



## COHEN MILSTEIN

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September 2, 2010

Elizabeth M. Murphy, Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549  
email:rule-comments@sec.gov  
**Submitted Electronically**

Dear Ms. Murphy:

I write in response to the Commission's invitation for comment on possible rulemaking under the recently passed Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111-203). I write to urge that the Commission use its rulemaking authority under the Dodd-Frank Act, or other appropriate rulemaking authority, to plug a disturbing loophole in current law which appears to effectively allow auditors based overseas to audit publicly traded U.S. registered companies while remaining beyond the reach of litigants who may have meritorious claims under the U.S. securities laws.

I believe that I am well qualified to comment on this matter. I am senior partner at the law firm of Cohen Milstein Sellers & Toll PLLC and have been representing plaintiffs in class action litigation for some forty years. My partners and I have prosecuted numerous securities cases in which some or all of the defendants were located overseas. Previously, I was a member of the staff of the Commission, with my last job as Chief Enforcement Attorney of the Division of Corporate Regulation.

As the Commission is aware, various accounting firms operate worldwide under a single name, but frequently through business entities organized separately in each country in which the firm operates. These international accounting firms routinely take the position that each of these national entities is a separate and independent legal entity whose conduct is not controlled by members of the accounting firm outside the entity's home country. These firms have argued that, because of the way they are organized, their affiliates outside the United States are not subject to the jurisdiction of the U.S. courts and consequently U.S. federal courts cannot compel them to comply with subpoenas in civil proceedings brought under the U.S. securities laws or hold them liable under the securities laws.



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A recently resolved case in which I represented a plaintiff class illustrates an inequity in the current situation. *In re LDK Solar Co. Ltd. Securities Litigation*, case number C-07-05182-WHA, was litigated in the U.S. District Court for the Northern District of California. The Defendants in the case were LDK Solar, a Chinese company which has traded on the New York Stock Exchange since its initial public offering in June 2007, and several of its officers and directors. Plaintiffs in the case alleged that Defendants had engaged in a securities fraud involving accounting irregularities. Defendants responded, among other defenses, that they could not be found to have acted with fraudulent intent because, in making relevant accounting decisions, they relied on the advice of Defendant LDK's outside auditors, the Chinese member firm of KPMG, KPMG Huazhen ("KPMG China"). Obviously the work papers of KPMG China related to its audit of LDK were highly relevant to the issues in the lawsuit. The Plaintiffs attempted to subpoena the work papers of KPMG China and the Defendants also requested that KPMG China produce these work papers. KPMG China refused to do so, asserting that "[d]ue to the applicable law and regulations in the People's Republic of China, KPMG Huazhen is unable to provide the requested documents." Plaintiffs also subpoenaed KPMG LLP, the U.S. member firm of KPMG, for the relevant work papers, but the U.S. entity took the position that it has no ownership interest or legal control over KPMG China and, consequently, had no way of obtaining these documents from KPMG China.

KPMG China had issued a "clean" opinion on LDK's relevant financial statements, which, accompanied by KPMG's opinion, were filed with the Commission in the registration statement that accompanied LDK's June 2007 initial public offering. KPMG China signed its opinion simply as "KPMG," giving investors no warning that KPMG China considered itself to be a separate entity from its U.S. counterpart and was, in its view, beyond the reach of U.S. courts.

The LDK Solar case was recently settled. At the settlement hearing, I explained to District Judge William Alsup, who presided over the case, that one of the reasons I thought that it was in the best interests of the class to settle rather than proceed to trial was the fact that the absence of the relevant work papers from KPMG China would make the case more difficult to prosecute. Judge Alsup approved the settlement, but expressed surprise and concern that a foreign firm could audit a publicly traded U.S. registered company and then refuse to turn over relevant documents in civil litigation. I think it is appropriate to quote Judge Alsup's remarks from the bench at some length:

The Court: The SEC is very strong ... in making sure that public companies that are trading on exchanges in the United States that they comply with various form 10-Ks and all of the requirements for financial statements that have been audited. And you seem to be saying that there's a big loophole, and that if you manage to have your principal headquarters in China, that you can't get at the [auditing firm's] workpapers.

