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October 5, 2012

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File Number PCAOB-2012-001, Public Company Accounting Oversight Board Proposed Rules on Auditing Standard No. 16, Communications with Audit Committees and Related Transitional Amendments to PCAOB Standards (Release No. 34-67807)

Dear Ms. Murphy:

The U.S. Chamber of Commerce (the "Chamber") is the world's largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy. The CCMC believes that businesses need to have systems of strong internal controls and recognizes the vital role external audits play in capital formation. Accordingly, the CCMC supports efforts to improve audit quality and appreciates the opportunity to comment on the Public Company Accounting Oversight Board ("PCAOB") *Proposed Rules on Auditing Standard No. 16 ("AS 16"), Communications with Audit Committees and Related Transitional Amendments to PCAOB Standards* ("the Proposed Rules").

The CCMC believes that the PCAOB in finalizing the Proposed Rules has failed to provide either the factual or analytic basis required for the Securities and Exchange Commission ("SEC") to meet its new statutory obligations under Section 103(a) (3) (C) of the Sarbanes-Oxley Act "SOX Act"), as amended by Section 104 of the Jumpstart Our Business Startup Act ("JOBS Act"). The CCMC believes that the Proposed Rule fails to follow the procedures required under the JOBS Act by not

demonstrating or providing the required analysis on how the imposition of the Proposed Rules to Emerging Growth Companies ("EGC's") will promote efficiency, competition and capital formation. Accordingly, the CCMC respectfully requests that the SEC remand the Proposed Rules to the PCAOB for further examination.

Discussion

The PCAOB articulates its vision statement as follows:

The PCAOB seeks to be a model regulatory organization. Using innovative and ***cost-effective tools***, the PCAOB aims to improve audit quality, reduce the risks of auditing failures in the U.S. public securities market and promote public trust in both the financial reporting process and auditing profession.[1] (Emphasis added).

The CCMC is supportive of that mission and believes that it is an important one for efficient capital markets. Clearly, an effective standard setting, inspection and compliance program is important for the PCAOB to be an effective regulator. The CCMC believes that public companies of all sizes should have strong internal controls and governance procedures, but that the costs and burdens involved should be scalable to the size and maturity of a company. Failure to incorporate scalable costs in the consideration of rules may create undue burdens that may inhibit the potential growth of a company.

Turning to the Proposed Rule, we note that the PCAOB issued the Proposed Rule on March 29, 2010, with a comment period closing on May 28, 2010. The CCMC filed a comment letter raising several concerns and requested that a Roundtable be held to allow for further discussion and airing of views. A Roundtable was held by the PCAOB on September 21, 2010 and a revised Proposed Rule was released on November 20, 2011, with a comment period closing on February 29, 2012. Congress passed the JOBS act with large bi-partisan majorities in March, 2012 and was signed into law by President Barack Obama on April 5, 2012. The PCAOB approved the Rule Proposal on August 15, 2012 and the SEC issued this request for comment for final approval on September 10, 2012.

[1] From the PCAOB website as of August 28, 2012.

The CCMC has previously commented on the Proposed Rule. While there have been some significant improvements made, the CCMC believes that important concerns remain.[2] In Part I of our letter, we raise the failure to address the new requirements imposed by the JOBS Act. This failure to properly consider and address this new requirement is a fundamental flaw. Absent substantiation from the PCAOB, we do not believe that the SEC will be able to make the determinations as required under the JOBS Act and approve the Proposed Rule. In Part II of our letter, we address some additional substantive comments and suggestions.

