms on particular engagements. In its current inspections of U.S. registered firms. The PCAOB staff commonly inspects the work performed by the U.S. principal auditor in gaining comfort on the work performed by non-U.S. auditors. Paragraph 19 of Auditing Standard No. 3, *Audit Documentation*, contains specific documentation requirements applicable to work performed by other auditors, including non-U.S affiliates. These requirements implicitly recognise that in certain non-U.S. jurisdictions there are legal restrictions against transmission of certain workpapers out of the country. In evaluating the oversight work performed by the principal auditor, PCAOB inspection staff ordinarily inquire about how the principal auditor obtained comfort as to the competency of the non-U.S. auditor and the adequacy of their work. In certain cases, this comfort is achieved through the principal auditor’s review of the workpapers in the foreign country. Since the inspection staff is already able to obtain much of the engagement-specific information contemplated by the disclosures in the Release, we believe the existing process should be sufficient for the present time. It is only when there are enhanced cooperative arrangements between the Board and non-

U.S. oversight authorities, leading to full mutual reliance, that we will have the complete comfort level sought by the Board.

**Conclusion;**

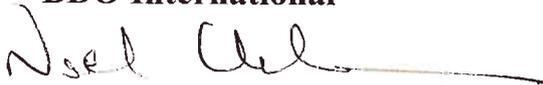
As recognised by the Board, many jurisdictions are developing audit oversight entities that share the objectives of the PCAOB, such as enhancing audit quality, giving greater protection to investors and assuring public trust in public company audits. We strongly support the willingness of the PCAOB to coordinate its inspection efforts with those non-US oversight bodies.

We are certain however, that legal, regulatory and other differences in foreign jurisdictions will inevitably cause audit oversight entities in those countries to follow somewhat different approaches in order to meet the imperatives above. We urge the Board therefore, to continue its collaborative efforts with non-US oversight bodies and to also consider amending the latest Release document with the longer term objectives in mind.

Should the PCAOB require any clarification of this comment letter or wish to discuss its views with us, we would welcome the opportunity to do so.

Yours faithfully,

**BDO International**



***Noel Clehane***

**Global Head of Regulatory and Public Policy Affairs,**



**CalPERS**

Investment Office

P.O. Box 2749

Sacramento, CA 95812-2749

Telecommunications Device for the Deaf - (916) 795-3240

Telephone: (916) 795-2731

February 2, 2009

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

**RE: PCAOB Release No. 2008—06 and 007, Rulemaking Docket Matter No. 027**

Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms

Dear Mr. Seymour:

I am writing you on behalf of the California Public Employees' Retirement System (CalPERS). CalPERS is the largest public pension fund, managing pension and health benefits for more than 1.6 million California public employees, retirees and their families. CalPERS manages approximately \$180.9 billion in assets.

The Public Company Accounting Oversight Board (PCAOB, Board) requested comments on adopting an amendment to the inspection frequency requirements of Rule 4003 and certain other issues and concepts related to inspections of non-U.S. firms.

As a long-term shareowner, CalPERS has a significant financial interest in seeking improvements in the integrity of financial reporting. Auditors play a vital role in helping to ensure the integrity of financial reporting and it is the important role of auditors that bring standardization and discipline to corporate accounting, which in turn enhances investor confidence. The Sarbanes-Oxley Act of 2002, sec. 101, (SOX) establishes the Board to oversee the audit of public companies in order to protect the interests of investors.

CalPERS is supportive of the Board and its efforts to strengthen audit quality and consistency globally. We are also supportive of the Board's efforts to deepen its relations with other independent auditor oversight entities. We agree that these actions are necessary as the markets move towards a single set of globally accepted accounting standards. Auditors, by the nature of their responsibilities, should be able to facilitate global consistency. Critical to this process is the inspection of these public accounting firms by an independent auditor oversight entity. CalPERS responded to PCAOB Release No. 2007-010 regarding inspections of foreign registered public accounting firms on

**California Public Employees' Retirement System  
Lincoln Plaza East - 400 Q Street, Suite E4800 - Sacramento, CA 95811**

PCAOB Release 2008-06 and 007  
February 2, 2009  
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March 5, 2008 and have attached as reference to the response of this letter. In the context of this previous letter we provide the following comments:

### **Conducting Inspections of Non-U.S. Firms**

CalPERS continues to support the Board's specific framework for working cooperatively with its non-U.S. counterparts to conduct joint inspections and PCAOB Rule 4011 which permits non-U.S. Firms, subject to inspection, to rely on a non-U.S. inspection to the extent deemed appropriate by the Board. We support Rule 4012 which describes aspects of the non-U.S. system that the Board will evaluate in making that determination.

### **Extension of the Deadline for Certain 2008 Inspections**

As outlined in our March 5, 2008 letter we supported cooperation and joint inspections before full reliance and understand that laws, regulations and enforcement by non-U.S. auditor oversight entities may cause sovereignty concerns or potential legal conflicts which may delay inspections. CalPERS understands the Board's need to adopt a new paragraph (f) to Rule 4003, which allows the Board to postpone for up to one year the first inspection of some non-U.S. audit firms. We also agree that the Board should not make any further adjustments to inspection frequency requirements whose first inspection was due no later than 2008.

### **Proposed Extension of the Deadline for Some 2009 Inspections**

CalPERS again understands the challenges the Board faces in completing the 70 non-U.S. audit firms scheduled for inspection by the end of 2009. We appreciate the Board's approach to ensure that certain criteria will be evaluated to determine the schedule of these inspections and the proposed adjustment to proposed Rule 4003(g), allowing postponement, for up to three years should not be understood as a reprieve that allows all affected firms to view 2012 as their deadline for PCAOB inspections. CalPERS believes criteria set at ensuring minimum thresholds relating to U.S. market capitalization of firms issuer audit clients is at least one method to ensure inspections of firms that may have higher risks associated with the issuers with a larger market capitalization. We feel strongly that the Board should outline on its website other risk factors that will be monitored to determine whether an inspection should occur at an earlier date.

### **Transparency Concerning Delayed Inspections**

Although CalPERS supports the amendments (extended timetables) as outlined above, it does so with reservations and strongly believes the Board should maintain on its website an up-to-date list of all registered firms that have not yet had their first inspection and the reason why (emphasis on) specifically if the firm or country jurisdiction is not cooperating with the PCAOB. Also, the Board should consider posting a list of countries where audit firms are registered which refuse cooperation or state violation of local law without some remediation efforts. We would suggest a twice a year accounting of the Board's progress in the inspections and any adjustments to the timetables with a description of the barriers and impediments. Though, the Board should hold itself accountable and not supersede the three-year period.

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### **Registered Firms' Obligations**

CalPERS agrees that all audit firms registered with the PCAOB as required by Section 102(b)(3) should continue to consent to cooperate and comply with the Board's requests for information and that disciplinary sanctions may be imposed. We support the Board in its actions which may restrict a firm from accepting any new issuer audit clients, or performing referred work on the audit of any issuer for which it has not previously performed referred work, until the firm cooperates with the inspection requirements. We also agree that the Board should not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense.

As stated above, in addition to listing on the Board's website all audit firms that have not yet had their first inspection we believe that listing of countries which repeatedly represent violation of local law or other sovereignty issues without some remediation should be identified for investors' knowledge. We also agree that requiring certain public disclosures by the principal auditor (as outlined in the release) in failing to provide information in response to an inspection demand should disclose that fact as part of, or in connection with, its audit report. We also support this type of disclosure should occur in using the work of other firms (under AU Section 543.04) as well as the division of responsibility as described in AU 543.07.

We continue to believe and support the Board's work through the International Forum of Independent Audit Regulators (IFIAR) which may help facilitate resolution of cross-border legal issues and suggest lobbying efforts to the IFIAR be elevated to ensure ongoing discussion and resolution.

Thank you for considering our comments. If you would like to discuss any of these points please do not hesitate to contact me at 916-795-4129.

Sincerely,



Mary Hartman Morris  
Investment Officer, CalPERS Corporate Governance

Enclosure: **PCAOB Release No. 2007-010** – *Inspections of Foreign Registered Public Accounting Firms*

cc: Eric Baggesen, Senior Investment Officer – Global Equity, CalPERS  
Kenneth W. Marzion – Interim Chief Operations Investment Officer, CalPERS  
Bill McGrew, Portfolio Manager – Corporate Governance, CalPERS  
Michael Riffle, Portfolio Manager – Corporate Governance, CalPERS



Russell Read, Ph.D., CFA  
Chief Investment Officer  
Investment Office  
P.O. Box 2749  
Sacramento, CA 95812-2749  
Telecommunications Device for the Deaf - (916) 795-3240  
Telephone: (916) 795-3400

March 5, 2008

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

**RE: PCAOB Release No. 2007-010 – *Inspections of Foreign Registered Public Accounting Firms***

Dear Mr. Seymour:

I am writing you on behalf of the California Public Employees' Retirement System (CalPERS). CalPERS is the 4<sup>th</sup> largest retirement system<sup>1</sup> in the world and the largest public pension system in the U.S., managing approximately \$238 billion in assets. CalPERS manages pension and health benefits for approximately 1.5 million California public employees, retirees and their families.

The PCAOB (Board) requested comments on a proposed statement to increase its level of reliance on non-U.S. Accounting firms' oversight programs. The proposed policy statement provides guidance on the Board's Rule 4012, *Inspections of Foreign Registered Public Accounting Firms* which permits the Board to adjust its reliance on the inspections of auditor oversight entities located in the home countries of registered non-U.S. audit firms, based upon the level of independence and rigor of those entities.

As a long-term shareowner, CalPERS has a significant financial interest in seeking improvement in the integrity of financial reporting. Auditors play a vital role in helping to ensure the integrity of financial reporting and it is the important role of auditors that brings standardization and discipline to corporate accounting, which in turn enhances investor confidence. The Sarbanes-Oxley Act of 2002, sec. 101, (SOX) establishes the

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<sup>1</sup> Pensions & Investments, "P&I/ Watson Wyatt world's 300 largest retirement plans", 2007 Databook, Page 28, December 24, 2007.

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March 5, 2008  
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Board to oversee the audit of public companies in order to protect the interests of investors.

CalPERS is supportive of the Board and its efforts to strengthen audit quality and consistency globally. We are also supportive of the Board's efforts to deepen its relations with other independent auditor oversight entities. We agree that these actions are necessary as the markets move towards a single set of globally accepted accounting standards. Auditors, by the nature of their responsibilities, should be able to facilitate global consistency. Critical to this process is the inspection of these public accounting firms by an independent auditor oversight entity. Although the Board's approach appears to be sound and we support the Board's professional judgment, we believe laws, regulations and enforcement by these non-U.S. auditor oversight entities should be fully considered prior to providing "full reliance" on the inspections programs of these oversight entities. We caution the Board to establish an appropriate time period for evaluation prior to relinquishing its oversight powers to these non-U.S. auditor oversight entities.

#### **Criteria to increase reliance on inspections by non-U.S. oversight entity**

The five broad principles designed to guide the Board in making a reliance determination appear to provide a sound basis for making a professional judgment to rely on non-U.S. auditor oversight entities. However, these broad principles may be impacted by the laws, rules and agreements of the home countries where the specific oversight entities are resident. CalPERS recommends that the Board ensure that similar guidelines on internal control over financial reporting are considered by these non-U.S. inspection systems. CalPERS supports the concept and benefits of full reliance but is unsure of the costs to the protection of investors' interest.

We believe the Board's work through the International Forum of Independent Audit Regulators (IFIAR) may facilitate the Board's due diligence and further the discussion of whether additional factors should be considered.

#### **Cooperation and joint inspections before full reliance**

We support the Board's desire to refine its policy of cross-border cooperation and agree that inspection systems of its non-U.S. counterparts must be sufficiently rigorous to meet the level of protection of investors that is required by SOX. Full reliance should in part be based on the ability of the oversight entity to obtain similar access and information that the PCAOB's inspectors can access when conducting inspections or investigations in the U.S. The Board should retain its overall authority under SOX regarding inspections, investigations and enforcement until an appropriate time period of full reliance is established and evaluated. The Board may decide not to rely on the non-U.S. auditor oversight entity and be stringent on the ability to do so.

Also, CalPERS believes that without full cooperation of these non-U.S. auditor oversight entities the Board will not attain its desired full reliance. CalPERS believes that home-

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country regulation may affect this cooperation and the ability to perform joint inspections. We also believe there may be confidentiality requirements established in the home-country regulation that may make joint inspections challenging.

CalPERS is prepared to provide assistance to the Board at its request. Please contact Dennis Johnson, Senior Portfolio Manager at (916) 795-2731 if you have any questions or if we can be of further assistance.

Sincerely,

A handwritten signature in black ink, appearing to read "Dennis Johnson".

cc: Fred Buenrostro, Chief Executive Officer, CalPERS  
Dennis Johnson, Senior Portfolio Manager, CalPERS

February 2, 2009

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

RE: PCAOB Rulemaking Docket Matter No. 027

Dear PCAOB Board Members and Staff:

Thank you for the opportunity to comment on the Board's Proposed Rule Amendments Concerning the Timing of Certain Inspections of Non-US Firms, and Other Issues Relating to Inspections of Non-US Firms.

The proposed rule amendment addresses three issues. First, it gives the PCAOB (Board) the ability to postpone, for up to one year, certain inspections of foreign registered public accounting firms that the Board was originally scheduled to complete before the end of 2008. Second, it gives the Board the ability to postpone, for up to three years, certain inspections of foreign registered public accounting firms that the Board was originally scheduled to complete before the end of 2009. Third, the Board seeks input on actions it might take when a foreign registered public accounting firm refuses to cooperate with an inspection request because of the firm's concern that such cooperation may violate local law.

In responding to the proposed rule amendment, I consider each issue from the perspective of the PCAOB's mission, "... to oversee the auditors of public companies in order to *protect the interests of investors* and to further the *public interest in the preparation of informative, fair, and independent audit reports*"(my emphasis).

**Postponement of Inspections of Foreign Registered Public Accounting Firms Originally Scheduled to be Completed Before the End of 2008**

The Board proposes to postpone the inspection of 21 (really 18 due to technical reasons) foreign registered public accounting firms, originally scheduled to be completed by the end of 2008, until the end of 2009. Under existing Board rules, 52 foreign registered public accounting firms were to be inspected for the first time by the end of 2008.

Therefore, the Board is deferring approximately 40 percent of the inspections required to be completed by the end of 2008 by an additional year. The number of firms not inspected on a timely basis is non-trivial, although the one-year deferral is relatively small. Since 2009 has already arrived, the Board's best option is to complete these inspections by the end of this year, which is consistent with the Board's proposal.

**Postponement of Inspections of Foreign Registered Public Accounting Firms Originally Scheduled to be Completed Before the End of 2009**

The Board proposes to postpone the inspection of 50 foreign registered public accounting firms, originally scheduled to be completed by the end of 2009, for up to three additional years (as late as 2012). Under existing Board rules, 70 foreign registered public accounting firms were to be inspected for the first time by the end of 2009. Therefore, the Board is deferring approximately 70 percent of the inspections required to be completed by the end of 2009 by up to an additional three years. Unlike the previous deferral, which is essentially unavoidable given the passage of time, this decision is not pre-ordained. Moreover, deferring a significant percentage (70%) of the required inspections by a non-trivial number of years (up to three) strikes me as potentially problematic.

The questions that need to be asked are how this deferral protects the interests of investors, and whether this deferral furthers the public interest in the preparation of informative, fair, and independent audit reports. There is both a short-term and an intermediate-term aspect to this decision. In the short-term, it is hard to argue that deferring inspections for up to an additional three years is in either the public interest or in investor interest. This is especially true since the Board, public accounting firm senior executives, and a growing body of academic studies find evidence that the PCAOB inspection process improves audit quality. However, the Board argues that these deferrals are at least partly to accommodate new audit regulators in foreign jurisdictions, and that investors are best served if the PCAOB can collaborate effectively with foreign regulators in conducting inspections of foreign registered public accounting firms.

Chairman Olson's comments at the PCAOB's Open Board Meeting indicate that the Board has sufficient resources to execute its originally planned inspection plan – "... our inspections have not been forestalled due to staffing or other resource constraint. We can meet our inspection goals with our current and projected resources." Given this fact, presumably the only reason to delay inspections due to be completed by the end of 2009 is as a good faith gesture to foreign oversight bodies, and the payoff to U.S. investors is a better working relationship with these foreign oversight bodies which the Board argues will lead to a superior inspection program. The cost of this decision is delayed inspections (by up to three years) and, presumably, a delay in the improvement to audit quality that is reasonably expected to follow from a Board inspection. Is this a good tradeoff for U.S. investors to make? I agree with comments from Board member Steve Harris that this is a "close call", but I would suggest that deferrals beyond 2009 are only reasonable for firms located in those countries that are making a good faith effort to develop strong auditor oversight bodies, preferably patterned closely after the PCAOB,

and that are working expeditiously to coordinate the necessary inspections with the Board. In other cases, no delay should be forthcoming.

I did find it curious that the Board has inspected non-U.S. firms located in Argentina, Australia, Bermuda, Brazil, Canada, Chile, Colombia, Greece, Hong Kong, India, Indonesia, Ireland, Israel, Japan, Kazakhstan, Mexico, New Zealand, Panama, Peru, Singapore, South Africa, South Korea, Taiwan, and the United Kingdom (footnote 9), whereas no firms have been inspected in countries such as Austria, Belgium, the Czech Republic, Denmark, Finland, France, Germany, Hungary, Italy, Luxembourg, Netherlands, Norway, Poland, Portugal, Spain, Sweden, Switzerland, and Turkey (partial list from footnote 10). These two lists reveal that a large number of the non-inspected firms are in Europe. So, I ask – will any delay allow the development of auditor oversight bodies in Europe (and certain other areas) or simply provide additional time for individuals in these countries to lobby for full reliance on foreign inspections (i.e., in such case the PCAOB will never be directly involved in inspecting firms in these countries). If the former, the proposed delay, while regrettable and potentially costly to U.S. investors, represents a reasonable accommodation; if the latter, any delay is not only unwise but it would serve to reward obstructionist behavior, behavior that clearly is at odds with U.S. law and with the best interests of U.S. investors.

The proposed rule amendments include certain provisions designed to minimize any adverse consequences with delaying inspections originally planned to be completed by the end of 2009. First, the Board's inspection plan would focus on inspecting foreign registered public accounting firms based on the size of U.S. clients audited (based on market capitalization). Firms auditing clients that constitute 35 percent of the total market capitalization would be inspected by the end of 2009, and firms auditing clients that constitute 90 percent of the total market capitalization would be inspected by the end of 2010. This plan represents a reasonable accommodation if the Board adopts the proposed three-year inspection delay. In addition, the Board proposes to include on its web site a list of firms not yet inspected within four years of the end of the calendar year when the firm first issued an audit report while registered with the Board. This type of transparency will enable investors to discount, if they deem appropriate, the quality of earnings reported by companies audited by these non-inspected firms. Although companies (and auditors) may oppose this provision, such disclosure is clearly in the best interest of investors. If this disclosure doesn't matter than investors will not react to it. Conversely, if the disclosure does matter, and investors react, than investors were rightly entitled to this information.

### **Failure of a Foreign Registered Public Accounting Firm to Cooperate with an Inspection Request**

The Board seeks comment on how it might proceed when a foreign registered public accounting firm fails to cooperate with an inspection request because of a concern that such cooperation might violate local law. Although firms that fail to cooperate may feel they have little choice, the Board's failure to aggressively address such non-cooperation could lead to regulatory arbitrage. Taken to the extreme, those U.S. companies seeking

maximum ability to manage earnings (alternatively, those companies seeking minimal audit quality) could retain an audit firm located in a jurisdiction that does not permit PCAOB inspections. Such a development would frustrate the Board's attempts to improve financial reporting quality in the U.S.

Foreign registered accounting firms knew they were to be inspected when they registered with the Board, and numerous firms located in a large number of foreign countries have cooperated with PCAOB inspections. If these firms were aware of legal obstacles to complying with PCAOB inspections, they should not have registered with the Board. Moreover, presumably the U.S. Congress was aware of these issues when they passed the Sarbanes-Oxley Act, and yet the law was written to require foreign firms to follow the same PCAOB rules as U.S. firms. Any accommodation for foreign firms should come from Congressional action and not from PCAOB inaction. Failure of a foreign registered accounting firm to permit a Board inspection should lead to PCAOB revocation of the firm's registration. Until such revocation of registration is effective, the Board's proposed disclosures (p. 17) are likely to be effective in providing transparent disclosure to U.S. investors of those firms not inspected due to non-cooperation, including the involvement of these firms in auditing subsidiaries of U.S. domestic firms. Finally, if the Board chooses not to revoke the registration of these firms, it might consider establishing a PCAOB office in certain foreign countries, staffed by foreign nationals, to conduct the necessary inspections, and to charge the incremental costs of staffing these offices to the registered firms located in the country.

Thank you for the opportunity to have commented on the PCAOB's proposal to defer the inspection of certain registered foreign accounting firms.

Sincerely,

A handwritten signature in blue ink that reads "Joseph V. Carcello". The signature is written in a cursive, flowing style.

Joseph V. Carcello  
Ernst & Young Professor  
Director of Research – Corporate Governance Center



FINANCIAL SERVICES AGENCY  
GOVERNMENT OF JAPAN

3-2-1 Kasumigaseki Chiyoda-ku Tokyo 100-8967 Japan

February 2, 2009

The Office of the Secretary,  
The Public Company Accounting Oversight Board  
1666 K Street, N.W.,  
Washington, D.C. 2006

**Re: PCAOB Rulemaking Docket Matter No. 027—Comment on rule amendments concerning the timing of certain inspections of non-U.S. firms, and other issues relating to inspections of non-U.S. firms**

Dear PCAOB members:

The Certified Public Accountants and Auditing Oversight Board of Japan (CPAAOB) and the Financial Services Agency of Japan (FSA) appreciate this opportunity to comment on "*Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms*". We highly commend the PCAOB (the Board) for its efforts to conclude the amendments of the rule in a transparent manner. We believe it is essential both for the PCAOB and us to develop a practical cooperative framework when dealing with cross-border issues; thus we would highly appreciate if the Board could give due consideration to our comments before finalizing the rule. Please note that our comments are limited to Part-II "Registered firms' obligations".

We are fully aware that independent audit regulators, such as the PCAOB and the CPAAOB/FSA, pursue common responsibilities to enhance public interests and investor protection in relevant jurisdictions through promoting higher quality audits. We understand the PCAOB's legitimate intention in the proposed amendments with a view to accessing necessary information held by registered foreign audit firms so as to fulfill its statutory responsibilities.

However, one complicated aspect here is that this issue is of a cross-border nature. Each country or jurisdiction has a different legal and regulatory framework and different thoughts to sovereignty. In principle, we believe it is necessary for a country or jurisdiction to give due consideration to the sovereignty and the national legal and regulatory framework of its counterpart when dealing with cross-border issues. This audit oversight area is no exception.

Especially, we would like to draw your attention to P.16 of the release which states, "*The Board could impose disciplinary sanctions in any case where a violation of Rule 4006 is established*", followed by the footnote 35 that "*the Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a*

*sufficient defense in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection”.*

Non-U.S. audit firms will find themselves in an extremely difficult position and may not concur with the rationale for why the disciplinary sanctions are taken against them, where violation of Rule 4006 occurs merely on the basis of non-U.S. legal or regulatory restrictions or sovereignty concerns that they have no control over. In this context, we suggest that the PCAOB closely consult with the competent supervisory authorities of relevant jurisdictions first to find out the background and reasons associated with the violation and seek a better solution.

In a broader context, the PCAOB may wish to explore an approach moving towards reliance on other audit oversight authorities with a principle of the “home-country based approach”, which we suggested in our public comment letter to the Board on the 4<sup>th</sup> of March, 2008 on your proposed policy statement “*Guidance Regarding Implementation of PCAOB Rule 4012*”, provided that they are found to be as independent and robust as the Board.

In addition, the Board may wish to work nationally in order to resolve the difficulties by talking with legislators about changing the legislation -- Sarbanes-Oxley Act of 2002.

We thank you again for this opportunity, and look forward to continuing dialogue in the future. Should you have any questions, please do not hesitate to contact us.

Sincerely yours,



Nobuyuki KINOSHITA  
Secretary General  
Certified Public Accountants and Auditing  
Oversight Board  
Government of Japan



Junichi MARUYAMA  
Deputy Commissioner for International Affairs  
Financial Services Agency,  
Government of Japan



Office of the Secretary  
Public Company Accounting Oversight Board (PCAOB)  
1666 K Street, N.W.  
Washington, DC 2006, U.S.A.  
E-mail to: comments@pcaobus.org

中国北京西城区金融大街19号富凯大厦100032  
Focus Place, 19 Jinrong Street  
Xicheng District, Beijing, P.R. China 100032  
Tel: (8610)66210205 Fax: (8610)66210206  
e-mail: intl@csrc.gov.cn; http://www.csrc.gov.cn

January 22, 2009

**RE: PCAOB Rulemaking Docket Matter No.027**

Dear Sir/Madam,

On behalf of China Securities Regulatory Commission (CSRC), we are writing to respond to the *Release No.2008-007, Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, And Other Issues Relating To Inspections Of Non-U.S. Firms, PCAOB Rulemaking Docket Matter No.027* (hereinafter referred to as "Release").

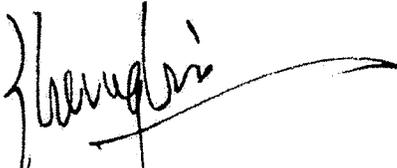
We have no objection towards PCAOB's amendments to the inspection frequency requirements of *Rule 4003* to postpone the timelines of inspections. Nevertheless, with regard to the inspection of Non-U.S firms, we hold it true that successful cross-border cooperation can only be achieved when certain general principles are practiced. Such principles may include, but not limited to, (1) equality and reciprocity; (2) observing laws in both jurisdictions and being to the common interests; (3) facilitating cross-border financial activities rather than creating obstacles; (4) respecting the consensus already reached between regulators instead of resorting to a unilateral departure from existing cooperative framework.

We are afraid that under the current Chinese laws and regulations, PCAOB is not allowed to perform any form of independent or joint on-site inspection in the Chinese territory. We hope PCAOB understand our standing, and continue the close communication and cooperation with Chinese regulators in our joint effort to safeguard our cross-border financial activities.

We would welcome the PCAOB to take the above mentioned points into consideration when deciding the amendments to its Rule 4003.

Sincerely yours,

TONG Daochi



ZHOU Zhonghui



Director-General  
Department of International Affairs  
China Securities Regulatory Commission

Chief Accountant  
China Securities Regulatory Commission

-----Original Message-----

From: Jack Ciesielski [mailto:jciesielski@accountingobserver.com]

Sent: Monday, February 02, 2009 1:39 PM

To: Comments

Subject: Docket 27

February 2, 2009

Public Company Accounting Oversight Board

Office of the Secretary

1666 K Street, NW

Washington, DC 20006-2803

I wish to comment on Rulemaking Docket 027: "Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms."

With some reservations, I support the amendment's adjustment for the timing of inspections of non-U.S. firms. I believe that the inspections are vital to the interests of U.S. investors and in the building of their confidence in the auditing profession. The importance of those non-U.S. inspections has been amplified by the current events involving Satyam in India. While not directly affecting investors here in the United States, it does have a negative effect on their overall confidence. As we know all too well, confidence matters tremendously in our current economic state.

The inspections are critical, and so is their proper execution; therefore I support the extended timetable so the inspections are done with due care and diligence. I believe there needs to be an offset, however, and I also support a public listing of those yet-to-be-inspected firms in a very obvious place in the PCAOB website. Further, I am concerned that the extended timetable might be extended indefinitely if there isn't public visibility into the progress being made. I would recommend that the PCAOB make an accounting to the public /at least /twice a year of its progress in the inspections, including an expected timetable for completion and a description of the barriers/impediments to completing all 50 inspections within the extended time frame.

Thank you for the opportunity to comment. If you have any questions, please don't hesitate to contact me. Best regards.

Sincerely,

Jack Ciesielski

\* \* \* \* \*

R.G. Associates, Inc.  
201 N. Charles Street, Ste. 806  
Baltimore, MD 21201-4132

Phone: (410)783-0672 x101  
Fax: (410)783-0687  
E-mail: [jciesielski@accountingobserver.com](mailto:jciesielski@accountingobserver.com)  
Website: [www.accountingobserver.com](http://www.accountingobserver.com)  
Weblog: [www.accountingobserver.com/blog](http://www.accountingobserver.com/blog)



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

February 2<sup>nd</sup>, 2009

*Subject : PCAOB Rulemaking Docket Matter n°027 - Request for public comment on proposed amendment to Rule 4003 concerning the timing of certain inspections of non-US firms and other issues relating to inspections of non-US firms*

Dear Mr. Seymour,

The CNCC ("Compagnie Nationale des Commissaires aux Comptes", the French Body of statutory auditors) is very pleased to have the opportunity to provide its comments on the proposed amendment to Rule 4003 of the Public Company Accounting Oversight Board (the "PCAOB" hereafter) concerning the timing of certain inspections of non-US firms and other issues relating to inspections of non-US firms.

The CNCC strongly supports the goal of the PCAOB to improve the quality of the inspections, on a longer term. CNCC nevertheless considers that mutual recognition and full reliance on third country public oversight bodies is the only practicable solution. As there are convergences between the proposed policy statement Rule 4012 and the provisions of the EU Audit Directive, the CNCC strongly urges the US and non-US oversight systems to strive to work towards reaching reciprocity, harmonization, and cooperation to better inspection process, even when full reliance cannot be achieved in the short term.

The significant benefits from a true "full reliance" approach would be increased opportunities to expand the focus of inspections on audit quality thereby better protecting investors, cost savings for oversight bodies and audit firms through the elimination of duplication of inspections, but also to prevent significant conflicts of laws and regulations for companies and audit firms, by recognizing the sovereignty of third countries.

In Europe, and therefore France, audit firms cannot be considered as responsible for the delay in PCAOB inspections, as adequacy decision of the European Commission has to take place first, in accordance with Article 47 of the Audit Directive. Moreover, in France, conflicts of law should be avoided, as due to strong French professional Secrecy laws, they cause a major issue.

... / ...

If, as stated in page 16 of the proposed document, “a registered firm's failure or refusal to provide requested information is a violation of Rule 4006 and is inconsistent with the condition reflected in Section 102(b)(3)” and “the Board could impose disciplinary sanctions in any case where a violation of Rule 4006 is established”, with the associated footnote 35 of a particular concern in this respect, underlining that “the Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection”, then the PCAOB Proposed Rule Amendments would force the French firms to choose between violating either their home country laws and regulations, or the PCAOB Rules. It is not for the firms to make this choice.

The CNCC respectfully submit its detailed comments below, and commend the Board for the transparency of its rule deliberation process.

**# 1 – CNCC comments on whether there are other factors that should be treated as a reason to consider moving an inspection to an earlier year (page 13).**

In general, the CNCC agrees with the Board’s approach in regard to the proposed extension of the deadline for some 2009 inspections as well as with the factors that may cause the acceleration of some of these inspections. The CNCC strongly urges the PCAOB and the non-US oversight systems to find common grounds in the area of jurisdiction-level work.

**# 2 – CNCC comments on whether it is appropriate that the PCAOB maintain on its web site an up-to-date list of all registered firms that have not yet had their first inspection as a means to provide public transparency related to delayed inspections. Are there other suitable alternatives (page 14)?**

The CNCC disagrees with the Board’s approach in regard to “web-listing” non-US firms that have not been inspected within the SOA required schedule. Although it may be consider more transparent, a “Web-listing” of non-US firms may be viewed as a negative mark against firms which have not yet been reviewed.

