



CENTER FOR CAPITAL MARKETS COMPETITIVENESS

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August 11, 2017

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Public Company Accounting Oversight Board: Notice of Filing of Proposed Rules on the Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion, and Departures from Unqualified Opinions and Other Reporting Circumstances, and Related Amendments to Auditing Standards (Release No. 34-81187; File Number PCAOB-2017-01)

Dear Mr. Fields:

The U.S. Chamber of Commerce (the “Chamber”)¹ 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. CCMC believes that businesses must have a strong system of internal controls and recognizes the vital role external audits play in capital formation and supports efforts to improve audit effectiveness. CCMC appreciates the opportunity to comment on the Public Company Accounting Oversight Board (“PCAOB”) Proposed Auditing Standard on *The Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion and Related Amendments to PCAOB Standards* (the “Proposed Standard” or “Proposal”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) on July 19, 2017.

The Chamber strongly recommends that the SEC not approve the provisions regarding Critical Audit Matters (“CAMs”) and audit tenure. As currently designed,

¹ 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.

this standard will lead to the disclosure of immaterial information, increase liability costs for businesses and audit firms, and create a chilling effect on audit committee-auditor communications. If approved, the Proposed Standard will contribute to disclosure ineffectiveness and overload, degrading the ability of the SEC to promote efficiency, competition and capital formation without a demonstration of the benefits of the proposal. Perhaps most troubling, the Proposed Standard fails to demonstrate the benefits that would accrue to public companies, investors, and the capital markets if the proposal were adopted.

If the SEC does decide to move forward with auditor reporting of CAMs, we recommend that the Commission provide a safe harbor, coordinate with the PCAOB for modified inspections, postpone the effective date of the Proposed Standard and include a sunset provision for auditor reporting of CAMs.

Background

Financial reporting is the responsibility of management and includes the GAAP financial statements and other disclosures, such as disclosures required by the Securities and Exchange Commission (“SEC”) in Management’s Discussion & Analysis (“MD&A”). In turn, the board of directors, largely through the audit committee, provides oversight of management’s reporting and disclosures. The independent auditor’s responsibility is to express an opinion on whether the company’s annual financial statements, including the notes thereto, are presented fairly, in all material respects, in conformity with generally accepted accounting principles (“GAAP”). Determining GAAP for U.S. companies is the responsibility of the Financial Accounting Standards Board (“FASB”).

Another core principle of financial reporting is that the auditor is not an original source of information about the company. Accordingly, if there is material, decision-useful financial information for investors, it is not the auditor, but management that should provide it based on guidance from FASB or the SEC.

The Proposal would supersede or amend various existing PCAOB auditing standards on financial statement audit reports. The Proposal would require auditors to communicate in the auditor’s report CAMs arising from the audit of the current period financial statements and certain information about each CAM. It would also add new language on auditor responsibilities regarding independence and obtaining reasonable assurance about whether the financial statements are free of material misstatements whether due to error or fraud and on audit firm tenure.

The Proposed Standard adopted by the PCAOB is substantially similar to the reproposal issued for comment in May 2016², even though the PCAOB received 88 comment letters. The Chamber's comment letter on the PCAOB's May 2016 exposure draft summarized our concerns:³

1. The need for the Proposal is not sufficiently addressed;
2. The required disclosure of CAMs is often duplicative and not decision-useful;
3. The treatment of original and confidential information and its potential adverse consequences upon internal controls;
4. The increase of legal liability for businesses and auditors;
5. Additional concerns with CAMs and adverse consequences for businesses, auditors, and investors;
6. The Proposal should not apply to emerging growth companies; and
7. The PCAOB has not demonstrated why disclosure of audit firm tenure is necessary.

With the exception of the emerging growth companies, these concerns were not addressed by the PCAOB. We believe that the failure to address these concerns, as well as the lack of a comprehensive economic analysis laying out the costs and benefits of the standard, should be tackled before this standard is approved.