....



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The Court: That seems to be a gigantic loophole.

Mr. Milstein: It's a gigantic loophole and a gigantic problem, not just for LDK, but for all the other Chinese companies, not just this company.

The Court: [The] SEC ought to say that if somebody is not going to make their workpapers available they cannot trade on the national exchanges. That's what I would do if I was the SEC. That seems ... unfair that someone could not stand behind their financial Statements.

....

Now, are you sure—I want to make sure you're telling me that I didn't misunderstand you. You're saying that to KPMG flat out said you cannot have these workpapers?

Mr. Milstein: KPMG in China said that, that is correct....

....

The Court: Well, maybe the SEC ought to say if it's a crime in China for you to do what we need to do in the United States, then the company ought to get an auditor who will be able to comply and not hide behind some law in China.

....

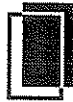
The Court: ....The papers that go to the investing public in the United States ... ought to be subject to the same discovery obligations as an auditor here in the United States.

Transcript of June 17, 2010 Settlement Hearing, 8:21-12:14, *In Re LDK Solar Securities Litigation*. A copy of the relevant pages of the transcript is attached to this letter. (The July 29, 2010 opinion approving the settlement in the case is available on Westlaw at 2010 WL 3001384.)

Section 929J of the Dodd-Frank Act provides a partial solution to the issue that emerged in *In re LDK Solar Co. Ltd. Securities Litigation*. This section establishes a procedure meant to allow the Commission or the Department of Justice to compel production of the work papers of a firm which acts as outside auditor to a U.S. registered company. But the provision does not apply to private litigants. As is widely recognized, given the size of the securities markets and, unfortunately, the extent of fraud at publicly traded companies, enforcement by the Commission is not, by itself, sufficient to adequately protect investors. As the Supreme Court has explained, "private actions to enforce federal antifraud securities laws are an essential supplement to criminal prosecutions and civil enforcement actions brought, respectively, by the Department of Justice and the Securities and Exchange Commission." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007).

Among other inequities, current law regarding foreign accounting firms auditing companies traded in the U.S. has the perverse effect of encouraging registrants to use foreign as opposed to domestic accounting firms. The law puts U.S. accounting firms at a disadvantage because they are required to produce their work papers in civil litigation while their foreign

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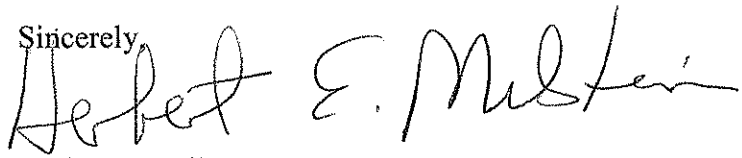
counterparts may be unwilling to do so. Moreover, given the pervasive use of similar, or even identical, trade names by the international accounting firms, investors in the U.S. may be wholly unaware of whether the auditor of the companies in which they invest are based in the United States or abroad.

I respectfully submit that it is in the interest of the Commission, the U.S. securities markets, and investors such as the state and municipal pension plans that my firm routinely represents, that the Commission adopt a rule that mandates that any company whose securities are registered to trade in the U.S. markets choose, as its outside auditor, a firm that has consented to the jurisdiction of the United States courts for service of process or subpoena and which has agreed to produce work papers and other documents relevant to its work for the company if they are validly requested in U.S. civil litigation.

I am sending a copy of this letter to Judge Alsup because, at the June 17 hearing, he requested that we provide him a copy of any correspondence filed with the SEC on this subject, as well as to Defendants' counsel in the LDK Solar case.

The views expressed in this letter are mine and do not necessarily reflect those of my firm's clients.

Sincerely,



Herbert E. Milstein

Enclosure

HEM/pas

cc: Hon. William Alsup, United States District Judge, Northern District of California (w/encl.)

David M. Becker, General Counsel and Senior Policy Director, United States Securities and Exchange Commission (w/encl.)