The CNCC believes that web-listing non-US firms in order to provide public transparency related to delayed inspections will be counter-productive and its costs will outweigh its benefits. Non US oversight systems may take reciprocal measures if this idea is implemented which can threaten the spirit of cooperation built since the inception of the board.

**# 3 – CNCC comments on whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006 (page 16).**

See comments above.

... / ...

In addition, the CNCC believes strongly that the Board and its non-US counterparts must exhaust all of the jurisdiction-level work before reaching the point of mutual disciplines and remedial sanctions. Non-US oversight systems that raise non-cooperation with the Board on legal restriction or sovereignty grounds are not doing so gingerly. It is a fundamental issue of legal sovereignty.

**# 4 – CNCC comments on whether there are possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information (page 17).**

The CNCC does not believe that there are any other possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information if due to the fact that non-cooperation is based on a non-US legal restriction or sovereignty concern.

**# 5 – CNCC comments on whether there are potential benefits and drawbacks of a rule along the lines described above (page 17).**

The CNCC believes that there are no potential benefits but only drawbacks of a rule along the lines described. These potential disclosures do not add any value to the quality of the audit engagement work or to the quality control systems of the principal auditor.

**# 6 – CNCC comments on whether there are generally other possible rulemaking approaches relating to those issues that might provide useful disclosure to investors or otherwise be in the public interest (page 18).**

The CNCC believes that there are generally no other possible rulemaking approaches relating to those issues that might provide useful disclosure to investors or otherwise be in the public interest. Non-US oversight systems that do not cooperate with the Board by refusing to provide information on the grounds that it may violate their sovereignty are in fact calling for negotiations with the Board. They want these negotiations to remain in the legal arena, not in the audit arena.

Yours sincerely,



Vincent Baillot  
President,

*Compagnie Nationale des Commissaires aux Comptes*



## Consumer Federation of America

February 2, 2009

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

Re: PCAOB Rulemaking Docket Matter No. 027

Dear Sir or Madam:

I am writing on behalf of the Consumer Federation of America (CFA)<sup>1</sup> to offer our reluctant and conditional support for the proposal to delay for up to three years first inspections of some foreign audit firms that play a significant role in the audits of U.S. public companies. It is highly unfortunate that such a delay is necessary. We do not share the Board's view that this proposal is "consistent with the Act, the public interest, and the protection of investors." However, it does not appear that the Board has left itself any options for addressing the current situation that meet that standard. This proposal appears to offer the best solution available.

Our support for the proposed inspection delay is conditioned on the following factors:

- ◆ **There must be no further delays.** Inspections of foreign audit firms must not follow the pattern of Section 404 implementation for small public companies, where delay follows delay and investors are denied essential protections promised by the Sarbanes-Oxley Act. Nothing is more central to the act than its requirement for independent oversight, including regular inspections, of those firms that audit U.S. public companies. Application of that requirement to foreign audit firms was adopted after thorough debate and must not be undermined either by the Board or by foreign entities that seek to impede its compliance with the law. Under no circumstances will we support further delays beyond those contemplated by this rulemaking.
- ◆ **There must be transparency.** The proposal includes two provisions designed to ensure the transparency both of the schedule for conducting inspections and those firms that have not been inspected. Publishing an inspection schedule should make it more difficult for countries to exert behind-the-scenes pressure to further delay implementation. Our experience to date indicates this is a necessary discipline on the process. In addition,

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<sup>1</sup> CFA is a non-profit association of nearly 300 national, state and local pro-consumer organizations. It was founded in 1968 to represent the consumer interest through research, education and advocacy.

publishing the names of uninspected firms will not only provide investors with valuable information they are entitled to receive, it will also provide those firms and the U.S. firms and public companies that rely on their work with an incentive to support timely inspections rather than seek continued delays. We do not support the proposal unless both these conditions are included without weakening amendments.

- ◆ **There must be accountability.** Going forward, it is not enough that we simply publish the names of firms that have not been inspected; there must be meaningful sanctions for firms that fail to comply with the U.S. inspection requirement. Recently, our policy in this area has been all carrot and no stick. Foreign jurisdictions have been given to understand that there will be no serious consequences for those who erect barriers to prevent U.S. inspections; on the contrary, they have been led to believe that the reward for non-cooperation would be a policy change from one of joint inspections to one of full reliance. That must end. While we support a cooperative approach to inspections where possible, we adamantly oppose fully relying on foreign oversight bodies to perform those inspections (as we have explained in detail elsewhere). We are hopeful that a decisive statement from the new administration that the full reliance proposal is off the table, combined with a clear commitment from the PCAOB to pursue sanctions for non-compliance, can bring foreign jurisdictions to the table to discuss a cooperative approach to joint inspections that benefits investors both here and abroad.
- ◆ **There must be improvements to the quality of foreign audits.** While the delay is unfortunate, investors could ultimately benefit if the Board uses the added time provided by the delay to address troubling weaknesses that have been identified with the quality of its inspections of foreign firms. In particular, steps must be taken to improve the risk assessments and pre-audit planning for foreign inspections, to better evaluate regional quality control functions relied on by global accounting networks, and to focus on risks related to referred work on audits of multi-national companies. Going forward, we must be confident that the audits of foreign firms are not only timely but of high quality.

Certain objections to this proposal are easy to predict. The first likely objection relates to respect for “sovereignty.” However, the requirement for PCAOB audits of foreign audit firms is designed to protect U.S. investors by ensuring compliance with U.S. laws and regulations in the audits of U.S. public companies. It is simply unreasonable for foreign oversight bodies – which do not have extensive expertise in U.S. laws and regulations – to erect and maintain barriers that prevent the Board from fulfilling its investor protection obligation in this regard. This would be a concern even if significant deficiencies in the independence, inspection procedures, and operational capacity of foreign oversight bodies had not been identified. Under the circumstances, it is unacceptable. It is also frankly incomprehensible why foreign oversight bodies don’t welcome the opportunity to have added resources brought to bear on a function that is essential to protect investors and promote market integrity.

A second, related objection certain to be raised is one of fairness. Foreign firms are likely to object that they should not be sanctioned for violations that result from home country laws preventing U.S. inspections, restrictions over which they have no control. This argument elevates concerns over repercussions to audit firms over concerns over repercussions to

investors, who have a right to expect that those firms that play a significant role in the audits of U.S. public companies are subject to oversight on the same terms as and to the same degree as U.S. firms. Moreover, it understates in our view the degree to which foreign audit firms have worked hand-in-hand with their home-country oversight bodies to impede U.S. inspections. Imposing meaningful sanctions for non-compliance – specifically the threat that their ability to audit U.S. public companies will be forfeit – may force those firms, and the companies they audit, to reconsider where their interests lie and use their influence with home-country oversight boards to encourage a more cooperative approach to joint inspections. That would benefit all investors.

The sanctions must be meaningful, however. Simple disclosure requirements, as outlined in the proposal, would not be adequate, first, because they do not satisfy the demands of the Sarbanes-Oxley Act and, second, because they do not offer adequate assurances of a quality audit to investors.

To some extent, the Board is responsible for the awkward situation in which it now finds itself, forced to choose between delaying statutorily mandated inspections or forcing firms to comply with inspection requests over the objections of their home-country regulatory authorities. By rolling out its full reliance proposal, the Board sent a clear message that non-cooperation by foreign oversight boards would be rewarded. The proposal's statement that "the Board does not intend ... to make any further adjustments to the inspection frequency requirements" is long overdue. We expect the Board to keep that pledge with respect to firms due to be inspected in 2008 and beyond.

Respectfully submitted,



Barbara Roper  
Director of Investor Protection

cc: Mark Olson, Chairman, PCAOB  
Daniel Goelzer, PCAOB Board Member  
Bill Gradison, PCAOB Board Member  
Steven Harris, PCAOB Board Member  
Charles Niemeier, PCAOB Board Member  
Mary Schapiro, Chairman, U.S. Securities and Exchange Commission

# COUNCIL OF INSTITUTIONAL INVESTORS

Suite 500 • 888 17<sup>th</sup> Street, NW • Washington, DC 20006 • (202) 822-0800 • Fax (202) 822-0801 • [www.cii.org](http://www.cii.org)

## Via Email

February 2, 2009

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

*Re: PCAOB Rulemaking Docket Matter No. 027*

Dear Mr. Seymour:

I am writing on behalf of the Council of Institutional Investors (“Council”) in response to the Public Company Accounting Oversight Board’s (“PCAOB” or “Board”) “Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms” (“Release”).<sup>1</sup> We appreciate the opportunity to provide our comments on the Release.

The Council is a nonprofit association of more than 140 public, union and corporate pension funds with combined assets that exceed \$3 trillion. Our member funds have fiduciary obligations to the millions of Americans whose retirement savings are invested through them.<sup>2</sup> Accordingly, the Council seeks to address investment issues that affect the size or security of plan assets.

As major long-term shareowners, the Council’s members have a keen interest in the health and integrity of the global capital market system. That interest is reflected in the Council’s policies that express our belief that “the efficiency of global markets—and the well-being of the investors who entrust their financial present and future to those markets—depends, in significant part, on the quality, comparability and reliability of the information provided by *audited* financial statements and disclosures.”<sup>3</sup> That interest is also reflected in the Council’s long-standing public support of the PCAOB and its vital role in restoring confidence of the investing public in financial reporting.<sup>4</sup>

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<sup>1</sup> Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms 1 (proposed Dec. 4, 2008) [hereinafter *Release*], [http://www.pcaobus.org/Rules/Docket\\_027/2008-12-04\\_Release\\_No\\_2008-007.pdf](http://www.pcaobus.org/Rules/Docket_027/2008-12-04_Release_No_2008-007.pdf).

<sup>2</sup> Additional information about the Council of Institutional Investors (“Council”) and its members is available at <http://www.cii.org/about>.

<sup>3</sup> Council Policies on Other Governance Issues, Independence of Accounting and Auditing Standard Setters 1 (updated Oct. 7, 2008) (emphasis added), [http://www.cii.org/UserFiles/file/council%20policies/CII%20Policies%20on%20Accounting%20and%20Auditing%2010-7-08\(1\).pdf](http://www.cii.org/UserFiles/file/council%20policies/CII%20Policies%20on%20Accounting%20and%20Auditing%2010-7-08(1).pdf).

<sup>4</sup> See, e.g., Brief of Amicus Curiae Council in Support of Defendants-Appellees & Urging Affirmance at 1, Free Enter. Fund v. PCAOB, No. 07-5127 (D.C. Cir. Feb. 21, 2008) (on file with Council), *available at* <http://law.du.edu/images/uploads/corporate-governance/fef-pcaob-amicus-cii.pdf>.

In fulfilling its responsibilities to investors, perhaps the most important function of the PCAOB is its inspections of registered firms. Those inspections not only involve reviewing auditors for technical compliance of standards, but delve into the broader business context of a firm's audit practices and influences on those practices.

In our view, regular and rigorous inspections by the PCAOB of U.S. and non-U.S. registered firms is critical to improving the odds of detecting violations of auditing standards, auditor-independence rules, and other substandard audit practices and influences.<sup>5</sup> Without prompt detection and correction of audit issues of concern, the issues may metastasize into major problems that unnecessarily corrode investor confidence and impair the efficient operation of the capital market system.<sup>6</sup> It is on this basis that we address the following specific matters raised by the Release.

### Extension of Deadline for Inspections

Given our aforementioned view of the importance of *regular* and rigorous inspections by the PCAOB of U.S. and non-U.S. registered firms, we obviously have great concern with the Release's proposal to "allow the Board to postpone, for up to three years, the first inspection of any non-U.S. firm that the Board is currently required to conduct by the end of 2009 and that is in a jurisdiction where the Board has not conducted an inspection before 2009."<sup>7</sup> Our concern has only grown in recent weeks with the daily press reports about Satyam Computer Services Ltd. accounting scandal and related allegations that the PCAOB inspection process has "gaping holes."<sup>8</sup> Our concern, however, is somewhat tempered by the comments of Board Member Charles D. Niemeier that the extension "allow us to do a better inspection in the end" by using the deferral period to improve certain aspects of the inspection process.<sup>9</sup> Our support for this proposal is, therefore, contingent on the final rule including or being accompanied by, at a minimum, the following conditions to ensure that the quality of the Board's inspections of U.S. and non-U.S. registered firms becomes "better" and more responsive to the needs of investors going forward:

- The scope of the final rule does not extend beyond the proposed "subset of first-time inspections" and the length of the extension does not extend beyond the proposed three-year period.<sup>10</sup>
- The final rule is accompanied by a commitment by the Board to prominently and conspicuously disclose on the PCAOB website:
  - A list of all registered firms that have not yet been inspected by the PCAOB under the Board's original timeframe.<sup>11</sup>

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<sup>5</sup> *Id.* at 19.

<sup>6</sup> *Id.* at 20.

<sup>7</sup> *Release, supra* note 1, at 10-11.

<sup>8</sup> Subramaniam Sharma et al., *India's Enron Puts Auditors Back Under Scrutiny*, Bloomberg.com, Jan. 13, 2009, at 1, [http://www.bloomberg.com/apps/news?pid=20601109&sid=aov\\_laRpSmno&refer=home](http://www.bloomberg.com/apps/news?pid=20601109&sid=aov_laRpSmno&refer=home).

<sup>9</sup> Statement of Board Member Charles D. Niemeier, Open Board Meeting To Consider a Recommendation to Adopt an Amendment to Rule 4003 as it Applies to Certain Non-U.S. Registered Public Accounting Firms, and Seek Public Comment on Other Proposals Also Related to the Inspections of Non-U.S. Firms 1 (Dec. 4, 2008) [hereinafter *Niemeier*], [http://www.pcaobus.org/News\\_and\\_Events/Events/2008/Speech/12-04\\_Niemeier.aspx](http://www.pcaobus.org/News_and_Events/Events/2008/Speech/12-04_Niemeier.aspx).

<sup>10</sup> See Statement of Chairman Mark W. Olson, Open Board Meeting to Consider a Recommendation to Adopt an Amendment to Rule 4003 As It Applies to Certain Non-US Registered Public Accounting Firms, and Seek Public Comment on Other Proposals Also Related to the Inspections of Non-US Firms 1 (Dec. 4, 2008), [http://www.pcaobus.org/News\\_and\\_Events/Events/2008/Speech/12-04\\_Olson.aspx](http://www.pcaobus.org/News_and_Events/Events/2008/Speech/12-04_Olson.aspx).

<sup>11</sup> See Statement of Board Member Daniel L. Goelzer, Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms and Other Issues Related to Inspections of Non-U.S. Firms 1 (Dec. 4, 2008) [Hereinafter *Goelzer*], [http://www.pcaobus.org/News\\_and\\_Events/Events/2008/Speech/12-04\\_Goelzer.aspx](http://www.pcaobus.org/News_and_Events/Events/2008/Speech/12-04_Goelzer.aspx); Statement of Board

- A list of the countries in which PCAOB inspections will be performed in the next twelve months<sup>12</sup>
- The final rule is accompanied by a Board directive to the PCAOB inspection division to promptly develop and implement a strategy to:
  - Begin inspecting those non-U.S. firms whose inspections have been deferred under the final rule based on the total market capitalization schedule described in the Release and adjusted on an ongoing basis for the presence of any risk factors that the Board believes are appropriate to consider in protecting investors<sup>13</sup>
  - Evaluate quality control functions in the context of local non-U.S. inspections<sup>14</sup>
  - Evaluate the “substantial risk that referred work on multi-national audits presents” to investors,<sup>15</sup> and
- The final rule is accompanied by a Board directive to the PCAOB Office of Research and Analysis to promptly develop and implement a strategy for providing planning advice for non-U.S. firm inspections consistent with the existing practice of providing such advice for U.S. firm inspections.<sup>16</sup>

### Transparency Concerning Delayed Inspections

As previously indicated, we support the Board’s proposed practice, described in the Release, to maintain “on its web site an up-to-date list of all registered firms that have not yet had their first Board inspection even though more than four years have passed since the end of the calendar year in which they first issued an audit report while registered with the Board.”<sup>17</sup> We agree with Board Member Daniel L. Goelzer that such a list “would afford investors transparency concerning cases in which they may be relying on audit reports of firms that have not been inspected according to the Board’s normal schedule.”<sup>18</sup>

### Registered Firms’ Obligations

We support the Board’s continuing efforts, described in the Release, “to develop cooperative relationships with its foreign counterparts” to enhance its ability to make timely and rigorous inspections of non-U.S. registered firms.<sup>19</sup> We also understand that “non-U.S. legal restrictions or the sovereignty concerns” may hinder the ability of the Board to conduct those inspections.<sup>20</sup> We, however, do not support any easing of Board sanctions on those non-U.S. firms that may be subject to such legal restrictions or sovereignty concerns.

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Member Steven B. Harris, Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms and Other Issues Related to Inspections of Non-U.S. Firms 1 (Dec. 4, 2008),

[http://www.pcaobus.org/News\\_and\\_Events/Events/2008/Speech/12-04\\_Harris.aspx](http://www.pcaobus.org/News_and_Events/Events/2008/Speech/12-04_Harris.aspx).

<sup>12</sup> See *Goelzer*, *supra* note 11, at 1.

<sup>13</sup> *Id.*

<sup>14</sup> *Niemeier*, *supra* note 9, at 1.

<sup>15</sup> *Id.* This condition appears particularly important in light of allegations that have arisen in the Satyam Computer Services Ltd. accounting scandal that the application and enforcement of auditing standards in India and many other countries “are not always what we’d expect them to be in North American or Western Europe.” *Shamra*, *supra* note 8, at 1.

<sup>16</sup> *Niemeier*, *supra* note 9, at 1.

<sup>17</sup> *Release*, *supra* note 1, at 14.

<sup>18</sup> *Goelzer*, *supra* note 11, at 1.

<sup>19</sup> *Release*, *supra* note 1, at 15.

<sup>20</sup> *Id.* at 16.

In our view, the Release fails to make a compelling case that investors would benefit from the imposition of weaker sanctions on those non-U.S. registered firms that decline PCAOB inspections based on non-U.S. legal restrictions or sovereignty concerns. Moreover, imposing weaker sanctions on those firms might have the perverse effect of lessening the incentive of those firms and other interested parties to actively advocate for the elimination of those restrictions or concerns.

Finally, we do not oppose the Board's consideration of a proposed rule, as described in the Release, that would require a principal auditor that "has failed to provide information in response to an inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns, [or who has used the work of any registered firm that has failed to provide such information] . . . to disclose that fact [and other related information] as part of, or in connection with, its audit report."<sup>21</sup> The extensive disclosures set forth in the Release would likely provide investors with useful information in evaluating the quality of the contents of the financial reports audited by those firms. If, however, such a proposed rule is pursued by the Board, it should not, in our view, serve as a replacement for the sanction of deregistering a firm when, after reasonable efforts by the PCAOB, the firm cannot or will not cooperate with the PCAOB's inspections.

Once again, we appreciate the opportunity to comment on the Release. Please feel free to contact me with any questions or comments at [jeff@cii.org](mailto:jeff@cii.org) or at 202.261.7081.

Sincerely,

A handwritten signature in cursive script that reads "Jeff Mahoney".

Jeff Mahoney  
General Counsel

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<sup>21</sup> *Id.*



Office of the Secretary  
PCAOB  
1666 K Street, N. W.  
Washington, DC 2006  
comments@pcaobus.org

January 30, 2009  
Case PCAOB  
/pkj

### PCAOB Rulemaking Docket Matter No. 027

The Public Company Accounting Oversight Board (“Board” or “PCAOB”) has requested for comments regarding Release No. 2008-007, Rule Amendments Concerning the Timing of Certain Inspections of non-U.S. Firms, and Other Issues Relating to Inspections of non-U.S. Firms, PCAOB Rulemaking Docket Matter No. 027 (the “Release”).

The Board is seeking comments on adopted and proposed amendments which postpone inspections of certain inspections of foreign registered public accountant firms. Furthermore the Board seeks comments on other issues and concepts related to inspections of non-U.S. firms, specifically on possible Board action in the event an non-U.S. firm declines to comply with an inspection demand because of a concern that doing so may violate the firm’s local law.

We welcome the opportunity to comment on the Release.

We support the adopted and proposed amendments of Rules 4003 which postpone the inspections of certain foreign accountant firms and the Board’s cooperative approach in carrying out its inspections.

Recognizing the requirements of the Board to carry out inspections of foreign accounting firms we believe that this should only take place in cooperation with local authorities where such authorities exist.

In Denmark a statutory quality assurance system has been in place since 2003 which covers all Danish accounting firms and auditors. July 1, 2008, a new Act on approved Auditors and Audit Firms entered into force. The new act has implemented a new EU Directive on statutory Audits (Directive 2006/43/EC).

#### **DANISH COMMERCE AND COMPANIES AGENCY**

Kampmannsgade 1  
DK-1780 København V  
Denmark

Tel +45 33 30 77 00  
Fax + 45 33 30 77 99  
VAT no. 10 15 08 17  
eogs@eogs.dk  
www.eogs.dk

#### **MINISTRY OF ECONOMIC AND BUSINESS AFFAIRES**

The provisions in Article 47 of the Directive regarding cooperation with third country audit regulator have been implemented in Section 48 of the Danish Act. This means that transfer of audit working papers and other documents held by auditors or audit firms can only take place via the Danish Commerce and Companies Agency. Auditors and audit firms are not allowed to transfer such papers. Doing so will be a violation of the Danish act and disciplinary actions will be taken.

Several conditions must be fulfilled before the Danish Commerce and Companies Agency can cooperate with PCAOB. This includes among other

- the European Commission has adopted a decision on adequacy of PCAOB
- a reciprocity agreement has entered into force between the Danish Commerce and Companies Agency and PCAOB
- the transfer of audit working papers and other documents respects the Danish Act on Approved Auditors and Audit Firms and the Danish Act on Processing of Personal Data.

The European Commission is expected to make an adequacy during 2009. When the decision has been adopted we will be in a position to discuss a reciprocity agreement between the Danish Commerce and Companies Agency and PCAOB.

A postponement of inspections of Danish audit firms therefore will put PCAOB into a position to comply with the inspection requirement.

The Release is addressing the timing of inspection foreign audit firms. We recommend that the timing of inspections of Danish audit firms takes into account the above. We believe that this is in the interest of PCAOB, investors and the issuer.

Finally, I can inform you that this letter does not prejudice the comments to the Release sent by the European Commission on behalf of the European Union.

If you have any questions, please do not hesitate to contact me.

Yours sincerely,

Peter Kroglund Jensen  
Chief Special Advisor  
Danish Commerce and Companies Agency

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Deloitte Touche Tohmatsu  
1633 Broadway  
New York, NY 10019-6754  
USA

Tel: +1 212 492 4000  
Fax: +1 212 492 4001  
[www.deloitte.com](http://www.deloitte.com)

February 2, 2009

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

*Re: Request for Public Comment on Rule Amendments Concerning The Timing Of Certain Inspections Of Non-U.S. Firms, And Other Issues Relating To Inspections Of Non-U.S. Firms (PCAOB Release No. 2008-007, Dec. 4, 2008, PCAOB Rulemaking Docket Matter No. 027)*

This letter is submitted on behalf of Deloitte Touche Tohmatsu and member firms of Deloitte Touche Tohmatsu. We are pleased to respond to the request for comments from the Public Company Accounting Oversight Board (the “PCAOB” or the “Board”) on its Rule Amendments Concerning The Timing Of Certain Inspections Of Non-U.S. Firms, And Other Issues Relating To Inspections Of Non-U.S. Firms (PCAOB Release No. 2008-007, Dec. 4, 2008, PCAOB Rulemaking Docket Matter No. 027) (the “Release”).

In the Release, the Board requests comment on a series of related matters, as follows: (1) a proposed rule amendment that would “postpone, for up to three years, the first inspection of any non-U.S. firm that the Board is currently required to conduct by the end of 2009 and that is in a jurisdiction where the Board has not conducted an inspection before 2009”; (2) the appropriateness of “maintaining on its web site an up-to-date list of all registered firms that have not yet had their first Board inspection even though more than four years have passed since the end of the calendar year in which they first

issued an audit report while registered with the Board”<sup>1</sup>; and (3) establishing an approach for sanctions and disclosures for non-U.S. firms that fail to cooperate with a Board information request.<sup>2</sup> The Board also announced, in the Release, the adoption of a related rule that will extend until 2009 the deadlines for inspections of non-U.S. firms that were originally set for 2008 and not completed.

First, as the Board notes, the delay in inspections should be used to continue developing cooperative working relationships with non-U.S. oversight authorities, as “[t]here is long-term value in accepting a limited delay in inspections to continue working toward cooperative arrangements where it appears reasonably possible to reach them.”<sup>3</sup> We strongly support the Board’s efforts to establish cooperative relationships with non-U.S. oversight authorities.<sup>4</sup> We believe that these efforts will be a key step in achieving a system whereby one country’s oversight authority relies on the results of an inspection performed by the home country oversight authority to satisfy its own inspection requirements. We recognize that the Board is faced with a myriad of challenges in forging these relationships. Significantly, there are complex and sensitive issues related to sovereignty, legal authority, comity, and logistics, and we recognize that the process to work through these issues is time-consuming.<sup>5</sup> Notwithstanding these challenges, we believe that establishing cooperative relationships with non-U.S. oversight authorities to facilitate inspections will undoubtedly further the Board’s goals

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<sup>1</sup> Section 104(b)(1) of the Sarbanes-Oxley Act of 2002 (“SOX”) requires that the PCAOB conduct inspections of registered firms that regularly provide audit reports for 100 or fewer issuers once every three years, unless the Board determines that a different inspection schedule is warranted pursuant to SOX § 104(b)(2). PCAOB Rule 4003(d)(1) permits the PCAOB to conduct an initial inspection in the fourth calendar year following the first calendar year in which the firm, while registered, issued (or played a substantial role in) an audit report.

<sup>2</sup> Release at 11, 14, and 15–16.

<sup>3</sup> *Id.* at 9.

<sup>4</sup> The Board’s cooperative arrangements presumably will address legal and other impediments to the Board’s inspection requests to non-U.S. firms.

<sup>5</sup> *See id.* at 6 (noting that the “need . . . to try to resolve potential conflicts of law, or to evaluate a non-U.S. system” involves “effort [that] can be substantial.”).

of protecting investors, improving audit quality, ensuring effective and efficient oversight of audit firms, and helping to preserve the public trust in the auditing profession. Given the importance of these cooperative arrangements, we support the deferral of the inspection schedules and, indeed, urge the Board to allow for additional flexibility beyond the proposed extension to achieve this objective.

Second, we believe the Board should consider the extent to which the transparency afforded by the publication of a list of audit firms that have not been inspected will actually enhance investor protection, and whether there are different types of disclosures that would better serve investors' interests in obtaining information about the PCAOB's progress in conducting inspections. In particular, we believe that listing only those firms that have not yet had their first Board inspection could seriously and unnecessarily harm non-U.S. firms and, potentially, the issuers whose financial statements they audit, and could cause confusion among investors. The proposed list also could be perceived as reflecting unwillingness on the part of a non-U.S. oversight authority to cooperate with the Board, or even a lack of good faith by such oversight authority in negotiating cooperative arrangements, and so hamper cooperation with them. If the Board nevertheless determines to move forward with a list, we suggest that a list of firms that have already been inspected, or a list that sets forth the status of inspections for all firms (in either case, along with appropriate explanatory language), would reduce, although not completely eliminate, the problems associated with publishing a list.

Third, we have concerns regarding the suggested disclosures for when information requested by the Board is not provided by the non-U.S. firm. Fundamentally, we question the premise for such disclosures: a purported Rule 4006 violation due to any instance of not providing information in the face of a legal impediment under the non-U.S. firm's home country law. This position places non-U.S. firms in a potentially untenable situation; the approach also would prejudice such firms' issuer clients as the disclosures could raise concerns about audit quality and, hence, the issuer's financial statements. Moreover, the specific disclosures regarding non-cooperation under consideration by the Board

represent a significant change from existing auditing standards, and would cause confusion for issuers and investors.

**I. The Board Should Extend Deadlines For 2009 Inspections Of Non-U.S. Registered Firms, Should Reserve The Flexibility For Further Extensions If Needed To Facilitate Cooperation With Non-U.S. Oversight Authorities, And Should Maintain Flexibility In Scheduling Inspections**

**A. An Extension Of Time Is Appropriate**

As the Board has noted, a delay in completing inspections can be justified where the delay serves investors' long-term interests of establishing cooperative arrangements that facilitate inspections of non-U.S. firms.<sup>6</sup> We therefore urge the Board to use the additional time that it would gain by adopting the proposed deferral to initiate, or continue, discussions with the relevant oversight authority in each applicable country, rather than proceeding with inspections where cooperative arrangements have not yet been finalized.

Several leaders within the global community of audit oversight authorities have recently discussed the more general point that greater cooperation is imperative for future regulatory effectiveness. Specifically, as Chairman Olson recently stated, the current financial crisis “demonstrates [that] the global nature of today’s markets demands a framework that emphasizes enhanced cross-border collaboration and cooperation among financial supervisors” and “[t]here is no doubt that current events fundamentally underscore the necessity of cross-border dialogue and cooperation.”<sup>7</sup> Charlie McCreevy, the EU Commissioner for Internal Markets, also has stated that “[Previously], I discussed the need for effective global cooperation between all auditing regulators.

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<sup>6</sup> *See id.* at 9 (“[T]he purposes of the Act, the public interest, and the protection of investors are better served by delaying a first inspection to work toward a cooperative resolution than by precipitating legal disputes involving conflicts between U.S. and non-U.S. law that could arise if the Board sought to enforce compliance with its preferred schedule without regard for the concerns of non-U.S. authorities.”). Although the Board states this is true only “[u]p to a point,” we believe that working toward cooperative arrangements is a critical first step.

<sup>7</sup> Speech by Mark W. Olson, PCAOB Chairman, to the Fédération des Experts Comptables Européens Conference on Audit Regulation (Dec. 9, 2008).

And today's economic situation only reinforces this need. We need to build a global dialogue to work together towards independent high quality audit oversight."<sup>8</sup> And the Japan Financial Services Agency has similarly noted that "it is critical both for the Board and the JFSA/CPAAOB to develop a practical cooperative framework in pursuing common responsibilities . . . ."<sup>9</sup> These sentiments were also expressed during the G20 summit in November 2008,<sup>10</sup> and build on themes that have been discussed more broadly over the preceding several years.

We agree that cross-border cooperation among audit oversight authorities is necessary, particularly for an effective and efficient inspection function.<sup>11</sup> We therefore support the Board's decision to extend the time in which initial inspections must be accomplished in order to allow the

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<sup>8</sup> Speech by Charlie McCreevy, European Commissioner for Internal Markets and Services, to the Fédération des Experts Comptables Européens Conference on Audit Regulation (Dec. 9, 2008).

<sup>9</sup> Letter from Junichi Maruyama, Deputy Commissioner for International Affairs, Japan Financial Services Agency, to the PCAOB (Mar. 4, 2008) (comments on 4012 proposal) (noting also that "we believe it essential to develop an effective cooperative arrangement between the JFSA/CPAAOB and the Board in conducting public oversight activities").