² The Chamber has commented on different forms of this proposal in the past. See the December 9, 2013 letter from the United States Chamber of Commerce Center for Capital Markets Competitiveness on the PCAOB Proposed Auditing Standards—*The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion; The Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report; and Related Amendments to PCAOB Standards* (PCAOB Release No. 2013-005, August 13, 2013; PCAOB Rulemaking Docket Matter No. 034) and the September 14, 2011 letter from the United States Chamber of Commerce Center for Capital Markets Competitiveness on the PCAOB *Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards* (PCAOB Release No. 2011-003, June 21, 2011, Rulemaking Docket Matter No. 034).

³ See the August 15, 2016 letter from the United States Chamber of Commerce Center for Capital Markets Competitiveness on the PCAOB Proposed Auditing Standard on *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion* (PCAOB Release No. 2016-003, May 11, 2016) (PCAOB Rulemaking Docket Matter No. 034). This letter is attached as an appendix for the full consideration by the SEC.

Chamber Concerns

I. Materiality and Confidentiality

The Proposed Standard would impose a new requirement for the auditor's report to include CAMs. The PCAOB defines CAMs as matters communicated or required to be communicated to the audit committee and that (1) relate to accounts or disclosures that are material to the financial statements and (2) involve especially challenging subjective, or complex auditor judgment. The auditor's report would be required to identify the CAM, describe the principal considerations that led the auditor to determine that the matter is a CAM, describe how the CAM was addressed in the audit, and refer to the relevant financial statement accounts or disclosures.

The PCAOB acknowledges that auditors could be disclosing immaterial information as CAMs. Additionally, the PCAOB recognizes that auditors may disclose original (confidential) information that would not otherwise be made public by the company. The PCAOB believes the Proposed Standard that provides for auditor disclosure of both immaterial and original (confidential) information is needed "in the public interest" and "to ensure that the fact that management did not provide a disclosure would not prevent the auditor from communicating a critical audit matter."⁴ Regardless of whether the auditor alone or both auditors and companies disclose this information, management will need to respond to inquiries from investors and analysts about otherwise immaterial and confidential matters. Indeed, the PCAOB characterizes this as a benefit of the Proposed Standard.⁵ An acknowledgement by the PCAOB that the Proposed Standard will lead to the disclosure of immaterial *and* confidential material should give the SEC pause.

To elaborate on immaterial matters, the Proposed Standard specifies that "each CAM relates to accounts or disclosures that are material to the financial statements" *rather* than specifying that a CAM itself has to be material (i.e., represents material matters arising from the audit of the financial statements taken as a whole). The PCAOB supports this fundamental aspect of the Proposed Standard by stating: "If the auditor were required to determine that a critical audit matter itself is material, rather than related to an account or disclosure that is material, it is likely that fewer matters would meet the definition of a critical audit matter and, thus, investors would

⁴ See the Proposed Standard, page 34 and pages 93-94, respectively.

⁵ For example, see the Proposed Standard pages 33-35. More generally, the PCAOB states that communication of CAMs in the auditor's report should "help investors and analysts who are interested in doing so to engage management and the audit committee with targeted questions about these issues" (page 67).

likely receive less, and less audit-specific, information than under the standard as adopted.”⁶

This PCAOB position is a fatal flaw with the Proposed Standard. A PCAOB requirement that involves the disclosure of immaterial information by design and/or implementation (and whether by auditors or both auditors and companies) is inconsistent with the securities laws and the regulations of the SEC, as well as generally accepted accounting principles (“GAAP”). It undermines the SEC’s entire framework for financial reporting and disclosures, and contravenes the SEC’s disclosure effectiveness initiatives. We question whether the PCAOB has the authority to promulgate a standard that provides for the disclosure of immaterial information. The SEC should not permit the PCAOB to usurp SEC authority and that of FASB in this regard.

