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March 24, 2014

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

**SEC Release Nos. 33-9497, 34-71120, 39-2493; File No. S7-11-13**  
***Proposed Rule Amendments for Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act***

Dear Ms. Murphy:

We appreciate the opportunity to respond to the Securities and Exchange Commission's (the "Commission") request for comments about its proposed rule, *Proposed Rule Amendments for Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act* (the "Proposed Rule"). Our comments on the Proposed Rule are limited to the following areas where the auditors' participation in the capital-raising process for smaller companies is specifically impacted by the Proposed Rule's provisions:

- **Audit and Independence Standards.** To balance the costs and benefits of requiring audited financial statements, the Commission should consider allowing additional flexibility with respect to which auditing and independence standards are required. Further, in order to avoid investor confusion, the Commission should consider requiring either (1) auditor involvement in a Tier 2 issuer's interim reporting similar to a Form 10-Q or (2) disclosure that a Tier 2 issuer's interim reporting is not subject to any level of auditor involvement.
- **Financial Reporting under U.S. GAAP.** Issuers of securities under Regulation A would meet the FASB's definition of a public business entity (PBE). Accordingly, to meet the Proposed Rule's requirements, Regulation A issuers that had previously prepared their financial statements in accordance with the FASB's alternative recognition, measurement and disclosure standards for private companies would need to revise their historical financial statements to comply with U.S. GAAP for public companies. This could be confusing and costly for smaller companies. We recommend that the Commission consider the implications of Regulation A issuers being considered PBEs, and either (1) clarify that they are, in fact, PBEs, and provide for an adoption transition period, or (2) work with the FASB to adjust the definition of a PBE.

In the following paragraphs we discuss our observations in these areas in greater detail.

**Audit and Independence Standards**

The Proposed Rule states that:

- **Financial statements for Tier 1** issuers would not be required to be audited. Tier 1 issuers would be required to provide audited financial statements to the extent an audit was obtained for

other purposes and the audits were performed in accordance with either AICPA auditing standards or PCAOB auditing standards and the auditor complied with SEC independence rules.

- **Financial statements for Tier 2** issuers would be required to have their financial statements audited. Auditors of Tier 2 issuer financial statements would be required to comply with PCAOB standards (including PCAOB auditing standards, and PCAOB requirements on auditor ethics, independence and quality control) as well as SEC independence rules.

We have the following suggestions with respect to the Proposed Rule's requirements related to audit and independence standards:

1. For both Tier 1 and Tier 2 financial statements, the Proposed Rule would require the auditor to comply with SEC independence rules. However, there are likely to be scenarios where a potential Regulation A issuer has financial statements available, but the auditor complied with AICPA independence rules and not SEC independence rules. For Tier 1 issuers, such a rule may result in no financial statements being included in Form 1-A, even when there are financial statements available that were audited by an auditor that complied with AICPA independence rules. The Proposed Rule could result in a Tier 2 issuer needing to obtain a new audit of its financial statements by an auditor that can comply with SEC independence rules. We encourage the Commission to consider the implications of requiring Regulation A issuers to be compliant with SEC independence rules and determine whether the cost to Regulation A issuers and to potential investors outweighs the benefits.
2. The Proposed Rule does not require a Regulation A issuer's auditor to be registered with or inspected by the PCAOB, which is appropriate given that a Regulation A issuer is exempt from certain securities laws and is therefore not a "public" company. We also note that audits of Regulation A issuers' financial statements would not be subject to inspection by the PCAOB, which could lead to investor confusion. In cases where the financial statements of Tier 2 issuers were originally audited in accordance with AICPA auditing standards, requiring the audit to now be conducted in accordance with PCAOB auditing standards may be costly. We encourage the Commission to consider whether any benefits from requiring the financial statements of Tier 2 issuers to be audited in accordance with PCAOB standards outweigh the potential costs.
3. We further note there may be a potential conflict in requiring the use of PCAOB standards. Because Regulation A issuers are not "issuers" (as defined by the PCAOB), when the audit is performed in accordance with PCAOB standards, we believe AICPA rules would require the audit to be compliant with both AICPA and PCAOB standards and for the auditor's report to reference both AICPA and PCAOB standards. However, given the relatively recent changes to the auditor's report under AICPA standards, it may not be possible for the auditor to be in compliance with both AICPA and PCAOB standards from a reporting perspective. While this may primarily be an issue that the AICPA needs to address, the Commission may want to consider this potential conflict in determining whether it should require the use of PCAOB standards for Tier 2 offerings.
4. We recommend that if a Tier 1 issuer files unaudited annual financial statements on Form 1-A, the Commission require the issuer to label those financial statements as unaudited in order to eliminate any confusion for investors about the extent of independent accountant involvement.