<sup>10</sup> *See* Group of Twenty Finance Ministers and Central Bank Governors, Declaration of the Summit on Financial Markets and the World Economy (Nov. 2008) ("We call upon our national and regional regulators to formulate their regulations and other measures in a consistent manner. Regulators should enhance their coordination and cooperation across all segments of financial markets, including with respect to cross-border capital flows. Regulators and other relevant authorities as a matter of priority should strengthen cooperation on crisis prevention, management, and resolution.").

<sup>11</sup> *See* Letter from Deloitte Touche Tohmatsu to the PCAOB at 2 (Jan. 26, 2004) (commenting on Rulemaking Docket No. 13 relating to the oversight of non-U.S. public accounting firms) ("We agree with the Board that its oversight of non-U.S. public accounting firms raises 'special concerns' and that the best way to address these concerns is through a 'cooperative arrangement' with non-U.S. regulators of the accounting profession. Specifically, we concur with the Board that it should 'seek[] to become partners' with non-U.S. regulators in their common enterprise to enhance audit quality and to protect the global capital markets from potential corporate reporting failures."); *see also* Letter from Deloitte Touche Tohmatsu to the PCAOB at 2 (Mar. 4, 2008) (commenting on Release No. 2007-11 relating to guidance regarding the implementation of Rule 4012) ("Full reliance by the Board on designated non-U.S. oversight entities will help to promote an efficient regulatory model that minimizes duplicative inspections and decreases the costs and burdens shouldered both by the Board and registered non-U.S. audit firms." Also, "collaboration will further the Board's goals of protecting investors, improving audit quality, ensuring effective oversight of audit firms, and helping to preserve the public trust in the auditing profession.").

Board sufficient time to negotiate cooperative arrangements with non-U.S. oversight entities that facilitate inspections.

**B. More Time, Beyond The Proposed Extension, May Be Needed To Achieve Cooperation**

We also urge the Board to consider whether additional time to complete inspections of non-U.S. firms, beyond that set forth in the proposed extension, may be warranted in some circumstances. As reflected in the Board’s proposal, the sovereignty, legal authority, comity, and logistical issues that have affected the inspection schedule thus far are complex and delicate. Indeed, it can be anticipated that in some circumstances legislative solutions may be required in order for an acceptable resolution to be achieved. Even absent the need for legislative action, the Board will require substantial time to:

- *Study the non-U.S. oversight entity’s regulatory framework and the rules within which it, and non-U.S. firms, operate.* In order to establish cooperative arrangements, the Board should form an understanding of the framework within which the non-U.S. oversight authority supervises its registered firms, and other legal restrictions, such as privacy laws, that may constrain the conduct of non-U.S. firms. As the Release recognizes, there are nearly as many countries where no inspections have yet occurred as there are countries where the Board has completed at least one inspection. As a result, it would seem that a significant additional amount of time may be needed to conduct the study of the relevant jurisdictions.
- *Finalize cooperative arrangements with the non-U.S. oversight authority.* As noted above, reaching agreements with non-U.S. oversight authorities can be a time-consuming process, both in terms of resolving sovereignty or legal impediment issues, as well as reaching agreement on numerous technical issues (for example, questions about the scope and timing of the inspection, as well as the production of documents and personnel for interviews) that cooperation requires.<sup>12</sup>
- *Coordinate the inspection process with the non-U.S. oversight authority.* The non-U.S. oversight authority may have a different inspection schedule and/or frequency timeline, and both it and the PCAOB should be sensitive to the need to modify schedules so that inspections can be synchronized to the extent feasible.

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<sup>12</sup> Also, at least with respect to countries within the European Union, implementation of Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts (May 17, 2006) may result in the need to negotiate “arrangements” under Article 47 of that Directive, regarding the transfer of working papers by non-U.S. firms, in order to achieve cooperation going forward.

We support the Board's efforts, and urge the Board to continue to push for cooperative arrangements. But, the number of moving parts in the inspection process, including the challenges listed above, calls for a high degree of flexibility on the part of all parties involved in order to engender a positive dialogue toward cooperation. This flexibility should allow for progress toward the overall objective of an effective and efficient inspection regime. We urge the Board to use its authority to reserve for itself in the final rule additional flexibility, beyond the three years currently contemplated by the Release, where, for example, the Board is engaged in productive dialogues regarding cooperative arrangements that have not yet concluded.

For the same reasons, the Board's new rule extending, by a single year, inspections originally scheduled in 2008 may not be sufficient to allow the Board and the non-U.S. oversight authorities to work through impediments to the Board's inspections. Inspections covered by this one-year extension may involve countries where the Board has a realistic possibility of establishing cooperative working relationships with those countries' oversight authorities, but not within the one-year allowed by the Board's rule. We are concerned, therefore, by the Board's statement that it "does not intend . . . to make any further adjustments to the inspection frequency requirements applicable to firms whose first inspection was due no later than 2008."<sup>13</sup> We understand that the Board may perceive that there are differences between the 2008 extension and the 2009 extension, to the extent that the Board is already prepared to conduct the 2009 inspections based on its preparations for the 2008 schedule. Yet, we believe that, in both instances, cooperation between oversight authorities is in the long-term interests of investors. We urge the Board to be mindful of the need for flexibility with respect to the time limit in its final rule on the 2009–2012 timetable, and, if appropriate, to extend further the 2008–2009 timeline for countries where additional time would facilitate the conduct of the inspections.

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<sup>13</sup> Release, at 9.

**C. The Board Should Maintain Flexibility In Scheduling Inspections**

The Board suggests that it would “sequence [its outstanding] inspections such that certain minimum thresholds [as to the non-U.S. firms to be inspected] would be satisfied in each of the years from 2009 to 2012. The minimum thresholds would relate to U.S. market capitalization of firms’ issuer audit clients.”<sup>14</sup> We believe the Board’s approach for prioritizing these inspections strictly according to “minimum thresholds” of issuer market capitalization, without consideration of other relevant factors, could result in interim deadlines that are counterproductive and inconsistent with investors’ long-term interests.

The Board proposes to place each non-U.S. firm into one of four groups, based solely on the market capitalization of the firms’ issuer audit clients, and then to inspect one group per year in each year from 2009 through 2012. This schedule does not appear to take into account where each individual firm is located and how complicated the path to cooperation might be in that jurisdiction. This proposal could unfairly disadvantage the non-U.S. firms that audit the largest issuers (and that may be therefore placed in the 2009 group) by affording them no extension of time whatsoever, even if they are located in jurisdictions where legal impediments to providing information to the PCAOB may exist, and the process of seeking cooperative arrangements is underway but may take longer to achieve. The Board’s proposal could similarly disadvantage firms whose inspections are scheduled for 2010 or 2011 (rather than 2012). Scheduling inspection deadlines based on criteria not related to the Board’s ability to reach agreement with non-U.S. oversight authorities seems to be inconsistent with the purpose of the extension and could harm these firms and impair the Board’s chances for achieving cooperative arrangements in some jurisdictions where the impediments are particularly difficult and it is evident that substantial time will be required to work through the issues. Investors’ long-term interests would be better served by allowing the Board to schedule inspections in such a way that

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<sup>14</sup> *Id.* at 11.

affords adequate time to establish cooperative arrangements in the greatest number of cases, including those presenting greater challenges.

We therefore recommend that the Board retain the flexibility to prioritize inspections based not on only market capitalization, but also on factors beyond the size of a non-U.S. firm's issuer audit clients. Other qualitative factors, such as the progress achieved toward developing cooperative arrangements, the extent to which inspections are currently conducted by the home country oversight authority and whether that oversight authority is strong, independent, and transparent, and the scheduling constraints or other difficulties encountered in conducting inspections in the non-U.S. country, should also be taken into consideration. This type of risk-based approach would be a more beneficial way to approach the scheduling of inspections, and we urge the Board to retain the flexibility to take these factors into consideration when developing its inspection schedule.

## **II. Public Disclosure Of A List Of Firms That Have Not Been Inspected Is Inadvisable**

The Board has expressed its interest in providing transparency to investors by “maintaining on its web site an up-to-date list of all registered firms that have not yet had their first Board inspection even though more than four years have passed since the end of the calendar year in which they first issued an audit report while registered with the Board.”<sup>15</sup> Although we recognize the benefits of transparency, we urge the Board to reconsider this proposal, for several reasons.

First, a stigma of deficiency may unnecessarily, though perhaps unintentionally, be associated with being named on a list that identifies certain firms that have not been inspected. Such a list may leave at least some investors with the impression that the non-U.S. firm had done something wrong, or failed to do something required, that warranted inclusion on the list. But this impression would be mistaken. The fact that a firm has not been inspected by the PCAOB does not mean that the firm is conducting substandard audits or is not being cooperative; a quality audit can be conducted absent a

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<sup>15</sup> *Id.* at 14.

PCAOB inspection. The mistaken impression that would be conveyed to investors by the proposed list could, in turn, lead to unwarranted uncertainty regarding the quality of the firm conducting the underlying audit work for a particular issuer and would prejudice issuers whose auditors are identified on the list, as doubt may unfairly be cast on the reliability of the issuer's financial statements

Second, the potential consequences to a firm that is named are particularly troubling because a firm's inclusion on the list is likely to be based on factors beyond the firm's control. Most significantly, the scheduling of the Board's inspections of non-U.S. firms is outside the control of the firms.

Third, it is unclear what caveats to or explanations of the list would be provided, or the extent to which such caveats or explanations could ameliorate the potentially negative conclusions to be drawn by issuers and investors as a result of a firm's being included on the list.

We therefore recommend that the Board refrain from publishing such a list at this time. If, however, the Board determines that some form of list related to the status of inspections is needed, we suggest that the Board implement a different type of disclosure. Specifically, one alternative would be for the Board to create a list of all the registered firms that have been inspected at least once by the Board. This list could include firms required to be inspected for which at least one inspection report has been issued, as well as firms for which the inspection process has been completed but no inspection report has yet been issued. To mitigate any potential risk of adverse inferences for those firms not on the list, the list could provide a disclosure to the effect that such firms are not included on the list for any number of reasons. To this end, we suggest that the Board consider the following text for such a disclosure:

Some registered firms are not included on this list; this may be because of one of any number of reasons, including, but not limited to: (i) the firm's inspection is underway but not yet completed; (ii) the firm's inspection has been scheduled but not yet begun; (iii) the firm's inspection has not yet been scheduled by the Board; (iv) the firm is located in a jurisdiction with which the Board has not developed a cooperative arrangement to facilitate inspections; (v) the firm is not required to be inspected under Rule 4003; or (vi) some combination of the above.

As a second alternative, the Board could create a list that sets forth all registered firms for which the Board is required, under its rules, to conduct inspections, and the status of each such firm's Board inspection, as follows: (a) inspected and a final report issued (with a hyperlink to the most recent report issued); (b) inspected but no report yet issued; and (c) not yet inspected. A disclosure incorporating the language proposed above also could be included with the list to clarify the reasons that a firm may fall within category (c). Although neither this alternative, nor the first alternative, would avoid completely the potential stigma for non-inspected firms, it would present the issue in the overall context of the Board's inspection program and provide transparency regarding all registered firms.

In sum, we recognize the importance of providing transparency to investors as to the status of the inspection process. However, the list proposed by the Board would not be the optimum approach and could trigger significant negative consequences. If the Board believes that some form of disclosure is appropriate, we request that the Board consider the alternatives above, either of which would reduce the potential adverse consequences of the Board's suggested list to non-U.S. firms, issuers, and investors.

**III. The Disclosures Suggested For When Information Is Not Provided For A PCAOB Inspection Should Be Rejected, In No Small Measure Because They Are Premised On The Faulty Notion That A Non-U.S. Firm Should Be Sanctioned When Information Is Not Provided Because Of A Legal Impediment In That Firm's Home Country**

In the Release, the Board requests comment on "whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006" where a non-U.S. firm declines to provide information in response to a PCAOB request.<sup>16</sup> The Board also states that apart from sanctions it would impose in such circumstances, the Board is also considering "requiring a principal auditor to make certain public

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<sup>16</sup> Release, at 16.

disclosures as part of, or in connection with, each audit report it issues for an issuer,” and requests comment “on the potential benefits and drawbacks of [such] a rule. . . .”<sup>17</sup> As a threshold matter, we question the premise underlying the suggested request for comment on sanctions: that non-cooperation proceedings should be initiated or sanctions imposed where a firm’s failure to provide information is attributable to a home country legal impediment. We also have significant concerns regarding the suggested disclosures themselves with respect to their structure, their impact on firms and existing auditing standards, and their impact on and utility to issuers and investors.

**A. Non-U.S. Firms Should Not Be Sanctioned For An Alleged Failure To Cooperate Attributable To A Legal Impediment, Particularly Where The Board Is Seeking To Negotiate Cooperative Arrangements**

In setting forth these suggested disclosures, the Release proceeds from the premise that a non-U.S. firm’s “failure or refusal to provide requested information is a violation of Rule 4006” even in situations where the inability to comply is attributable to a legal impediment.<sup>18</sup> Although the Board seeks comment on what sanctions might be appropriate in this situation, as well as comments on the suggested disclosures, we believe the Board is starting from an incorrect premise in considering these issues.

We recognize the difficulty that the Board faces when it is unable to obtain access to audit working papers or other information that it has requested in connection with its inspections. Yet, the dilemma facing non-U.S. firms is significant in this situation: they have two options, neither of which is desirable. The first option is to decline to provide the information and risk being deemed to have violated the Board’s rules—in which case the Release states that the Board could seek sanctions which may include, among other things, censure, imposition of a fine, or even suspension or revocation of

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<sup>17</sup> *Id.*

<sup>18</sup> *Id.* at 16; *see also id.* n.35 (“The Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection.”).

registration. The second option is to provide the information and risk sanctions for violating their home country's laws, thereby subjecting the firm to home country discipline, which could include revocation of the firm's or an individual auditor's license. As such, we strongly urge the Board to reconsider its proposed application of Rule 4006 and how it proposes to balance the competing interests in this situation, in light of the considerations set forth below.

First and foremost, it is counter-productive to place non-U.S. firms in a position where they are forced to decide between violating U.S. or home country laws. An international conflict of law is often a matter between sovereigns, and therefore is a matter that is principally to be resolved at a governmental level. It is not something that the firms can resolve themselves, although we believe that firms generally should be willing to help in resolving such matters through providing insight and comments to oversight authorities in their consideration of solutions to these issues. In addition, as a practical matter, the Board may be able to avoid placing non-U.S. firms in this untenable position by undertaking to resolve certain legal impediments through negotiation with non-U.S. oversight authorities. We recognize that certain legal impediments, such as the data protection provisions in the European Union, may be outside the jurisdiction of the non-U.S. oversight authorities with which the Board is negotiating. However, the non-U.S. oversight authorities and non-U.S. firms nevertheless still may be able to assist in developing approaches to the production of information that would avoid violating legal impediments and would enable the Board to obtain information necessary to its inspections.

Moreover, the home country laws that non-U.S. firms risk violating are significant. Firms that are based in the European Union, for example, are subject to extensive data privacy regulations. *See* Directive 95/46/EC, as implemented (Article 25 of this directive restricts an EU firm's ability to transfer data to a third country unless the third country provides an "adequate level of protection" for the data). Non-U.S. firms also are subject to confidentiality restrictions—some of which include

criminal sanctions that apply to individuals who violate the regulation<sup>19</sup>—as well as restrictions on the transfer of working papers, such as under EU Directive 2006/43/EC. Potential legal conflicts also arise under the CPA laws, auditing standards, and codes of professional conduct of several other countries. Failure to comply with home country laws could have severe adverse consequences on the non-U.S. firm, including revocation of the firm’s home country license. Simply put, the legal risks for non-U.S. firms are not just hypothetical—they are real and substantial.

Disciplinary action by the Board for a non-U.S. firm’s decision to comply with its home country laws could directly or indirectly prevent the non-U.S. firm from performing audits for SEC issuers. Such a result would not be in the best interests of public companies or their investors, if for no other reason than it would limit issuers’ choice of auditors. In any particular case, the issuer could be forced to seek to hire new auditors, and incur the costs of getting them up to speed to perform the audit. Or, where the non-U.S. firm plays a substantial role in auditing the subsidiary of a U.S. issuer audit client, a U.S. auditor could be forced to seek a replacement firm.

Moreover, this search by the issuer (or the U.S. auditor) to find a replacement auditor may well be unsuccessful. There may not be another auditor that has the ability to perform the work and that is not also subject to the same considerations the auditor being replaced had faced—i.e., the prospect of violating local laws. An auditor from outside the country likely would not be an option: it would not be as well positioned as a local auditor to perform the audit, given factors such as location of the relevant client documents and personnel, and linguistic and cultural barriers; it could be subject to the same legal impediments as the auditor being replaced; and, in any event, it likely would not be licensed to practice in the country.

In addition, the Board’s suggested approach to Rule 4006 could undermine the formation of cooperative arrangements with relevant non-U.S. oversight authorities. PCAOB demands asking non-

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<sup>19</sup> See, e.g., Denmark STRL 2004 § 152 (imposing penal sanctions for certain dissemination of information in violation of the professional obligation of confidentiality).

U.S. firms to violate the laws of their home countries will not engender cooperation with non-U.S. oversight authorities, particularly where the law that would be violated is enforced by the non-U.S. oversight authority itself. There is no need to jeopardize cooperative arrangements with non-U.S. oversight authorities by threatening the firms regulated by those oversight authorities with non-cooperation or discipline for their good faith compliance with the laws of their home country.

**B. Public Disclosures Related To A Non-U.S. Firm’s Not Having Provided Information Are Unwarranted**

In the Release, the Board seeks comment on “possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information,” noting that “[o]ne example that the Board has begun to consider would involve requiring a principal auditor to make certain public disclosures as part of, or in connection with, each audit report it issues for an issuer. . . .”<sup>20</sup> As discussed further below, we urge the Board to reject this idea.

**1. The Overall Disclosure Concept Should Be Reconsidered**

The Release suggests various potential disclosures related to a non-U.S. firm’s failure to comply with the Board’s requests. We believe that the disclosures being considered would be confusing and unhelpful to investors, would therefore be harmful to issuers, would be detrimental to establishing cooperative arrangements with non-U.S. oversight authorities, are contrary to current PCAOB standards, and would be unnecessarily punitive for firms. As such, we believe the Board should not further consider or propose any such disclosures.

The types of disclosures described in the Release would not be beneficial to investors. The fact of non-cooperation with a Board’s inspection demand does not communicate information related to the quality of the audit or the quality of the issuer’s underlying financial statements. The fact that a PCAOB inspection of a particular non-U.S. firm has not occurred does not mean that the non-U.S. firm’s audits are flawed. Similarly, non-cooperation with a Board request—particularly where the

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<sup>20</sup> Release, at 16.

non-cooperation is directly attributable to the non-U.S. firm's compliance with its home country laws—does not mean that the firm has performed substandard audits. Moreover, the period in which the non-U.S. firm is alleged not to have cooperated may have no relationship to the period being audited and reported on. Yet, the suggested disclosures risk misleading investors into believing that there is a problem with the financial statements or the audit work, or both. Issuers would, in turn, be harmed by investors harboring such a misconception.

In addition, the suggested disclosures could obscure other disclosures in the current auditor's report—disclosures that are relevant to users of the financial statements because they bear on the presentation of the issuer's financial statements or on the nature and scope of the audit. Moreover, the Release does not address how or whether the suggested disclosures would be affected in instances where not providing information because of a legal impediment does not impact the Board's ability to complete an inspection.

## **2. The Specific Disclosures/Representations Suggested In The Release Are Problematic**

In addition to the general concerns discussed above, the individual disclosures identified in the Release raise a number of significant issues. Where we discuss below issues present with respect to one of the proposed disclosures, we do not repeat in detail our discussion of these issues for each subsequent disclosure to which they are applicable.

*Part A: "If the principal auditor has failed to provide information in response to an inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns, the principal auditor would need to disclose that fact as part of, or in connection with, its audit report."*

First, it is not clear what would be the objective of such a disclosure. As discussed above, it is questionable whether investors or issuers would benefit from the disclosures, and it is likely that non-U.S. firms would be harmed. Second, it is not clear where—in the audit report or otherwise “in connection with the audit report”—this information would be provided. We believe that the audit report is not an appropriate place for these disclosures. Audit reports fulfill a specific, established role

with regard to the examination of the financial statements of an issuer, as set out in PCAOB auditing standards: they are carefully crafted to present information relating to the audit of the issuer's financial statements for a specific time period. The proposed disclosures would thus run contrary to the purpose of the audit report, focusing instead on the conduct of the auditor in relation to the Board's oversight function.

Second, it is not clear what a reader of the audit report is to take from such a disclosure—the implication seems to be that the principal auditor does not perform quality audits, but there is no specific relationship between the two. Subjecting the audit report to the type of disclosures identified in the release raises the risk that the audit report will become a repository of statements and assertions unrelated to its purpose—which is to provide information to investors about the nature and scope of the audit and whether the accompanying financial statements are reasonably stated. If the suggested disclosures are contemplated to be provided in connection with (but not as a part of) the audit report, it is also unclear how, where, when, and to whom these disclosures would be provided.

*Part B: "In each case, the principal auditor would need to make a representation about whether the principal auditor used the work of any registered firm that has declined to provide information or documents in response to a Board inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns."*

The parameters and nature of the suggested "representation" are unclear, and the answers to several clarifying questions would facilitate our providing more focused comments on this disclosure. For example, this suggestion does not address how the principal auditor could or would learn of the participating auditor's declining to provide information. This suggestion also does not address: what form these representations would take (e.g., are they intended to appear as part of audit reports, or otherwise); to whom the representations would be directed (e.g., to issuers, to regulators, to investors);

for how long the disclosure would be required; and whether the representations would be required regardless of whether the principal auditor assumes responsibility for the participating firm's work.<sup>21</sup>

*Part C: "If the principal auditor uses the work of any [non-cooperative] firm and assumes responsibility for that work . . . the principal auditor would have to disclose (a) the identity of the firm, (b) the nature of the work performed by the firm, (c) any steps the principal auditor took to assure itself concerning the firm's and the relevant individuals' familiarity with relevant professional standards, ability to perform the work adequately, and the adequate performance of the work, (d) any other procedures on which the principal auditor relies to monitor or assess the firm's performance of audit procedures in the audits of issuers, and (e) a brief summary of any information available to the principal auditor about deficiencies in the firm's performance of any such procedures in the two-year period preceding the date of the audit report."*

As noted with respect to the previous disclosure suggestions, it is not clear how or where these disclosures would be made, or to whom. If it is suggested that such disclosures would appear in the audit report, this would be inconsistent with current standards: where the principal auditor takes responsibility for the overall audit, only the principal auditor is named in the audit report, and mention of any participating auditors is omitted. Specifically, PCAOB's Interim Auditing Standard ("AU") 543.03, *Part of Audit Performed by Other Independent Auditors*, states, "[i]f the principal auditor decides to assume responsibility for the work of the other auditor insofar as that work relates to the principal auditor's expression of an opinion on the financial statements taken as a whole, no reference should be made to the other auditor's work or report." (Emphasis added.)<sup>22</sup> Similar statements are made in AU 543.04, explaining that referring to another auditor when the principal auditor takes responsibility "may cause a reader to misinterpret the degree of responsibility being assumed." It is not clear how these standards would be harmonized with the contemplated disclosures, which may instead require that the participating auditor be specifically named and discussed, even where the primary auditor takes full responsibility for the work.

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<sup>21</sup> In addition, the suggested disclosure does not address any obligations the principal auditor may have with respect to the decision of the participating auditor not to provide information.

<sup>22</sup> Of course, were the principal auditor to decide, under AU 543.06, to make reference to the other auditor's work, the concerns expressed in our comments to Part D of the proposal would be raised here instead.

In addition, AU 543.12 describes procedures that must be undertaken if a principal auditor decides not to make reference to a participating auditor's work. It is not clear how the suggested disclosures would relate to AU 543.12. For example, under this standard, the principal auditor must review the engagement completion document, a list of significant fraud factors, the auditor's response, the results of related procedures, and significant deficiencies in internal control. The Board's contemplated disclosures would need to be specifically harmonized with these existing requirements.

*Part D: "If the principal auditor used the work of any [non-cooperative] firm and makes reference to the audit of the other auditor . . . the auditor would have to disclose, in addition to the division of responsibility described in AU 543.07, the identity of the firm and the other information described in the preceding sentence."*

The disclosures discussed in Part D would apply, unlike those in Part C, to circumstances in which the principal auditor has decided that it will, under AU 543.06, make reference to the work of another auditor. These suggestions are problematic for two reasons.

First, AU 543.07 provides that "[t]he other auditor may be named but only with his express permission and provided his report is presented together with that of the principal auditor." The Board's suggestion would require that the firm be named, regardless of whether it consented, which is a potential conflict with AU 543.07, if the other auditor does not consent.

Second, AU 543.08 states that "[r]eference in the report of the principal auditor to the fact that part of the audit was made by another auditor is not to be construed as a qualification of the opinion but rather as an indication of the divided responsibility between the auditors who conducted the audits of various components of the overall financial statements." The example provided in AU 543.09 of the type of reference currently required to be made is a brief one, focusing on explaining the division of authority. The additional disclosures called for in Part D conflict with the direction in AU 543.08/.09 and are a source of potential confusion for investors, who may perceive the disclosure to constitute a qualification of the opinion.

**3. A Report Providing An Overview Of Information Related To Negotiations With Non-U.S. Oversight Authorities Could Provide An Effective Alternative To The Disclosures Proposed By The Board**

If the Board perceives that additional transparency regarding these issues is needed, then, in place of the suggested disclosures discussed above, the Board should consider publishing a report—for example, under Rule 4010—that provides information related to its inspections and cooperative arrangements with non-U.S. oversight authorities. Adequate transparency could be provided to investors through this report.

The report could inform Congress and the public about the issues the Board has encountered in seeking to achieve cooperative arrangements. A PCAOB report detailing obstacles faced in trying to conduct inspections would allow for focus to turn to objective impediments which apply across particular audits and non-U.S. jurisdictions, as opposed to adoption of the proposed disclosures that provide little if any context and questionable benefit to interested parties. In addition, such a report could, in a fair and objective manner, identify the nature (including the extent) of the conflict. Investors would also be able to review the information to determine the importance of these obstacles to their investment decisions.

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In sum, we support the Board's recognition that international cooperation in the oversight of auditors is in the best interests of investors, issuers, firms, and other stakeholders in the capital markets. We urge the Board to reexamine the matters discussed above relating to scheduling inspections of non-U.S. firms, providing disclosures about non-U.S. firms that have not received an inspection, sanctioning non-U.S. firms for declining to provide information because of a legal impediment, and requiring disclosures of such actions, because we believe these proposals and suggestions in many respects are harmful to investors, issuers, and non-U.S. firms, and would not advance the formation of cooperative arrangements. We thank the Board for the opportunity to

comment on the Release. If the Board has any questions about the contents of our comments, please contact Jens Simonsen at (212) 492-3689.

Very truly yours,

/s/ Deloitte Touche Tohmatsu

cc: Mark W. Olson, Chairman of the Board  
Daniel L. Goelzer, Board Member  
Bill Gradison, Board Member  
Steven B. Harris, Board Member  
Charles D. Niemeier, Board Member  
Thomas J. Ray, Chief Auditor  
George H. Diacont, Director

Mary L. Schapiro, Chairman  
Kathleen L. Casey, Commissioner  
Elisse B. Walter, Commissioner  
Luis A. Aguilar, Commissioner  
Troy A. Paredes, Commissioner  
James L. Kroeker, Acting Chief Accountant  
Paul A. Beswick, Deputy Chief Accountant



Ernst & Young LLP  
5 Times Square  
New York, New York 10036  
Tel: +1 212-773-2500  
Fax: +1 212-773-0004  
www.ey.com

February 2, 2009

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

**Re: PCAOB Rulemaking Docket Matter No. 027**

Dear Sir/Madam:

Ernst & Young LLP (“EY”), the U.S. member firm of Ernst & Young Global (“EYG”), appreciates the opportunity to comment on the PCAOB’s proposed rule amendments, *Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms* (“the Rule Amendments”). The comments below reflect the views of EY and of the other member firms of EYG.

The Board’s proposing release (“the Release”) states that the Board is proposing the Rule Amendments to address “interconnected issues that relate to the Board’s responsibility to conduct inspections of registered firms, including non-U.S. firms, and the corresponding obligation of firms to cooperate with Board inspections.” Part I of the Release deals with amendments to the Board’s rule governing the minimum frequency with which the Board must conduct inspections under Sections 102(a) and 106 of the Sarbanes Oxley Act (“the Act”). Part II of the Release describes potential consequences for non-U.S. firms unable to cooperate fully with Board inspections because of conflicts arising from local laws.

We do, of course, recognize that the Act’s requirements for inspections of non-U.S. firms pose special issues for the Board and for the foreign firms. We commend the Board for working through many of these issues and encourage it to explore sensible solutions with its regulatory counterparts throughout the world on those issues that remain. We agree it is appropriate under the circumstances to adjust the inspection schedule to the one proposed by the Board for the reasons set forth in the Release.

In the long-run, we urge mutual recognition of regulatory regimes, whereby the PCAOB could rely fully on inspections conducted by non-U.S. regulators in fulfilling the PCAOB’s own statutory mandate. As an intermediate measure, we support the Board’s efforts to conduct inspections of non-U.S. firms jointly with local authorities both to take

advantage of potential efficiencies and to avoid imposing unnecessary regulatory burdens on the firms. In our comment letter on the Board's proposed policy statement, *Guidance Regarding Implementation of PCAOB Rule 4012*, we stated that, in a world of cross-border markets and investors, regulatory cooperation is essential to improve audit quality globally. Therefore, we encourage the Board to continue to work with relevant local authorities to try to resolve potential conflicts of law for non-U.S. firms. In this regard, we have some concerns with the proposed actions set forth in Part I. E. and Part II of the Release. We believe the proposed actions described could impede rather than promote increased regulatory cooperation and could have significant negative consequences for the non-U.S. firms and their clients.

## **I. Part I: Rule Amendments Concerning the Timing of Certain Inspections**

### *E. Transparency Concerning Delayed Inspections*

We believe that investors have an interest in knowing that the PCAOB is inspecting firms reasonably within the timeframe set forth in the Act and that, to the extent adjustments are needed to its inspection schedule, the Board is making adjustments that are consistent with the purposes of the Act, the public interest, and the protection of investors. We believe the plan set forth in the proposed Rule Amendments to adjust the inspection schedule accomplishes that objective.

However, despite the disclaimers proposed in the Release, publishing a list solely of delayed inspections likely would have unintended adverse consequences to the firms. Simply being included on the list may well carry a negative connotation and could be misinterpreted to imply that the firms have potential quality defects even though, as described in the Release, it is necessary for the Board to delay the inspections for matters that are not controllable by the firms. In addition, the PCAOB currently publishes lists of the registered firms and of the inspection reports issued. As a result, there could be confusion about the status of inspections that have been performed but for which inspection reports have not yet been issued.

## **II. Part II: Registered Firms' Obligations**

We encourage the Board to continue its efforts to develop cooperative relationships with its foreign counterparts. However, until such time as the Board and its foreign counterparts resolve sovereignty concerns or legal objections of local authorities, we do not believe that placing the firms in the middle of competing sovereign interests will facilitate regulatory objectives. Registered accounting firms should not be required to violate their local laws. Furthermore, we do not believe that a firm's legitimate concerns should be a basis for concluding the firm has violated Rule 4006 and that the Board should consider imposing disciplinary sanctions. Making demands on firms that cannot be met by them without violating local law does not address the fundamental issues impeding the Board's efforts to conduct inspections.

