CENTER FOR CAPITAL MARKETS COMPETITIVENESS

TOM QUAADMAN
VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
[redacted]

September 8, 2015

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

Re: **Concept Release on Possible Revisions to Audit Committee Disclosures; 17 CFR Part 240; Release Nos. 33-9862, 34-75344; File No. S7-13-15; RIN 3235-AL70**

Dear Mr. Fields:

The U.S. Chamber of Commerce[1] ("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 global economy. To achieve this objective it is an important priority of the CCMC to advance strong corporate governance structures. The CCMC welcomes the opportunity to comment on the concept release issued by the Securities and Exchange Commission ("SEC" or "Commission") on July 1, 2015, in the release entitled Possible Revisions to Audit Committee Disclosures (the "Concept Release").

The CCMC believes that audit committees perform an important role in overseeing the integrity of the financial reporting process and, by extension, protecting investors and facilitating capital formation. The CCMC has written to the SEC, Public Company Accounting Oversight Board ("PCAOB") and Financial Accounting Standards Board ("FASB") with proposals on how to improve financial reporting generally.[2] While we understand a desire to review rules and policies periodically, it should be noted at the outset that audit quality is high and that there

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[1] The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than three million businesses and organizations of every size, sector, and region.

[2] *See* October 9, 2013 letter form the CCMC to SEC Chair White on financial reporting modernization. A copy of the letter is affixed as an attachment.

does not appear to be a crisis in how audit committees discharge their affairs. Moreover, except for a relatively small number of controlled or transitional companies, audit committees are composed entirely of independent directors. By any measure, audit committees are performing at a higher level now than ever before.

At the same time, the PCAOB has significantly expanded the scope of its standard-setting and inspection processes. Indeed, PCAOB Auditing Standard No. 16 on auditor "Communication with Audit Committees" only recently took effect (i.e., for fiscal years beginning on or after December 15, 2012), and audit communications with audit committees will continue to evolve. As discussed below, we believe the costs and unintended consequences of the potential reforms contemplated by the Concept Release far outweigh any discernable benefits. In short, it does not appear that the Concept Release's potential reforms address any pending issues or will provide the benefits needed to promote investor protection, capital formation, or competition.

We outline our concerns in greater detail below.

Discussion

The Chamber believes that some of the reforms required under the Sarbanes-Oxley Act ("SOX") have played an important role in improving both the functioning of audit committees and financial reporting quality. Chief among those reforms is the creation of the PCAOB, which provides comprehensive regulation and oversight of the audit profession, supplementing the Commission's expansive enforcement authority over the industry and reassuring investors that a second independent regulator is ensuring the integrity of the audit process.

1. The Concept Release Seeks the Disclosure of Immaterial Information.

In the eight decades since the securities laws were enacted, public company disclosure requirements have increasingly expanded and become more complex, as evidenced by the voluminous SEC reports public companies are now required to file.[3] This expansion and increased complexity of disclosure has contributed to the phenomenon of "disclosure overload", whereby investors are so inundated with information it becomes difficult for them to determine the most salient factors they need to make informed voting and investment decisions. Retail investors are particularly vulnerable, as they often do not have the resources to help them make sense of the detailed SEC filings of the companies they invest in. In fact, we believe the disclosure overload phenomenon is the leading contributor to why retail shareholder participation has dropped to levels as low as five percent at some annual shareholder meetings. In a very real way, information overload has led to the disenfranchisement of retail shareholders at many public companies.[4]

The Chamber has welcomed the efforts by Chair White and Corporation Finance Director Higgins to start a Disclosure Effectiveness project to address these long-outstanding issues. In 2014, the Chamber released a report discussing these issues and outlining some steps the Commission should take to improve disclosure.[5] However, we are concerned that the Concept Release conflicts with the apparent objectives of the Disclosure Effectiveness project.

The CCMC has long believed that the lodestar for SEC disclosure should be whether an incremental piece of information satisfies the traditional test of materiality set forth by the Supreme Court in the seminal case of *TSC Industries Inc. v. Northway Inc.*[6] There, Justice Thurgood Marshall, writing for the Court, explained "[M]anagement's fear of exposing itself to substantial liability may cause it simply to bury the shareholders in an avalanche of trivial information—a result that is hardly

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[3] For example, a 2012 report by Ernst & Young estimated that the average number of pages in annual reports devoted to footnotes and Management's Discussion and Analysis ("MD&A") has quadrupled over the last 20 years. Should this trend continue, companies would be devoting roughly 500 pages to MD&A by the year 2032. The Ernst & Young report can be found at: http://www.ey.com/Publication/vwLUAssets/ToThePoint_BB2367_DisclosureOverload_21June2012/$FILE/ToThePoint_BB2367_DisclosureOverload_21June2012.pdf

[4] Retail shareholders aren't alone. A recent study by Professor David Larcker of Stanford University found that 55% of institutional investors surveyed felt the typical public company proxy statement was too long and 48% believe the typical proxy statement is too difficult to read and understand. The investors surveyed had a total of $17 trillion under management. The study can be found at: http://www.gsb.stanford.edu/faculty-research/publications/2015-investor-survey-deconstructing-proxy-statements-what-matters.

[5] The study on Corporate Disclosure Effectiveness can be found at: http://www.centerforcapitalmarkets.com/wp-content/uploads/2014/07/CCMC_Disclosure_Reform_Final_7-28-20141.pdf.