Robert Khuzami, Director of the Division of Enforcement, United States Securities and Exchange Commission (w/encl.)

James J. Farrell, Esq., Latham & Watkins Los Angeles (w/encl.)

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UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF CALIFORNIA

BEFORE THE HONORABLE WILLIAM ALSUP, JUDGE

IN RE LDK SOLAR SECURITIES ) PAGES 1 - 26  
LITIGATION, )  
 ) C07-5182 WHA  
THIS DOCUMENT RELATES TO: ALL )  
ACTIONS. ) THURSDAY, JUNE 17, 2010  
 )  
 )

SAN FRANCISCO, CALIFORNIA ,

TRANSCRIPT OF PROCEEDINGS

APPEARANCES:

FOR PLAINTIFFS: COHEN MILSTEIN  
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AND

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ESQUIRE  
ANTHONY D. PHILLIPS, ESQUIRE

FURTHER APPEARANCES ON NEXT PAGE

REPORTED BY: KATHERINE POPE WYATT, CSR, RPR, RMR  
OFFICIAL REPORTER, USDC

COMPUTERIZED TRANSCRIPTION BY ECLIPSE

1 E-MAIL ADDRESS. AND WE ARRANGED A NUMBER OF PHONE CALLS WITH  
2 HIM, AND THEN HE CANCELLED EACH ONE OF THEM, SO WE NEVER  
3 SUCCEEDED IN TALKING AND WE NEVER GOT ANY OF THEM.

4 WE MADE A NUMBER OF ATTEMPTS TO INVITE HIM TO COME TO  
5 WASHINGTON, SAN FRANCISCO, WHEREVER HE WAS, AND SAID WE WOULD  
6 MEET HIM AND CERTAINLY ADVANCE THE PLANE FARE AND COST OF HOTEL,  
7 BUT IT WAS NOT SUCCESSFUL.

8 SO THE CASE BECAME AN ACCOUNTING CASE. NOT AN EASY  
9 CASE, A CASE WE BELIEVED IN. AND WE THOUGHT THE CASE WAS  
10 PROVABLE AND WAS A VERY GOOD CASE.

11 BUT THE DEFENDANTS DENIED IT. WE HAD NO ACCESS TO THE  
12 ACCOUNTING WORKPAPERS, WHICH WERE DONE BY KPMG CHINA, WHICH TOOK  
13 THE POSITION THAT ALTHOUGH WE SENT PROCESS TO THEM, THEY SAID  
14 YOU CAN GET KPMG'S PAPERS IN THE UNITED STATES. WE GOT THOSE,  
15 BUT YOU COULDN'T GET THE PAPERS IN CHINA. IT WAS A CRIME. THEY  
16 ALSO SORT OF HINTED THAT THEY WERE SORT OF AN AFFILIATE OF THE  
17 GOVERNMENT.

18 **THE COURT:** LET ME STOP YOU AND ASK YOU A QUESTION  
19 ABOUT THAT.

20 **MR. MILSTEIN:** YES.

21 **THE COURT:** THE SEC IS VERY STRONG --

22 **MR. MILSTEIN:** YES.

23 **THE COURT:** -- IN MAKING SURE THAT PUBLIC COMPANIES  
24 THAT ARE TRADING ON EXCHANGES IN THE UNITED STATES THAT THEY  
25 COMPLY WITH VARIOUS FORM 10-K'S AND ALL OF THE REQUIREMENTS FOR

1 FINANCIAL STATEMENTS THAT HAVE BEEN AUDITED. AND YOU SEEM TO BE  
2 SAYING THAT THERE'S A BIG LOOPHOLE, AND THAT IF YOU MANAGE TO  
3 HAVE YOUR PRINCIPAL HEADQUARTERS IN CHINA, THAT YOU CAN'T GET AT  
4 THE WORKPAPERS.

5 **MR. MILSTEIN:** I THINK THAT IS CORRECT, YOUR HONOR.  
6 I KNOW --

7 **THE COURT:** HOW CAN THERE BE SUCH A LOOPHOLE?