I. The Commission's Required Determination of Efficiency, Competition and Capital Formation

Section 104 of the JOBS Act states, with added emphasis on relevant language:

> Section 103(a) (3) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7213(a) (3)) is amended by adding at the end the following:
>
> (C) TRANSITION PERIOD FOR EMERGING GROWTH COMPANIES- Any rules of the Board requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer (auditor discussion and analysis) shall not apply to an audit of an emerging growth company, as defined in section 3 of the Securities Exchange Act of 1934. ***Any additional rules adopted by the Board after the date of enactment of this subparagraph shall not apply to an audit of any emerging growth company, unless the Commission determines that the application of such additional requirements is necessary or appropriate in the public interest, after***

[2] *See* the May 28, 2010 and February 29, 2012 letters from the United States Chamber of Commerce Center for Capital Markets Competitiveness on PCAOB *Proposed Auditing Standard Related to Communications with Audit Committees; Related Amendments to PCAOB Standards and Transitional Amendments to AU Sec. 380 (*PCAOB Release No. 2011-008, December 20, 2011 and PCAOB Rulemaking Docket Matter No. 030). As subsequently discussed, the February 29, 2012 letter is attached.

> ***considering the protection of investors and whether the action will promote efficiency, competition, and capital formation.***[3]

Section 103(a) (3) of the JOBS Act represents a fundamental change in the PCAOB rule-making process. It provides an automatic exemption for EGCs from all new PCAOB rules unless the SEC makes an explicit contrary determination. If the SEC is unable to make this affirmative finding, there is a statutory exemption for EGCs. As explained in legislative history of the JOBS Act, this dramatic change in regulation reflects a determination by Congress that EGC's are an important driver of economic growth. It therefore imposes a special burden on regulators. The SEC must specifically find that imposing the new requirement on ECGs is necessary or appropriate in the public interest. In making this public interest finding, it must consider both the protection of investors and whether the action will promote efficiency, competition and capital formation.

In order to reverse a clear Congressional directive in favor of an EGC exemption, the SEC has a substantial responsibility to carefully consider all relevant information on both the costs of a new rule and its benefits. In effect this is a greater burden than the requirement to weigh costs and benefits for SEC rules as discussed by the U.S. Court of Appeals for the District of Columbia Circuit in the case of *Business Roundtable and Chamber of Commerce of the United States of America v. Securities and Exchange Commission*: as follows:

> Under the APA (Administrative Procedures Act), we will set aside agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 5 U.S.C. § 706(2) (A). We must assure ourselves the agency has "examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a rational connection between the facts found and the choices made." *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43, 103 S.Ct. 2856, 77 L.Ed.2d 443 (1983) (internal quotation marks omitted). The Commission also has a "statutory obligation to determine as best it can the economic implications of

[3] Public Law 112-106

> the rule." *Chamber of Commerce v. SEC,* 412 F.3d 133, 143 (D.C.Cir.2005).
>
> Indeed, the Commission has a unique obligation to consider the effect of a new rule upon "efficiency, competition, and capital formation," 15 U.S.C. §§ 78c (f), 78w (a) (2), 80a-2(c), and its failure to "apprise itself—and hence the public and the Congress—of the economic consequences of a proposed regulation" makes promulgation of the rule arbitrary and capricious and not in accordance with law. *Chamber of Commerce,* 412 F.3d at 144; *Pub. Citizen v. Fed. Motor Carrier Safety Admin.,* 374 F.3d 1209, 1216 (D.C.Cir.2004) (rule was arbitrary and capricious because agency failed to consider a factor required by statute).[4]

Because Congress created this presumption of an exemption for EGCs the SEC analysis must be specific to EGCs. Therefore, under Section 103(a) (3) (C) of the Sarbanes-Oxley Act, as recently amended, any new proposed standard of the PCAOB that seeks to regulate EGC's as defined in the JOBS Act must undergo an economic analysis and public appraisal to meet the efficiency, competition and capital formation test. This analysis and appraisal must be specific to the clear definition that Congress provided for EGC's, and it must take into account their differing characteristics and the impact of regulatory burdens as compared to other types of companies. Furthermore, through the use of data, analysis and public input, the PCAOB must clearly specify the reasons why a standard should affirmatively apply to an Emerging Growth Company taking into account a legislative mandate to promote efficiency, competition and capital formation by such issuers. Indeed, the legislative history of the JOBS Act reflects a determination by Congress that EGC's are an important driver of economic growth, and therefore imposes a special burden on regulators to demonstrate that the benefits of the Proposed Rule outweigh any impediments to efficiency, competition, and capital formation.