In addition to immaterial information (that is not required to be disclosed by companies themselves), the PCAOB’s definition of CAMs may require auditors to disclose information specifically exempt from disclosure. A significant deficiency in internal control over financial reporting (“ICFR”) is one example of a matter specifically exempt from disclosure under both SEC and PCAOB rules.⁷

The PCAOB attempts to soften the requirements of the Proposed Standard with regard to disclosing significant deficiencies in ICFR, first by stating that a significant deficiency cannot be a CAM, in and of itself.⁸ Nonetheless, the Proposed Standard recognizes that requirements for auditors to identify CAMs and describe the principal considerations that led to determining the matter was a CAM could involve disclosing a significant deficiency. Accordingly, Release Text in the Proposed Standard instructs auditors to simply describe the matter in “broader” terms and not use the words “significant deficiency.”⁹

This does not solve the essential problem—namely the definition of CAMs and related reporting requirements of CAMs that will give rise to the disclosure of immaterial information, whether immateriality is determined by judgment, or defined by regulation or GAAP. We also discuss this issue in later sections of the letter as well.

⁶ For example, see the Proposed Standard, pages 19-20.

⁷ Illegal acts are given as another example. We subsequently discuss both significant deficiencies in ICFR and illegal acts in more detail.

⁸ See the Proposed Standard, page 21.

⁹ See the Proposed Standard, page 35.

This is also an example as to why CCMC has repeatedly called for the SEC, PCAOB and FASB to issue a common definition of materiality in financial reporting.¹⁰ We believe that this should be a priority to facilitate more efficient financial reporting and avoid the problems presented in the Proposed Standard.

II. Conflict with the Role and Duties of the Auditor

The CCMC continues to believe that the Proposed Standard undermines the role and responsibilities of auditors. As an example, management (not the auditor) is the source of original information about the company. The auditor's responsibility is to opine on whether the reporting by management is in conformity with GAAP. This long-standing premise is reinforced by client confidentiality requirements under state laws and codes of professional ethics. However, the PCAOB now maintains that these obligations should not apply to or be allowed to preempt PCAOB standards, specifically auditor reporting of CAMs as would be required by the Proposed Standard.¹¹

This places both auditors and management in an untenable position that may lead to conflict of legal obligations and increased liability. Auditors will run the risk of violating state laws and professional ethics requirements in order to comply with PCAOB requirements. Or, to avoid this situation, companies will be forced to make disclosures that they are not otherwise obliged to provide under GAAP or judicial interpretation of requirements to disclose under securities laws. Similar situations in other areas of corporate disclosure have led to "defensive" reporting through duplication and rote disclosures. Such a situation does not provide any benefits to businesses or their investors.

The Proposed Standard puts the PCAOB in the position of being a defacto regulator of financial reporting and disclosures, which exceeds the PCAOB's authority and represents a fatal flaw with the Proposed Standard.

¹⁰ See letter from CCMC to SEC Chair Mary Jo White, October 9, 2013, Page 2.

¹¹ The Proposed Standard states that professional or state law obligations to maintain client confidentiality should be preempted by reporting obligations arising under federal law and regulations, including PCAOB standards (page 33). Yet, in amending AU Section 431 as part of promulgating Auditing Standard No. 6 ("AS No. 6"), the PCAOB reaffirmed the propriety of confidentiality requirements imposed on auditors by other authorities. The PCAOB has been urged to adopt its own rule on confidentiality of client information. For example, in approving AS No. 6, the Commission encouraged the PCAOB "to develop and adopt a rule addressing the auditor's responsibility with respect to maintaining the confidentiality of client information" (Public Company Accounting Oversight Board; Order Approving Proposed Rule on Auditing Standard No. 6, Evaluating Consistency of Financial Statements, and Conforming Amendments (SEC Release No. 34-58555; File No. PCAOB-2009-01) September 16, 2008, page 6-7). The PCAOB has not acted on this recommendation from the SEC.

The PCAOB maintains the Proposed Standard that may result in auditors disclosing original (confidential) client information is no different than, for example, certain circumstances whereby auditors may be required to report to the SEC on an illegal act that has a material effect on the financial statements.¹² We respectfully disagree. The circumstances for auditor disclosure of illegal acts to the SEC are limited and exceptional—plus, they reflect legislative decisions that balance competing interests. These limited and exceptional circumstances are hardly similar to disclosing original (confidential) client information through CAMs in the auditor’s report.