8 **MR. MILSTEIN:** IT'S AN ENORMOUS LOOPHOLE. I USED TO  
9 BE CHIEF ENFORCEMENT ATTORNEY OF ONE OF THE SEC'S DIVISIONS, AND  
10 IT'S SOMETHING THAT REALLY DISTURBS ME.

11 AND WHEN THIS CASE IS OFFICIALLY OVER, I INTEND TO  
12 SEND A LETTER TO THEM AND TRY TO MEET WITH THEM JUST TO TELL  
13 THEM NOT ABOUT THIS, BUT JUST TO TELL THEM THAT I THINK THEY --

14 **THE COURT:** WOULD YOU SEND A COPY OF THAT LETTER TO  
15 ME --

16 **MR. MILSTEIN:** ABSOLUTELY, YOUR HONOR.

17 **THE COURT:** -- SO I CAN BE APPRISED OF WHAT FOLLOWS  
18 UP WITH THAT?

19 **MR. MILSTEIN:** ABSOLUTELY, YOUR HONOR.

20 **THE COURT:** THAT SEEMS TO BE A GIGANTIC LOOPHOLE.

21 **MR. MILSTEIN:** IT'S A GIGANTIC LOOPHOLE AND A  
22 GIGANTIC PROBLEM, NOT JUST FOR LDK, BUT FOR ALL THE OTHER  
23 CHINESE COMPANIES, NOT JUST THIS COMPANY.

24 **THE COURT:** SEC OUGHT TO SAY THAT IF SOMEBODY IS NOT  
25 GOING TO MAKE THEIR WORKPAPERS AVAILABLE THEY CANNOT TRADE ON

1 THE NATIONAL EXCHANGES.

2 THAT'S WHAT I WOULD DO IF I WAS THE SEC. THAT SEEMS  
3 LIKE UNFAIR THAT SOMEONE COULD NOT STAND BEHIND THEIR FINANCIAL  
4 STATEMENTS.

5 **MR. MILSTEIN:** YES, I AGREE WITH THAT.

6 **THE COURT:** OR, FOR THAT MATTER, AN ACCOUNTING FIRM.  
7 NOW, ARE YOU SURE -- I WANT TO MAKE SURE YOU'RE  
8 TELLING ME THAT I DIDN'T MISUNDERSTAND YOU.

9 YOU'RE SAYING THAT TO KPMG FLAT OUT SAID YOU CANNOT  
10 HAVE THESE WORKPAPERS?

11 **MR. MILSTEIN:** KPMG IN CHINA SAID THAT, THAT IS  
12 CORRECT. AND KPMG IN THE UNITED STATES GAVE US -- PURPORTED TO  
13 GIVE US WHAT THEY HAD, BUT THAT WAS NOT THE ESSENCE --

14 **THE COURT:** BUT WHO WAS IT THAT SIGNED THE AUDIT  
15 OPINION?

16 **MR. MILSTEIN:** THE AUDIT OPINION WAS SIGNED BY KPMG  
17 CHINA.

18 **THE COURT:** SO THE ENTITY THAT SIGNED THE 10-K; IS  
19 THAT RIGHT?

20 **MR. MILSTEIN:** YES.

21 **THE COURT:** I MEAN, THEY DO HAVE TO SIGN SOMETHING ON  
22 THE 10-K, DON'T THEY?

23 **MR. MILSTEIN:** THEY HAVE TO SIGN AN OPINION, AND I  
24 DON'T KNOW WHETHER THEIR SIGNATURE IS ON THE 10-K, BUT, IN  
25 ESSENCE, IT IS.



1           **THE COURT:** BUT DON'T THEY RECOGNIZE THAT IT'S GOING  
2 TO BE USED FOR THE 10-K?

3           **MR. MILSTEIN:** NO QUESTION ABOUT IT, YOUR HONOR.

4           **THE COURT:** MY MEMORY OF IT IS THAT THEY HAVE TO --  
5 THAT THEY MUST ACKNOWLEDGE THAT THEY KNOW IT'S GOING TO BE USED  
6 FOR THE 10-K.