The CCMC believes that the Proposed Rule fails to meet this test on several different levels. Its explanation of the presumed benefits of the rule is purely conclusory and lacks any form of meaningful cost-benefit analysis. Even the factual

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[4] *See* Business Roundtable and Chamber of Commerce vs. SEC, 647 F.3d 1144, 1148 (DC Cir. 2011)

support contained in the nearly 200 page SEC release of the Proposed Rule ("release") is of little substance: "[f]or example, some inspection observations indicate that auditors have not made all required audit committee communications, possibly because they are not aware of the varying sources of communication requirements contained throughout the Board's standards and rules."[5] There is no quantification of the number of inspections in which this finding was made, no indication whether the communication failures were material or inconsequential, and no indication whether the oversight was isolated or systemic. Most importantly for the JOBS Act finding, there was no indication whether any of these communications failures involved the audit of an EGC. This is symptomatic of a fundamental problem with this proposal. It provides only the most cursory reference to EGCs and makes no effort to differentiate them from other issuers. Satisfactorily meeting the JOBS Act standard requires more.

Similarly when it speaks of the public interest, the release relies on general arguments describing the general benefits of audit committee oversight. "For example, research conducted by the Center for Audit Quality and published in its March 2008, *Report on the Survey of Audit Committee Members*, found that increased audit committee oversight was believed to have had a positive impact on the overall quality of audits by 92% of its audit committee member respondents."[6] A finding four years ago that audit committee oversight was having a positive impact provides no basis for mandating more oversight or for concluding that more oversight will be an improvement that outweighs the costs.

The PCAOB proposal is also devoid of any semblance of an analysis of the cost of compliance with the rule for all issuers or for EGCs. For example the release explains:

> There will be some costs associated with audit committee communications under the new standard, including additional costs incurred by companies. As previously discussed the costs for a company to operate and maintain an audit committee may increase

[5] File Number PCAOB-2012-001, Public Company Accounting Oversight Board Proposed Rules on Auditing Standard No. 16, Communications with Audit Committees and Related Transitional Amendments to PCAOB Standards (Release No. 34-67807), Page 148.
[6] Ibid, Page 175.

> because of the need for additional meetings and increased audit committee member time demands. However, for the reasons explained above, the Board does not believe these additional costs will significantly expand the time or resources companies spend on audit committees.[7]

Again, the PCAOB makes only the most casual reference to the JOBS Act requirement, when it proffers that compliance will be "scalable". Given that the proposal contains highly prescriptive mandatory communication requirements between an auditor and an audit committee, it is unclear why the PCAOB believes that it will be less costly for EGCs. The assumption that smaller companies, typically with shorter operating histories, will have less to talk about with their auditors in complying with the Standard simply because they are smaller is unsupported, and in our view not necessarily accurate. In this respect, the failure of the PCAOB to carefully consider the consequences of its actions is reminiscent of its failures when it proposed AS 2 governing compliance with section 404 of the Sarbanes-Oxley Act. The consequences of that policy are known to all.

Even if evidence suggested that smaller companies did in fact face fewer or more straightforward accounting issues, or simply have fewer discussions about them, the benefits of the Proposed Rule must be identified, supported, and analyzed, and the burden on such companies imposed by the new rules must nonetheless be balanced against the benefits. This must be done with the consideration of each new proposed standard of the PCAOB.

While the PCAOB points out that in some respects the Proposed Rule is consistent with prior standards this is not consequential. There is no exception to the requirements of Section 103(a) (3) (C) for proposals that are consistent with earlier standards. If the PCAOB wishes to apply prior standards as part of a new rule, it is required to go through the same process demanded of any other new rule. As a policy matter, this is sensible, since older standards mixed with new requirements, together with recent developments in the capital markets, can mean that even old standards have new and differing impacts on efficiency, competition, and capital formation.

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[7] Ibid, Page 177.