III. Determination and Description of CAMs

The PCAOB recognizes that the determination and disclosure of CAMs will require significant auditor judgment. The PCAOB received a number of comments expressing concerns over the lack of clarity as to what constitutes a CAM and confusion over how to describe the principal considerations that led the auditor to determine that the matter is a CAM and how the CAM was addressed in the audit.

We find it problematic and disappointing that the PCAOB did not attempt to address these concerns and that the Proposed Standard actually exacerbates them. For example, the PCAOB did not field-test CAMs in advance of approving the Proposed Standard; the PCAOB provides few examples of CAMs in the Proposed Standard and the discussion of these examples reveals logical inconsistencies with the definition of CAMs; and the PCAOB does not provide any examples in the Proposed Standard of auditor reports illustrating the communication of CAMs. In fact, the PCAOB deleted the two illustrative examples provided in the May 2016 reproposal.

We are surprised that the PCAOB conducted no field-testing of CAMs. Given the lengthy period devoted to this standard-setting initiative, the PCAOB had ample time to mitigate uncertainties and avoid confusion by field-testing CAMs before adopting the Proposed Standard.¹³ The failure to do so will increase the likelihood of adverse unforeseen consequences that will be costly to both businesses and their investors. Field testing should have been used in the development of this Standard as a means to determine problems, unforeseen consequences and flaws. The tool should have been used to evaluate the viability of the proposal and whether flaws could be

¹² See the Proposed Standard, page 33. The Proposed Standard also uses auditor reporting on going concern as another example. This example appears misplaced because it is tethered to the auditor’s actual opinion and based on public policy decisions as to the circumstances for modifying that opinion.

¹³ The Center for Audit Quality’s letter to the PCAOB dated June 19, 2014 summarizes findings and recommendations from field-testing auditor reporting of CAMs on 51 audit engagements based on the PCAOB’s initial exposure draft on auditor reporting issued August 13, 2013.

fixed. Field testing should be used as a standard operating procedure in standard development.¹⁴

Further, the Proposed Standard actually contributes to uncertainty and creates confusion on the determination of CAMs by providing a few examples (in Release Text) of what would and would not be CAMs. For example, the PCAOB explains:

- The auditor's evaluation of the company's goodwill impairment assessment could be a CAM if goodwill was material to the financial statements, even if there was no impairment. This is because it would relate to goodwill recorded on the balance sheet and the disclosure in the notes to the financial statements about the company's impairment policy and goodwill.¹⁵

On the other hand, the PCAOB also states:

- A potential loss contingency that was communicated to the audit committee, but that was determined to be remote and was not recorded in the financial statements or otherwise disclosed under the applicable financial reporting framework, would not meet the definition of a CAM.¹⁶

Given that most companies have GAAP footnote disclosures on loss contingencies, it is very difficult to understand how this example would not "relate to disclosures that are material to the financial statements," similar to the goodwill impairment example—even though the particular loss contingency was eventually determined to be remote and not itself disclosed. While neither FASB accounting standards nor the Proposed Standard would require the disclosure of remote loss contingencies, the differing rationales are inconsistent and will create confusion for auditors and issuers.

Similarly, the PCAOB provides the following example:

- An illegal act (communicated or required to be communicated to the audit committee) would not meet the definition of a CAM if an appropriate determination had been made that no disclosure was required in the financial statements (footnotes), as the matter would not relate to an account or disclosure that is material to the financial statements.¹⁷

¹⁴ See letter from CCMC to SEC Chair Mary Jo White, October 9, 2013, Page 7.

¹⁵ See the Proposed Standard, page 20.

¹⁶ See the Proposed Standard, pages 20-21.

¹⁷ See the Proposed Standard, page 21.

Here, too, presumably an illegal act would relate to some account or disclosure, such as revenue, and (in accordance with the definition of CAMs in the Proposed Standard) the auditor should determine whether that account or disclosure is material to the financial statements—consistent with and specified in the goodwill impairment example.