In this regard, we are particularly surprised at footnote 35 of the Release, which states: “The Board does not view non-U.S. legal restrictions of the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection.” Longstanding principles of international comity require that one country’s regulator not act in a way that demeans the laws and regulations of another jurisdiction. Other countries may have legitimate interests in enforcing their laws relating to confidentiality, bank secrecy, and so on, and regulators have learned to work together precisely to deal with the challenges of cross-border supervision and enforcement in the face of such national laws and interests. We urge the PCAOB to continue to respect those laws and develop mechanisms for cooperating with its counterparts through mutual recognition or reliance.

Indeed, in some jurisdictions the proposed approach could inhibit issuers’ willingness to provide certain information to their auditors. We are aware that in Canada, for instance, concerns have been raised about whether issuers would continue to provide certain legally privileged information to their auditors if such information might later be provided to the PCAOB and thereby result in a loss of privilege. Audit quality would be negatively affected if issuers were to restrict the scope and nature of information provided to their auditors.

Likewise, we do not believe that requiring principal auditors to make public disclosures of the type described in the Release would be appropriate. We believe such disclosures would have many significant adverse consequences, including confusing the users of audit reports and inappropriately tainting the reports.

In our view, many users of the reports would misinterpret the disclosures described in the Release and would misinterpret what the lack of disclosures would mean. For example, under the proposal, a principal auditor would not be required to make any disclosures where the principal auditor and all of the other firms performing audit work in a “substantial role” were inspected by the PCAOB sometime over the prior three years. The lack of disclosure could be interpreted by the users of the report as meaning that an additional or higher level of confidence in the financial statements is appropriate. But there are limitations in the inspection process. Almost all registered firms around the world are not inspected by the PCAOB every year and, even when they are inspected, the inspections do not include all of the work performed by the firms for all issuers they serve as principal auditor or in a substantial role.

In addition, making the disclosures described in the Release solely because a portion of the audit work was performed by a firm that has not been timely inspected by the PCAOB would almost certainly carry a negative connotation and be misinterpreted to imply the firm has potential quality defects. Indeed, such negative implications could even give rise to claims in litigation that the principal auditor and the audit client should have known better than to have had an uninspected firm perform a portion of the audit. To avoid such negative implications, the client and the auditor might decide to have the work performed by an audit firm from another jurisdiction where an inspection has occurred, even though it would be better both from the standpoint of quality and cost to

have the work performed locally. Such a result would not be in the best interests of investors.

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We would welcome the opportunity to respond to any questions the PCAOB or its staff might have with respect to the foregoing comments. Please feel free to contact Randy Fletchall at 212-773-4043, Rick Miller at 216-583-2071, or Tom Riesenberg at 202-327-7605.

Sincerely,

*Ernst + Young LLP*



27 January 2009

Mr. J. Gordon Seymour  
Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, NW  
USA – Washington DC 20006-2803

Email: [comments@pcaobus.org](mailto:comments@pcaobus.org)

Ref.: AUD/HvD/HB/SH

Dear Mr. Seymour,

**Re: FEE Comments on PCAOB Release No. 2008-007, Rulemaking Docket Matter No. 027, Rule Amendments concerning the Timing of Certain Inspections of non-US Firms, and Other Issues relating to Inspections of Non-US Firms**

FEE is pleased to provide you below with its comments on the Public Company Accounting Oversight Board (PCAOB) Rule Amendments concerning the Timing of Certain Inspections of non-US Firms, and Other Issues relating to Inspections of Non-US Firms of 4 December 2008 (the Proposed Rule Amendments).

FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 43 professional institutes of accountants and auditors from 32 European countries, including all of the 27 EU Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 500.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

FEE's objectives are:

- To promote and advance the interests of the European accountancy profession in the broadest sense recognising the public interest in the work of the profession;
- To work towards the enhancement, harmonisation and liberalisation of the practice and regulation of accountancy, statutory audit and financial reporting in Europe in both the public and private sector, taking account of developments at a worldwide level and, where necessary, promoting and defending specific European interests;
- To promote co-operation among the professional accountancy bodies in Europe in relation to issues of common interest in both the public and private sector;
- To identify developments that may have an impact on the practice of accountancy, statutory audit and financial reporting at an early stage, to advise Member Bodies of such developments and, in conjunction with Member Bodies, to seek to influence the outcome;
- To be the sole representative and consultative organisation of the European accountancy profession in relation to the EU institutions;
- To represent the European accountancy profession at the international level.



FEE notes with interest the PCAOB Proposed Rule Amendments giving regard to FEE's own substantial contribution to recent discussions in Europe over the future direction of requirements and guidance relating to quality assurance and inspection systems. In particular FEE:

- Published in December 2006 its Position Paper "Quality Assurance Arrangements Across Europe"<sup>1</sup>;
- Organised a first high level conference on 12 October 2006<sup>2</sup> (at which the Chairman and a Board Member from the PCAOB spoke) including a session on the issues raised by the Position Paper;
- Held a second high level conference on 27 November 2007<sup>3</sup> (at which the Chairman and a senior staff member from the PCAOB spoke) including a panel discussion on quality assurance systems in Europe;
- Held a third high level conference on 9 December 2008<sup>4</sup> (at which the Chairman and a senior staff member from the PCAOB spoke) including an international panel debate on Home Country Oversight, Mutual Reliance on Joint Inspections: Achievements, Challenges and Practicalities;
- Issued from June 2007 to September 2008 seven comment letters to the European Commission on the Possible contents of the future Commission Recommendation on quality assurance for statutory auditors and audit firms auditing public interest entities and on a possible proposed adequacy decision for third country competent authorities; and
- Submitted a comment letter to the PCOAB on 29 February 2008 on the Proposed Policy Statement: Guidance Regarding Implementation of PCAOB Rule 4012.

Although non-U.S. audit firms are rarely responsible for the delay in PCAOB inspections and whilst we doubt that the proposed deferral times will be adequate in every case to fully resolve outstanding issues, we are generally supportive of the initiative underlying the proposed Rule Amendments Concerning the Timing of Certain Inspections and the Extension of the Deadline for Certain 2008 and 2009 Inspections on Non-U.S. Firms as well as the Transparency Concerning Delayed Inspections.

However, we would like to repeat a number of major comments we had made previously, which appear to be winning international recognition and outline a series of concerns about the Registered Firms' Obligations as suggested in the Proposed Rule Amendments.

### **Mutual recognition and full reliance on third country public oversight bodies is the only practicable solution**

In the light of the extraterritoriality of oversight and quality assurance regulations, FEE repeats that it strongly encourages coordination, cooperation and mutual recognition between European Union and third countries to minimise duplication of inspections and to avoid legal conflicts by effective full reliance on home country oversight systems.

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1 [http://www.fee.be/publications/default.asp?library\\_ref=4&content\\_ref=629](http://www.fee.be/publications/default.asp?library_ref=4&content_ref=629)

2 [http://www.fee.be/news/default.asp?library\\_ref=2&content\\_ref=574](http://www.fee.be/news/default.asp?library_ref=2&content_ref=574)

3 [http://www.fee.be/news/default.asp?library\\_ref=2&category\\_ref=124&wp=1&content\\_ref=951](http://www.fee.be/news/default.asp?library_ref=2&category_ref=124&wp=1&content_ref=951)

4 [http://www.fee.be/news/default.asp?library\\_ref=2&category\\_ref=214&content\\_ref=937](http://www.fee.be/news/default.asp?library_ref=2&category_ref=214&content_ref=937)



The significant benefits from a true “full reliance” approach are:

- Cost savings for oversight bodies and audit firms through the elimination of duplication of inspections;
- Increased opportunities to expand the focus of inspections on audit quality thereby better protecting investors;
- Prevent conflicts of laws and regulations for oversight bodies, companies and audit firms by recognising the sovereignty of third countries and their right to oversee audit firms in their domestic markets.

As avoiding duplication of inspections and thus their convergence ought to be the ultimate goal, mutual recognition of public oversight systems should be aimed at.

The establishment of the International Forum of Independent Audit Regulators (IFIAR) on 15 September 2006 is relevant in this respect. Regulators from within the European Union and outside the European Union should be encouraged to co-ordinate and co-operate with each other to ensure that oversight regimes are of equivalent quality, to promote confidence and minimise, or at least accommodate to a reasonable degree, the serious concerns and issues related to duplication of oversight, quality assurance reviews, inspections and penalties for statutory auditors and audit firms. At a European Union level, the Statutory Audit Directive forms the basis for such co-ordination and co-operation with third countries, the application of which is monitored by the European Commission.

At the European Commission International Conference on Auditor Oversight on 10 December 2008 in Brussels, there was a strong call to work towards mutual recognition and full reliance on home country oversight systems from the majority of auditor’s oversight bodies present, from EU Member States and non-EU countries alike.

### **The Sarbanes-Oxley Act and PCAOB Rules should be reconsidered to not preclude international cooperation**

As mentioned above, at European Union level, the Statutory Audit Directive forms the basis for co-ordination and co-operation with third countries and for mutual recognition of and full reliance on European auditor’s oversight bodies. The implementation of the Statutory Audit Directive in EU Member States is nearing completion and its application is closely monitored by the European Commission. The European Commission actually enforces its authority and has taken certain EU Member States to court for delaying the implementation of the Directive and those which will not implement the court’s ruling may face significant fines.

Seven years after the issuance of the Sarbanes-Oxley Act (the Act), we believe that the circumstances in some parts of the world, notably in Europe, have significantly changed and warrant reconsideration of certain parts of the Act and/or PCOAB rules.

In this respect, FEE ventures to make reference to Section 106 on Foreign public accounting firms of the Act and more specifically to the Exemption authority in subsection (c) which allows the Board and/or the US Securities and Exchange Commission (SEC), by rule, regulation or order to exempt any foreign public accounting firm, or any class of such firms, from any provision of the Act, the rules of the PCAOB or the SEC.

FEE strongly encourages the PCAOB and the SEC to give due consideration to such reconsideration of certain parts of the Act and/or PCAOB rules.



## **Conflicts of laws are counterproductive and should be avoided**

Conflicts of law are a major issue for regulators, oversight bodies and audit firms alike. The PCAOB Proposed Rule Amendments would essentially force non-U.S. firms in some countries to choose between violating either their home country laws and regulations or the PCAOB Rules.

Non-U.S. audit firms are looking for their national regulators, the PCAOB and the European Commission to contribute to resolving such legal obstacles as they are not of the making of the audit firms. It should be noted that all audit firms in a particular jurisdiction are ordinarily in a similar situation, which could lead to the impossibility for entities of having their financial statements audited. Footnote 35 in the Proposed Rule Amendments is of particular concern to us in this respect.

It also needs to be observed that violation of law, regulations or rules as such calls the integrity of all parties and indeed the law itself into question and is therefore decidedly not in the public interest. This means that this particular aspect of the PCAOB proposals fail the test of being in the public interest or for the protection of investors, which cannot be the intention of the Act.

## **Additional disclosures related to the firm's inspection in audit reports are inappropriate**

FEE is fully supportive of the use of International Standards on Auditing (ISAs) as a framework to conduct audits of financial statements. In respect of the audit report, the objective for the auditor is to form an opinion and to report on the financial statements of a specific entity or group of entities; the goal of an audit report is not to report on certain matters related to the auditor or his audit firm. Additionally, as the audit report forms an integral part of the annual report of the audited entity or group of entities, such entities are unwilling to have to include information related to the audit firm's inspection in their annual reports.

Therefore, FEE strongly opposes the proposed additional disclosures related to the firm's inspection in the audit report as suggested in the Proposed Rule Amendments.

For further information on this letter, please contact Mrs. Hilde Blomme from the FEE Secretariat.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Hans van Damme', written over a horizontal line.

Hans van Damme  
FEE President



Office of the Secretary  
 Public Company Accounting Oversight Board  
 1666 K Street, NW  
 Washington, DC 20006  
[comments@pcaobus.org](mailto:comments@pcaobus.org)

Grant Thornton International Ltd  
 201 S College Street, Suite 2500  
 Charlotte, NC 28244-0100  
 United States

T 704.632.6781  
 F 704.632.6899  
[www.gti.org](http://www.gti.org)

2 February 2009

**Re: PCAOB Rulemaking Docket Matter No. 027 – Rule Amendments  
 Concerning the Timing of Certain Inspections of Non-U.S. Firms, and  
 Other Issues Relating to Inspections of Non-U.S. Firms**

Dear Sir or Madam:

Grant Thornton International is one of the world's leading international organizations of independently owned and managed accounting and consulting organizations. Grant Thornton International member firms operate in over 100 countries and employ over 29,000 persons worldwide. This includes 50 offices in the United States, and nearly 6,000 persons employed by Grant Thornton LLP, the U.S. member firm of Grant Thornton International.

Grant Thornton International welcomes the opportunity to provide comments on the Public Company Accounting Oversight Board's (PCAOB or Board) proposed rule to delay some inspections of non-U.S. audit firms. In summary:

- We support the PCAOB's proposed amendment to Rule 4003. We agree that the amendment would provide the Board with additional time to reach cooperative agreements with non-U.S. oversight entities, without forcing non-U.S. audit firms to make the difficult choice between violating their home country laws and violating PCOAB rules.
- We believe that the proposal to amend Rule 4003 is closely related to the PCAOB's proposed policy statement pursuant to Rule 4012 and "full reliance." The finalization of the full reliance policy statement – in a principles-based manner – would be of great help in resolving conflicts and improving cooperation with non-U.S. regulators. This would ultimately serve to protect investors and increase investor confidence in audit quality.
- We have significant concerns about some of the possible public disclosures discussed in the release regarding audit firms that have not yet been inspected and audit firms that are unable to cooperate with the Board requests for information.

### Proposed Extension of the Deadline for Some 2009 PCAOB Inspections

Grant Thornton International supports the adoption of proposed Rule 4003(g) because it would allow the Board additional time to continue to make determinations about whether, and to what extent, the Board may rely on a non-U.S. oversight system and to pursue cooperative arrangements with non-U.S. oversight entities. We believe that this would ultimately benefit investors and would best serve the public interest.

In the release, the Board notes that it faces two choices, neither of which is ideal: (1) postpone inspections of those 50 audit firms at issue while continuing discussions with non-U.S. regulators; or (2) make inspection demands on individual audit firms over the objection of local authorities, including those instances where local law prohibits audit firms from cooperating with a PCAOB inspection demand.

Were the PCAOB to choose the latter option, it would force non-U.S. audit firms to: (1) violate the law of their home country; (2) violate PCOAB Rule 4006; or (3) cease issuing audit reports for U.S. issuers. Faced with these choices, we believe that non-U.S. audit firms would choose to cease issuing audit reports for U.S. issuers, which would not be in the best interests of investors or the capital markets.

We recognize that Section 106(a) of the Sarbanes-Oxley Act states that non-U.S. audit firms that prepare or furnish audit reports for U.S. issuers are subject to the Sarbanes-Oxley Act and the Board's rules "in the same manner and to the same extent" as U.S. audit firms, subject to the exemptive authority found in Section 106(c) of the Sarbanes-Oxley Act. We also understand the PCAOB's desire to protect U.S. investors by inspecting those non-U.S. audit firms that issue audit reports for U.S. issuers. However, the practical effect of sanctioning non-U.S. firms for violating Rule 4006 or forcing them to cease issuing audit reports for U.S. issuers will ultimately harm U.S. investors. The inspection of non-U.S. firms poses different issues and challenges, and it would be preferable to acknowledge and deal with the critical issues than to force an undesirable result.

Requiring a non-U.S. audit firm to withdraw from registration could make it very difficult for the U.S. issuer being audited by the non-U.S. firm to register and list its securities in the United States. This is because many of those countries that prohibit audit firms in their jurisdiction from complying with PCAOB inspection requests also prohibit audit firms outside that country from auditing issuers in that country. Consequently, if the non-U.S. audit firm is forced to withdraw, there may be no audit firm that can take its place. Thus, the end result could be that an affected issuer may have to delist its securities in the U.S.

The only tenable solution, therefore, is for the PCAOB to continue to work with its non-U.S. counterparts to reach cooperative solutions. We believe that these cooperative relationships between oversight bodies will be increasingly important to the public interest and the efficient functioning of the global capital markets. Allowing itself more time to reach mutual agreements will likely be successful in most instances, as governments, audit firms and issuers all have

strong incentives to remove roadblocks and formulate work-around solutions to the non-U.S. legal restrictions and sovereignty concerns.

To this end, we urge the PCAOB to finalize its proposed policy statement regarding “full reliance” under Rule 4012, taking a principles-based approach in doing so. We believe that a cooperative, principles-based approach under Rule 4012 will ultimately result in increased investor protection, as it will encourage other jurisdictions to establish audit oversight entities based upon key principles designed to ensure audit quality. We will not repeat the points made in our comment letter with respect to the full reliance policy statement, but we offer a few observations relevant to the PCAOB’s proposal regarding Rule 4003.

- The PCAOB should take a principles-based approach when it considers full reliance, and should not seek to require that non-U.S. oversight entities have virtually identical structures as that of the PCAOB.
- The PCAOB should respect the legitimate decisions of other governments who chose to set up audit oversight entities with slightly different characteristics than those of the PCAOB.
- Granting equivalence (i.e., full reliance) is critical, as it will likely cause foreign governments to do the same.

#### Schedule of Inspections Based Upon U.S. Market Capitalization

We generally support the Board’s proposal to set a schedule of inspections from 2009 through 2012 based upon market capitalization of the audit firm’s issuer audit clients. We concur that market capitalization is the most readily measurable way of assessing the impact of a firm’s audit work on U.S. investors.

In the proposal, the Board notes that the setting of a schedule would not operate to prevent an inspection from occurring earlier than called for by the schedule. We support this idea. If the PCAOB is able to reach a cooperative arrangement with a specific non-U.S. jurisdiction, we see no reason why the PCAOB should not inspect firms organized under the laws of such jurisdiction.

The proposal suggests, however, that the PCAOB would opt to have an inspection occur later than called for by the initial schedule only in very limited circumstances. We believe that the PCAOB should make it clear that modifying the schedule to delay inspections would be permissible – especially if there were sovereignty concerns that could not be worked out between the PCAOB and the non-U.S. regulator. It would be counter-productive and not in the best interests of U.S. investors if the PCAOB and a particular non-U.S. regulator were engaged in fruitful, yet incomplete, discussions about cooperation, only to have the PCAOB issue an inspection demand before the cooperative arrangements could be finalized.

Given the foregoing, we suggest that the Board not publish the inspection schedule in order to give itself maximum flexibility. We believe publishing the schedule, only to revise it later due to the inability to resolve sovereignty concerns, would reflect negatively on the audit firm so affected and would imply that such audit firm lacked quality. Instead, the likely reason for the Board not inspecting a firm during the scheduled year would be the inability of the Board and the non-U.S. jurisdiction from reaching an agreement on sovereignty – which would be no fault of the audit firm.

#### Public List of Registered Firms that Have Not Had First PCAOB Inspection

The PCAOB has invited comment on whether it should maintain on its website a list of all registered firms that have not had their first PCAOB inspection even though more than four years have passed since the end of the calendar year in which they issued their first audit report.

We do not support the publication of such a list, because we believe that – despite the comments on page 14 of the release – it would imply that the audit firms so listed lack quality or have not cooperated with the Board.

Rather than providing a list of such firms, we suggest that the Board maintain a list of those countries where non-U.S. legal restrictions and sovereignty concerns have prevented inspections of all such audit firms organized under the laws of those countries. This would benefit investors because it would provide information regarding the countries that do not allow PCAOB inspections, while at the same time it would not single out specific audit firms.

If the PCAOB decides to make public a list of audit firms that have not been inspected, however, we request that the Board include substantial cautionary language in connection with the list, stating among other things:

- That the failure to have been inspected does not mean that the audit firm lacks quality; and
- That the failure to have been inspected does not reflect that the audit firm is at fault in any way and does not evidence a lack of cooperation, but instead, reflects the inability of the PCOAB and the non-U.S. regulator to reach a cooperative agreement regarding non-U.S. legal restrictions or sovereignty concerns.

#### Whether and how a non-U.S. legal restriction or sovereignty concern should be factored into the PCAOB's consideration of an appropriate sanction

The PCAOB has invited comment on whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into its consideration of the appropriate sanction for violating Rule 4006.

Grant Thornton International believes that non-U.S. legal restrictions or the sovereignty concerns of local authorities should be factored into the Board's consideration in any PCAOB disciplinary proceeding for failing to provide information requested in an inspection. We

believe that a non-U.S. audit firm should not be sanctioned for not providing information in response to PCAOB requests due to legal restrictions, which should have been fully explained and supported in the legal opinion filed with the PCAOB in the firm's application for registration.

The inability of an audit firm to cooperate due to legal restrictions does not reflect a voluntary choice or failure to voluntarily cooperate by the audit firm in question; rather, it reflects the failure of two national regulators to reach a cooperative agreement to overcome the legal restrictions or sovereignty concerns. In these situations, the audit firm should not be sanctioned.

### Public Disclosure Proposals

The Board has asked for comment with respect to the benefits and drawbacks of a rule requiring certain disclosures when audit firms are unable to produce information in response to inspection demands due to non-U.S. legal restrictions or sovereignty concerns.

Grant Thornton International believes that the disclosures outlined on page 17 of the release would cause investors to doubt unnecessarily the quality of the audit firm and audit in question and would suggest a willful failure to cooperate.

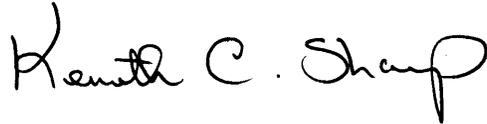
We also believe that the disclosure options are unnecessary – particularly the latter three bullet points on page 17 – because existing disclosure requirements are sufficient to ensure investors that the PCAOB has sufficient oversight over the audit firm. Specifically, the latter three bullet points would target, among other things, the situation where the U.S. member firm of a global audit network uses the work of another member firm in the course of an audit. In such a situation, it is typical for the U.S. audit firm (which is the principal auditor and which has been inspected by the PCAOB) not to refer to the foreign member firm. It is, however, unnecessary to make such a disclosure because the U.S. firm takes responsibility for the audit as a whole, and in the process, performs appropriate audit procedures and obtains supporting documentation as required by professional standards. Given that the U.S. member firm is subject to PCAOB registration and inspection requirements, the PCAOB should be able to confirm through the inspection process that the audits in question were performed in accordance with PCAOB standards.

We feel strongly that the disclosures suggested in the release would serve only to confuse investors, as the principal auditor may be required to disclose a long list of audit firms in a variety of countries, a description of the work performed by the non-U.S. audit firms, and information regarding the principal auditor's policies and procedures. These disclosures could be quite lengthy and boilerplate in nature, and thus not provide any meaningful information to investors. The proposed disclosures also do not acknowledge that non-U.S. audit firms that are unable to provide information because of sovereignty concerns might be subject to inspections by their home country audit oversight entity.

\* \* \*

Thank you for your consideration to the comments mentioned herein. If you have any questions about this letter, please contact me at [ken.sharp@gt.com](mailto:ken.sharp@gt.com) or +1 704.632.6781, or Jon Block at [jon.block@gt.com](mailto:jon.block@gt.com) or +1 202.861.4100.

Sincerely,



Kenneth C. Sharp  
Global Leader – Assurance Service  
Grant Thornton International



**Private & Confidential**

2 February 2009

Office of the Secretary  
PCAOB  
1666 K Street  
N.W.  
Washington D.C.  
2006  
United States of America

Dear Sirs,

**PCAOB Rulemaking Docket Matter No. 027**

The Hong Kong Institute of Certified Public Accountants (HKICPA) is the only statutory licensing body of accountants in Hong Kong responsible for the professional training, development and regulation of the accountancy profession. The HKICPA is responsible for registration, inspection and sanctions over all auditors in Hong Kong.

The HKICPA acknowledges the importance of regulation and oversight of audit firms in maintaining public confidence in financial reporting and we take our regulatory responsibility very seriously in view of Hong Kong's position as a major international capital market. We welcome the opportunity to provide you with our comments on the captioned document.

As the regulator of the audit profession in Hong Kong the HKICPA recognizes the importance of any regulatory or oversight mechanism being comprehensive and applied equivalently to all firms subject to regulation.

However, the HKICPA believes that there must be an acceptance that in some jurisdictions conflicts between local legal constraints or sovereignty issues may take significant amounts of time and effort to resolve, if resolution is possible at all. To minimise the potential effects of such situations the HKICPA would encourage that the maximum possible effort is made to achieve PCAOB aims and requirements in collaboration with local oversight and regulatory bodies. The HKICPA is of the view that collaboration and steps towards mutual recognition between oversight and inspection authorities in national jurisdictions is the best route to effective international oversight.

We believe that the resolution to problems caused by impediments to the PCAOB inspection process through legal constraints or sovereignty issues would best be achieved through collaboration rather than the introduction of additional specific rules.



As a general principle the HKICPA would be concerned if sanctions were to be applied to firms that had been unable to comply with PCAOB inspection requirements as a result of local laws or regulations that a firm is compelled to follow. The HKICPA acknowledges the PCAOB commitment to transparency but has concerns that disclosure of delays to the inspection programme that identifies firms, whether directly by the PCAOB or through the auditor's report, may result in users and investors drawing unsubstantiated conclusions on the quality of firms where the firm's failing is a result of circumstances that the firm itself cannot affect.

The HKICPA recognizes that there needs to be a practical element to the application of regulation and oversight and accordingly appreciates the extension of deadlines for inspection that have been made by the PCAOB to allow more jurisdictions time to resolve potential conflicts between local legal constraints or sovereignty issues and PCAOB oversight requirements.

We trust that our comments are of assistance to you. If you require any additional information on this matter or auditor regulation in Hong Kong in general we may be contacted at [chris@hkiipa.org.hk](mailto:chris@hkiipa.org.hk) .

Yours faithfully,

Chris Joy  
Executive Director

CJ/dy



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

By e-mail: [comments@pcaobus.org](mailto:comments@pcaobus.org)

February 2, 2009

541/584

Dear Sir / Madam

**PCAOB Rulemaking Docket Matter No. 027 – Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms and Other Issues Relating to Inspections of Non-U.S. Firms**

The Institut der Wirtschaftsprüfer [Institute of German Public Auditors] (IDW) is pleased to have the opportunity to comment on the above-mentioned PCAOB Rulemaking Docket Matter concerning inspections of non-U.S. firms. We wish to comment on this issue, since a number of our members, who are registered with the PCAOB, are likely to be directly affected by the proposals.

We view the proposals in general as a step in the right direction, and welcome the fact that, in taking this action, the Board concedes that there is a need for more time to address certain problems it is currently facing in its inspection program, including that of legal conflicts. As at the date of this letter there are certain conflicts between the relevant German and U.S. laws, which prevent German firms from fully cooperating with the PCAOB. Indeed, adequate time is needed if this situation is to be resolved in a satisfactory manner, preferably by means of cooperation between oversight authorities in accordance with the concept of mutual reliance. We would like to stress that, in our opinion, it is neither justifiable nor necessary to penalize German audit firms in any way in the meantime.

Whilst we appreciate the position in which the PCAOB is currently placed, given the special issues posed in respect of non-U.S. firms, we do not support all the actions proposed by the PCAOB at this stage because certain initiatives on the

Institut der Wirtschaftsprüfer  
in Deutschland e.V.

Wirtschaftsprüferhaus  
Tersteegenstraße 14  
40474 Düsseldorf  
Postfach 32 05 80  
40420 Düsseldorf

TELEFONZENTRALE:  
+49 (0)211 / 45 61 - 0

FAX GESCHÄFTSLEITUNG:  
+49 (0)211 / 454 10 97

INTERNET:  
[www.idw.de](http://www.idw.de)

E-MAIL:  
[info@idw.de](mailto:info@idw.de)

BANKVERBINDUNG:  
Deutsche Bank AG Düsseldorf  
BLZ 300 700 10  
Kto.-Nr. 7480 213

GESCHÄFTSFÜHRENDER VORSTAND:  
Prof. Dr. Klaus-Peter Naumann,  
WP StB, Sprecher des Vorstands;  
Dr. Klaus-Peter Feld, WP StB CPA;  
Manfred Hamannt, RA



**Page 2/11** Comment letter to the PCAOB dated February 2, 2009

part of other parties, including counterpart oversight authorities that are currently in progress may require further time for completion. For example, we note that in the European Union discussion of practicalities relating to Article 47 of the 8<sup>th</sup> EU Directive<sup>1</sup>, which deals with cooperation with competent authorities from third countries, will be continuing into early 2009. We realize that the PCAOB has stated in the Release that it remains hopeful that ongoing discussions with certain local authorities will result in the resolution of outstanding issues, but suggest the Board may, in some cases, also need to provide further leeway, should this not prove to be the case in the timeframe envisaged.

We also share the PCAOB's view that there is long-term value in accepting a delay in inspections to continue working toward cooperative arrangements and agree that this is indeed preferable to precipitating legal disputes involving conflicts between U.S. and non-U.S. law. However, as mentioned above, we are not convinced that the envisaged length of time for the postponement of overdue initial inspections will be adequate in every case to allow measures to be established to satisfactorily address the problems posed by legal conflicts. As opposed to forging ahead with its own program of inspections and thus forcing certain individual firms to either violate local law or risk being sanctioned by the PCAOB, we suggest the Board consider whether it could place some degree of reliance on inspections carried out by a foreign oversight authority possibly with disclosure of such fact as an interim measure whilst the Board completes its own negotiations with, or evaluation of, the respective authority, which as we discuss below, should be carried out with a view to achieving full reliance within an agreement on mutual recognition wherever possible. We believe that such interim measures would be in the wider public interest and the protection of investors. Furthermore, as we explain in more detail below, we believe that certain other aspects of the proposals are not in the public interest.

In this letter, we firstly discuss these general concerns, and then comment on specific details of the proposals put forward in the above-mentioned PCAOB Rulemaking Docket Matter. We also discuss certain further aspects of this issue which did not feature in the discussion in the above-mentioned Release, and include suggest possible courses of action related thereto.

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<sup>1</sup> DIRECTIVE 2006/43/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/ 660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC



**Page 3/11** Comment letter to the PCAOB dated February 2, 2009

## **General Matters of Concern**

### *Coordination and Cooperation with Foreign Oversight Authorities*

We are concerned that the above-mentioned PCAOB Rulemaking Docket Matter refers only to initial inspections performed either jointly with counterpart foreign oversight authorities or solely by PCAOB inspectors, but does not refer at all to the possibility of the PCAOB placing reliance on the work of counterpart foreign oversight authorities, despite the fact that the PCAOB itself recognizes that this may be one way in which legal conflicts may be addressed. Since the issue of reliance on the work of counterpart foreign oversight authorities is highly relevant to any consideration of the PCAOB's inspections program as a whole, we do not believe the timing of certain inspections can be dealt with without considering the issue of such reliance.

We infer from remarks on page 5 et seq. of the Release that whilst the Board confirms its willingness to coordinate with foreign oversight authorities, it may not yet be actively seeking to place full reliance on inspections performed by foreign oversight authorities. Indeed, to date the PCAOB has apparently made little or no discernable progress towards mutual recognition based on full reliance, since the Release states that all of the 123 non-U.S. inspections completed to date have involved either joint inspections (57) or PCAOB-only inspections (66).