[6] 426 U.S. 438 (1976).

conducive to informed decision making."[7] Marshall was concerned about information overload harming investors and therefore set a more demanding test of materiality. A fact is material, the Court held, if "there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote."[8]

The information sought to be disclosed by the Concept Release does not meet this high standard. Many of the proposed disclosures delve into minutiae and would require discussion of a litany of trivial and immaterial information. In addition, many of the disclosures described in the Concept Release are qualitative and call for open-ended narrative that would likely be lengthy and dense, exacerbate disclosure overload, and over time devolve to boilerplate. Information of this type certainly does not meet the Supreme Court's standard for materiality—whether for making investment decisions, making voting decisions, or determining whether to ratify the appointment of the audit firm.

Additionally, as will be explained in further detail below, we believe that the Concept Release will fail to provide investors with decision-useful information to understand the companies in which they invest. The Concept Release would, we believe, layer even more complex disclosures into the proxy statement and other SEC reports, making it even more difficult for investors to decipher and understand the surrounding information in those disclosure documents.

2. The Concept Release Does Not Call for Information That Is Decision-Useful to Investors.

The Concept Release requests comments on a large number of disclosures related to the audit committee's responsibilities with respect to appointment, compensation, retention, and oversight of the audit firm and how the audit committee discharges those responsibilities. Most of these specific disclosures are qualitative and many would involve disclosing inconsequential details on inputs and processes to describe how the audit committee carried out its responsibilities, the information considered and judgments made by the audit committee, and the nature of the

[7] *Id.* at 448-49.
[8] *Id.* at 449.

information discussed with the external auditor. We do not believe that this sort of immaterial information is decision-useful to investors.[9]

SOX reaffirmed the audit committee's responsibility for oversight of the external audit, created the PCAOB to regulate the accounting firms and individuals that audit public companies, and assigned the SEC oversight of the PCAOB. The Concept Release fails to appreciate that there is no need for mandating audit committee disclosures of the type described in the Concept Release because investors trust the processes and structures created by the SOX on their behalf. Moreover, mandating the disclosures described in the Concept Release will never put investors "in the shoes" of audit committees. Nonetheless, such disclosures may result in investors and others unnecessarily second-guessing audit committee decisions based on partial and incomplete information, which could in turn undermine trust in audit committees and governance processes.

Further, the SEC should avoid compelling a laundry list of audit committee disclosures that applies to all companies regardless of their individual facts and circumstances. In this regard, the Concept Release discusses divergence in current audit committee reporting practices and implies that this is a problem. However, the Concept Release fails to appreciate that this divergence largely reflects that many boards are already responsive to the needs of investors on this topic and that private ordering is important to maintain.

The CCMC has long eschewed one-size-fits-all disclosure. Voluntary disclosure has the benefit of being flexible to accommodate each company's facts and circumstances and permit tailoring of disclosures to the unique needs of a company's investor base. In addition, voluntary disclosure appreciates that governance processes and audit committee practices continue to evolve. Voluntary disclosure avoids the problem that mandated requirements can become impediments to the evolution of audit committee processes and practices and thereby chill innovation.

Additionally, mandating any of the detailed disclosures described in the Concept Release (in particular, those related to matters discussed with external or

[9] As the Concept Release wisely notes, companies are already required to make robust disclosures about audit committees and the auditor selection process. See, for example, Item 407 of Regulation S-K and Item 9 of Schedule 14A.

internal auditors) will chill open and frank communications among management, audit committees, and external auditors. Furthermore, disclosure by an audit committee of matters such as the external auditor's strategy and plan could reveal proprietary information about the company or the auditor's methodology.

Certain of the disclosures listed in the Concept Release appear intended to change the behavior of audit committees, despite the lack of demonstration of any problem or crisis. Rather it appears that some of the positions presented reflect the agendas of selected special interest groups. Two disclosures—audit firm tenure and the name of the engagement partner—have already been proposed by the PCAOB for disclosure by audit firms.[10] The CCMC has commented at length on the PCAOB proposals, which we have included as attachments to this letter.[11] In short, we do not support disclosing either the identity of the audit partner(s) or audit firm tenure.

The CCMC's comment letters to the PCAOB also highlight many of our concerns with the Concept Release. For example, on partner naming the CCMC noted that:

> …there is a marked failure to show how this change in disclosure will benefit investors and the arguments in support of the Proposal, including those related to audit quality, are superficial…The Proposal does not articulate the problem that will be resolved through the adoption of the Proposal, or how the Proposal is the best option to

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[10] To the extent the PCAOB advances these initiatives any further, we see no need for duplicative or redundant disclosure in SEC documents.

[11] On disclosing the name of the engagement partner, *see* CCMC letter dated Aug. 31, 2015 on PCAOB Supplemental Request for Comment on *Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form* (PCAOB Release No. 2015-004, June 30, 2015; PCAOB Rulemaking Docket Matter No. 029); CCMC letter dated March 10, 2014 on PCAOB Exposure Draft on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor's Report of Certain Participants in the Audit* (PCAOB Release No. 2013-009, Dec. 4, 2013; PCAOB Rulemaking Docket Matter No. 029); and CCMC letter dated January 9, 2012 on Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, Oct. 11, 2011; PCAOB Rulemaking Docket Matter no. 029). On disclosing audit firm tenure, *see* CCMC letter dated Dec. 9, 2013 on 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 in PCAOB Standards* (PCAOB Release No. 2013-005, Aug. 13, 2013; PCAOB Rulemaking Docket Matter No. 034) and CCMC letter dated Oct. 20, 2011 on PCAOB *Concept Release on Auditor Independence and Audit Firm Rotation and Notice of Roundtable* (PCAOB Release No. 2011-006, Aug. 16, 2011; PCAOB Rulemaking Docket Matter No. 37).