Again, we quote from the *Business Roundtable and Chamber of Commerce* decision, where the court held these types of arguments to be unpersuasive, stating that:

> [T]he Commission inconsistently and opportunistically framed the costs and benefits of the rule; failed adequately to quantify the certain costs or to explain why those costs could not be quantified; neglected to support its predictive judgments; contradicted itself; and failed to respond to substantial problems raised by commenters. For these and other reasons, its decision to apply the rule to investment companies was also arbitrary.[8]

It is also important to highlight one additional procedural flaw. The public was never afforded an opportunity to comment upon the JOBS Act requirements and the impacts of the Proposed Rule on EGC's. It is impossible to meaningfully comment on the Commission's analysis and proposed determination under Section 103(a) (3) (C) of the Sarbanes-Oxley Act unless the proposing release includes appropriate disclosure. The chronology of the consideration of the Proposed Rule show that the second comment period closed on February 29, 2012, the JOBS Act was signed into law on April 5, 2012 and the Proposed Rule was approved by the PCAOB on August 15, 2012. Following the passage of the JOBS Act, the PCAOB did not issue for public review or comment an economic analysis demonstrating why EGC's should be included in the Proposed Rule.

These flaws and omissions in the proposal make it impossible for the Commission to satisfy the new standard under Section 103(a) (3) (C), or to satisfy its long-standing responsibilities as articulated by the court's ruling in the *Business Roundtable and Chamber of Commerce* decision. Because the Proposed Rule, as submitted, fails to address mandatory statutory requirements, we believe that it should be returned to the PCAOB as improperly filed. The PCAOB should be requested to reopen its rulemaking process and carefully examine whether the requirements should be imposed upon EGCs. This examination should be conducted in a manner that specifically addresses the impact of the new requirements on EGCs.

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[8] See Business Roundtable and Chamber of Commerce vs. SEC, 647 F.3d 1144, 1149 (DC Cir. 2011)

II. Other Comments on the Rule Proposal

a. Additional Cost-Benefit Concerns

The CCMC has some additional concerns about the PCAOB's cost-benefit analysis. One of the PCAOB's primary arguments in support of AS 16 from a cost-benefit standpoint is the following: "Auditing Standard No. 16 is scalable, based on a company's size and complexity." As noted earlier, this is simply a conjecture; there is no evidence to support this claim.[9] Unsupported claims cannot as a matter of law support an analysis of the costs and benefits of rulemaking. Moreover, AS 16 is not a principles-based standard that allows for auditor judgment. Rather, as the CCMC comment letter to the PCAOB dated February 29, 2012 (attached) points out, AS 16 is prescriptive. Experience has shown, for example with AS 2, that prescriptive auditing standards are much more difficult to scale.

As additional support for the Proposed Rules from a cost-benefit standpoint, the PCAOB states: "The original proposal asked for comment on whether any of the requirements of the proposed standard were inappropriate based on the size or industry of the company. Commenters considered the proposed requirements to be applicable and appropriate to companies of different sizes and industries."[10] While this statement may be technically correct, it ignores the fact that the PCAOB's second exposure draft requested comments on the applicability of the proposed standard to securities brokers and dealers. The CCMC's February 29, 2012 letter expressed some concerns about the applicability of the proposed standard to brokers and dealers, which will be discussed in greater detail below. Thus, this appears to be an example of an area of comment that may be inadequately addressed in both the cost-benefit section and the release text of the Proposed Rule.

b. Broker-Dealers

Since the issuance of the initial exposure draft, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") has given the PCAOB oversight of the audits of brokers and dealers registered with the Securities and

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[9] In addition, the evidence on the nature of EGCs provided in the Proposed Rule demonstrates that they are heterogeneous and a number appear to be neither small nor less complex.
[10] *See* Federal Register/Vol. 77, No. 180/Monday, September 17, 2012/Notices.