5. The Proposed Rule requires Tier 2 issuers to file semi-annual unaudited financial statements on Form 1-SA. However, the Proposed Rule does not require the semi-annual unaudited financial statements to be reviewed by an independent accountant and does not require Form 1-SA to specifically disclose that the financial statements have not been subject to a review. Given that interim period financial statements filed by an issuer on Form 10-Q require review by an independent accountant (and the review is not disclosed), the absence of such a disclosure in a Form 1-SA of a Tier 2 issuer could create an expectation gap about the extent of an independent accountant's involvement with the semi-annual unaudited financial statements. We encourage the Commission to either require that the semi-annual unaudited financial statements included in a Form 1-SA of a Tier 2 issuer be reviewed by an independent accountant or require Form 1-SA for a Tier 2 issuer to specifically disclose that the financial statements have not been subject to a review.

### **Financial Reporting under U.S. GAAP**

The FASB, at the request of the Private Company Council, recently issued guidance that includes a new definition for a PBE, which will be used to determine the scope of new accounting standards that provide exceptions or alternatives to U.S. GAAP for private companies.<sup>1</sup> A domestic entity that offers securities under Regulation A meets the definition of a PBE and therefore would not be permitted to prepare its financial statements using private company alternatives. This would require potential Regulation A issuers to revise their historical financial statements prior to an offering if they had previously applied private company alternatives. Or, for Tier 1 issuers, it may mean that available (audited or unaudited) financial statements would not be included in Form 1-A because they were prepared using private company alternatives.

We encourage the Commission to consider the additional costs to be incurred by a Regulation A issuer and potential delays in capital formation while the historical financial statements are being revised, or, in the case of Tier 1 issuers, the omission of otherwise available audited or unaudited financial statements prepared using private company alternatives. If the Commission determines that it is important for potential Regulation A issuers to use public company GAAP, we encourage the Commission to explicitly state that Regulation A issuers meet the definition of a PBE, which would preclude them from preparing their financial statements using private company alternatives, and to provide for a practical manner for Regulation A issuers to transition to public company GAAP other than requiring retrospective revision of the financial statements. If the Commission determines that the costs of complying with PBE accounting standards for Regulation A issuers outweigh the benefits to investors, we encourage the Commission to work with the FASB to revise the definition of a PBE to exclude Regulation A issuers.

We also encourage the Commission to consider allowing Regulation A issuers to apply the effective date provisions for nonpublic companies when adopting new or revised accounting standards issued by the FASB. This would be consistent with the relief offered to emerging growth companies that conduct

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<sup>1</sup> See FASB Accounting Standards Update No. 2013-12, Definition of a Public Business Entity: An Addition to the Master Glossary. The FASB has recently issued standards on accounting for goodwill and interest rate swaps that provide recognition and measurement alternatives for private companies (See FASB Accounting Standards Update No. 2014-02, Accounting for Goodwill, and FASB Accounting Standards Update No. 2014-03, Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps – Simplified Hedge Accounting Approach). The differences in accounting standards for PBEs and private companies are expected to increase.

registered offerings under the JOBS Act in excess of the \$50 million threshold included in the Proposed Rule for Regulation A issuers.

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We appreciate the opportunity to submit our comments on the Proposed Rule. If you have any questions regarding our comments or other information included in this letter, please do not hesitate to contact Glen Davison, (212) 909-5839, [gdavison@kpmg.com](mailto:gdavison@kpmg.com), or Melanie Dolan, (202) 533-4934, [mdolan@kpmg.com](mailto:mdolan@kpmg.com).

Very truly yours,

**KPMG LLP**

cc:

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