> solve the undefined problem. Moreover, the Proposal fails to show how investor needs will be enhanced through the naming of the engagement partner.[12]

Likewise, the CCMC observed:

> Naming the engagement partner does not enable investors or other third-parties to even begin to approach "stepping into the shoes" of the PCAOB or audit committee. Indeed, third-parties may instead get an incorrect view of the role of the engagement partner related to audit quality based on the information available from the name of the engagement partner. Investors are better served by relying on the regulatory and governance processes rather than trying to second guess these processes based on a disclosure of the name of the engagement partner.[13]

And, on disclosing audit firm tenure and the need for evidence that the disclosure involves material information:

> By including tenure information in the auditor's report, the Proposal implies some systematic connection between audit quality and tenure. However, as explained in the Proposal and emphasized by one Board member, the PCAOB 'has not reached a conclusion regarding the relationship between audit quality and auditor tenure and the Board's inspection process has not been designed to determine a relationship between audit quality and audit tenure.' Thus, the PCAOB does not have 'any data indicating that audit tenure has any correlation with audit quality.' Yet, 'the mere fact that the Board requires a disclosure about audit tenure, however, might suggest that the Board believes the information to be meaningful.' By that token, as an example, anecdotal musings, by the SEC, of ethical lapses by attorney would not pass muster for regulatory action requiring disclosure of law firm tenure by companies.[14]

[12] CCMC letter to the PCAOB dated Mar. 10, 2014, at 3.
[13] Id. at 4.
[14] CCMC letter to PCAOB dated Dec. 9, 2013, at 12-13

Moreover, we have also expressed our concern that:

> The PCAOB does not provide any evidence from its own activities, including from its inspection process, that audit firm tenure is an issue. Indeed, the PCAOB admits that it has no evidence from its inspection process that audit firm tenure has any systematic relationship with inspection deficiencies.[15]

We also believe the Concept Release's focus with disclosure developments outside the United States is misguided. Different legal systems and liability regimes outside the US limit the comparability of foreign reporting systems. Indeed, the adoption and pending implementation of the Europe Union's ("E.U.") audit firm rotation policies should give pause. The member state interpretation of these policies is expected to differ wildly hampering the ability of the E.U. to form an integrated capital market. Financial reports are integral to capital formation and the U.S. framework is the gold standard that has served businesses and investors well. Accordingly, we do not believe that events outside the U.S. should influence SEC audit committee reporting requirements.

3. The Concept Release Would Significantly Increase Litigation Risks and Attendant Costs.

The CCMC is concerned that the proposed additional disclosures, if adopted, will exacerbate an already overly-litigious environment in the financial reporting world. In particular, the contemplated disclosures will increase litigation risks to issuers, audit committee members, and auditors while providing little useful information to investors. These same investors will ultimately bear the costs of any new litigation.

It is axiomatic that issuer litigation risks increase with greater disclosure requirements. This is particularly true where disclosures are qualitative and open-ended such as, for example, the proposed disclosure, in narrative form, of (i) an audit committee's consideration of matters discussed with the auditor, and (ii) how the committee assesses, promotes, and reinforces the auditor's objectivity and

[15] CCMC letter to PCAOB dated Oct. 20, 2011.

professional skepticism. This proposed audit committee discussion and analysis, which would undoubtedly fill multiple pages of text, would create new opportunities for potential litigants to second guess or nitpick an issuer's already voluminous disclosures.

The proposed additional disclosures also increase audit committee member litigation risks. For example, disclosure about the number of consultations between the audit committee and the external auditor could lead, on the one hand, to an assumption that an audit committee is doing so too infrequently when compared to its peer group. On the other hand, if the number of consultations is high relative to the peer group, investors may incorrectly assume that an accounting problem is brewing. Further, disclosing the audit committee's detailed discussions with the external auditor about audit strategies and plans will create new opportunities for potential plaintiffs to second-guess audit work.

The contemplated disclosures would also become de facto regulation of audit committee activities and the specific ways in which audit committees carry out their general oversight responsibilities. For example, the proposed disclosure of an audit committee's discussions regarding the auditor's most recent PCAOB inspection report will become a de facto audit committee duty to discuss the inspection report, rather than just a good practice. Similarly, the proposed disclosure of an audit committee's consideration of key members of the audit engagement team (in addition to the engagement partner) will transform into a new duty to consider those individuals. Potential litigants may claim audit committees breached fiduciary duties for failure to undertake these new "duties" stemming from the new disclosure requirements. It is already difficult to recruit and retain qualified audit committee members; adding a list of new specific duties (masquerading as disclosure requirements) for potential litigants to seize upon will not help.