The treatment of a significant deficiency in ICFR is also confusing and liable to lead to disclosure inconsistency. According to the PCAOB:

- A determination there is a significant deficiency in ICFR in and of itself, cannot be a CAM. Such determination, in and of itself, does not relate to an account or disclosure that is material to the financial statements as no disclosure of the determination is required.¹⁸ However, a significant deficiency could be among the principal considerations that led the auditor to determine that a matter is a CAM, for example, regarding revenue recognition. In this situation, the PCAOB advises auditors to describe the relevant control-related issues over revenue recognition in the broader context of the CAM without using the term “significant deficiency.”¹⁹

The PCAOB’s instructions to auditors via these examples may be intended to address earlier concerns that CAMs will require the auditor to disclose immaterial and original (confidential) client information, not required to by GAAP or the SEC. The PCAOB received a number of comments on these issues that raised concerns specifically to illegal acts and significant deficiencies in ICFR. But, not every such circumstance can be identified in advance for the PCAOB to decide whether to exclude from being a CAM.

Moreover, a closer look at these three examples: remote loss contingency, immaterial illegal act, and significant deficiency in ICFR, reveals a logical inconsistency in the PCAOB’s application of the definition of CAMs. Such an inconsistency is diametrically opposed to a system of coherent disclosures necessary for investor decision making and efficient capital formation.

GAAP, the SEC and PCAOB rules determine that each of the items need not be disclosed because it is immaterial. Thus, in stating these three items are not CAMs, the PCAOB is actually determining whether or not a matter is a CAM based on the materiality of the matter itself, rather than whether the matter relates to an account or disclosure that is material to the financial statements. In each example, the PCAOB

¹⁸ See the Proposed Standard, page 21.

¹⁹ See the Proposed Standard, page 35.

purports as if there is no related account or disclosure for the auditor to consider when, in reality, each of these three items must be tethered to some account or disclosure.

While we agree that the materiality of the matter itself should be the basis for determining a CAM,²⁰ it is *not* the PCAOB's definition in the Proposed Standard. Importantly, all matters of this nature cannot be enumerated in advance and others will likely arise. Since the PCAOB has established a rubric for resolving them that is logically inconsistent with the definition of CAMs in the Proposed Standard, the PCAOB has sowed another basis for confusion in auditor reporting of CAMs.

The Proposed Standard also lacks any illustrative examples of an auditor's report with CAM disclosures. The lack of any such illustrative examples—whether in Release Text or Rule Text—will only add to uncertainties and confusion for auditors in reporting CAMs.

This situation is exacerbated by the fact that the PCAOB's May 2016 exposure draft (in Rule Text) provided two illustrations of auditor reports that communicated CAMs. The PCAOB deleted these illustrations from the Proposed Standard. The PCAOB explains this deletion by saying that CAMs should be tailored communications of audit-specific information.²¹ But, this explanation does not sufficiently justify the omission of sample audit reports that illustrate the communication of CAMs. It begs the question of what the PCAOB really intends regarding the determination and description of CAMs and reinforces that auditor reporting of CAMs will be a giant experiment.

IV. Litigation Concerns

These issues have consequences that are important to consider. The PCAOB acknowledges that including CAMs will change the auditor's report in ways that could affect auditors' potential liability. Commenters, including CCMC, expressed concern that the requirements for auditor reporting of CAMs will increase litigation risk for both auditors and companies.²² The failure of the Proposed Standard to take steps to mitigate the uncertainties and confusion about CAMs [e.g., through field-testing, by providing logically consistent examples of items that are (or are not) CAMs, and by

²⁰ In addition, we agree that remote loss contingencies, immaterial illegal acts, and significant deficiencies in ICFR should not be CAMs.

²¹ See the Proposed Standard, page 29.

²² See the Proposed Standard, pages 40-44.

illustrating auditor reporting of CAMs in the Proposed Standard] only exacerbates these litigation risks.