7           SO KPMG IN CHINA IS ALLOWED TO -- IS ALLOWED TO SIGN,  
8 SATISFY THAT SEC REQUIREMENT. BUT THEN, WHEN THE TIME COMES TO  
9 LOOK AT THE WORKPAPERS, THEY SAY:

10                       "NO, YOU CAN'T DO THAT."

11           **MR. MILSTEIN:** NO. IT'S A CRIME TO PRODUCE THOSE  
12 PAPERS IN CHINA. AND, ACTUALLY, IT'S NOT ONLY AN AUDIT FOR A  
13 10-K, BUT IT WAS AN AUDIT FOR A REGISTRATION STATEMENT, SO THE  
14 SAME --

15           **THE COURT:** WELL, MAYBE THE SEC OUGHT TO SAY IF IT'S  
16 A CRIME IN CHINA FOR YOU TO DO WHAT WE NEED TO DO IN THE UNITED  
17 STATES, THEN THE COMPANY OUGHT TO GET AN AUDITOR WHO WILL BE  
18 ABLE TO COMPLY AND NOT HIDE BEHIND SOME LAW IN CHINA.

19           **MR. MILSTEIN:** LDK DID NOT OPPOSE US GETTING THE  
20 PAPERS.

21           **THE COURT:** I UNDERSTAND THAT.

22           **MR. MILSTEIN:** YES.

23           **THE COURT:** I'M NOT BLAMING LDK.

24           **MR. MILSTEIN:** NO.

25           **THE COURT:** BUT LDK HAD THE RIGHT TO GO AND GET

1 SOMEBODY IN THE UNITED STATES TO COME TO DO IT AND DO THE AUDIT,  
2 AND THEN THE PAPERWORK, PAPERS WOULD HAVE BEEN --

3 **MR. MILSTEIN:** YES. YES. WELL, THE CONFUSING THING,  
4 TOO, IS KPMG. I'M NOT PICKING ON THEM, PARTICULARLY, BUT ALL  
5 THESE FOUR VERY LARGE ACCOUNTING FIRMS ALL HAVE THESE  
6 SUBSIDIARIES NATIONALLY ALL OVER THE WORLD, AND THEY TAKE THE  
7 POSITION THAT IT'S A LOOSE AFFILIATION, BUT, OF COURSE, THEY ALL  
8 USE THE SAME NAME.

9 **THE COURT:** EVEN IF THEY ARE NOT, THAT'S A SEPARATE  
10 PROBLEM. LET'S JUST SAY IT WAS CALLED "ABC AUDIT SERVICES OF  
11 CHINA," IF THAT'S WHO IT IS THAT IS GOING TO BE SIGNING OFF ON  
12 THE PAPERS THAT GO TO THE INVESTING PUBLIC IN THE UNITED STATES  
13 THEN THEY OUGHT TO BE SUBJECT TO THE SAME DISCOVERY OBLIGATIONS  
14 AS AN AUDITOR HERE IN THE UNITED STATES.

15 **MR. MILSTEIN:** I WOULD AGREE WITH THAT, YOUR HONOR.

16 **THE COURT:** ALL RIGHT. ALL RIGHT. ALL RIGHT. SO  
17 YOU DID THE BEST YOU COULD DO ON THAT.

18 **MR. MILSTEIN:** DID THE BEST WE COULD. WE ALL HIRED  
19 EXPERTS. THEY ALL DISAGREED. SO IT WOULD HAVE BEEN AN ISSUE  
20 FOR THE JURY, ISSUE FOR THE COURT. IT WOULD HAVE BEEN VERY  
21 DIFFICULT TO PROVE SCIENTER FOR THE ACCOUNTING CASE.

22 WAS IT INTENTIONAL OR RECKLESS? DEFENDANTS SAY THEY  
23 RELIED ON KPMG, THAT WE HAD NO ACCESS TO, AND THEY RELIED ON  
24 THEIR LAWYERS.

25 AND THERE WAS A LOSS CAUSATION PROBLEM, LARGELY