Finally, the proposed disclosures will have the unintended consequence of needlessly increasing litigation risks to auditors. Auditors are not currently required to disclose publicly details relating to their audit plans and strategies, or identification of significant risks. The proposed audit committee disclosures contemplate that audit committees would disclose the nature of communications with auditors on these topics. Similarly, an audit committee's narrative disclosure regarding its oversight of the auditor and assessment and promotion of the auditor's objectivity and skepticism, would likely include details about the auditor that are not currently subject to disclosure requirements. Here again, potential litigants could use the contents of these new disclosures to second guess the work of auditors. And, as rationale economic actors, audit firms will simply pass related compliance and litigation costs on to their clients, with investors ultimately suffering the consequences.

At bottom, the CCMC continues to strongly believe that a "liability-neutral" threshold represents a minimum level for proceeding with any initiative that has the potential to expand litigation risks to issuers, their boards and their outside auditors. We urge the Commission to recognize that anything other than liability neutral standards will ultimately harm investors. Such a precondition should also be a central part of any economic analysis. Economic analysis should be used to determine if a proposed standard or revision to a standard is liability neutral and, if not, what the costs to investors, issuers and auditors will be.

4. The Proposed Disclosures Would be Burdensome on Smaller Reporting Companies and Emerging Growth Companies.

As the prolonged experience implementing SOX Section 404 bears out, the requirements of the Concept Release would prove to be disproportionately burdensome and costly for smaller reporting companies and emerging growth companies. With their limited resources, neither smaller reporting companies nor emerging growth companies (together with their board members and outside auditors) should be required to face new incremental litigation risks. Like any other rulemaking, we urge the Commission to consider the unique reporting challenges faced by these categories of issuers as it weighs future action.

5. The Government Should Collaborate With the Private Sector on Improving Businesses' Cybersecurity

While not addressed by the concept release, it has become the practice of some companies to include cybersecurity within the purview of the audit committee. The Chamber wants to add these comments within the record and hopes to engage with the SEC to create a dialogue on cybersecurity issues of importance to both businesses and investors. More importantly, we believe that it is imperative for the SEC to coordinate with other governmental agencies to address these issues. Clear rules of the road and responsibilities for all stakeholders are needed, and enforcement should not be the means of creating ad-hoc policies.

The Chamber is aware that some policymakers have been pressuring the SEC to leverage securities law and policy to compel businesses to report cyber risk and incident data with increasing specificity. According to news accounts, the Commission is actively investigating companies about their cybersecurity reporting practices and is considering filing sanctions against some companies, which is troubling to many in industry on a number of fronts.

First, federal securities law and policy already require registrants to disclose material cyber risks and incidents. Indeed, compelled disclosure that is injurious to a business may not pass judicial muster.[16] The Chamber is concerned about efforts to expand the commission's role in deciding what a public company must report and, apparently, what cybersecurity practices they must use.

Instead of forcing companies to disclose cyber incidents, the Chamber believes that passing information-sharing legislation, such as S. 754, the Cybersecurity Information Sharing Act of 2015 ("CISA"), with safeguards for businesses needs urgent attention by lawmakers and the administration. We are advocating for businesses to disclose cyber incidents and threat data through a protected information-sharing program.

Second, in addition, layering on regulations would disrupt or damage trusted relationships between business and government needed to counter advanced and persistent attacks, which tend to originate overseas. Chamber members have constructive partnerships with federal agencies and departments—including Defense, DHS (the Secret Service), Energy, the FBI, and Treasury—to help companies manage cybersecurity incidents. We do not want these partnerships harmed because of new SEC reporting rules. Similarly, companies that contract with the government would face confusion when deciding how and when to report cyber information given the

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[16] *See National Association of Manufacturers, U.S. Chamber of Commerce, and the Business Roundtable v. Securities and Exchange Commission*, 748 F.3d 359 (D.C. Cir. 2014).

multiple and often conflicting guidance and rules, which the Office of Management and Budget is currently wrestling.[17]

As we noted in similar comments last October to the SEC, the Chamber believes that going beyond the SEC's 2011 guidance on cybersecurity[18]could paint a target on registrants' backs—including industry peers and supply chain partners—for no appreciable benefit to investors. Moreover, it is not clear that investors have asked for more disclosure from businesses regarding cybersecurity.[19] It is constructive that the SEC guidance recognizes that highly detailed disclosures could compromise a company's cybersecurity efforts by providing a road map for malicious actors that would seek to infiltrate a registrant's information networks. The Commission appreciates that disclosures of this nature are not required under federal securities law.

Third, it is important to call out that the Chamber favors constructive approaches to cybersecurity that reward creativity, speed, and innovation. Businesses need relatively minimal structure—such as the positive *Framework for Improving Critical Infrastructure Cybersecurity* (the "framework")—and maximum autonomy to counter, in partnership with government, rapidly changing cyber threats.