In a letter to the PCAOB dated 29 February 2008, we had commented on the Proposed Policy Statement concerning the PCAOB's potential reliance on inspection work performed by foreign oversight authorities. In particular, we had urged the PCAOB to undertake a constructive evaluation of individual oversight systems taken as a whole, including due consideration of the environment in which they operate, with the ultimate view to allowing the PCAOB to place full reliance on the foreign oversight authority once the Board is satisfied as to the effectiveness of the respective oversight system. This would, in our opinion, facilitate the establishment of cooperative arrangements with the relevant counterpart oversight authorities such that joint inspections would not be a permanent feature, but would be replaced by consultation on work programs and notification of subsequent results and so forth following initial assessment of the individual country's system.

While we appreciate that, as stated on page 6 of the Release, the Board may need to expend a substantial effort in evaluating a particular non-U.S. system or trying to resolve potential conflicts of interest, we remain of the opinion that mutual recognition, where this can reasonably be achieved, would involve a "one-



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off” effort, which, in the long term, is in the best interests of investors in the relevant capital markets, foreign oversight authorities and the PCAOB itself. Accordingly, we would like to once again urge the PCAOB to take appropriate steps and also to allow sufficient time to seek mutual recognition with its foreign counterparts to the full extent possible.

In this context, we would like to remind the Board that we had also commented upon the fact that in the Proposed Policy Statement the PCAOB itself had not given sufficient regard to, for example, the significant factors the EU Statutory Audit Directive (8<sup>th</sup> EU Directive) specifies as prerequisites for cooperation between auditor oversight authorities of EU Member States with the competent authorities from other countries. In our opinion, this issue also needs to be addressed as a part of the “solution”, at least as far as Europe is concerned. In a European context, the relevant article of the Directive states that the European Commission would need to be satisfied that the PCAOB is able to treat certain information as confidential before it can be made available.

### *Legal Conflicts*

The satisfactory resolution of conflicts between U.S. and non-U.S. law is not only in the interests of individual firms affected and the PCAOB, but also in the public interest, both in the U.S. and in the individual foreign jurisdiction affected, because public accounting firms must fully uphold the laws valid in the jurisdiction in which they operate at all times – and be seen so to do. If firms were to be coerced or forced by the PCAOB in its capacity as an auditor oversight authority into violating “selected” aspects of their home-country law public confidence in their integrity, that of oversight authorities and indeed the integrity of the law itself would be severely damaged. It is for the respective legislator(s) to amend laws to the extent necessary to facilitate cross-border oversight measures; not for individual firms to [or to be forced to] violate their home-country law, irrespective of how valid the reason may be to individual parties. The Act, and in particular Sec. 104(d)(1) of that Act, possibly did not foresee the extent of the legal conflicts the PCAOB would face, neither were home country laws designed to accommodate PCAOB inspections. Reaching satisfactory solutions requires much deliberation, consultation and above all cannot be achieved hastily. In this context we would also like to point out that Sec.106 of the Act does provide a means by which exemptions may be made in some cases. We note with concern that this possibility has not been mentioned at all in the Release, as this omission leads us to the conclusion that the Board has either not even countenanced the idea that exceptions of any sort could be made, or, alternatively that



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the Board has considered and dismissed this idea without disclosing this fact in this or other public Releases, thus precluding public discussion. In our opinion, this is an issue worthy of further discussion in the public forum, not only within the confines of the PCAOB itself.

We cannot support the PCAOB's implied contention that it may be necessary for non-U.S. audit firms to be forced to either deny their cooperation or comply with requests of the PCAOB in violation of their local law, simply because adequate constructs have not (yet) been established to address legal conflicts. It is untenable to use individual non-U.S. audit firms as what would amount to "pawns" to highlight those inconsistencies in lawmaking that become apparent in cross border situations. The individual non-U.S. firms affected find themselves in this situation through no fault of their own, but, at the same time, are not in a position to influence legislators to hasten the resolution of such legal conflicts. As we have stated above, before firms are placed in this situation, reasonable but adequate time needs to be allowed for the PCAOB to continue negotiations with its foreign counterparts and, where appropriate, with national legislators or transnational legislative bodies such as the European Commission in order to arrive at solutions that are acceptable to all parties affected. There may also be a need to devise an alternative measure in the meantime, perhaps along the lines as we have suggested above. We question whether the Board might not avail itself of the possibility of exempting firms or classes of firms from specified provisions of the Act or the Rules of the Board, pursuant to Sec.106 (c) of the Act in this regard.

### **Specific Comments on PCAOB's Proposals**

#### *Adoption of an Amendment to Rule 4003 Extending the Deadline for Certain 2008 Inspections – Addition of Rule 4003(f)*

We support the Board's amendment to Rule 4003 to allow the Board to postpone the inspections of those foreign registered public accounting firms that are currently required to be conducted before the end of 2008 for up to one year as a first, but not necessarily final step.

This notwithstanding, in our view, the statement on page 9 that the Board does not intend to make any further adjustments to the inspection frequency requirements for initial inspections that were due to have been performed by the end of 2008 may be premature. We are extremely concerned as to the stance taken by the PCAOB in respect of a reluctance to cooperate on the part of an *individual* firm which finds itself in the situation of not yet having undergone an initial in-



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spection involving the PCAOB which has become overdue, should the issue of legal conflicts the firm is faced with not have been satisfactorily resolved within the extended timeframe. In any case, we do not understand the rationale for the PCAOB's belief that all initial inspections due to have been performed by the end of 2008 should be postponed by only one year, whereas initial inspections otherwise due by the end of 2009 may, in some cases, be postponed further – i.e., for up to 3 years. We note that, in proposing the 3 year extension, the Board makes a distinction between firms headquartered in countries in which no foreign registered public accounting firm that the Board inspected is headquartered and those where this is not the case. This distinction may be equally appropriate in respect of initial inspections due to have been performed by the end of 2008. As a minimum, we suggest the PCAOB consider whether a staggered approach such as that proposed for the latter inspections' postponement might be equally appropriate for those initial inspections due to have been performed by the end of 2008.

*Proposed Amendment to Rule 4003 Extending the Deadline for Certain Inspections Otherwise Due to be Performed in 2009– Addition of Rule 4003(g)*

We generally support the proposal to extend, for a further three years, the period in which initial inspections of the 70 certain non-U.S. firms otherwise due by the end of 2009 shall be performed. As discussed above, we believe that more time will be needed for, among other things, the PCAOB to finalize individual agreements relating to the implementation of PCAOB Rule 4012 together with its foreign counterparts.

*Transparency Concerning Delayed Inspections*

A completed inspection report alone can provide truly useful information to an investor. We doubt whether publishing the identity of firms that have not been inspected within the timeframe would provide investors with meaningful information. In particular, we are concerned if the information is made public in the manner proposed in the Release, investors and other interested parties may inappropriately attach negative connotations to that information. Indeed, such publication may unintentionally lead to a certain amount of “stigmatism” of the individual firms affected. For example, a non-U.S. firm servicing a U.S. issuer(s) may be “un-inspected” either because no inspection is yet due, in which case the public would not be specifically informed that there has yet to be an inspection; or the inspection has become overdue and the public would not be so informed. The resultant “negative publicity” could have an unwanted impact on



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auditor selection, should public perception lead to the discrimination of firms falling into the latter category.

*Obligations of Registered Firms*

Notwithstanding the fact that firms registered with the PCAOB are required to cooperate in an inspection, as we have reasoned above, we believe it is in the public interest that individual firms in a particular country have legal certainty that they will not violate home country law in making their audit documentation available to the PCAOB. As the Board observes, firms may, in the absence of this legal certainty, be reluctant to provide requested information to the PCAOB.

We are concerned that the statement on page 15: “The Board cannot, however, let the prospect of such refusals dictate delays in the Board’s efforts to conduct inspections.” and the text in footnote 35: “The Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding instituted under section 105(c) of the Act for failing or refusing to provide information requested in an inspection.” do not take account of the fact that there may be firms, that through no fault of their own, genuinely find themselves in a situation in which they need to obtain legal certainty before making audit documentation available to the PCAOB. These firms are not being willfully uncooperative and, on this basis, we do not agree that their registration with the Board should necessarily be jeopardized. Indeed, the intent underlying these two statements appears, to us, to be in conflict with the statement on page 16 in which the Board states that “consideration of any actual noncooperation case will be based on the facts of the case”.

As we have explained above, we find it unacceptable that the PCAOB should attempt to force individual firms to violate or potentially violate their home-country law, irrespective of how valid the reason may be to individual parties. Rather, we suggest that the PCAOB needs to take appropriate but differing measures to deal, on the one hand, with those outright refusals to cooperate that section 102(b)(3)(B) of the Act was clearly designed to guard against and, on the other, with reasoned delays that do not reflect any intent not to cooperate on the part of the firm. In the case of the latter, as we have explained above, we do not believe it is in the public interest for the PCAOB to request information at a point in time where the firm is not in a position to make that information available, inevitably forcing sanctions.

In addition, the PCAOB might like to note that in respect of sovereignty concerns Article 47 of the EU 8<sup>th</sup> Directive specifically provides that “...the request from a competent authority of a third country for audit working papers or other documents held by a statutory auditor or audit firm can be refused where the



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provision of those working papers or documents would adversely affect the sovereignty, security or public order of the Community or of the requested Member State ....". This is in direct conflict to the text of PCAOB Release's footnote 35 quoted above.

### *Sanctions Resulting from Noncooperation*

We note that on page 16 of the Release, the Board invites public comment generally on whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006.

In our opinion, sanctions as foreseen by the Act, including deregistration as a last resort, may be appropriate in some, but not necessarily all circumstances. We therefore agree with the spirit behind most of the proposed actions. However, as we have argued above, forcing a non-U.S. firm to choose between denying PCAOB inspectors access to audit documentation, thus requiring the PCAOB to instigate sanctions for a violation of PCAOB Rule 4006, or alternatively violating its home-country law, and thus occasioning sanction in the country the firm is headquartered, is undesirable, and would furthermore, result in sanctions that were to all intents and purposes "underserved" from the viewpoint of an individual firm so sanctioned. In our view such ultimate sanctions should be reserved for cases of willful non-cooperation. Indeed, we have argued above that postponing an inspection to allow legal uncertainties to be clarified, provided there is reason to believe that such clarification will be forthcoming in the near future, is a far more appropriate course of action than requesting full cooperation when that cooperation on the part of an individual firm cannot be immediately forthcoming. In such circumstances, in our opinion, delaying an inspection is preferable as it may well obviate the need for the PCAOB to impose sanctions at all. In any case, sanctions involving revocation of a firm's registration with the Board will not be appropriate in all circumstances. We would also like to remind the Board that many non-U.S. firms registering with the Board initially did not do so entirely of their own volition, rather they were placed in the situation where having accepted an audit engagement they were subsequently required to register with the PCAOB. Given these circumstances the act of registration did not reflect a willing consent on the part of the German firms, who at that time, being aware of the legal conflicts involved did not confirm such consent originally. Sanctions involving the revocation of a firm's registration, therefore need to be viewed as course of last resort.



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Indeed, in many cases these very non-U.S. firms are the only auditors empowered by home country law to perform statutory audits of the companies concerned, such that these firms would also be best placed to perform any audit work on a significant subsidiary of a U.S. parent company to the extent that they are not also the principal auditor. Revoking registration of such firms would mean a significant duplication of audit work, assuming indeed it were even practicable from a legal perspective for firms from a foreign jurisdiction, including the U.S., to perform the necessary audit work in respect of an U.S. issuer previously performed by a deregistered non-U.S. firm. Clearly such doubling of efforts and associated costs should be avoided whenever possible. Furthermore, when the non-U.S. firm is also the principal auditor for a foreign company or group listed in the U.S., certainly in Germany, and we believe in most countries, statutory audits could not be performed by firms other than those licensed in the particular country; thus there could be no audit performed to satisfy U.S. requirements if those firms were not authorized. Clearly, forcing such a situation is undesirable.

#### *Transparency of Noncooperation in the Public Interest*

We refer to our comments above in respect of the proposal to inform the public as to the inspections carried out and also as to those not performed on schedule as these comments apply equally to a group audit situation. We do not believe that information such as that proposed on page 17 should be placed within the auditor's report. As we have suggested above, additional information about inspections undertaken by the home-country oversight authority in the absence of initial inspections by the PCAOB might be useful to investors.

We are concerned that in proposing that a principal auditor collect and present the information outlined in the third and fourth bullet points on page 17, the PCAOB would be requiring principal auditors to assume certain duties that amount, albeit in a limited way, to an oversight function and to make public the results thereof. In this context, we note that auditing standards generally require principal auditors to be satisfied that the standard of work performed by other auditors, for example in respect of a subsidiary company, is of appropriate quality for the purpose of a group audit; this includes certain considerations as to the audit firm performing that audit work. In complying with such requirements, the principal auditor essentially "checks the quality" of the work performed and further considers the "suitability" of the other audit firm. Consequently, inspection of that same firm and review of that same work by the PCAOB would represent a doubling of effort. In any case, the very fact that an inspection of that other



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firm had been carried out by the PCAOB would not relieve the principal auditor of the obligation to “check the quality” of this work performed by the other audit firm; this fact would only be relevant to the principal auditor’s consideration of the “suitability” of the other audit firm.

Following on from this, we would like to point out that whereas the PCAOB interim auditing standards require a principal auditor make inquiries concerning the professional reputation and independence of the other auditor, irrespective of whether or not the principal auditor decides to make reference to the audit performed by the other auditor, Revised and Redrafted International Standard on Auditing 600 “Special Considerations— Audits of Group Financial Statements (Including the Work of Component Auditors) specifies, among other things, in more detail the understanding the group engagement team is required to obtain of the “other” or component auditor at the stage when there are plans to request a component auditor to perform work on the financial information of a component. This understanding extends, in paragraph 19(d) of that Standard, to whether the component auditor operates in a regulatory environment that actively oversees auditors. The requirements in ISA 600 for participation in, and review of work performed by component auditors are also considerably more comprehensive than those in the PCAOB’s interim auditing standards.

In our view, such requirements properly belong in auditing standards, as they serve to ensure audit quality. We do not agree that oversight measures such as publishing relevant material on deficiencies in a firm’s performance in other engagements in prior years should be passed on to principal auditors as proposed in the Release. Consideration of whether a principal auditor has adhered to the requirements of auditing standards designed to ensure the quality of work performed by other auditors is a matter for oversight authorities, but not for publication in an auditor’s report. In our opinion, it would be more appropriate for this type of information to be documented by the principal auditor to evidence the audit work performed in this regard. The question that arises is whether the interim auditing standards used by the PCAOB may need to be revised to address this specific aspect in more detail, in particular given the fact that in some cases a principal auditor may, pursuant to AU 543. 06 et seq. decide not to take responsibility for work performed by an other auditor (division of responsibility).

Furthermore, when the audit firm is not also the principal auditor, the significance of any work the principal auditor uses, which has been performed by a firm that has declined to provide information or documents in response to a Board inspection demand on the basis of non-U.S. legal restrictions or sovereignty issues, ought to be considered in determining whether, and, if so, what



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information would best serve the needs of investors. Indeed, if the role of such an audit firm is not a “substantial role” investors are unlikely to benefit from this information as proposed.

We hope that our comments will be useful in your further consideration of the various issues discussed. Should you have any questions about our comments, we would be pleased to be of assistance.

Yours very truly



Klaus-Peter Feld  
Executive Officer

**KPMG LLP**  
8 Salisbury Square  
London EC4Y 8BB  
United Kingdom

Tel +44 (0) 20 7311 1316  
Fax +44 (0) 20 7311 4242  
DX 38050 Blackfriars

Office of the Secretary  
PCAOB  
1666 K Street, N.W.,  
Washington,  
DC 2006  
United States of America

Our ref hpa/dlg/181

2 February 2009

Dear Madam or Sir

**PCAOB RELEASE 2008-007 (RULE 4003) of 4 December 2008**

We very much welcome the opportunity to comment on the Board's release on adopting an amendment to Rule 4003 on the inspection of foreign registrants on behalf of KPMG International, the KPMG network of independent member firms. KPMG acknowledges the Board's mission to protect investors in the US capital markets and the strong support of the Board for closer international cooperation among oversight bodies. There are 50 KPMG member firms from outside the United States that are registered with the PCAOB, of which at least 39 registrants have requested home country reliance under Rule 4011.

KPMG has always supported robust oversight based on international cooperation and home country control principle where an audit firm is subject to a single regulatory framework, led by the independent home country regulator, that works with and shares relevant information on methodologies and outcomes with other regulators that have a relevant interest, but who place full reliance on that home country regulator. Therefore, we believe the broad thrust of the Policy Statement of 5 December 2007 does allow some greater flexibility and time toward regulators around the globe operating within a home country-led framework supported by shared protocols, thus avoiding multiple and overlapping inspections.

**Inspection Timing:** Within this context, KPMG broadly agrees with the more realistic timescale set out for outstanding inspections and recognise the immense work load and challenge which the cyclical inspections of ex-US audit firms impose on the PCAOB. We appreciate the flexibility which the PCAOB shows in order to find the right balance between its mandate to oversee all registered audit firms and the difficulties encountered when performing this task which are not only due to the immense number of firms to inspect but also due to legal conflicts which arise when performing inspections in foreign territories.

**Registered Firms' Obligations:** KPMG has greater concerns in relation to the approach described on page 15 of Release No. 2008-007 and as expressed in footnote 35 (page 16 of the Release). If adopted,

it could place the registered foreign audit firms in an invidious deadlocked position of either not being compliant with the PCAOB rules or not being compliant with applicable local laws. Hitherto, the PCAOB had shown great sensitivity in trying to avoid such conflict.

Foreign audit firms have to register with the PCAOB in order to be able to issue audit reports on ex-US issuers with US listings and/or to participate in the audit of US-domestic issuers that have significant overseas operations (“substantial role” criterion). If foreign audit firms had not registered with the PCAOB, both US and ex-US issuers would have come into a situation where they could not present audited financial statements to the public. This would have a serious negative impact on the US capital markets. Thus, it is not fair to say that foreign firms register voluntarily and that they may withdraw from registration. In the interest of the issuers and the capital markets, there was no practical alternative for ex-US audit firms that act as principal auditor or in a “substantial role” on the audit other than to register with the PCAOB. When registering, KPMG member firms undertook to comply with PCAOB requests for cooperation to the fullest extent permissible under applicable law.

Therefore, where local laws prevent foreign audit firms from fully cooperating with the PCAOB, they cannot reasonably be expected to breach local laws, and where there are conflicts between PCAOB requests and local laws, these need to be resolved in a manner that is satisfactory to both PCAOB as well as local governmental bodies, whose valid interest in enforcing local laws and regulations need to be appropriately acknowledged and respected. We would strongly oppose any sanction on a foreign registrant merely for following locally applicable laws.

In certain jurisdictions, the ability of an audit firm to submit to inspection by the PCAOB is limited by the broader stance taken by home country authorities that may regard inspections by non local regulators as an infringement of their sovereignty. As more fully explained in the attached detailed response, the proposed stance and sanctions by the PCAOB on registered firms that are unable to fully comply with requests for information due to home country legal or sovereignty impediments, which could include revocation of registration, could be detrimental to audit quality, could result in expectations that a registered audit firm should contemplate violating local laws, and may undermine efforts to find effective solutions to those issues.

### **Conclusion**

KPMG supports the Board’s goal of closer international cooperation among oversight bodies. We believe that the International Forum of Independent Audit Regulators (IFIAR) is the right platform for discussion of further convergence of oversight systems and on promoting best practice in inspections. Equally, we would hope that the PCAOB will work through IFIAR with their peers in other countries to find pragmatic ways around legal conflicts while ensuring that investors (in whatever territory) are protected and can have full confidence in the quality and integrity of the audit firm and process.

Our detailed response is set out below and we would be very willing to participate in any Round Table, or to provide further evidence, to explore workable solutions to these issues. If you have any further queries, please contact Hans-Peter Aicher ([hpaicher@kpmg.com](mailto:hpaicher@kpmg.com)) on +49 89 9282-1453 or David Gardner ([david.l.gardner@kpmg.co.uk](mailto:david.l.gardner@kpmg.co.uk)) on +44 20 7311 1316.

Yours faithfully

*KPMG International*

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## **I. Part I of Release No. 2008-007 – Timing of Certain Inspections**

- The slippage in timing underlines the necessity that regulators across the globe converge their oversight systems and coordinate their inspection activities; no regulator will ever be able to have the resources necessary for performing inspections worldwide.
- Only mutual recognition and reliance on home country inspections can overcome this lack of resources and help the oversight bodies to concentrate on the audit firms originating in their own country; as more and more jurisdictions implement oversight systems which are equivalent to the PCAOB system, such move to mutual recognition should remain in the focus of further PCAOB rulemaking; the Policy Statement of 5 December 2007 points in this direction (but does not go far enough because it only discusses “full reliance” which is less than “mutual recognition”, see our Comment Letter on the Policy Statement of February 2008).
- The PCAOB itself recognises that joint inspections allow to take advantage of potential efficiencies and to avoid imposing unnecessary regulatory burdens on the firm. Where adequate oversight systems are implemented, we are convinced that the quality of inspections will improve when performed by the local regulator or jointly with the PCAOB.
- In those jurisdictions where the PCAOB has still not reached a cooperative arrangement with the local regulator and is, therefore, behind its own inspection schedule, this is not an issue of non-cooperation by audit firms but is due to the inability to fully comply with requests for co-operation due to local legal and sovereignty issues which are beyond the control of the registered firm to resolve.
- KPMG's position always has been that we welcome a robust and balanced inspection system based on home country control and that all registered KPMG member firms have, and will always, cooperate with the PCAOB to the extent legally possible and KPMG supports joint inspections and recommends the PCAOB's move towards mutual recognition. This is why, the vast majority of ex-US KPMG registrants (at least 39 out of 50) submitted the Rule 4011 statement expressing their request that the PCAOB relies on home country inspections.
- We appreciate the constructive approach of the PCAOB when performing inspections outside the US which indicates that the PCAOB is sensitised to respect local law, where possible.
- Where there is a prospect of reaching a co-operative arrangement on joint inspections with the local oversight body, we would encourage the PCAOB to postpone their sole inspection. Otherwise, audit firms could find themselves in a situation where they appear to be expected to breach one law in order to comply with another law. Such situation would expose audit firms to sanctions by the PCAOB, the local regulator and/or law enforcement agencies; this would send the wrong signals to the capital markets, the issuers and investors because it would undermine the confidence in the integrity of the audit firm; the breach of either law would occur for reasons which are beyond the audit firm's control.
- Therefore, we encourage the PCAOB to follow this path even if this makes any further adjustments to the inspection frequency requirements necessary beyond 2009.
- We do not support the proposed transparency concerning delayed inspections; the contemplated list of all registered firms that have not yet had their first Board inspection seems to run the risk of being a

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black list irrespective of however the PCAOB describes it. Investors can more or less work out which firms the PCAOB has inspected by virtue of the PCAOB having issued a report. The proposed list seems to serve to highlight something that the local auditor has no control over – either due to local legal/sovereignty impediments that may delay an inspection, or due to the timing determined by PCAOB when it chooses to carry out an inspection. Furthermore, as noted below, whether or not an auditor has been inspected is different to the question as to whether that auditor has done sufficient audit work – either as principal auditor or where it participates on an audit. So such lists may confuse investors and negatively impact on the perception of the reliability of the audits of those issuers whose auditors have not yet been inspected, thereby potentially adding to instability of the capital markets.

## **II. Part II of Release No. 2008-007 – Registered Firms’ Obligations**

1. KPMG supports registered firms’ compliance with PCAOB requests for cooperation, subject to compliance with local laws. KPMG opposes any sanction or de-registration of registrants simply for being unable to submit to PCAOB inspection to avoid violating locally applicable laws. Though this conflict is not resolvable by the audit firm, stakeholders might lose confidence in the audit firm, including the issuer itself. It would not be in the interest of the issuer or investors if, for example, a local auditor is de-registered due to local sovereignty / legal impediments in a location where the US issuer has substantive operations.

The Sarbanes-Oxley Act provides in Sec. 106(c) for an exemption authority according to which the PCAOB could, either unconditionally or upon specified terms and conditions, exempt any foreign public accounting firm, or any class of such firms, from any provision of this Act or the PCAOB Rules. So, it is in the discretion of the PCAOB to avoid this delicate position of the audit firms and not to put at risk the confidence of the investors’ community in the (US) capital markets.

It is understood that, of course, this deadlock situation is not due to a non-cooperative behaviour of the foreign audit firms but to the local legal environment which is beyond the control of the audit firms. It must therefore be resolved at regulator and governmental level as we suggest in the opening letter.

2. As regards the contemplated sanctions in case of a registered firm’s failure to cooperate in an inspection (page 16 of Release No. 2008-007), we would like to comment as follows:
  - Restricting a firm from accepting any new issuer audit client would not help to solve the problem because the issuer would not be able to find any other audit firm in that respective jurisdiction which could cooperate with the PCAOB. The reason for this is that non-cooperation is not due to the unwillingness of the audit firm but to the local legal and sovereignty environment; this environment is applicable to all audit firms in that jurisdiction, so the same issue arises for the issuer when selecting any auditor in that jurisdiction.
  - The restriction to perform referred work on the audit of any issuer entails the same problems. For the same reason as described above, the principal auditor (or the client, respectively) could not replace the auditor performing referred work by another registered auditor from the same jurisdiction.

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The only option the client and the principal auditor might have in this situation is that they could engage a non-registered audit firm from that jurisdiction (on the assumption that the referred work is not “substantial” in the sense of the PCAOB Rules) because only such non-registered audit firms would not be exposed to inspections of the PCAOB and, therefore, would not face such a legal conflict.

However, it is doubtful if this would be the right signal to the capital markets and whether this would not have a negative impact on the audit quality if the principal auditor / client would have to choose a local, non-registered audit firm which does not belong to one of the international networks of audit firms.

- Such sanctions would not enhance the competitiveness of the US capital markets, as many all issuers, both US and ex-US, are affected indirectly by the legal and sovereignty impediments their auditors face.
- The PCAOB should consider the negative impact on both US and ex-US issuers which might face a situation where no audit firm would be available in the certain jurisdictions to perform some, or, the entire audit.

To avoid this situation, an issuer might be forced to appoint a US audit firm (or a registered audit firm which is based in another “non-conflicting” jurisdiction) as their principal or “substantial role” auditor, but this would, for various practical reasons, not enhance audit quality, and in any case, may not actually resolve the local legal or sovereignty impediments to provide information concerning audit work undertaken in respect of that local jurisdiction.

### 3. Comments on the contemplated public disclosure requirements:

#### 3.1 Disclosure that the principal auditor has failed to provide information in response to an inspection demand on the basis of non-US legal restrictions could create confusion in the capital markets, including where the auditor has complied with requests from the PCAOB to the fullest extent permissible under local laws. Such inability to provide requested information has no relevance for the financial statements of the issuer.

- However, such disclosure would entail the risk that investors are misled in a way that they misinterpret this non-cooperation as an unwillingness of the audit firm (which is not the case because the audit firm is bound by its local legal restrictions).
- Further, such disclosure could have a negative influence on the competitiveness of the principal auditor because investors could be led to believe that specifically this audit firm does not cooperate with the PCAOB without being aware that all other audit firms from that respective jurisdiction would be in the same position, i.e. could not comply with the PCAOB’s inspection demand.

#### 3.2 Any representation of the principal auditor about whether the principal auditor used the work of any registered firm that had to decline to cooperate with the PCAOB on the basis of non-US legal restrictions or sovereignty concerns could be misleading for the public and the investors because such representation would only be required in cases where the participating auditor is PCAOB-registered. This concept would disregard that not all audit firms are required to register with the PCAOB

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(because they do not play a “substantial role” in the audit) and, therefore, by chance, the representation would not be necessary if the participating audit firm is not registered (and, therefore, not subject to PCAOB inspections).

- This effect is confusing, undermines confidence in the capital markets and negatively affects the competition among audit firms. Finally, such representation would not give any indication about the quality of the audit work performed by the participating audit firm.
- Such a concept may not be helpful to maintain confidence in the quality of audits and the audit oversight system.

3.3 The proposed disclosure requirements in the case when the principal auditor uses the work of any such firm and assumes responsibility for that work (under AU § 543.04) or makes reference to the audit of the other auditor (under AU § 543.06) also confuse registered and non-registered audit firms in an inappropriate manner.

- Existing auditing standards sufficiently stipulate the requirements that have to be met in order to allow the principal auditor to use, and take responsibility for, the work of other auditors. The principal auditor determines whether he may take responsibility for the work of local auditors; however, that determination is distinct from establishing the extent of impediments that may govern the local auditor in complying with requests from PCAOB and their implications on PCAOB’s inspection regime.
- The mere fact that an inspection has been performed would become a sign of quality in this specific audit and may create the expectation of the capital markets and investors that only inspected audit firms could perform high quality audits.
- The proposed disclosure requirements would cover references to all registered audit firms that participate on the audit (irrespective of materiality of the local entity). Auditors in many non-US jurisdictions have various legal impediments that may restrict provision of information by them to the PCAOB. Therefore, the contemplated disclosures could be very lengthy and of no real benefit to investors, given that where the principal auditor takes sole responsibility for the audit report, the burden of obtaining sufficient audit evidence is on that principal auditor. Furthermore, the fact that there may be impediments on participating auditors in complying with PCAOB requests for information does not mean that there were similar impediments on the local auditor to appropriately cooperate with the principal auditor and respond to requests for information from the principal auditor. Nor does it mean, as noted earlier, that the local audits were deficient. However, making disclosures as contemplated could confuse investors.
- Finally, if there was no request for inspection which is at the discretion of the PCAOB, an audit firm would not be “caught” by the disclosure requirement even if there were legal or sovereignty obstacles which would have prevented that audit firm from fully cooperating with the PCAOB. It does not appear appropriate to single out those instances for disclosure where there is an inability of the foreign audit firm to fully cooperate whilst other circumstances which may have more relevance for the public and investors are disregarded.

4. Other possible rulemaking approaches

ABCD

***KPMG International***  
*KPMG Comment Letter to PCAOB on Rule 4003 Amendments*  
*2 February 2009*

- We do not see any appropriate disclosure requirements (nor do we see the need for them) in such situations where audit firms are not able to fully cooperate due to local legal restrictions.
- We see, however, the risk of the creation of new expectation gaps and possible confusion at investor level.
- Rather than imposing additional burdens on audit firms, the PCAOB might consider publishing its own assessment as to the adequacy of foreign oversight systems to the effect that investors will be informed whether or not the principal auditor is subject to a robust oversight regime in its home country in the eyes of the PCAOB (irrelevant of the fact whether or not the PCAOB has achieved a cooperative arrangement on joint inspections with the local regulator); this is also the approach the EU is considering with regard to Art. 47 of the 8<sup>th</sup> Directive.



Paris La Defense, February 2, 2009

Public Company Accounting Oversight Board  
Office of the Secretary  
1666 K Street, N.W.  
Washington, DC 20006, USA  
Attention: J. Gordon Seymour, Secretary, and the Members of the Board

Re: PCAOB Rulemaking Docket Matter No. 027 – Request for public comment on proposed amendment to Rule 4003, concerning the timing of certain inspections of non-US firms and other issues relating to inspections of non-US firms

Dear Sirs,

Mazars is an international organization of European origin, specialized in audit, accounting, tax and advisory services. Its integrated partnership assembles more than 10,500 professionals operating in 50 countries, and there are 12 additional countries where Mazars is present through correspondents and joint ventures. Moreover, via the International Praxity Alliance of which Mazars is a founding member, the group can access the skills and expertise of a further 13,000 professionals in another 23 countries, all of whom possess a common desire to adhere to strong quality guidelines and a collective determination to exceed technical and ethical standards.