Exchange Commission ("SEC"). The SEC has proposed to amend its rules to require that audits of the financial statements of brokers and dealers be performed under PCAOB standards. If so, the Proposal would apply to audits of broker-dealers. However, the CCMC is concerned that the PCAOB may not fully understand the governance structures and complexities of broker-dealers and, accordingly, whether the proposed requirements could be applied for these organizations as a practical matter.

For example, the Proposed Rule acknowledges that some broker-dealers may have governance structures that do not include boards of directors or audit committees. In these circumstances, for non-public broker-dealers, the Proposal would extend the definition of audit committees to include those persons designated to oversee the accounting and financial reporting processes of the company and its financial statement audit. The CCMC suggests that the PCAOB provide more clarity on the oversight level intended. In doing so, the CCMC recommends that the designated persons not be a chief financial officer ("CFO") or similar officer, but rather a chief executive officer ("CEO"). This suggestion fails to recognize the one inherent difference between an audit committee and a CFO or similar officer. Audit committees are composed of independent Board members while a CFO or similar officer is by definition not independent. The presumed benefits of independent oversight of the auditor that are the foundation of this proposal will not and cannot be achieved by mandating the same communications with a CFO or similar officer.

This is an area where a proposed standard that seems to work in the abstract may not in fact operate properly in actual implementation as a result of differing business models that the PCAOB may not sufficiently understand or have contemplated. We believe that these questions are relevant both to the soundness of the Proposed Rule as a policy matter, as well as to the cost-benefit requirements discussed in Part I of our letter above.

Another example is the circumstances that can occur in investment company complexes ("ICCs") where issuers (with audit committees) that have investment houses (with audit committees) that are corporate parents for broker-dealer subsidiaries that have no audit committees. Perhaps it would be worthwhile for the PCAOB to clarify that the intended communications should be with the audit

committee of the parent of the broker-dealer subsidiary, and not to the audit committee of the issuer or to both.

c. Potential Regulatory Conflicts

In its previous comment letters the Chamber has expressed concern that the Proposed Rule may go outside of the scope of the PCAOB's jurisdiction over the audit and infringe upon the corporate governance responsibilities of the SEC or under applicable state law in overseeing the audit committee. Our concerns focus on the potential confusion that could distort both corporate governance and audit oversight. We believe that the PCAOB had some of these concerns in mind when reviewing the public commentary of the Proposed Rule, but we ask that the SEC also review the Proposed Rule with an eye towards eliminating any potential regulatory conflict.

d. Convergence of Auditing Standards

The CCMC has been a strong supporter of working to achieve one set of global high quality auditing standards through the convergence of PCAOB auditing standards with those of the International Auditing and Assurance Standards Board ("IAASB") and the Auditing Standards Board ("ASB") of the American Institute of Certified Public Accountants ("AICPA"). While the Proposal, describes the differences between AS 16 and the relevant auditing standards of the IAASB and ASB, it does not adequately identify and explain the rationale for those differences. The CCMC believes the SEC is obligated to emphasize to the PCAOB the importance of having one set of global high quality auditing standards and, in this spirit, to work together with the IAASB and ASB to minimize any unnecessary differences among auditing standards.

Conclusion

The CCMC has significant concerns regarding the process employed in the consideration and approval of the Proposed Rule by the PCAOB, particularly in relation to the cost benefit analysis and other required findings in relation to EGCs and the lack of any solicitation of public comment thereon. Accordingly, we respectfully request that the Proposed Standard be remanded to the PCAOB for full consideration, analysis and public comment as required under the JOBS Act, SOX

and the Administrative Procedures Act. Additionally, the CCMC has additional concerns about the potential adverse impacts of the Proposed Standard upon broker-dealers, scalability and regulatory conflicts that the SEC should consider as it contemplates the Proposed Standard.

Sincerely,

Tom Quaadman

Cc: James R. Doty, Public Company Accounting Oversight Board
Lewis Ferguson, Public Company Accounting Oversight Board
Jeanette Franzel, Public Company Accounting Oversight Board
Jay Hanson, Public Company Accounting Oversight Board
Steven Harris, Public Company Accounting Oversight Board

Attachment