The business community takes cyber threats incredibly seriously, and the Chamber has witnessed significant support for risk-management tools like the framework. We enthusiastically promote businesses of all sizes—from big corporations to small startups—to treat cybersecurity as an enterprise risk rather than an IT risk. Corporate boards are increasingly putting cybersecurity on their agendas, viewing cyber risk and threats as strategic and enterprise risk management priorities, which our organization strongly encourages.[20]

In 2014, the Chamber launched its national cybersecurity campaign, *Improving Today. Protecting Tomorrow*™, which recommends that businesses adopt fundamental Internet security practices. We have organized roundtable events in several major U.S. cities, including Chicago, Austin, Seattle, Phoenix, and Atlanta. The Chamber is

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[17] www.nextgov.com/cybersecurity/cybersecurity-report/2011/10/sec-guidelines-good-intentions-fall-short/54930; https://policy.cio.gov
[18] www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm.
[19] *See* June 6, 2011, letter to the Senate from the SEC, which states that investors are not asking for more disclosure in the area of cybersecurity.
[20] *See*, for example, www.sec.gov/comments/4-673/4673-3.pdf, www.nacdonline.org/Cyber, and www.pwc.com/us/en/increasing-it-effectiveness/publications/us-cybercrime-survey-2015.jhtml.

hosting additional roundtables this fall in Minneapolis and Las Vegas as well as holding our Fourth Annual Cybersecurity Summit on October 6 in Washington, D.C.

Accordingly, the Chamber has respectfully requests the administration and the independent agencies to collaborate—rather than flex their regulatory authority—with the private sector on improving businesses' cybersecurity and resilience.

Conclusion

In closing, we reiterate that audit committees are functioning today at the highest level in history. By and large, audit committees are composed entirely of independent directors. And audit committee members—like all directors—have fiduciary duties of care and loyalty to their companies and their shareholders. But after reading the Concept Release, a casual observer could easily be left with the erroneous impression that there is widespread dereliction of duty on the part of audit committees and that misconduct abounds.

While we do believe that it is prudent to review rules from time to time, we believe that the quality of audit committees and the audit itself is at a high point. Absent a showing to the contrary, it would appear that a radical overhaul is not needed at this time. Rather, we would hope that the SEC look at emerging tools such as data analytics to better understand how boards and investors can better disseminate and receive information to make investment and capital formation decisions. Tweaking the existing systems to create another lengthy set of immaterial mandated disclosures will do nothing to enhance audit committee performance, but will accelerate a check-the-box compliance mindset. We respectfully urge the Commission to let boards of directors and their audit committees continue their important work in the manner most effective to fulfill their fiduciary duty.

Thank you for considering our views on the Concept Release. We would be pleased to discuss them further with the staff and Commissioners.

Sincerely,

Tom Quaadman

Cc: The Honorable Mary Jo White
The Honorable Luis A. Aguilar
The Honorable Daniel M. Gallagher
The Honorable Kara M. Stein
The Honorable Michael S. Piwowar

ATTACHMENTS

CENTER FOR CAPITAL MARKETS COMPETITIVENESS

TOM QUAADMAN
VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
(202) 463-5540
tquaadman@uschamber.com

October 9, 2013

The Honorable Mary Jo White
Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chair White:

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. To achieve these goals, the CCMC has supported the development of robust financial reporting systems and strong internal controls to promote efficient capital markets and capital formation.

We have read with interest recent reports that the Securities and Exchange Commission ("SEC") will step up its enforcement efforts, particularly focusing on potential accounting fraud and financial disclosure irregularities. The CCMC applauds the efforts of SEC to drive bad actors from the market place and create a level playing field for participants who operate in good faith and abide by the law. As SEC uses accounting fraud and financial reporting irregularities as a means to achieve this goal, we also believe that it is incumbent for SEC to modernize financial reporting policies to facilitate the release of relevant disclosures, reduce complexity, and achieve more efficient capital formation and competition. Accordingly, we would also respectfully request an update on the status of SEC's implementation of the recommendations of the Advisory Committee on Improvements to Financial Reporting ("CIFiR").

Modernization of financial reporting policies is well overdue.

In the wake of the Enron and WorldCom scandals and the subsequent passage of the Sarbanes-Oxley Act ("SOX"), financial reporting has undergone significant changes and transitions. Policy makers realized that financial reporting must keep pace with those changes. Consequently, then SEC Chairman Chris Cox formed CIFiR, which released its report and recommendations to improve financial reporting in August 2008. Unfortunately, the demands of the financial crisis diverted the time and attention of the agency from its ongoing agenda of modernizing financial reporting. We believe that the implementation of these recommendations remains an urgent item on SEC's agenda.

Adding to the urgency of these recommendations is the pace of change in financial reporting that has taken place since the financial crisis. Among the many new legislative, regulatory, and standard-setting requirements that have influenced financial reporting in the last few years is the Jumpstart Our Business Startups Act ("JOBS Act"). This law exempts emerging growth companies ("EGCs") from new rules of the Public Company Accounting Oversight Board ("PCAOB"), unless SEC determines that those rules are necessary and in the public interest[1], and allows EGCs to comply with any new or revised Financial Accounting Standards Board ("FASB") standards in the same timeframe as companies that are not issuers. Similarly, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") has profoundly impacted and exacerbated many of the issues identified in the CIFiR report.

For these reasons, it is important for SEC to adopt a comprehensive approach to modernizing financial reporting policies that includes, in addition to stepped-up enforcement, increased communication and cooperation among regulators, standard setters and stakeholders. This will reinforce SEC's efforts to drive bad actors out of the marketplace, by eliminating the complexity and ambiguity on which they thrive. In fact, the CIFiR report found that financial reporting complexity is a key driver in the disconnection between current financial reporting and the information necessary to make sound investment decisions. Since keeping a clear focus on SEC's mission to ensure that investors receive relevant decision-useful information and to promote capital formation will maximize the agency's chances of success in stamping out accounting fraud and financial disclosure irregularities, we view this as a win-win for SEC and its stakeholders.