In North America, Mazars has a long standing presence via Mazars USA (created in 1988/1989, and registered with the PCAOB). As a natural extension of its development strategy, Mazars has formed several joint ventures with members of Moores Rowland International (MRI) since 2000 to assist its clients in various corners of the world. At the end of 2006, Mazars and the American members of MRI, decided to optimize their relationship, and signed an agreement to launch a new international alliance between independent structures, named Praxity, an international non-profit association registered in Belgium, which became operational in 2007.

We want to preface our comments with general consideration that we fully support implementation of rules strengthening the audit quality, and the contribution of these rules to restore the public confidence in financial reporting and in the world's capital markets. Mazars is therefore fully committed to support PCAOB initiative, as well as those of IFAC, European Commission and other key European or national regulators or oversight that have been already doing good work and are implementing stronger controls in these areas of common concern.

We are pleased to submit this letter in response to the PCAOB's invitation to comment on its proposed amendment to Rule 4003, and we would like to make a few remarks before delving into the questions posed.



2

In general, we are proponents of full reliance, as we stated in our comment letter on Rule 4012<sup>1</sup> dated March 4, 2008. As we stated then and now, there are convergences between the proposed policy statement Rule 4012 and the provisions of the European Audit Directive. We strongly urge the US and non-US oversight systems (EU, H3C, and other) to strive to work towards reaching reciprocity, harmonization, and cooperation to better inspection process.

When full reliance cannot be achieved in the short term, we do believe that joint inspections can improve the quality of inspections in the longer term. But we also consider that mutual recognition and full reliance on third country public oversight bodies is the only practicable solution.

The significant benefits from a true “full reliance” approach would be increased opportunities to expand the focus of inspections on audit quality thereby better protecting investors, cost savings for oversight bodies and audit firms through the elimination of duplication of inspections, but also to prevent significant conflicts of laws and regulations for companies and audit firms, by recognizing the sovereignty of third countries.

We are not proponent of singling out or web-listing non-US oversight systems that legitimately claim the legal restriction exception to not provide information to the PCAOB.

Finally, in Europe, and therefore France, audit firms cannot be held responsible for the delay in PCAOB inspections, as an adequacy decision of the European Commission has to take place first, in accordance with Article 47 of the European Audit Directive. If, as stated in page 16 of the proposed document, “*a registered firm's failure or refusal to provide requested information is a violation of Rule 4006 and is inconsistent with the condition reflected in Section 102(b)(3)*” and “*the Board could impose disciplinary sanctions in any case where a violation of Rule 4006 is established*”, with the associated footnote 35 of a particular concern in this respect, underlining that “*the Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection*”, then the PCAOB Proposed Rule Amendments would force most European audit firms to choose between violating either the European or their home country laws and regulations, or the PCAOB Rules.

We respectfully submit our detailed comments below. We commend the Board for the transparency of its rule deliberation process.

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<sup>1</sup> Rule 4012 - Inspections of Foreign Registered Public Accounting Firms



**# 1 – Mazars’ comments on whether there are other factors that should be treated as a reason to consider moving an inspection to an earlier year (page 13).**

Paragraph D, *Proposed Extension of the Deadline for Some 2009 Inspections*, of this PCAOB proposal noted that under Rule 4003, the PCAOB is required to inspect 70 non-U.S. firms located in 37 jurisdictions for the first time by the end of 2009. 50 out of the 70 non-US firms are located in 24 jurisdictions where the PCAOB will not have conducted any inspections by the end of 2008. Some of these jurisdictions have new local auditor oversight authorities requiring cooperative arrangements before inspections. The steps involved in concluding arrangements and evaluations of the local oversight systems are challenging and time-consuming. Thus, the PCAOB believes that the most practical approach to the jurisdiction-level work is to allow three years beyond 2009 to perform that work. In the meantime, the Board will work toward cooperation and coordination with the relevant local authorities and evaluate relevant systems in response to rule 4011 requests without delaying inspection demands on the selected firms.

The Board will prioritize inspections using U.S. market capitalization of firms’ issuer audit clients (ranking the 50 firms according to the total US market capitalization top to bottom) and certain criteria concerning the number of those 50 firms that would be inspected in each year.

Per the Board any inspection may be moved to an earlier year depending upon certain factors such as:

- 1) presence of certain risk factors (including referred work performed as non principal auditor)
- 2) synchronization of schedules with a local regulator for purposes of a joint inspection
- 3) opportunity to do an inspection earlier
- 4) availability of resources, including availability of inspectors with specialized industry knowledge and relevant language skills
- 5) changes warranted by annual review of market capitalization data

We believe that other potential factors could be considered as a reason to consider moving an inspection to an earlier year such as:

- a) PCAOB deregistration before inspection – If a registered firm up for inspection elected to be deregistered prior to inspection
- b) sanctions by local regulators or evidence of fraud or illegal acts
- c) reorganization of a non-US firm – Merger

In general, Mazars agrees with the Board’s approach in regard to the proposed extension of the deadline for some 2009 inspections as well as with the factors that may cause the acceleration of some of these inspections. Mazars strongly urges the PCAOB and the non-US oversight systems to find common grounds in the area of jurisdiction-level work.



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**# 2 – Mazars’ comments on whether it is appropriate that the PCAOB maintain on its web site an up-to-date list of all registered firms that have not yet had their first inspection as a means to provide public transparency related to delayed inspections. Are there other suitable alternatives (page 14)?**

Per the Board, investors may have an interest in the identity of firms that have not been inspected within the timeframe that investors could reasonably have expected an inspection to occur (2008 and 2009 non-U.S. inspections). Thus, the Board is considering maintaining on its web site an up-to-date list of all registered firms that have not yet had their first PCAOB inspection even though more than four years have passed since the end of the calendar year in which they first issued an audit report while registered with the Board.

Inclusion on the list would not be an indication that a firm has not cooperated with the PCAOB or is at fault in any way, nor would the list be intended as a substitute for action the PCAOB might take in the event that a firm did fail to cooperate. The list would be intended only to provide public transparency related to delayed inspections.

Mazars disagrees with the Board’s approach in regard to “web-listing” non-US firms that have not been inspected within the SOA required schedule. Although it may be consider more transparent, a “Web-listing” of non-US firms may be viewed as a negative mark against firms which have not yet been reviewed. Several other factors to consider are:

- a) It will appear like a double-standard. There are no current plans to list US firms that are at no-fault of their own for non-inspection. Section 106(a) (1) of SOA calls for all registered firms to be subject to SOA and the PCAOB’s rules irrespective of their location.
- b) “Black-listing” non-US firms can create in the minds of US investors the idea that non-US firms are a special category of firms providing sub-standard audit work that US investors may not rely upon in their investment decisions.
- c) This will appear like blackmail with the Board telling the non-US oversight systems that refuse to cooperate on the sovereignty grounds that doing so will get them “web-listed.”
- d) It could also be confusing in the mind of certain investors who may assume that inclusion on the PCAOB list would be an indication that a firm has not cooperated with the PCAOB or is at fault.

Mazars believes that web-listing non-US firms in order to provide public transparency related to delayed inspections will be counter-productive and its costs will outweigh its benefits. Non-US oversight systems may take reciprocal measures if this idea is implemented which can threaten the spirit of cooperation built since the inception of the board.



**# 3 – Mazars’ comments on whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006 (page 16).**

It is noted that the PCAOB plans to continue its efforts to develop cooperative relationships with its foreign counterparts. However, it will also need to make inspection demands on non-U.S. firms even in circumstances where the sovereignty concerns or legal objections of local authorities have not been overcome. The Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense. Even the invocation of Rule 2105<sup>2</sup> which allows a firm's registration application to be considered complete, for purposes of registering the firm, even in the absence of the consent to cooperate will not be sufficient.

A registered firm's failure or refusal to provide requested information is a violation of Rule 4006<sup>3</sup>. The Board could impose disciplinary sanctions in any case where a violation of Rule 4006 is established. There are a range of disciplinary and remedial sanctions available to the Board, for violation of Rule 4006, including revocation of a firm's registration or sanctions short of revocation such as restrict a firm from accepting any new issuer audit clients, or performing referred work on the audit of any issuer for which it has not previously performed referred work, until the firm cooperates in an inspection.

But in the case of non-U.S. legal restrictions or sovereignty concerns of local authorities, no other firm in the country will be in the position to accept these engagements, which we consider as a major issue for the Board.

Consideration of any actual non cooperation case will be based on facts and circumstances. The Board takes into account several factors:

- 1) The importance of the inspection process to the oversight regime established by SOA
- 2) The sensibility to the fact that no cooperation with the board means no registration
- 3) The fact that non-cooperation on a non-US legal restriction or sovereignty concern is different from other non-cooperation circumstances

Mazars believes strongly that the Board and its non-US counterparts must exhaust all of the jurisdiction-level work before reaching the point of mutual disciplines and remedial sanctions. Non-US oversight systems that raise non-cooperation with the Board on legal restriction or sovereignty grounds are not doing so gingerly. It is a fundamental issue of legal sovereignty. No matter how the Board massages it or raises the hammer-sanctions, most non-US oversight systems won't give a blank check to the Board to inspect their systems at will without reciprocity or least to do it jointly. The Board inspection process as conceived now is too intrusive.

Most of the leading EU countries (Germany, France, UK, and Holland) meet most of the Rule 4012 principles which call for full reliance on their non-US inspection process and they still claim the legal restriction exception which is the heart of the issue.

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<sup>2</sup> Rule 2105 Conflicting Non-U.S. Laws.

<sup>3</sup> Rule 4006 Duty to Cooperate With Inspectors



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Meeting requirements for Rule 4012 shall be a prerequisite for Rule 4006 and Rule 4003.

We agree with the Board that the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006. However, we believe that the Board shall seek widespread agreements on this issue before proceeding with sanctions.

**# 4 – Mazars' comments on whether there are possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information (page 17).**

Mazars does not believe that there are any other possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information if due to the fact that non-cooperation is based on a non-US legal restriction or sovereignty concern.

**# 5 – Mazars' comments on whether there are potential benefits and drawbacks of a rule along the lines described above (page 17).**

The Board is proposing that a principal auditor make certain public disclosures as part of, or in connection with, each audit report it issues for an issuer. For example, if the principal auditor has failed to provide information in response to an inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns, the principal auditor would need to disclose that fact as part of, or in connection with, its audit report.

In each case, the principal auditor would need to make a representation about whether the principal auditor used the work of any registered firm that has declined to provide information or documents in response to a Board inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns. The principal auditor would have an obligation to make this inquiry to any registered firm whose work the principal auditor uses, regardless of whether that work constituted a "substantial role" as defined in PCAOB Rule 1001(p) (ii). The principal auditor would also have to retain documentation of the inquiry and response.

Mazars believes that there are no potential benefits but only drawbacks of a rule along the lines described above. These potential disclosures do not add any value to the quality of the audit engagement work or to the quality control systems of the principal auditor. The role of the principal auditor is not to act as a substitute for the Board. Such disclosures have the potential to create backlashes from non-US oversight boards. They also do not support current focus on risk-based approach.

These potential disclosures will not bring about any improvements to the financial reporting as called for by the SEC's Advisory Committee on Improvements to Financial Reporting or the Treasury's Advisory Committee on the Auditing Profession.



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**# 6 – Mazars’ comments on whether there are generally other possible rulemaking approaches relating to those issues that might provide useful disclosure to investors or otherwise be in the public interest (page 18).**

Mazars believes that there are generally no other possible rulemaking approaches relating to those issues that might provide useful disclosure to investors or otherwise be in the public interest. Non-US oversight systems that do not cooperate with the Board by refusing to provide information on the grounds that it may violate their sovereignty are in fact calling for negotiations with the Board. They want these negotiations to remain in the legal arena not in the audit arena. Providing such disclosures to investors or otherwise may be detrimental to the non-US firms reputation in the eyes of the investor as they may consider those firms to be of a lesser quality than US firms. This in turn may inhibit the growth US companies wishing to invest outside the US with no hopes of finding non-US Firms capable of properly providing them services required.

We hope the above comments will be helpful and remain available for further considerations. If you would like to discuss our submission further, please do not hesitate to contact us.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'JL Barlet'.

**Jean-Luc Barlet**  
**Mazars**  
*Risk Management & Audit Quality*



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

Date February 2, 2009  
 Our reference TA-JFPo-09012114  
 Page 1 of 3  
 Concerning PCAOB Rulemaking Docket Matter No. 027

Dear Sir, Madam,

On behalf of the Netherlands Authority for the Financial Markets (AFM) we are pleased to respond to the request for comments from the Public Company Accounting Oversight Board (PCAOB) regarding Release No. 2008-007, Rule Amendments Concerning the Timing of certain Inspections of non-US Firms, PCAOB Rulemaking Docket Matter No. 027.

*Inspections – amendments to Rule 4003*

We are pleased to be informed of the proposed amendments to Rule 4003 that will give the Board the ability to postpone, for up to one year (i.e., to the end of 2009), first inspections of the remaining non-U.S. firms that the Board is currently required to conduct before the end of 2008, and to postpone, for up to three years, first inspections that the Board is currently required to conduct before the end of 2009 in jurisdictions where the Board has conducted no inspections before 2009.

*Conflicts of law*

We would like to point out that at present the Sarbanes Oxley Act and Dutch legislation (as based on the European Statutory Audit Directive, 'Directive') are not compatible. Dutch audit firms need to comply with national legislation which is based on the Directive and which requires that certain conditions have to be met before confidential information can be transferred to foreign regulators. We would like to give the PCAOB into consideration that these non-US audit firms cannot be forced to breach their national legislation, and that as such solutions need to be found for solving the existing conflicts of law.

*Violation of rule 4006 due to conflicts of law*

We are of the opinion that the sanctions against non-US audit firms as proposed in Release No. 2008-007, Rule Amendments Concerning the Timing of certain Inspections of non-US Firms, PCAOB Rulemaking Docket Matter No. 027 are not an effective solution for the above mentioned situation where a violation of Rule 4006 is the result of conflicts of law. These conflicts of law are outside the control of the concerned audit firms who also have reported on these conflicts upon registration with the PCAOB using Rule 2105. We therefore would like to ask the PCAOB to reconsider whether the proposed example of a sanction, being a disclosure in the audit report of the fact that no inspection has taken place by the PCAOB, is an effective solution for the structural problem of

Netherlands Authority for the Financial Markets  
 Chamber of Commerce Amsterdam, no. 41207759  
 Reference of this letter: TA-JFPo-09012114

Netherlands Authority for the Financial Markets  
 Visiting address Vijzelgracht 50  
 P.O. Box 11723 • 1001 GS Amsterdam  
 Phone +31 (0)20 - 79 72 000 • Fax +31 (0)20 - 79 73 800 • www.afm.nl



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conflicts of law. In this respect we like to point out that a sanction does not contribute to a structural solution of the problem of conflicting legislation and it also impacts the audit client negatively. Furthermore, we like to raise the issue of how the users of the audit report should understand the proposed additional disclosure in connection with the audit opinion expressed.

*Exchange of information*

In our view, the core element of cooperation between foreign audit oversight bodies consists of the possibility to exchange information. The Sarbanes Oxley Act does not provide the PCAOB with the possibility to exchange information with the AFM. Under Dutch legislation a foreign competent authority like the PCAOB must have the ability to cooperate with the AFM on the exchange information. As such we consider the principle of mutual recognition and reciprocity as an important prerequisite for effective cooperation.

Furthermore we would like to point out that as the PCAOB is not part of the "Safe Harbor" scheme. The transfer of information to the PCAOB is only possible on the basis of a transfer agreement concluded under Article 26 (2) of Directive 95/46. Such agreement should contain special safeguards which are put in place with respect to the protection of the privacy and fundamental rights and freedom of individuals and as regards the exercise of the corresponding rights.

Due to the above, in order to be able to share confidential information with the PCAOB in view of inspections, there needs to be sufficient time to solve the existing legal barriers and to enter into a transfer and cooperation agreement.

*Possible way forward*

We understand that in accordance with Section 106 (c) of the Sarbanes Oxley Act, the Securities and Exchange Commission ("SEC") and the PCAOB may, by rule, regulation, or order, and as the SEC or the PCAOB determines necessary or appropriate in the public interest or for the protection of investors, either unconditionally or upon specified terms and conditions exempt any foreign public accounting firm, or any class of such firms, from any provision of the Sarbanes Oxley Act or the rules of the Board or the SEC issued under the Sarbanes Oxley Act.

In relation to what is mentioned in the above section on 'Violation of Rule 4006 due to conflicts of law' we would like to give the PCAOB into consideration to exempt EU audit firms from Rule 4006, in so far these audit firms cannot provide information in response to an inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns.

Furthermore, as solving the existing conflicts of law is key for an effective future cooperation between the PCAOB and AFM, we are of the opinion that it is worthwhile first taking the necessary time to have these conflicts of law solved and to conclude on the working arrangements by a transfer and cooperation agreement. According to the Commission Decision of 29 July 2008 the transitional period for audit activities of certain third country auditors and audit entities is applicable to the United States (OJ L 202/70). This means that EU Member States shall not apply Article 45 of Directive 2006/43/EC in relation to audit reports concerning annual accounts or consolidated accounts, as referred to in Article 45(1) of that Directive, for financial years starting during the period



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from 29 June 2008 to 1 July 2010, which are issued by auditors or audit entities from the United States, in cases where the third-country auditor or audit entity concerned provides the competent authorities of the Member State with all of the information mentioned in Section 1 of the Commission Decision.

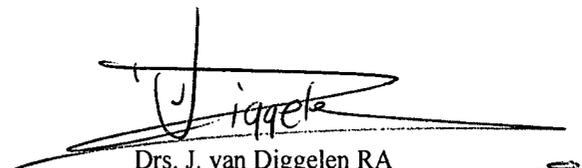
Based on this, we would like to give the PCAOB and/or SEC into consideration to apply a similar transitional period for audit activities of EU audit firms in the United States and exempt these EU audit firms from Section 106 of the Sarbanes Oxley Act and from the PCAOB Rules. The transitional period could be used by the PCAOB and the Member States' oversight bodies to further continue their dialogue on cooperation, to become more familiar with each others structure, operations and approach to inspections and to enter into the necessary working arrangements by means of a transfer and cooperation agreement. Moreover, a transitional period would allow the PCAOB, the European Commission and Member States to address and solve conflicts of law regarding confidentiality issues.

We would welcome the PCAOB to take the above mentioned points into consideration when deciding on the proposed amendments to its Rule 4003.

Yours sincerely,  
Netherlands Authority for the Financial Markets



Prof. dr. S.J. Maijor  
Managing Director



Drs. J. van Diggelen RA  
Head of Audit Firm Oversight



PricewaterhouseCoopers LLP  
Suite 800W  
1301 K St., N.W.  
Washington DC 20005-3333  
Telephone (202) 414 1000  
Facsimile (202) 414 1301  
www.pwc.com

2 February, 2009

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

**RE: Rulemaking Docket Matter No. 027, PCAOB Release No. 2008-007, *Rule Amendments Concerning the Timing of Certain Inspections of Non-US Firms, And Other Issues Relating to Inspections of Non-U.S. Firms***

Dear Sirs:

PricewaterhouseCoopers is pleased to comment on the above-referenced Rule Amendments. We are responding on behalf of the network member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

The oversight and inspection of auditing firms are important elements in maintaining public trust and confidence in financial reporting. We acknowledge the need for the PCAOB to faithfully carry out the legislative mandate for inspection of audit firms as set forth in the Sarbanes-Oxley Act of 2002.

#### **Deferral of Due Dates for 2008 and 2009 Inspections**

We acknowledge the PCAOB's reasons for proposing to defer the due dates for 2008 and 2009 inspections, and the need to modify the inspections schedule. The 3-year schedule described in the proposing release is reasonable, and the proposed transparency requirements surrounding any changes in the review schedule are appropriate.

The Board has indicated that it intends to begin publishing a list of firms for which inspections have not been completed due to local legal impediment. At least some Board members have expressed strong support for the need to do this. We understand the need for the Board to be transparent about matters that have an impact on its ability to meet its legislative mandate. In principle, we have no objection to making the public aware of situations in which legal impediments in a firm's home country have made it impossible to complete the inspection of all or some of the registered firms in that country. However, we think that in practice, it will be extremely difficult to maintain and publish such a list without causing at least some observers to draw inappropriate and negative inferences about the listed firms' capabilities and/or cooperation with the Board. We therefore hope that if the Board adopts such a practice, it will do so only after fully considering all relevant issues and concerns, including but not limited to:

- How can such a list be formatted and arranged so that it emphasizes that the country has imposed the impediment, rather than the individual firm or firms within that country?
- What language will appear, and where, to clearly indicate that a firm's inclusion on the list should not be deemed a reflection on its audit quality or its cooperation with the Board?



- Will firms be on the list when the inspection field work is completed, but the inspection report has not been issued within the requisite time period?
- Will firms be on the list if an impediment delays the start of inspection for part of the three-year period, and subsequent scheduling conflicts force a delay for the remainder of that period?
- In the absence of a legal impediment, will firms be on the list because of inspection delays as a result of accommodating the schedule of the local inspection authority?
- When will firms be taken off of the list – when inspection field work begins, when it ends, when the report is issued, or at some other time?

### **Recognition of Cross-Border Inspection Issues**

The PCAOB has acknowledged on numerous occasions that the laws of other countries can and do introduce impediments to the inspection of non-U.S. firms. In PCAOB Release No. 2004-005, *Final Rules Relating to the Oversight of Non-U.S. Public Accounting Firms* (June 9, 2004), and again in PCAOB Release No. 2007-011, *Request for Public Comment on Proposed Policy Statement: Guidance Regarding Implementation of PCAOB Rule 4012* (5 December, 2007), however, the Board stated its belief that most conflicts of law can be resolved through an approach in which the Board works with the non-U.S. regulator or through the use of special procedures such as voluntary consents and waivers. We do not believe that all such instances can be successfully resolved, and do not think the non-U.S. registered firm should be penalized for home-country law.

We believe that there are two very different environments that impair a registered firm's ability to participate in a PCAOB inspection. One is generally within the control of the registered firm, and one is not. As discussed below, we think the consequences to a registered firm of not providing requested information should be different depending on which environment exists.

- In some jurisdictions, a firm must follow a specified administrative process before it can be inspected or provide requested information. Although these processes may take time and effort to complete, successful navigation of the requirements generally allow inspections to be performed.
- In other jurisdictions, a country's regulatory, judicial and/or legal system does not permit foreign entities to conduct inspections of local audit firms under any circumstances either because of issues of sovereignty or because of stringent rules against disclosing client information and other confidential information. These environments may preclude disclosure of any client information or other confidential information to third parties. These laws cannot be overcome by administrative process. Similarly, there are jurisdictions where the legal framework is not explicit, but government officials with relevant legal authority will not permit inspections to take place. Despite rigorous efforts by a firm in that country, consent for inspection may be denied by those government officials.

In either environment, there may be consequences for firms who violate the law and provide information to the PCAOB inspection teams, including significant penalties, loss of practicing licenses, and criminal sanctions, possibly resulting in imprisonment.

### **Sanctions for Failure to Provide Information**

We support the mandate rooted in Sarbanes-Oxley Act and the obligation for all firms registered with the PCAOB to cooperate with inspections insofar as permitted by their local laws. The PCAOB's original registration process reflected this understanding. We fully support the proposal to consider sanctions against those firms that use local administrative processes as a pretext for failure to



cooperate with a PCAOB inspection. However, for the reasons explained below, we do not believe firms operating in environments that do not permit foreign inspections, in situations beyond their control, should be sanctioned in the same way.

In countries where there are national laws or in which the exercise of governmental authority under the law prevents a firm from providing information to the PCAOB necessary to conduct the inspection, every firm in these countries is subject to the same environment. These firms could not be reasonably expected to act in a way that would subject them to legal consequence; as a result, none of them would likely be able to participate in a PCAOB inspection. As a result, due to circumstances beyond their control, foreign private issuers from such countries would not be able to meet their U.S. statutory obligation to provide audited financial statements, and would therefore be unable to maintain registration of their securities in U.S. We do not believe that this result is in the best interests of the investors who currently hold those securities.

Audit firms should not be required to violate their national law. For this reason, we fundamentally disagree with the Board's view expressed in Footnote 35 that "the Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defence in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection". We believe that firms in such countries should not be subject to sanction.

For registered firms in countries where legal impediments to the PCAOB's inspection can be overcome by following administrative process, we believe a good faith effort should be made by the firm, in cooperation with the PCAOB, the government and/or the home country inspection body, to allow the PCAOB to complete an inspection<sup>1</sup>. In these countries, it is appropriate to expect that all parties will endeavour to take all reasonably necessary steps to allow the inspection to occur.

We suggest that the PCAOB's approach to sanctions reflect the following principles, which are responsive to the different environments that may exist:

- Where administrative process can overcome legal impediment, we agree that firms who fail to follow appropriate process should be subject to sanction. The difficulties of the administrative process should not be used to avoid inspection. However, any sanction taken against a registered firm for failure to provide information in response to an inspection request should consider the firm's efforts to overcome legal impediments to providing that information. In this regard, the firm should be permitted to evidence its efforts to overcome the legal impediments by providing its communications with government officials to the PCAOB to the extent that it is legal to do so.
- In environments where regulatory, judicial and/or legal systems do not permit foreign entities to conduct inspections of local audit firms, we do not believe firms should be subject to sanction as a result of lack of cooperation. Such firms should provide a valid legal opinion that confirms that participation in the inspection process is precluded by law. Similarly, they should not be sanctioned if they have been informed by a government official with relevant authority that the inspection is not permitted, or that restricts the information that may be transmitted.

In our 4 March, 2008 response to PCAOB Release No. 2007-011, *Request for Public Comment on Proposed Policy Statement: Guidance Regarding Implementation of PCAOB Rule 4012*, we encouraged the PCAOB to work closely with other inspection bodies toward the objective of increasing

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<sup>1</sup> For example, national law may require the firm to apply for permission on the part of a governmental authority to permit the inspection to take place, or to submit information to the PCAOB only through the home country's audit oversight body. In other instances, the firm may be required to redact client information from the work papers or to obtain assurances about the confidentiality of the information it provides as a precondition to permitting the PCAOB staff to review those papers.



cooperation on inspections, with the ultimate goal of allowing PCAOB reliance on home country oversight bodies. We continue to believe that inspection by the home country oversight authority is ultimately the best solution to the issue of legal impediments, and we encourage the PCAOB to continue working toward this objective. In the interim, this same spirit of cooperation should apply with regard to overcoming impediments to PCAOB inspection. We have also come to believe that the relevant governmental authorities should become directly involved in efforts to overcome impediments to PCAOB inspection as well as the longer-term objective of establishing reciprocal arrangements for auditor oversight.

#### **Disclosure of Failure to Cooperate in an Inspection**

The Board seeks comment on whether to require a principal auditor to disclose if it, or other firms it has relied upon or referenced, has failed to provide information to the Board in response to an inspection demand on the basis of non-U.S. legal restrictions or sovereignty concerns. Such disclosure would be provided either in, or in connection with, the auditor's report.

The auditor's report provides the auditor's opinion on the financial statements, describes the nature of the audit work performed to support that opinion, and provides other information about the financial statements as permitted or required by generally accepted auditing standards. We believe that information about compliance processes followed by the audit firm, even processes as important as an outside inspection, is at best extraneous to the subject of the audit report and has the potential to detract from the important information included therein. At worst, it would place the reader in a position of being asked to evaluate the competence of the auditor, which they do not have sufficient information to be able to do. Thus we would not support a requirement to include such disclosures in the auditor's report.

Any disclosures in connection with (but outside of) the auditor's report would only be presented to investors if they are included along with information provided by the issuer about the audit firm. This information is generally included in the non-financial disclosures of the filing. Issuers are required by SEC rules to provide certain information; for example, the breakdown of fees paid to the auditor. To our knowledge, there is nothing preventing an issuer from providing information it deems relevant to investors about the status of the firm's PCAOB inspection. In order to require such disclosure, the SEC would need to determine that information about PCAOB inspection status is relevant to investors and amend relevant disclosure requirements accordingly.

#### **Connection between Reliance on Other Auditors and PCAOB Inspection**

Certain of the possible approaches offered by the Board involve disclosures in the event that the principal auditor places reliance on firms that have been unable to participate in a PCAOB inspection. This approach appears to draw a link between the PCAOB's inspection process and the auditor's responsibilities when relying on the work of another auditor.

PCAOB auditing standard AU Section 543, *Part of Audit Performed by Other Independent Auditors*, requires principal auditors to perform procedures to assess the professional reputation and independence of other auditors. These requirements apply whether or not the auditor decides to make reference to the report of the other auditor in his or her audit report. Such procedures include making inquiries regarding the other auditor's professional reputation and obtaining a representation letter regarding the other auditor's independence. Additionally, the principal auditor is required to ascertain certain matters through communication with the other auditor, including:

- that the other auditor is aware that the financial statements of the component will be included in the financial statements being audited by the principal auditor and the principal auditor's planned reliance on the other auditor's audit report;



- that he or she is familiar with generally accepted auditing standards in the U.S.; and
- that he or she has knowledge of the relevant financial reporting requirements.

If the results of these procedures lead the auditor to conclude that he or she can neither assume responsibility for the work of the other auditor nor make reference to the audit of the other auditor in the audit report, the auditor is required to qualify or disclaim an opinion on the financial statements taken as a whole.

We believe that the requirements in the Board's standards for the principal auditor to determine whether to assume responsibility for the work of another auditor, to make reference to the work of another auditor, or to modify his or her audit report provide an appropriate model that serves investors and other users of audit reports well.

The above process represents procedures designed to assess the extent, materiality, and quality of the work of the other auditor. We do not think it would be appropriate to combine this requirement with inquiry related to PCAOB inspection. As noted above, doing so implies that firms that are not inspected are not of sufficient quality.

### **Principal Auditor's Inquiries**

We support the requirement for the principal auditor to make inquiries of other auditors, but we believe they should be limited to other auditors with "substantial roles". We have fundamental concerns about extending this requirement to all firms on which the principal auditor places reliance.

Existing PCAOB rules only require the principal auditor to make inquiries of firms with "substantial roles" to determine if such firm is registered. Thus the proposed requirement would expand the number of inquiries that need to be made and documented for the purpose of PCAOB compliance, with no benefit to the conduct of the audit.

### **Disclosure when Relying on Registered Audit Firm that has Declined to Participate**

We do not believe that it would be appropriate for a principal auditor to disclose information in the audit report about whether or not the PCAOB has inspected the other auditors. Auditors do not currently disclose to users the procedures they performed or the results of those procedures with respect to evaluating the competence and independence of another auditor, and neither do they disclose the work performed by internal auditors or specialists. The auditor is expected (appropriately) to exercise professional judgment in evaluating such information as a basis for concluding whether, for example, the auditor can take responsibility for the work of another auditor, divide responsibility with another auditor as a basis for the consolidated opinion, or use the work of internal audit or a specialist. It would not be appropriate to require users to form their own conclusions, particularly when they will have insufficient information on which to base their conclusion. Disclosure in the audit report whether or not a PCAOB inspection has been performed would place users of an auditor's report in the untenable position of having to interpret and evaluate the implications of this information on an individual company's audit opinion (e.g., users might inappropriately attempt to evaluate whether the auditor obtained a lower or higher level of assurance depending on the information disclosed). We do not believe that this information provides users of audit reports with appropriate or sufficient information from which to draw meaningful conclusions about potential implications for audit quality much less the reliability of the individual company's financial statements.