We believe that the SEC should not approve the Proposed Standard because of the uncertainties and confusion around CAMs and heightened litigation risk for both auditors and companies. However, if the SEC decides to proceed, we have two recommendations to help reduce the negative consequences:

- **Safe Harbor:** The SEC should provide a safe harbor around auditor reporting of CAMs. The safe harbor should apply to all information disclosed in the auditor's report regarding CAMs, as well as determinations by auditors that information was not required to be disclosed as CAMs. The safe harbor should be enacted before the first effective date for auditor reporting of CAMs. It should also be in place until a post-implementation review has been conducted and the SEC has made a determination on whether to continue auditor reporting of CAMs, in accordance with our subsequent discussion of a sunset provision. We believe that any necessary SEC rulemaking to create a safe harbor be done before the Proposed Standard is implemented.
- **Modified Approach to PCAOB Inspections of CAMs:** The SEC should work with the PCAOB to develop and publicly describe a modified approach to PCAOB inspection of CAMs for a reasonable (and specified) period of years as auditors implement the Proposed Standard. Such a modified approach should focus on identifying best practices and resolving uncertainties and confusion over auditor reporting of CAMs, with the results to be shared broadly—rather than using the inspection process to identify deficiencies in auditor reporting of CAMs, in order to include such deficiencies in individual audit firm inspection reports as Part I or Part II findings. This modified inspection approach would be in the spirit of the coordination that occurred between the SEC and PCAOB more than a decade ago in developing and implementing Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated With An Audit of Financial Statements*.

V. Effective Date

The Proposed Standard provides that all provisions other than those related to CAMs, take effect for audits for fiscal years ending on or after December 15, 2017; and, provisions related to CAMs take effect for audits for fiscal years ending on or after June 30, 2019 (December 15, 2020) for large accelerated filers (for all other

companies to which the requirements apply). We strongly recommend that the SEC postpone each of these effective dates by one-year, or at a minimum six months.

A postponement is necessary for several reasons. First, expecting audit firms around the globe to implement *any* new auditor reporting provisions in 2017 was very aggressive of the PCAOB, considering that the PCAOB Board adopted the Proposed Standard at an open meeting on June 1, 2017. It is even more so given that the PCAOB did not file the Form 19b-4 with the SEC until July 19, 2017 and appropriate time must be allowed for due process, before the SEC can decide on the Proposed Standard. Further, we question the wisdom of implementing a new auditor reporting model, especially auditor communication of CAMs, as companies and auditors are dealing with the initial implementation or the aftermath of implementing significant new GAAP standards, including for revenue, leases, and credit losses.

VI. Sunset Provision

Considering that auditor reporting of CAMs is rife with so many unresolved substantive issues, CCMC recommends that if the SEC approves the Proposed Standard, it does so with a sunset provision. Under a sunset provision, auditor reporting of CAMs would expire after three to five years from the first effective date for large accelerated filers, unless a post-implementation review demonstrates that the Proposed Standard promotes investor protection, capital formation, and competition. This will allow for an evidence-based review to determine if auditor reporting of CAMs is a positive or negative for the capital markets and if the Proposed Standard should remain in place, expire or be modified.

The economic analysis in the Proposed Standard reinforces our recommendation for a sunset provision. It raises a number of issues, but leaves them unresolved for lack of evidence on the economic impacts of auditor reporting of CAMs. The Proposed Standard lacks quantitative analysis and the qualitative discussion is only speculative on the costs and benefits of auditor reporting of CAMs, including how and if investors will use the reported information.

VII. Auditor Tenure

We strongly agree with PCAOB Board member Jeanette Franzel that the PCAOB has not done the analysis to make the case for why disclosure of audit firm tenure is necessary in the auditor's report. We recommend that the SEC not approve this portion of the Proposed Standard.

As Board member Jeanette Franzel stated in voting against the tenure provision, the Proposed Standard “expressly disclaims any relationship between an auditor’s tenure and either audit quality or auditor independence.” Yet, “including this information in the auditor’s report may convey an implication that there is a generalizable relationship between auditor tenure and audit quality and/or auditor independence.”²³ The PCAOB’s rationale for including this information (based on a reduction in search costs for those seeking the information) is very thin—especially considering the information is readily available through public filings and a large number of companies already provide it in annual proxy statements.

Furthermore, tenure would be calculated taking into account audit firm or company mergers, acquisitions, or changes in ownership structure. Under these provisions, a company could make a minor (immaterial) acquisition of a company that has the same audit firm but for a longer period of time. In this situation, the audit firm would be required to compute its tenure for the acquiring firm and extend it to include the beginning of its association with the small acquired company. This is misleading. Further, it may result in companies disclosing a different period of tenure for the audit firm (e.g., in proxy statements) than the auditor in the auditor’s report. Needless to say, this situation will only confuse investors.