Listed below are some of the issues and suggested solutions to improve financial reporting.

Issues and Proposed Solutions

Issue 1: Provide Investors with Information Needed for Sound Decision Making

Problem: Inconsistent definitions of materiality.

Solution: The SEC should supplement existing guidance and coordinate in such a way to ensure that SEC, FASB and PCAOB use a common definition of materiality.

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[1] *See* letter from the Chamber to the SEC (October 5, 2012) that Section 104 of the JOBS Act requires an analysis and finding that new PCAOB standards and revisions must promote efficiency, competition and capital formation in order to apply to EGCs.

Background: FASB has defined materiality for U.S. Generally Accepted Accounting Principles ("U.S. GAAP") differently than the securities laws, while the PCAOB is using the definition from the federal securities laws.

PCAOB Auditing Standard No. 11 states in part:

> *In interpreting the federal securities laws, the Supreme Court of the United States has held that a fact is material if there is 'a substantial likelihood that the … fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available.' As the Supreme Court has noted, determinations of materiality require 'delicate assessments' of the inferences a 'reasonable shareholder' would draw from a given set of facts and the significance of those inferences to him …*

FASB Concept Statement No. 8 uses the following definition: "Information is material if omitting it or misstating it *could* influence decisions that users make on the basis of the financial information of a specific reporting entity."[2]

Additionally, FASB's Invitation to Comment on Disclosure Framework (File Reference 2012-220), states that reporting entities would assess the relevance of each disclosure using the basic criterion that "information should be disclosed if it has the potential to make a difference in users' decisions about providing resources to the reporting entity."[3] [4]

CIFiR recommended that the FASB or SEC, as appropriate, should supplement existing guidance to reinforce that:

> *Those who evaluate the materiality of an error should make the decision based upon the perspective of a reasonable investor; and, materiality should be judged based* on *how an error affects the total mix of information available to a reasonable investor, including through a consideration of qualitative and quantitative factors*.[5]

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[2] Par. QC11, Chapter 3
[3] FASB Invitation to Comment on Disclosure Framework, paragraph 4.5 (page 45).
[4] For additional insights on the issues, see "What is Materiality? SEC & PCAOB v. FASB & ASB" by Samuel P. Gunther in *Bloomberg BNA* (May 7, 2012).
[5] Recommendation 3.1, page 80, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

It should also be noted that the International Integrated Reporting Council ("IIRC") and the Sustainability Accounting Standards Board ("SASB") are creating their own concepts of materiality in attempting to develop voluntary standards of non-financial reporting and disclosure – with the SASB's disclosures intended to be included within Management Discussion and Analysis ("MD&A") in Form 10-K and 10-Q filings with SEC. The Chamber has written to both organizations expressing concerns that the development of these standards needs to be done with SEC and that any work in this area must conform to the definitions, usage, and enforcement of materiality as defined in the Securities Acts and their progeny.[6] Similarly, in testimony before the U.S. Senate Subcommittee on Securities, Insurance, and Investment the Chamber stated:

> *The SEC, FASB, and PCAOB should develop standards of materiality for investors, as well as the scope of outreach to the investor community. This will provide perspective on various accounting and auditing issues such as the need for restatements on the one end, while framing the picture for input on the front end of standard setting.*[7]

<u>Problem</u>: Information overload from multiple overlapping and sometimes contradictory reporting and disclosure requirements and standards.

<u>Solution:</u> Develop a Disclosure Framework.

<u>Background:</u> CIFiR recommended that SEC and FASB work together to develop a disclosure framework to, among other things:

> *Integrate existing SEC and FASB disclosure requirements into a cohesive whole to ensure meaningful communication and logical presentation of disclosures, based on consistent objectives and principles. This would eliminate redundancies and provide a single source of disclosure guidance across all financial reporting standards.*[8]

A disclosure framework would also address issues of placement of information within audited U.S. GAAP financial statements versus MD&A which is unaudited, has safe harbors and provides forward looking information.[9]

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[6] *See* letters from the Chamber to IIRC (July 15, 2013) and SASB (July 26, 2013).

[7] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance and Investment (April 6, 2011).

[8] Recommendation 1.2, page 8, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

[9] FASB currently has a disclosure framework project in progress and the SEC Chief Accountant announced in February, 2013 that a SEC Staff Paper on disclosure is expected to be released with roundtables planned to follow.

__Problem:__ The accounting standards setters continue down the path of including the recognition, measurement, and disclosure of more fair values and accounting estimates that require judgment and, therefore, investors and others cannot expect there to be a single "right answer" in accounting and auditing matters.