We further believe that providing the suggested disclosures about firms on which the principal auditor places reliance (either in or in connection with the auditor's report) may be misleading to readers of the auditor's report. This is because in many multinational audit engagements it is possible that many of



the firms whose work is used by the principal auditor may not have been subject to PCAOB inspection. This group includes:

- i) firms that have declined to participate because of legal impediment;
- ii) firms that are not required to and have not registered with the PCAOB; and
- iii) PCAOB-registered firms that have not been asked to participate in an inspection.

To disclose the lack of inspection only with respect to those firms that have been prevented from participating solely because of a restriction in their national law would present an incomplete and potentially misleading picture. Thus we do not support requiring the suggested disclosures.

### **Reliance on Other Auditors**

We believe there is no basis for requiring the principal auditor to provide incremental disclosures about other auditors that have violated Rule 4006 in cases where the principal auditor is not relying on the other auditor, and the other auditor's report is included in the issuer's SEC filing.

### **Reciprocal Arrangements between National Oversight Bodies**

Capital markets, the public interest and investors are best served by the establishment of reciprocal arrangements between national oversight bodies based on mutual reliance on equivalent objectives, standards and systems. Reciprocal arrangements based on equivalent oversight is a preferable inspection option, particularly with home country oversight bodies becoming more prevalent, and where home country regulators are more familiar with the legal and practice environment, culture, customs and audit risks. We acknowledge this process will take time before it is effective in a satisfactory way, but every effort should be made by regulators and oversight bodies themselves, as well as legislators, to facilitate and expedite that process.

In the long term auditor oversight can work best when oversight entities operate on the basis of mutual trust, having recognized that there is a basis for placing full reliance on their respective systems. The creation of the International Forum of Independent Audit Regulators (IFIAR) and active participation therein by the PCAOB should continue. Where possible, principles for cooperation on inspections could be determined through IFIAR in addition to the bilateral arrangements between the PCAOB and individual country inspection bodies.

This approach is consistent with the exhortation in the G-20 communiqué of 15 November, 2008 for better coordination among regulators in financial markets.

\* \* \* \* \*

We would be pleased to discuss our comments with you. If you have any questions regarding this letter, please contact Peter L. Wyman at +44 20 7213 4777 or Kenneth R. Chatelain at +1 202 312 7740.

Sincerely,

A handwritten signature in cursive script that reads "PricewaterhouseCoopers".

PricewaterhouseCoopers



by e-mail only (comments@pcaobus.org)

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

Reference:  
Your sign:  
Our sign: PCAOB/DAS/0902  
Berne, February 2, 2009

## PCAOB Rulemaking Docket Matter No. 027

Dear Sirs

We refer to your request for public comment on the proposed amendment to PCAOB Rule 4003 (PCAOB Release No. 2008-007, December 4, 2008). The Swiss Federal Audit Oversight Authority (hereafter referred to as 'FAOA') welcomes the opportunity to comment on the proposed amendment.

### General remarks

The FAOA shares the U.S. view that a strong and independent audit oversight authority is necessary. On September 1, 2007 the Swiss Audit Oversight Act (hereafter referred to as 'AOA') came into force. The AOA aims at assuring the proper performance and quality of audit services and constitutes the formal basis for the activities of the FAOA. It governs in particular the authorization and registration of individuals and companies providing statutory audit services, the oversight of auditors and audit firms of public companies, and international cooperation in the field of audit regulation.

The increasing globalization of the capital markets clearly calls for cooperative relationships between audit oversight authorities. The auditing of the financial statements of an international public company is a cross-border activity in which usually audit teams from a number of countries are involved. An effective public oversight is therefore only possible in close cooperation with the involved national public oversight bodies. One of the main challenges in the field of audit oversight is to ensure that comparable public oversight systems are in place in the various countries, acting along the same principles.

For legal and factual (language, mentality) reasons the FAOA is convinced that the quality of audit services will be most efficiently improved if the inspections are conducted by the competent national oversight body. Consequently, the FAOA believes that principally no inspectors should be sent abroad and that audit oversight bodies should rely on their foreign coun-

terparts to the largest extent possible. As stated in our comment letter to the draft PCAOB Policy Statement regarding the implementation of PCAOB Rule 4012 (PCAOB Release No. 2007-011, December 5, 2007), dated March 4, 2008, the FAOA understands that this final objective can only be reached if there is enough confidence in the quality and independence of the counterpart oversight entities. From this perspective, joint inspections are useful, but must be limited to a transitional period.

Following the above, the FAOA expressed its willingness to allow joint inspections in Switzerland in its letter dated March 4, 2008. It made this offer under the condition however, that a bilateral agreement be concluded in order to create a legal framework for such inspections. The FAOA and the PCAOB are currently negotiating a Statement of Protocol with a view of conducting joint inspections in Switzerland in 2009.

**A. Proposed amendments to PCAOB Rule 4003**

**a. Extension of deadline for certain 2008 inspections**

The FAOA had basically no objections to conducting joint inspections in Switzerland in 2008. However, the FAOA inspections schedules for 2008 did not coincide with the PCAOB inspection schedule, and the efforts to negotiate a Statement of Protocol could not be completed in 2008. Negotiations are ongoing, and the FAOA is confident that in 2009, the PCAOB and the FAOA will be able to jointly inspect the audit firms that were to be inspected by the end of 2008. The extension of the deadline for up to one year is therefore appropriate and will allow both authorities to carefully prepare the inspections.

**b. Proposed extension of deadline for some 2009 inspections**

In the light of the reasons stated above, and under the condition that joint inspections are considered a transitional measure, the FAOA supports the proposed extension of the deadline for some 2009 inspections until no later than 2012. The FAOA understands that the schedule of inspections for 2009 to 2012 will depend on the U.S. market capitalization of firms' issuer audit clients. The FAOA proposes to make this inspection schedule public as soon as possible so that the home authorities and the firms can assess when they have to expect a joint inspection.

**c. Transparency concerning delayed inspections**

The FAOA welcomes a web-based up-to-date list on the firms that have not yet run through their first PCAOB inspection. In order to avoid any misinterpretation however, the FAOA proposes an indication, for each individual firm, of the reason why a due inspection was postponed.

**d. Registered firms' obligations**

As stated above, and also due to sovereignty rules, joint inspections on Swiss territory depend on the prior conclusion of a bilateral agreement between the PCAOB and the FAOA. We are confident that a Statement of Protocol will be concluded soon. We therefore do not expect sanctions to come into consideration as regards Swiss firms.

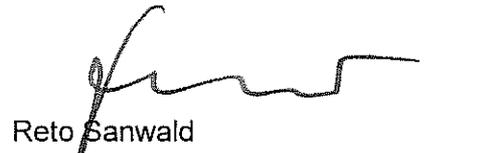
Please do not hesitate to contact us if you have any questions on the above. We kindly ask you to consider the FAOA's concerns as noted above, and we look forward to a constructive cooperation with the PCAOB.

Kind regards

Federal Audit Oversight Authority FAOA



Frank Schneider  
Director



Reto Sanwald  
Head Legal and International Affairs

by e-mail only to: [comments@pcaobus.org](mailto:comments@pcaobus.org)

Public Company Accounting Oversight Board  
 Office of the Secretary  
[comments@pcaobus.org](mailto:comments@pcaobus.org)

**PCAOB RELEASE NO. 2007-007 DOCKET MATTER NO 027 – COMMENTS BY THE AUDITING BOARD OF THE CENTRAL CHAMBER OF COMMERCE OF FINLAND**

The Auditing Board of the Central Chamber of Commerce (AB3C) wishes to respond to the request for comments from the Public Company Accounting Oversight Board (PCAOB) regarding Release No. 2008-007, Rule Amendments Concerning the Timing of certain Inspections of non-US Firms, PCAOB Rulemaking Docket Matter No. 027.

The AB3C is the supervising body of audit professionals in Finland. At bilateral level it is a task of the AB3C to find ways in order to successfully cooperate with the oversight bodies of other countries, such as the PCAOB in the US. We share the views presented by the European Commission in its response to the consultation. Thus we do not see joint inspections as a permanent solution for cooperation. However, we are prepared to approve joint inspections as an interim solution. The supervisory cooperation shall be based on full mutual reliance between oversight systems as discussed in many instances before.

We sympathize with the reasons behind the PCAOB's decision on adopting an amendment to Rule 4003 that will give the PCAOB ability to postpone first inspections of the remaining non-US firms that the PCAOB is currently required to conduct before the end of 2008 to the end of 2009. We also understand the reasons why the PCAOB is proposing an amendment to Rule 4003, which would allow the PCAOB to postpone, up to 3 years, the first inspections of any non-US firm that the PCAOB is currently required to conduct by the end of 2009 and that is in a jurisdiction where the PCAOB has not conducted an inspection before 2009. We have no remarks on these.

However, we would like to welcome clarification to

- the criteria of PCAOB's selection of the audit firms to be inspected on a certain year
- what is PCAOB's intention on inspecting audit firms of subsidiaries of SEC registered listed firms
- what is PCAOB's intention on inspecting audit firms whose clients have deregistered according to SEC rules
- how market capitalization is assessed and calculated

As regards the organisation of mutual cooperation with the PCOAB we are strongly committed to support the positions taken by the European Commission. These views have been discussed many times in the bilateral meetings between the PCAOB and the European counterparts such as the European Group of Independent Oversight Bodies (EGAOB) of which AB3C is a member. In

The Central Chamber of Commerce of Finland

Aleksanterinkatu 17, P.O. Box 1000, FI-00101 Helsinki, Finland, Tel +358 9 4242 6200, Fax +358 9 650 303, Business ID: 0201469-2

addition to supporting Commission's remarks, we would like to highlight a few aspects that mainly relate to the conduct of inspections and some relevant matters which are mostly of practical nature.

We share the same concerns with many other EU Member States that the following issues shall be dealt before joint inspections can be conducted:

- There shall be a Commission's decision in place regarding the adequacy of the third country regulators to conclude agreements about transfer of information to the PCAOB by the AB3C
- There shall be a bilateral agreement concluded between the PCAOB and the AB3C
- The transfers can only be organised between the PCAOB and the AB3C
- The Finnish data protection legislation shall be respected and this needs to be safeguarded
- Confidentiality of information i.e. the protection of business secrecy shall be respected and this needs to be safeguarded. This data may not be transferred further nor used for any other purpose.

In addition we would like to suggest that joint inspections are organised in a way which does not risk to offend the state sovereignty of Finland.

In practice, close preparation of inspection techniques and plans is required in order to agree on the joint inspections. This requires transparency and mutual trust between the oversight organisations.

We are quite concerned about the way how the PCAOB intends to deal with conflict of law issues according to its Release. We think that conflict of law issues must be identified and solved without sanctioning the audit firms which must comply with the national law. Cooperative arrangements and mutual trust between oversight organizations is a key issue in avoiding clashes deriving from conflict of law issues.

Despite the legal concerns, we have a strong will to find pragmatic solutions. International cooperation between oversight bodies is essential in supervision of global audit networks and internationally operating audit firms. The AB3C is willing to overcome the difficulties relating to building such cooperation and mutual reliance, and collaborate with the PCAOB and other oversight bodies in other countries to find appropriate solutions to global challenges facing the audit market.

Yours sincerely



Aatto Prihti  
Chairman of the AB3C



EUROPEAN COMMISSION  
Internal Market and Services DG

Director General

Brussels, **09 FEB. 2009** - 19718  
JR/markt.f.4 (2009) 19990

Office of the Secretary  
PCAOB  
1666 K Street, N.W.  
Washington, DC 20006  
comments@pcaobus.org

**Subject: PCAOB Rulemaking Docket Matter No. 027**

Madam, Sir,

On behalf of the Commission services, I am pleased to respond to the request for comments from the Public Company Accounting Oversight Board (the "PCAOB" or the "Board") regarding Release No. 2008-007, Rule Amendments Concerning the Timing of certain Inspections of non-US Firms, PCAOB Rulemaking Docket Matter No. 027 (the "Release").

I support the PCAOB's intention to establish and implement cooperative solutions with non-US oversight bodies. The leaders of the Group of Twenty (G20) have also called for regulatory cooperation in the field of auditor oversight.<sup>1</sup>

The European Commission believes that appropriate and effective cooperation with the PCAOB could result in benefits not only to the audit firms and investors, but also to the Board's inspection process. The Board has the authority, under PCAOB Rules 4011 and 4012, to rely on the inspections of non-US audit firms made by non-US regulatory authorities. The European Commission believes that joint inspections, as an ultimate objective, are not desirable. Joint inspections as a confidence building measure might be useful, but it is not a sustainable concept or even a policy objective. We would therefore welcome the PCAOB adopting its proposed policy statement giving guidance on the implementation of its Rule 4012. Adoption of this policy statement is also a premise to what is set out below.

Our response focuses in particular on the aspect of conflicts of law (see section 1). We also take the opportunity in this context to make comments on other points (see section 2).

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<sup>1</sup> Declaration Summit on Financial Markets and the World Economy, November 15 2008, paragraph 9, third and fourth bullet point.

## **1. CONFLICT OF LAW ISSUE**

The PCAOB proposes to solve conflicts of law via enhanced transparency towards US investors. However, it is unclear on its arguments in the context of sanctions on conflicts of law.

### **1.1. The situation in Europe has changed**

Before the adoption of the Statutory Audit Directive and the regulations transposing its provisions in Member States' law, the situation was as follows: the national legislation of most EU Member States did not allow an EU audit firm to fulfil its obligations under PCAOB Rule 4006.

In order to facilitate the registration process, the PCAOB therefore allows audit firms under its Rule 2105 to withhold information from its application for registration if such information would cause a conflict of law. EU audit firms used this Rule when declining to include the statement in which they would agree to co-operate with the PCAOB and to comply with its requests for information and documents in their possession as requested by Section 102 (b) (3) of the Sarbanes Oxley Act. The refusal was motivated by the impossibility for them to commit in advance to comply with all the PCAOB's future requests for information and documents, because their domestic law effectively would not allow them to do so.

Since the adoption of the European Statutory Audit Directive in 2006, EU Member States are required to establish an independent auditor oversight system, a quality assurance system and an investigations and penalties system. Member States accordingly adopted legislation to transpose these requirements into their national law. All Member States concerned by these issues have now implemented appropriate measures. Auditor oversight bodies have been established to carry out inspections and investigations on the auditors and audit firms registered with them. The starting point for co-operation is therefore no longer individual auditors or audit firms but oversight bodies. This change of custody is a proper way for handling professional secrecy issues regarding auditors and audit working papers. Professional secrecy is acknowledged as a principle under Article 23 of the Statutory Audit Directive. Exemptions related to professional secrecy are not just handled on the basis of obtaining the consent of the client company which could anyway be withdrawn at any moment. Instead, public oversight bodies are involved and should take responsibility for these issues in bilateral arrangements with public oversight bodies from third countries as required under Article 47 of the Statutory Audit Directive. Thus, the EU promotes and facilitates international cooperation between EU auditor regulators and third country auditor regulators like the PCAOB.

Under the new European audit legislation, however, a number of conditions need to be fulfilled before a transfer of information to the PCAOB by an EU auditor regulator is allowed, such as:

- a Commission decision determining the adequacy of the third country regulators to conclude such agreements with the EU oversight bodies;

- a bilateral mutual agreement concluded between the PCAOB and the EU auditor regulators;
- the transfers may only be organized between the foreign regulators and the EU oversight bodies; and
- the transfer of information respects European data protection legislation.

Today, EU audit firms have to comply with both their domestic legislation, which prevents them from transferring any documents to foreign regulators, and with the PCAOB requests for documents.

### **1.2. No sanctions for EU audit firms if they meet 4 conditions**

The PCAOB should consider that non-US audit firms cannot be forced to breach their national legislation and that solutions need to be found for solving such situations.

For this reason, we do not support sanctions in the case where the following four conditions are met.

- (1) Auditors of companies with dual listings. Imposing sanctions would otherwise force these companies to have two auditors: one for their US listing and one for their (in our case) EU listing. This might even result in more EU companies deregistering from US securities markets.
- (2) The audit firm used Rule 2105 during its registration.
- (3) The audit firm falls under a Commission Decision on Article 47 of the European Statutory Audit Directive. The Commission proposal foresees a time limitation for two reasons:
  - (a) There is at present a regulatory gap between the Sarbanes Oxley Act and EU legislation. The Sarbanes Oxley Act does not provide the PCAOB with the possibility to exchange information with EU audit regulators. Under the EU legislation, a foreign competent authority must have the ability to cooperate with the EU auditor regulators on the exchange of information. Moreover, such an exchange can only take place between EU and foreign competent authorities; and,
  - (b) there is a need for a test phase in view of mutual reliance.

This Commission proposal is intended to facilitate international cooperation through mutual agreements between EU Member States and third country auditor regulators like the PCAOB.

- (4) Data protection legislation applies. With regard to transfer of information containing personal data to the US, only transfers made within the "Safe Harbor" scheme are considered by the EU to ensure the adequate level of protection required by the EU Data Protection Directive 95/46 on the Protection of Individuals with regard to the Processing of Personal Data. Transfers to US organizations (public or private) that are not "Safe Harbor"

members do not ensure this adequate level of protection. As PCAOB is not part of the "Safe Harbor" scheme, a national data protection authority in a Member State of the European Union can only authorise a transfer on the basis of a transfer agreement concluded under Article 26 (2) of the Directive 95/46. Such agreement should contain special safeguards which are put in place with respect to the protection of the privacy and fundamental rights and freedom of individuals and as regards the exercise of the corresponding rights.

### **1.3. Clarification on how PCAOB deals with conflict of law issues**

We would also like clarification on an inconsistency in the Release. The PCAOB acknowledges that conflicts of law might exist and that they need to be solved. To this purpose, it refers to PCAOB release No. 2004-005. This release states on page A2-18 that, even though not set out in a separate rule (like Rule 2105), the opportunity for audit firms to be heard regarding the conflict of law that may arise in the context of inspections and investigations (thus also regarding Rule 4006) is provided under the Sarbanes Oxley Act and the Board's rules regarding disciplinary hearings. But in PCAOB release 2008-007 the PCAOB states that it does not view non-US legal restrictions or the sovereignty concerns of local authorities as a sufficient defence<sup>2</sup>. This might create the impression that the outcome of such disciplinary hearings would be predetermined.

Conflicts of law need to be addressed and avoided by moving to cooperative agreements among regulators. I also agree that assessing each other's oversight systems to be able to rely on each other's inspections is a long term process. In the meanwhile, the issues related to conflicts of law have to be dealt with: either the competent authorities concerned find ways to avoid them, or they need to be addressed and solved by the national legislators involved. But they cannot be dealt with by audit firms or companies.

## **2. OTHER COMMENTS ON THE ISSUES ADDRESSED IN THE RELEASE**

### **2.1. Comments whether there are other factors that should be treated as a reason to consider moving an inspection to an earlier year (see page 13 of the Release).**

We consider that one other factor should be taken into account in this regard and that one factor requires further clarification by the PCAOB.

#### *Willingness to build co-operation*

It is in the interest of our capital markets to move to cooperative agreements with each other. We would welcome the PCAOB using 2009 to assess the jurisdictions interested in full cooperation, like the EU Member States. This should lead to acceptance under the full reliance scheme under the policy statement proposed by the PCAOB in December 2007. Willingness to build such co-operation should be given the same weight as existing market capitalisation.

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<sup>2</sup> See footnote 35 on page 16 of the Release.

The European Commission advances on a parallel track. The EU granted a transitional period to a number of jurisdictions, including the US, with a view to achieving equivalence and mutual reliance on each other's oversight systems. During the transitional period, which ends in July 2010, the auditors of these jurisdictions are allowed to continue performing audits of EU issuers while not yet falling under the oversight (and thus inspections) of EU auditor oversight entities.<sup>3</sup>

*Excluding deregistered US issuers from market capitalisation calculations*

I would welcome further clarification on the issue of market capitalisation. The PCAOB proposes to base its ranking of the audit firms on the market capitalisation of their US issuer clients. If market capitalisation is used to rank audit firms, we support the PCAOB excluding from its calculations US issuers which deregistered according to SEC rules. There is no good reason for protecting US investors through inspections if the audit firm has no US clients according to SEC rules.

**2.2. Comments on the proposed public list on the PCAOB website (see page 14 of the Release)**

I support transparency on jurisdictions in which inspections have not yet taken place as a means to inform investors. Such transparency might be similar to the European Commission's transparency regarding the jurisdictions which have been granted a transitional period during which their audit firms would not fall under the oversight of our Member States.<sup>4</sup> The Decision grants the audit firms concerned a transitional period in respect to registration requirements until 1 July 2010, provided they comply with the minimum information requirements necessary for investors in Europe. Audit firms from third countries that do not fall under the transitional regime will be subject to full registration and oversight by the competent EU Member State.

Along the same lines, the proposed transparency by the PCOAB should focus on the jurisdictions concerned instead of the individual auditors or audit firms. Conflicts of law need addressing in cooperation with public oversight bodies, preferably in 2009.

**2.3. Comments on the potential benefits and drawbacks of disclosures in the audit report of delays of PCAOB inspections resulting from conflicts of law (see page 17 of the Release)**

The EU does not support disclosing information on delayed inspections in the audit report as this would sanction the company.

The final report of the advisory committee on the auditing profession to the US Department of the Treasury required the PCAOB to require larger audit firms to produce a public annual report with the information required by the EU's transparency report. We consider this transparency report as a better place for such disclosures as the information

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<sup>3</sup> The Commission proposal on the adequacy of competent authorities of third countries for the transfer of audit working papers follows the same line of building solutions towards full reliance and the same time schedule.

<sup>4</sup> See Commission Decision of 29 July 2008 concerning a transitional period for audit activities of certain third country auditors and audit entities.

applies to the auditor and not to individual audit engagements. EU audit firms are already required to publish such reports under Article 40 of the Statutory Audit Directive.

Furthermore, disclosure of this information in the audit opinion would result in companies being forced to have one audit opinion for each jurisdiction where they are listed. Multiple audit opinions are not in the interest of investors.

Finally, I would welcome clarification as to why the PCAOB does not intend to inspect auditors of subsidiaries but at the same time proposes disclosure on whether or not they were inspected by the PCAOB in the audit report.

\*\*\*\*\*

We would welcome the PCAOB to take the above mentioned points into consideration when deciding the amendments to its Rule 4003.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'J. Holmquist', with a stylized flourish at the end.

Jörgen HOLMQUIST

## Professional Oversight Board

Aldwych House, 71-91 Aldwych, London WC2B 4HN

Telephone: 020 7492 2341 Fax: 020 7492 2359

[www.frc.org.uk/pob](http://www.frc.org.uk/pob)

Mark Olson,  
Chairman,  
PCAOB,  
1666 K Street,  
N.W.,  
Washington,  
D. C. 20006-2803.

2 February 2009

Dear Mark

### **PCAOB Rulemaking Docket Matter No. 027 – Release 2008-007**

I am pleased to respond on behalf of the UK's Professional Oversight Board of the Financial Reporting Council to your request for comments on the proposed rule amendment and other issues related to PCAOB inspections of non-US firms raised in Release No. 2008-007.

The Board continues to believe in the importance of effective co-operation between audit regulators internationally in discharging our respective regulatory responsibilities and, in that context, welcomes the opportunity to provide you with our views.

Our principal comments are set out below. We respond to the specific matters on which views were invited in the Appendix to this letter.

### **Importance of moving towards a full reliance approach**

We wish to reiterate the importance we attach to the PCAOB moving towards placing full reliance on the work of independent audit regulators in other jurisdictions, as soon as possible, in particular where the PCAOB already has had the opportunity to work with the independent regulator and gain confidence in their work. A system of reliance on other independent regulators' work with effective two way communication is likely to be the most efficient way of achieving our mutual objective of safeguarding audit quality. Such a system would avoid the significant unnecessary duplication of regulatory effort that currently exists and would promote a cost effective system of regulation which best serves the interests of our respective stakeholders. There are a number of comments in the Release that

would seem to support this view. We consider that this now needs to be followed through into the specific proposals. Such an approach should reduce significantly the practical problems faced by the PCAOB in conducting inspections of non-US firms. Accordingly any proposals aimed at addressing the challenges of inspecting non-US registered firms should be taken forward together with substantive proposals for moving towards a full reliance approach as envisaged by your consultation on Rule 4012 and comments received thereon.

### **Scope of consultation**

We note that the Release focuses primarily on first inspections of non-US firms. In so doing the proposals treat those non-US firms who have already been subject to inspection either directly by the PCAOB or jointly with the local regulator less fairly than those who have not. In particular we consider that it would be wrong in principle, and unfair, for the PCAOB to try to press ahead with 2009 second inspections of a firm which because of legal restrictions, was unable to cooperate fully on a second 2009 inspection. This could lead, on the PCAOB's current proposals, to the imposition of sanctions on such a firm, even where the firm's independent national regulator (with whom the PCAOB had already worked), could provide the PCAOB with the outcome of its independent inspection. We strongly believe that stakeholder interests would be best served were the PCAOB to direct its resources towards non-US firms who had not previously been inspected, and/or where detailed information was not available to the PCAOB on the outcome of independent inspection from that firm's national regulator.

### **European statutory audit directive**

As you aware the European statutory audit directive contains provisions aimed at facilitating the effective sharing of information between regulators within a confidential framework. The implementation of these arrangements requires a decision to be taken in Europe on the adequacy of the PCAOB's arrangements for maintaining confidentiality and will require reciprocal information sharing provisions. From a UK perspective, an adequacy decision and reciprocal arrangements will be necessary before further PCAOB inspections can be freely conducted in the UK. We believe that transitional arrangements similar to those offered in relation to first time inspections should be extended to all firms whilst appropriate adequacy decisions are taken and reciprocal arrangements established.

### **Sanctions**

Where further inspections of firms in a particular jurisdiction are not possible due to legal provisions, the PCAOB should be able to obtain appropriate comfort regarding the competence of the local regulator and the rigour of its work from its experience of working with the local regulator in conducting previous inspections. If, in this

situation, the local regulator is able to provide the PCAOB with a report on a recent inspection undertaken by it of a firm for which a PCAOB inspection has become due, no sanctions should be placed on the firm concerned due solely to the firm's inability to participate in an inspection involving the PCAOB.

### **Transparency proposals**

As a principle the Professional Oversight Board supports transparency proposals aimed at improving investor confidence in audit quality. However, we are concerned that the PCAOB's current proposals may have the unintended consequence of reducing investor confidence inappropriately. Investors may incorrectly conclude that any firm included on the list of firms with a delayed PCAOB inspection is not subject to independent inspection and may have weak or inadequate quality control procedures. If it is deemed necessary to make any disclosure of such firms, then the disclosure should make clear the reasons for the delay, the extent to which the firm has been subject to alternative independent inspection and, where available, the findings from such inspection.

Please feel free to contact me should you wish to discuss with us any of the comments we have made.

Yours sincerely



**Paul George**  
Director of Auditing and  
Director of the Professional Oversight Board  
DDI: 020 7492 2340  
Email: [p.george@frc-pob.org.uk](mailto:p.george@frc-pob.org.uk)

## Responses to specific matters raised in PCAOB Release No. 2008-007

### Part I

#### Rule amendments concerning the timing of certain inspections

*The Board is adopting an amendment to Rule 4003 that will give the Board the ability to postpone, for up to one year (i.e., to the end of 2009), first inspections of the remaining non-U.S. firms that the Board is currently required to conduct before the end of 2008. The Board is also proposing, and seeking comment on, an amendment that will give the Board the ability to postpone, for up to three years, first inspections that the Board is currently required to conduct before the end of 2009 in jurisdictions where the Board has conducted no inspections before 2009.*

We believe that the actions proposed by the PCAOB in relation to first time inspections are a pragmatic response to the specific challenges it has faced in conducting such inspections. However, we also believe that there is an urgent need for the PCAOB to broaden its proposals to include actions necessary to meet the challenges of further inspections of firms already inspected once, and actions aimed at moving towards a full reliance approach, as envisaged by its consultation on Rule 4012 and comments received thereon.

### Part II

#### Registered firms' obligations

*The Board recognizes that a refusal to provide information based on non-U.S. legal restrictions or the sovereignty concerns of local authorities implicates considerations not present in other non-cooperation circumstances. The Board invites public comment generally on whether and how the fact of a non-U.S. legal restriction or sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006.*

In our view, full account of all circumstances including information made available to the PCAOB on the conduct of inspections undertaken by the firm's national regulator should be taken in determining what, if any, sanction should be imposed on a firm for not co-operating with the PCAOB in an inspection.

*The Board is also considering whether there are possible rulemaking approaches that would help address aspects of the problems created by a refusal to produce information. One example that the Board has begun to consider would involve requiring a principal auditor to make certain public disclosures as part of, or in connection with, each audit report it issues for an issuer.*

*The Board invites comment on the potential benefits and drawbacks of a rule along the lines described above. The Board also invites comment more generally on other possible rulemaking approaches relating to those issues that might provide useful disclosure to investors or otherwise be in the public interest.*

We do not believe that disclosures of the type proposed would provide useful information to investors since they would not be in a position to make an informed assessment of any implications for the reliability of the audit opinions to which the disclosures relate. Disclosures relating to another firm whose work has been used by the group auditor would be particularly inappropriate, in our view, where the group auditor assumes full responsibility for the group audit. We are concerned that these proposals are inconsistent with the PCAOB's approach towards the inspection of auditors of significant subsidiaries who are not also auditors of US issuers. Further, such disclosures may have an adverse impact on investor confidence in the reliability of audit opinions where this is not merited and therefore would not be in the public interest.

We believe that the practical problems faced by the PCAOB in conducting inspections of non-US firms, to which the proposals are looking to respond, should reduce significantly if it moves quickly towards placing full reliance on the work of audit regulators in other jurisdictions, where appropriate. We therefore urge the Board to focus its attention on taking forward its proposed Policy Statement on moving towards a full reliance approach as soon as possible.



1666 K Street, N.W.  
Washington, DC 20006  
Telephone: (202) 207-9100  
Facsimile: (202) 862-8430  
www.pcaobus.org

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FINAL RULE )  
CONCERNING THE TIMING OF )  
CERTAIN INSPECTIONS OF )  
NON-U.S. FIRMS, AND OTHER )  
ISSUES RELATING TO )  
INSPECTIONS OF NON-U.S. FIRMS )  
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PCAOB Release No. 2009-003  
June 25, 2009

PCAOB Rulemaking  
Docket Matter No. 027

Summary: After public comment, the Public Company Accounting Oversight Board ("Board" or "PCAOB") adopts an amendment to the inspection frequency requirements of Rule 4003 that will give the Board the ability to postpone, for up to three years, the first inspection of any foreign registered public accounting firms that the Board is otherwise required to conduct before the end of 2009 and that is in a jurisdiction where the Board has not conducted an inspection before 2009. The Board also announces that it will implement certain transparency measures related to the PCAOB's international inspections program. The amendment to Rule 4003 will take effect upon approval by the Securities and Exchange Commission ("Commission").

Board Contacts: Rhonda Schnare, Director of International Affairs (202-207-9167; [schnarer@pcaobus.org](mailto:schnarer@pcaobus.org)).

**Introduction**

On December 4, 2008, the Board proposed, and sought public comment on, an amendment to Rule 4003 that would give the Board the ability to postpone, for up to three years, certain inspections of foreign registered public accounting firms that the Board is otherwise required to conduct before the end of 2009.<sup>1/</sup> The Board is now adopting proposed Rule 4003(g) as final without changes.