VIII. Role of the SEC Investor Advocate

The SEC’s Investor Advocate submitted a comment letter to the PCAOB strongly supporting the May 2016 exposure draft on auditor reporting.²⁴ The comments of the SEC’s Investor Advocate figured prominently in the Proposed Standard, and are used to counter comments of others and justify the Proposed Standard. For example:

- “The SEC’s Investor Advocate said that the Board’s economic analysis made a compelling case as to why the required reporting of critical audit matters would reduce information asymmetries and add to the total mix of information available to investors.”²⁵

²³ See Statement on Adoption of an Auditing Standard on the Auditor’s Report by Jeanette M. Franzel, Board Member (June 1, 2017).

²⁴ See letter dated August 15, 2016 from Rick A. Fleming, SEC Investor Advocate, to the PCAOB on PCAOB Rulemaking Docket Matter No. 034. The letter included the standard disclaimer that the views expressed were solely those of the Investor Advocate and did not necessarily reflect the views of the Commission, the Commissioners, or the staff of the Commission and the Commission disclaims responsibility for the letter and all analyses, findings, and conclusions contained therein.

²⁵ See the Proposed Standard, page 64.

- “Commenting on the reproposal, the SEC’s Investor Advocate noted that investors want to hear directly from the auditor...This commenter agreed with the premise in the reproposal that, because the auditor is required to be independent, information provided by the auditor may be viewed by investors as having greater credibility than information provided by management alone.”²⁶
- “The SEC’s Investor Advocate stated that he ‘strongly support[s] requirements for public disclosure of auditor tenure,’ recognizing that there were different opinions about the best party and location to make that disclosure...[T]he SEC’s Investor Advocate stated that he believed the SEC should ultimately decide these questions. In light of these considerations, the SEC’s Investor Advocate recommended that the PCAOB act to require disclosure of auditor tenure (either in the auditor’s report or in Form AP), but also consider including a contingent sunset clause such that the auditor disclosure requirement would expire if and when the SEC imposed any form of a company disclosure requirement.”²⁷

CCMC finds it very troubling that the SEC Investor Advocate inserted himself into the PCAOB’s due process for the Proposed Standard when any final standard adopted by the PCAOB is subject to approval by the Commission. The SEC’s Investor Advocate does not have the standing of a Presidentially-appointed Commissioner. While he can only speak for himself, we question the wisdom of his comment letter to the PCAOB on the Proposed Standard. The SEC’s Investor Advocate’s voice should not be used to circumvent or undermine the due process for PCAOB standard-setting, nor should it be used by the PCAOB to justify dismissing concerns expressed by others during the PCAOB’s due process; and, it should not be used to undermine the oversight authority of the Commission or the delegated authority of Offices and Divisions within the SEC.

We strongly recommend that the SEC reconsider the role of the SEC Investor Advocate in PCAOB standard-setting and rulemaking.

Conclusion

CCMC is very concerned with the inconsistency of the Proposed Standard, the lack of a sufficient economic analysis and the failure to do any pre-implementation

²⁶ See the Proposed Standard, page. 68.

²⁷ See the Proposed Standard, page 46.

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field testing of the Proposed Standard. As a result, we believe that the approval of this standard will lead to the disclosure of immaterial, confidential and confusing information that will obfuscate disclosures for investors and make capital formation less efficient. Furthermore, liability for businesses and audit firms will increase and create a chilling effect on audit committee and auditor communications.

If the SEC decides to move forward with auditor reporting of CAMs, we recommend that the Commission provide a safe harbor, coordinate with the PCAOB for modified inspections, postpone the effective date of the Proposed Standard, and include a sunset provision for auditor reporting of CAMs.

Thank you for your consideration of these views and we stand ready to discuss these issues with you further

Sincerely,

A handwritten signature in black ink, appearing to read "David Hasenmann". The signature is written in a cursive, slightly slanted style.