__Solution:__ Issue a policy statement articulating how SEC evaluates the reasonableness of accounting judgments.

__Background:__ CIFiR recommended that:

> *The SEC issue a statement of policy articulating how it evaluates the reasonableness of accounting judgments and include factors that it considers when making this evaluation. The statement of policy applicable to accounting-related judgments should address the choice and application of accounting principles, as well as estimates and evidence related to the application of an accounting principle. … We believe that it would be useful if the SEC also set forth in the statement of policy factors that it looks to when evaluating the reasonableness of preparers' accounting judgments.*[10]

__Solution__: The PCAOB should issue a policy statement on how it evaluates the reasonableness of audit judgments.[11]

__Background:__ CIFiR recommended that:

> *[T]he PCAOB develop and articulate guidance related to how the PCAOB, including its inspections and enforcement divisions, would evaluate the reasonableness of judgments made based on PCAOB auditing standards. The PCAOB's statement of policy should acknowledge that the PCAOB would look to SEC's statement of policy to the extent that the PCAOB would be evaluating the appropriateness of accounting judgments as part of an auditor's compliance with PCAOB auditing standards.*[12]

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[10] Recommendation 3.5, pages 13-14, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

[11] *See* various CCMC comment letters including to the PCAOB on Request for Public Comment on Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards and Notice of Roundtable (PCAOB Release No. 2011-003, June 21, 2011, Rulemaking Docket Matter No. 34).

[12] Recommendation 3.5, page 14, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

<u>Solution</u>: The SEC work with the FASB and PCAOB to consider the auditability of GAAP when developing accounting standards and disclosure requirements.

<u>Background</u>: Again in testimony before the U.S. Senate Subcommittee on Securities, Insurance, and Investment the Chamber stated:

> *A formal, ongoing, and transparent dialogue should be created to consider the auditability of accounting standards. This would allow for the auditing of accounting standards to work in conjunction with standard development. It would also provide for the identification and resolution of issues that arise in practice. A similar process should be created to ensure that regulators have an understanding of standards and that different entities are not working at cross purposes. The era of "not my problem" needs to end.*[13]

<u>Solution</u>: Conduct formal pre and post-implementation reviews.

<u>Background</u>: CIFiR recommended that the Financial Accounting Foundation ("FAF"), FASB, and other participants in the financial reporting system:

> *Enhance the consistency and transparency of key aspects of FASB's field work, including cost-benefit analyses, field visits, and field tests.*
>
> *Formalize post-adoption reviews of each significant new standard to address interpretive questions and reduce the diversity of practice in applying the standard, if needed.*
>
> *Formalize periodic assessments of existing accounting and related disclosure standards to keep them current.* [14]

The Chamber reinforced this notion by stating that standards should be field tested and put through a rigorous process to identify unintended consequences before implementation and after implementation.[15]

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[13] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance and Investment (April 6, 2011).

[14] Included in recommendation 2.3, page 11, Final Report of the SEC Advisory Committee on Improvements to Financial Reporting, August 1, 2008.

[15] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance, and Investment (April 6, 2011).

The Chamber appreciates that the FAF and FASB are moving in the direction of this recommendation and we suggest that the PCAOB should do likewise and that SEC should ensure that the FASB and PCAOB are coordinated in these efforts.

Issue 2: Increase Communication and Coordination amongst Regulator and Standard Setters

Problem: **Lack of transparent communication and coordination among regulators, standard setters and market participants.**

Solution: **Establish a Financial Reporting Forum ("FRF").**

Background: CIFiR recommended the creation of a FRF, made up of the SEC, FASB, PCAOB, financial regulators, investors (broadly defined), and businesses, with a mission to identify and propose solutions to problems before they reach the crisis stage. A FRF will also provide a mechanism to allow for appropriate coordination amongst regulators and input from investors and businesses.[16] It should also be noted that in the 111th Congress, the House of Representatives passed a version of H.R. 4173, the precursor bill of the Dodd-Frank Act, which contained an amendment by Rep. Gary Miller to create an FRF.

Problem: **Potential expectation gap created by the PCAOB's recent definition of an audit failure.**

Solution: **Through the exercise of SEC's oversight authority over the PCAOB reestablish the long-standing definition of an audit failure.**

Background: Several years ago and without explanation, the PCAOB began describing Part I deficiencies as audit failures in inspection reports for annually inspected firms (although the PCAOB does not use these terms in inspection reports for tri-annually inspected firms). This change in definition contradicted the long-standing and widely used definition of an audit failure as used by the Government Accountability Office ("GAO"). GAO defined audit failures as:

> *[A]udits for which audited financial statements filed with the SEC contained material misstatements whether due to errors or fraud, and reasonable third parties with knowledge of the relevant facts and circumstances would have concluded that the audit was not conducted in accordance with generally accepted auditing standards, and, therefore, the auditor failed to appropriately detect and/or deal with known material misstatements by (1) ensuring that*

[16] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance, and Investment (April 6, 2011).

> *appropriate adjustments, related disclosures, and other changes were made to the financial statements to prevent them from being materially misstated, (2) modifying the auditor's opinion on the financial statements if appropriate adjustments and other changes were not made, or (3) if warranted, resigning as the public company's auditor of record and reporting the reason for the resignation to the SEC.*[17]

In other words, for example, differences of opinion in the exercise of judgment on audit procedures or other audit deficiencies – which do not occur in conjunction with any material misstatement of the financial statements – could not be considered an audit failure.

You will also find with this letter, as an attachment, a letter sent by the Chamber to PCAOB Chairman James Doty that contains a more robust discussion of our concerns on the failure to properly define audit failure, the communication, and portrayal of inspections findings and how it may undermine public confidence in financial reporting.

Issue 3: Reduce Fraudulent Financial Reporting

Problem: Lack of a comprehensive and holistic approach to understanding fraudulent financial reporting, diagnosing its root causes and detecting fraud through the application of useful and appropriate methodologies and technologies.

Solution: Establish a Fraud Center.