<sup>1/</sup> See Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms, PCAOB



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### I. Background

Under the Sarbanes-Oxley Act of 2002 (the "Act") and PCAOB Rules, it is unlawful for any public accounting firm to prepare or issue an audit report with respect to any issuer or play a substantial role in the preparation or furnishing of any such audit report without being registered with the PCAOB.<sup>2/</sup> For non-U.S. firms, this registration requirement took effect on July 19, 2004.

The Act directs the Board to conduct a continuing program of inspections to assess registered public accounting firms' compliance with certain requirements.<sup>3/</sup> With respect to each registered firm that regularly provides audit reports for 100 or fewer issuers, the Act requires the Board to conduct an inspection at least once every three years.<sup>4/</sup> The Act authorizes the Board to adjust that inspection frequency requirement by rule if the Board finds that a different inspection schedule is consistent with the purposes of the Act, the public interest, and the protection of investors.<sup>5/</sup>

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Release No. 2008-007 (Dec. 4, 2008) (the "Proposing Release"). The Board also adopted on December 4, 2008 a related rule amendment. Rule 4003(f) allows the Board to postpone for up to one year the first inspection of any non-U.S. firm that the Board is otherwise required to conduct by the end of 2008. Because the Board's action with regard to this rule was final, the Board did not seek comment on it. The Securities and Exchange Commission approved Rule 4003(f) on May 28, 2009.

<sup>2/</sup> See Sections 102(a) and 106 of the Act and PCAOB Rule 2100. For these purposes, the term "issuer" is defined by Section 2(a)(7) of the Act and generally encompasses entities that have issued securities that are registered under Section 12 of the Securities Exchange Act of 1934, or that otherwise have certain reporting obligations to the Securities and Exchange Commission, or that have filed registration statements with the Commission that have not yet become effective.

<sup>3/</sup> See Section 104(a) of the Act.

<sup>4/</sup> See Section 104(b)(1)(B) of the Act.

<sup>5/</sup> See Section 104(b)(2) of the Act.



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Inspection frequency requirements adopted by the Board are set out in PCAOB Rule 4003, "Frequency of Inspections."<sup>6/</sup> Under Rule 4003, when a firm issues an audit report while registered,<sup>7/</sup> the Board must conduct an inspection of that firm within a certain number of calendar years following the year of the audit report.<sup>8/</sup>

The Board began a regular cycle of inspections of U.S. firms in 2004 and has conducted 982 such inspections, including annual inspections of the largest firms and two or more inspections of many other firms. Inspections of non-U.S. firms began in 2005, and the Board has inspected 140 non-U.S. firms<sup>9/</sup> located in 26 jurisdictions.<sup>10/</sup>

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<sup>6/</sup> Registered non-U.S. firms are subject to the Act and the Board's rules "in the same manner and to the same extent as" registered U.S. firms (see Section 106(a) of the Act), including the requirement to cooperate in periodic PCAOB inspections.

<sup>7/</sup> Section 2(a)(4) of the Act defines "audit report" to mean, in essence, an audit report with respect to the financial statements of an "issuer," and that is how the term is used in this release.

<sup>8/</sup> In general, if a firm issues audit reports for 100 or fewer issuers in a calendar year, Rule 4003(b) requires that the Board inspect the firm within the following three calendar years. Rule 4003(d), however, provides that the first such inspection of firms that registered in 2003 or 2004 is not required sooner than the fourth calendar year (after the first calendar year in which the firm, while registered, issues an audit report). This release focuses on firms that become subject to Board inspection by virtue of issuing an audit report, but Rules 4003(b) and (d) also describe inspection frequency requirements for firms that play a substantial role in the preparation or furnishing of an audit report (as defined in PCAOB Rule 1001(p)(ii)) but do not issue an audit report. The Board has adopted and submitted for Commission approval amendments that would eliminate the requirement that the Board regularly inspect such firms although the Board will, each year, inspect some such firms.

<sup>9/</sup> The Board has issued reports on 893 of the 1,122 inspections conducted to date, including reports on 44 of the 140 non-U.S. inspections. Reports on the other inspections are in process.

<sup>10/</sup> The Board has inspected non-U.S. firms located in Argentina, Australia, Bermuda, Brazil, Canada, Chile, Colombia, Greece, Hong Kong, India, Indonesia, Ireland, Israel, Japan, Kazakhstan, Mexico, New Zealand, Norway, Panama, Peru, the Russian Federation, Singapore, South Africa, South Korea, Chinese-Taipei, and the United Kingdom.



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Under Rule 4003's current inspection frequency requirements, there are 129 additional non-U.S. firms in 42 jurisdictions that, by virtue of their having issued audit reports, the Board is currently required to inspect but has not yet inspected.<sup>11/</sup> Those 129 pending "first inspections" of non-U.S. firms (with deadlines ranging from 2009 to 2012 under the existing rule) are in addition to other pending inspections of non-U.S. firms that the Board has already inspected at least once.

The rule amendment that the Board is adopting will affect a portion of those pending first inspections. Specifically, the amendment to Rule 4003 will give the Board the ability to postpone, for up to three years, first inspections that the Board is currently required to conduct before the end of 2009 in jurisdictions where the Board has conducted no inspections before 2009. The amendment does not affect inspection frequency requirements concerning any other first inspections or concerning any second, or later, inspections of a firm.

## II. Inspections of Non-U.S. Firms

The PCAOB has recognized since the outset of its inspection program that inspections of non-U.S. firms pose special issues.<sup>12/</sup> In its oversight of non-U.S. firms, the Board seeks, to the extent reasonably possible, to coordinate and cooperate with local authorities. Since 2003, when the PCAOB began operations, a number of jurisdictions have developed their own auditor oversight authorities with inspection responsibilities or enhanced existing oversight systems.<sup>13/</sup> The Board believes that it is

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<sup>11/</sup> Those 129 firms are located in Argentina, Australia, Austria, Belgium, Canada, Cayman Islands, China, Cyprus, the Czech Republic, Denmark, Finland, France, Germany, Greece, Hong Kong, Hungary, India, Indonesia, Ireland, Israel, Italy, Japan, Kazakhstan, Luxembourg, Malaysia, Netherlands, Norway, Panama, Papua New Guinea, Philippines, Poland, Portugal, the Russian Federation, Singapore, South Korea, Spain, Sweden, Switzerland, Turkey, the United Arab Emirates, the United Kingdom, and Venezuela.

<sup>12/</sup> See Briefing Paper, Oversight of Non-U.S. Public Accounting Firms (October 28, 2003) (hereinafter "Oversight of Non-U.S. Firms"); Final Rules Relating to the Oversight of Non-U.S. Public Accounting Firms, PCAOB Release No. 2004-005 (June 9, 2004).

<sup>13/</sup> In 2006, for instance, the European Union enacted a directive requiring the creation of an effective system of public oversight for statutory auditors and audit firms within each Member State. See The Directive 2006/43/EC of the European Parliament and the Council (May 17, 2006) (the "Eighth Directive"). In addition, among



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in the interests of the public and investors for the Board to develop efficient and effective cooperative arrangements with its non-U.S. counterparts.<sup>14/</sup> In jurisdictions that have their own inspection programs, this may include conducting joint inspections of firms that are subject to both regulators' authority. Indeed, the Board has a specific framework for working cooperatively with its non-U.S. counterparts to conduct joint inspections and, to the extent deemed appropriate by the Board in any particular case, relying on inspection work performed by that counterpart.<sup>15/</sup> PCAOB Rule 4011 permits non-U.S. firms that are subject to Board inspection to formally request that the Board, in conducting its inspection, rely on a non-U.S. inspection to the extent deemed appropriate by the Board. If a Rule 4011 request is made, Rule 4012 provides that the Board will, at an appropriate time before each inspection of the firm, determine the degree, if any, to which the Board may rely on the non-U.S. inspection. Rule 4012 describes aspects of the non-U.S. system that the Board will evaluate in making that determination. Even where the Board does not work with a local regulator to conduct joint inspections, the Board communicates with its counterpart or other local authorities (such as securities regulators or other government agencies and ministries) regarding its inspections to be conducted in the jurisdiction.

In some jurisdictions, the PCAOB's ability to conduct inspections, either by itself or jointly with a local regulator, is complicated by the concerns of local authorities about potential legal obstacles and sovereignty issues. The Board seeks to work with the home-country authorities to try to resolve these and any other concerns.<sup>16/</sup>

The effort involved in attempting to resolve potential conflicts of law, or to evaluate a non-U.S. system in response to a Rule 4011 request, can be substantial. The effort typically involves negotiating the principles of an arrangement for cooperation consistent with the inspection obligations that the Act imposes on the Board. It also

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others, Canada created the Canadian Public Accountability Board, and in Australia, the responsibilities of the Australian Securities and Investments Commission were expanded to include auditor oversight. In Asia, Japan established the Certified Public Accountants and Auditing Oversight Board, South Korea delegated responsibility for auditor oversight to its Financial Supervisory Service, and Singapore established the Accounting and Corporate Regulatory Authority.

<sup>14/</sup> See Oversight of Non-U.S. Firms at 2-3.

<sup>15/</sup> See PCAOB Rules 4011 and 4012; see also Oversight of Non-U.S. Firms at 2-3.

<sup>16/</sup> See Oversight of Non-U.S. Firms at 3.



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involves the Board gaining a detailed understanding of the other jurisdiction's auditor oversight system in order for the Board to determine the degree of reliance it is willing to place on inspection work performed under that system in a particular inspection year. Additional effort is involved in coordinating the scheduling of specific inspections. Where possible, the Board seeks to conduct inspections jointly with local authorities both to take advantage of potential efficiencies and to avoid imposing unnecessary regulatory burdens on firms. Like the PCAOB, several of these other authorities proceed according to inspection frequency requirements. While some of the Board's counterparts are established and have inspection programs, many have only recently begun inspections or are still building up their inspections resources. As a result, synchronizing the inspections schedules of these authorities and the PCAOB's requirements is sometimes difficult.

Notwithstanding these challenges, the Board has so far conducted 140 non-U.S. inspections. Moreover, 61 of those inspections, in six jurisdictions, have been conducted jointly with other auditor oversight authorities, while inspections in 20 jurisdictions have been conducted solely by the PCAOB.<sup>17/</sup>

### **III. Extension of the Deadline for Some 2009 Inspections**

Under existing Rule 4003, there are currently 68 non-U.S. firms that, by virtue of when they first issued audit reports after registering with the PCAOB, the Board is required to inspect for the first time by the end of 2009.<sup>18/</sup> Those firms are located in 36 jurisdictions, including several jurisdictions in which the Board has already conducted first inspections of other firms. Of those firms, 49 are located in 24 jurisdictions where the Board has not conducted any inspections to date. Most of those 24 jurisdictions have or soon will have a local auditor oversight authority with which the Board would seek to work toward cooperative arrangements before conducting inspections. Because of the steps involved in concluding such arrangements and to evaluate the local system (described above), the Board has concerns about proceeding as if that work can be completed for all of the jurisdictions in which the PCAOB has not previously conducted inspections in time to conduct the required inspections by the end of 2009.

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<sup>17/</sup> Joint inspections have been conducted in Australia, Canada, South Korea Norway, Singapore and the United Kingdom.

<sup>18/</sup> This discussion does not include, or apply to, those 21 non-U.S. firms whose first inspection deadline has been moved from 2008 to 2009 under Rule 4003(f).



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Accordingly, the Board is adopting a new paragraph (g) to Rule 4003 to allow the Board to postpone, for up to three years, the first inspection of any non-U.S. firm that the Board is currently required to conduct by the end of 2009 and that is in a jurisdiction where the Board has not conducted an inspection before 2009.

In determining the schedule for completion of the inspections subject to new paragraph (g), the Board will implement its proposal to sequence these 49 inspections such that certain minimum thresholds will be satisfied in each of the years from 2009 to 2012. The minimum thresholds relate to U.S. market capitalization of firms' issuer audit clients. The Board will begin by ranking the 49 firms according to the total U.S. market capitalization of a firm's foreign private issuer audit clients.<sup>19/</sup> Working from the top of the list (highest U.S. market capitalization total) down, the 49 firms will be distributed over 2009 to 2012 such that, at a minimum, the following criteria are satisfied:

- by the end of 2009, the Board will inspect firms whose combined issuer audit clients' U.S. market capitalization constitutes at least 35 percent of the aggregate U.S. market capitalization of the audit clients of all 49 firms;
- by the end of 2010, the Board will inspect firms whose combined issuer audit clients' U.S. market capitalization constitutes at least 90 percent of that aggregate;
- by the end of 2011, the Board will inspect firms whose combined issuer audit clients' U.S. market capitalization constitutes at least 99.9 percent of that aggregate; and
- the Board will inspect the remaining firms in 2012.<sup>20/</sup>

In addition to meeting those market capitalization thresholds, the Board also will satisfy certain criteria concerning the number of those 49 firms that will be inspected in

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<sup>19/</sup> For purposes of the ranking described here, the Board will use the average monthly market capitalization on which each issuer's share of the Board's 2008 accounting support fee was based. Thus, the market capitalization figure used for the ranking does not include the value of any referred work performed by the firm.

<sup>20/</sup> Under existing provisions of Rule 4003 that are not affected by this amendment, 2012 would also be the deadline for the Board to conduct the second inspection of those of the 49 firms whose first inspection occurs in 2009.



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each year. Specifically, the Board will conduct at least four of the 49 inspections in 2009, at least 11 more in 2010, and at least 14 more in 2011.<sup>21/</sup>

It is important to note that the distribution described above will not operate to prevent an inspection from occurring earlier than called for by the schedule. Any inspection may be moved to an earlier year for a variety of reasons, such as the presence of risk factors (including risk factors relating to referred work<sup>22/</sup> that the firm performs on audits for which it is not the principal auditor), synchronization of schedules with a local regulator for purposes of a joint inspection, or simply the opportunity and the availability of resources to do an inspection earlier (including availability of inspectors with specialized industry knowledge and relevant language skills). In addition, the Board will at least annually review updated market capitalization data and consider whether there have been any changes that warrant moving a particular inspection forward to an earlier year.

Conversely, the Board does not intend to make changes that would move an inspection of one of these 49 firms to a later year than in the initial distribution except as the result of a development relating to the market capitalization of the firm's issuer clients. Specifically, if a firm's issuer audit client market capitalization drops significantly and the firm performs no significant amount of referred work on audits, its inspection might be delayed to a later year. In any event, the Board will not, for any reason, move one of these 49 inspections to a later year than in the initial distribution without publicly describing the change and the reason for it.

In response to the Board's request for comment on the proposed extension of the 2009 inspection deadline, several commenters suggested that the Board exercise its authority under Section 106 of the Act to exempt firms that cannot cooperate with PCAOB inspections due to legal conflicts or sovereignty-based opposition from their local governments. 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

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<sup>21/</sup> The issuer audit client U.S. market capitalization currently associated with a significant number of the 49 firms is relatively low, and even zero in a number of cases where firms appear to have stopped issuing audit reports for issuers. As a result, approximately 92% of the relevant issuer market capitalization is associated with 15 of the 49 firms.

<sup>22/</sup> Because the PCAOB is still in the process of gathering information about each firm's referred work, the 2009 inspections will not use referred work as a risk factor for purposes of scheduling.



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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.<sup>23/</sup>

The Board also received several comment letters addressing the length of the proposed extension for certain firms with 2009 deadlines. Some comment letters expressed concern about the inspection delay of up to three years but ultimately expressed qualified support for the Board's decision. These comments urged the Board to permit no further delays and to proceed as described above by sequencing the inspection of firms subject to the extension based on certain thresholds relating to the U.S. market capitalization of firms' issuer audit clients. These comments also supported the Board's suggestion that the Board announce at the beginning of each calendar year until 2012 all of the non-U.S. jurisdictions in which there are firms whose inspection the Board will conduct in that year. Some comments also suggested that the Board should utilize the additional time provided by the proposed extension to enhance its international inspections program, particularly in the areas of risk assessment and pre-inspection planning.

Other comment letters supported the Board's decision to extend the inspection deadlines, but some qualified their support by noting that three years may not be enough time to overcome the legal conflicts and sovereignty concerns in all relevant jurisdictions. Several comments expressed support for the Board's plan to sequence the deferred inspections in time based on the U.S. market capitalization of the firms' clients, but some also noted that this plan did not adequately take into account the varying degree of legal conflicts present in the different jurisdictions and might have the effect of requiring early on during the three year period the inspection of firms in jurisdictions with legal obstacles that cannot be overcome quickly.

As explained above, the Board believes that an extension of up to three years for the relevant firms is the appropriate course. Distributing the affected firms across three years strikes the proper balance between avoiding unnecessary delays in the inspection of registered firms and allowing reasonable time for the Board to continue its efforts to reach cooperative arrangements with the relevant home-country regulators. The Board

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<sup>23/</sup> When it first became operational, the Board considered whether to exempt non-U.S. firms from registration with the Board. The Board determined that exempting non-U.S. firms would not protect the interests of investors or further the public interest given that registration is the predicate to all of the Board's other oversight programs. See Registration System for Public Accounting Firms, PCAOB Release No. 2003-007 (May 6, 2003) at 13.



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believes that any longer or further extension would not be in the interests of investors or the public.

In the Board's view, this adjustment to the inspection frequency requirement is consistent with the purposes of the Act, the public interest, and the protection of investors. The Board believes that its approach to implementing Rules 4011 and 4012, developing cooperative arrangements, and conducting joint inspections with foreign regulators is enhancing the Board's efforts to carry out its inspection responsibilities. There is long-term value in accepting a limited delay in inspections to continue working toward cooperative arrangements where it appears reasonably possible to reach them. As suggested by some comments, the Board also believes that the additional time to conduct certain inspections will have the added benefit of giving the Board more time to continue to enhance its inspection program, particularly in the areas of risk assessment and pre-inspection planning, and the Board intends to do so.

The Board recognizes that some non-U.S. firms may be reluctant to comply with PCAOB inspection demands because of a concern that doing so might violate local law or the sovereignty of their home country. The Board believes that the purposes of the Act, the public interest, and the protection of investors are better served, up to a point, by delaying some of the first inspections to work toward a cooperative resolution than by precipitating legal disputes involving conflicts between U.S. and non-U.S. law that could arise if the Board sought to enforce compliance with its preferred schedule without regard for the concerns of non-U.S. authorities.

The Board does not intend, however, to make any further adjustments to the inspection frequency requirements applicable to firms whose first inspection was due no later than 2009. While the Board will continue to work toward cooperation and coordination with authorities in the relevant jurisdictions, the Board will make inspection demands on the firms early enough in the year in which they are scheduled for inspection according to the above described sequencing to allow the Board to conduct the inspections during that year.

**IV. Transparency Concerning International Inspections Program**

In order to provide additional transparency with regard to the Board's international inspections program, the Board has implemented its proposal to announce publicly, near the beginning of each year until 2012, all of the non-U.S. jurisdictions in which there are firms whose inspections the Board will conduct in that year (including, but not limited to, jurisdictions relevant to the 49 inspections discussed above). Once such announcement is made, the Board will not remove a jurisdiction from the list



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unless the Board publicly explains why the schedule has changed with respect to that jurisdiction.<sup>24/</sup>

In addition, because the Board recognizes that investors have an interest in the identity of firms that have not been inspected within the timeframe that investors could reasonably have expected an inspection to occur, the Board intends to implement its proposal to maintain on its web site an up-to-date list of all registered firms that have not yet had their first Board inspection even though more than four years have passed since the end of the calendar year in which they first issued an audit report while registered with the Board.<sup>25/</sup> Inclusion on the list is not an indication that a firm has not cooperated with the Board or is at fault in any way, nor is the list intended as a substitute for action the Board might take in the event that a firm fails to cooperate in an inspection. The list is intended only to provide transparency to the public with regard to delayed inspections.

The Board received a number of comments addressing transparency issues. Several comment letters support the Board's proposal to maintain a list of firms that have not yet been inspected as described above. Two comments suggested that the Board should provide regular (e.g. biannual) updates on the progress it has made in inspecting the 49 firms subject to the extension. Several comment letters asserted that along with listing the firms that have not been inspected, the Board should explain the reason for the failure to conduct the inspection.

Other commenters expressed opposition to the Board's proposed list of firms. Concerns include the possibility that the list would unfairly raise questions about the

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<sup>24/</sup> A list of the non-U.S. jurisdictions in which there are firms that the Board intends to inspect in 2009 is available at:

[http://www.pcaobus.org/Inspections/Other/2009/List\\_of\\_Jurisdictions\\_2009.pdf](http://www.pcaobus.org/Inspections/Other/2009/List_of_Jurisdictions_2009.pdf).

The Board also maintains on its web site a list of those jurisdictions in which there are registered firms that the Board has inspected:

[http://www.pcaobus.org/Inspections/Other/2009/Inspections\\_Non\\_US.pdf](http://www.pcaobus.org/Inspections/Other/2009/Inspections_Non_US.pdf)

The current list of those jurisdictions also is provided in footnote 10 above.

<sup>25/</sup> See PCAOB Rules 4003(b) and 4003(d); see also Amendments to Board Rules Relating to Inspections, PCAOB Release No. 2006-008 (Dec. 19, 2006).



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firms' quality of work even though no inspection has taken place, potentially through no fault of the firm. Some comment letters also suggested that the list could cause a loss of investor confidence in the listed firms' clients or in other audit firms in jurisdictions with firms on the list. Several commenters urged that the proposed list should be accompanied by language explaining that inclusion on the list does not constitute a reflection of the firms' quality of work, and/or that the list should explain the reason for each firm's inclusion on the list.

Several alternatives to the list of firms proposed by the Board were suggested by the comment letters, including (1) listing only the jurisdictions where inspections have not been conducted rather than listing individual firms, (2) listing firms that have been inspected in lieu of firms that have not, or (3) creating a comprehensive list of all firms subject to inspection with three categories – firms that have been inspected and a report has been issued, firms that have been inspected but where no report has been issued yet, and firms that have not been inspected.

As explained above, the Board believes that the expectation created by the Act and the Board's rules as to the frequency of inspections should be addressed through transparency about the Board's progress. However, the Board agrees with those commenters who suggested that a list of uninspected firms could falsely suggest that the listed firms are being uncooperative without any reason or that the quality of their work is poor. The Board therefore intends to preface the list with language clarifying that inclusion on the list is not intended to create any positive or negative inferences about the quality of the firm's audit work, its systems, policies, procedures, practices or conduct, or about the strength of its home-country oversight system.

The Board does not believe that it would be appropriate to provide an explanation for each firm's inclusion on the list. The Board may not be in a position to know all of the reasons for a firm's position with respect to an inspection demand by the Board. In addition, given the possibility of disciplinary proceedings to determine whether a particular firm's conduct violates the Act or PCAOB rules, it would be inappropriate for the Board to comment publicly on the firm's position with respect to an inspection demand. The Board will include in the prefatory language to the list a statement that inclusion on the list should not be construed as supporting any positive or negative inferences about the reason(s) for inclusion on the list.

Further, the Board does not believe that the alternative suggestions to the proposed list of uninspected firms – such as listing jurisdictions where inspections have not taken place or listing firms where inspections *have* been conducted – are sufficiently transparent. In some jurisdictions, some firms may have been inspected within the relevant four-year time period while other firms were not. Listing the relevant jurisdiction



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therefore would misrepresent the inspection status of those firms that were inspected. In addition, the Board does not believe that listing firms that have been inspected, rather than those that have not, would provide the necessary transparency about the fact that other firms were not inspected during the normal timeframe required by the Act and Board rules, as some firms registered with the PCAOB are not currently required to be regularly inspected under the Board's rules.

Finally, the Board agrees with the comments suggesting that the Board should provide biannual updates about the progress it has made in inspecting the 49 firms subject to the amendment to Rule 4003(g). Thus, the Board will announce biannually its progress toward the thresholds described above with respect to the number of firms to be inspected each year and the aggregate market capitalization of firm clients. An additional measure of transparency of the Board's progress in international inspections in general is provided by the Board maintaining a list on its web site of those jurisdictions in which there are registered firms that the Board has already inspected, as noted in footnote 24 above.

### V. Registered Firms' Obligations

As described above, the Board intends to continue its efforts to develop cooperative relationships with its foreign counterparts. However, in light of its statutory obligation, as the Board explained above and in the Proposing Release, it will need to make inspection demands on non-U.S. firms even in circumstances where the sovereignty concerns or legal objections of local authorities have not been overcome. The Board recognizes that, in those circumstances, some non-U.S. firms may be reluctant to comply with PCAOB inspection demands. The Board cannot, however, let the prospect of such refusals dictate delays in the Board's efforts to conduct inspections.

As explained in the Proposing Release, firms must register with the Board in order to engage in certain professional activity directly related to, and affecting, U.S. financial markets, and all registered firms are subject to the Act and the rules of the Board irrespective of their location.<sup>26/</sup> A registered firm is subject to various requirements and conditions, including PCAOB Rule 4006's requirement to cooperate in an inspection. In addition, as reflected in Section 102(b)(3) of the Act, a firm's

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<sup>26/</sup> See Section 106(a)(1) of the Act.



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compliance with Board requests for information is a condition of the continuing effectiveness of the firm's registration with the Board.<sup>27/</sup>

The Board noted in the Proposing Release that a registered firm's failure or refusal to provide requested information is a violation of Rule 4006 and that the Board does not view non-U.S. legal restrictions or the sovereignty concerns of local authorities as a sufficient defense in a Board disciplinary proceeding instituted under Section 105(c) of the Act for failing or refusing to provide information requested in an inspection.

The Proposing Release explained that when a violation of Rule 4006 is established through a disciplinary proceeding in accordance with the Act and the Board's rules, the Board may impose disciplinary sanctions. The Board noted that there is a range of disciplinary and remedial sanctions available to the Board, including revocation of a firm's registration. While the Board's consideration of any actual noncooperation case will be based on the facts of the case, the Board must take into account the importance of the inspection process to the oversight regime established by the Act. Moreover, the Board must be sensitive to the legislative premise reflected in Section 102(b)(3) – that firms that cannot or will not cooperate with Board requests for information should not be registered. That being said, at the same time, the Board recognizes that a refusal to provide information based on non-U.S. legal restrictions or the sovereignty concerns of local authorities implicates considerations not present in other noncooperation circumstances.

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<sup>27/</sup> Section 102(b)(3) requires that a firm's registration application include a statement that the firm consents to cooperate in and comply with Board requests for information and that the firm understands and agrees that such cooperation and compliance is a condition to the continuing effectiveness of the firm's registration with the Board. Some non-U.S. firms, invoking PCAOB Rule 2105, declined to include such statements in their applications on the ground that, because of the possibility that the Board someday might request information that local law would restrict the firm from providing, the firm could not represent in advance that it would comply with every request that the Board might make. As long as certain criteria are satisfied, PCAOB Rule 2105 allows a firm's registration application to be considered complete, for purposes of registering the firm, even in the absence of the consent to cooperate. The absence from the application of the broad consent to cooperate, however, does not absolve a firm of the underlying obligation to cooperate if and when the Board seeks information, a point that the Board conveys in writing to any such firm when notifying the firm that its application is approved. See also Final Rules Relating to the Oversight of Non-U.S. Public Accounting Firms, PCAOB Release No. 2004-005 (June 9, 2004) at A2-15 – A2-19.



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To assist the Board in its consideration of these issues, the Board invited the public to comment on whether and how a non-U.S. legal restriction or refusal to cooperate due to a sovereignty concern should be factored into the Board's consideration of the appropriate sanction to impose for a violation of Rule 4006.

A number of comment letters urged the Board to adopt meaningful sanctions, including revoking a firm's registration, for non-compliance with Board inspection demands, even if the non-compliance is due to legal conflicts faced by the non-U.S. firm. These comments stated that investors have an interest in the inspections of audit firms who audit, or play a substantial role in the audits of, U.S. issuers and that investors would not benefit from the imposition of weaker sanctions on firms that do not cooperate with PCAOB inspection demands. Several comments stated that weak sanctions in this situation would create an incentive for firms to refuse to cooperate with the PCAOB and could lead to regulatory arbitrage, frustrating the Board's efforts to improve the quality of financial reporting in the U.S. These comments asked the Board to make a clear statement that sanctions will be pursued for non-compliance with inspections.

Conversely, a number of other commenters expressed concerns about the Board sanctioning firms whose refusals to cooperate with Board inspection demands are based on legal conflicts in the firms' respective home jurisdictions. These comments argued that sanctions in that situation would be unfair to the firms who have no control over local legal obstacles and who would be forced to choose between violating the Act and violating their home-country law. On the other hand, several comments stated that this fairness argument inappropriately elevates the concerns of firms over those of investors, who have a right to expect that those firms that play a significant role in the audits of U.S. public companies are subject to oversight on the same terms and to the same degree as U.S. firms.

Several comment letters also expressed concern that the imposition by the PCAOB of sanctions in this situation will harm the relationship of the PCAOB with the non-U.S. jurisdictions whose laws give rise to the conflict. Other comments suggested that the sanctions would impact not only audit firms but also U.S. issuers or their subsidiaries, because, according to the commenters, the sanctions referenced by the Board in the Proposing Release (restricting firms from accepting new clients or revoking firm registrations) would have to be imposed on all firms in a jurisdiction with a conflicting law and would leave available no registered firm to perform the necessary audit work, particularly in jurisdictions where the law requires that local firms perform the relevant audit work.



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The Board appreciates the comments submitted on this point. As previously stated, the Board believes that most, if not all, legal conflicts relating to inspections can be resolved through cooperative arrangements, consents, or redaction of certain types of information that is otherwise not relevant to the inspection. Should a conflict prove to be unsolvable, however, the Board does not believe it would protect the interests of investors or further the public interest for the Board to decline as a matter of general policy to impose any sanctions on firms that do not cooperate with the Board's inspection demands because of legal conflicts or sovereignty concerns. Doing so would be tantamount to exempting those firms from the inspection requirement. The Board ultimately will weigh each case on its facts and will consider the comments further if and when the issue arises in a particular case.<sup>28/</sup>

On the 25th day of June, in the year 2009, the foregoing was, in accordance with the bylaws of the Public Company Accounting Oversight Board,

ADOPTED BY THE BOARD.

/s/ J. Gordon Seymour

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J. Gordon Seymour  
Secretary

June 25, 2009

APPENDIX A –  
Amendment to PCAOB Rule 4003

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<sup>28/</sup> The Board also requested comment on a possible rulemaking approach with regard to disclosures by a principal auditor that would be triggered in the case of noncooperation with a PCAOB inspection demand. The Board has made no final decision on this issue and will continue to consider the comments received in determining whether to undertake rulemaking in this area.



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### Appendix A – Amendment to Rule 4003

The Board is amending Section 4 of its rules by amending Rule 4003. The relevant portion of the rule, as amended, is set out below. Language added by the amendments is shown in bold italics. Other text in Section 4, including notes to the Rules, remains unchanged and is indicated by " \* \* \* " in the text below.

#### RULES OF THE BOARD

\* \* \*

#### SECTION 4. INSPECTIONS

\* \* \*

##### Rule 4003. Frequency of Inspections

\* \* \*

*(g) With respect to any foreign registered public accounting firm concerning which the preceding provisions of this Rule, other than paragraphs (a) and (f), would set a 2009 deadline for the first Board inspection and that is headquartered in a country in which no foreign registered public accounting firm that the Board inspected before 2009 is headquartered, such deadline is extended to 2012, provided, however, that from among the group of all such firms, the Board shall conduct some first inspections in each of the years from 2009 to 2012, scheduled according to such criteria as the Board shall publicly announce.*