Background: The Advisory Committee on the Audit Profession ("ACAP") recommended:

> *SEC and Congress, as appropriate, provide for the creation by the PCAOB of a national center to facilitate auditing firms' and other market participants' sharing of fraud prevention and detection methodologies and technologies, and commission research and other fact-finding regarding fraud prevention and detection, and further, the development of best practices regarding fraud prevention and detection.*[18]

Financial reporting frauds undermine investor confidence in the capital markets. In October 2010, the Center for Audit Quality (CAQ) formally joined forces to form an Anti-Fraud Collaboration with Financial Executives International, The Institute of Internal Auditors, and the

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[17] *See* GAO 04-217 Public Accounting Firms Required Study on the Potential Effects of Mandatory Audit Firm Rotation (2003) page 6.
[18] ACAP Final Report (October 6, 2008), page VII:1

National Association of Corporate Directors to develop thought leadership, awareness programs, educational opportunities, and other related resources specifically targeted to the unique roles and responsibilities of the primary participants in the financial reporting supply chain. The projects and activities under this Anti-Fraud Collaboration are designed to enhance awareness and understanding of factors that contribute to financial reporting fraud, as well as strengthen the abilities of all applicable parties' efforts to deter and/or detect financial reporting fraud. These types of private sector initiatives can lead to long term progress in combating threats to investor confidence in the U.S. capital markets.

Since fraud can never be completely prevented, efforts to combat fraud must be continuous. All key participants in the financial reporting supply chain – preparers, audit committee members, auditors, *and regulators* – have important roles to play with regard to deterring and detecting financial reporting fraud. We believe the PCAOB can and should do more with the information it has accumulated through its various programs to identify trends, best practices, and specific actions that could be shared with auditors and preparers to assist in the deterrence or detection of financial statement fraud.

Issue 4: Increase Transparency and Accountability of FASB and PCAOB

Problem: Neither the FASB nor the PCAOB are formally subject to the traditional regulatory provisions for accountability and transparency.

Solution: Both the FASB and PCAOB and their attendant advisory groups should abide by the same rules of procedures as required of regulatory agencies by the Administrative Procedures Act and Federal Advisory Committee Act, including any advisory groups should be balanced in presentation and open in process.[19]

Solution: The PCAOB should form a Business Advisory Group to understand the role of companies as investors, their use of investments, and the potential impact of standard setting on businesses. The PCAOB should also establish an Audit Advisory Group to more substantively bring the expertise of practicing auditors to inform the PCAOB's activities and initiatives.[20]

Background: For example, a Business Advisory Group would provide the PCAOB another means of input and broader understanding of issues that need to be addressed in the development of standards and other means of resolving important issues related to audited

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[19] *See* testimony of the U.S. Chamber of Commerce on The Role of the Accounting and Auditing Profession in Preventing Another Financial Crisis at the hearings of the U.S. Senate Subcommittee on Securities, Insurance and Investment (April 6, 2011).
[20] Ibid.

financial statements. This dialogue could help the PCAOB better appreciate business operations and the unintended consequences that may impact businesses through the development and implementation of accounting and auditing standards. The avoidance of adverse outcomes for businesses is critical to protect the investors who invest in them.[21]

Issue 5: Addressing the needs of Private Company financial statement users

Problem: Private company financial statement users have differing needs and find public company U.S. GAAP to be too complex and burdensome.

Solution: Preserve U.S. GAAP as the accounting language, while empowering the Private Company Council to address the needs of private company users.

Background: Any modernization of financial reporting policies requires that the differing needs of users of the financial statements be considered and addressed. In particular, privately held users do not require the same information as users those entities that are owned by the public. It is imperative that any changes made to standards do not have the unintended consequence of requiring privately held entities to follow standards which may provide information critically important to users of publically held entity financial statements but which is not relevant to their users. While CIFiR did not address these issues, following extensive study and research, the Blue Ribbon Panel on Standard Setting for Private Companies ("Blue Ribbon Panel") made several recommendations which eventually led to the creation of the Private Company Council under the auspices of the FAF. Additionally, Congress, in passing the JOBS Act, made the public policy decision that users of financial reports are not monolithic and different business structures (ie. public company, emerging growth companies) will dictate the needs of financial statement users. Accordingly, we believe the SEC, FRF, and FAF should closely monitor the activities of the PCC to ensure the needs of private company users are met and that the Congressional intent of the JOBS Act is fulfilled.

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This is not an exhaustive list of reforms or issues that should be addressed. Rather, we view this as a starting point of discussion and would respectfully request to meet with you to discuss these ideas and proposals in greater depth and detail. While we know and appreciate the workload of SEC, it is our belief that the many changes in financial reporting over the past decade require a response to prevent disharmony in financial reporting that can adversely impact the capital markets, businesses and the investors who provide them with the resources to grow and operate on a daily basis.

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[21] *See* CCMC letter to Martin F. Baumann (May 10, 2013).

Thank you for your consideration of these views, and we look forward to further discussion with you and SEC staff as well as an update on the implementation of the CIFiR recommendations.

Sincerely,

Tom Quaadman

cc: The Honorable Luis A. Aguilar, U.S. Securities and Exchange Commission
The Honorable Daniel Gallagher, U.S. Securities and Exchange Commission
The Honorable Kara Stein, U.S. Securities and Exchange Commission
The Honorable Michael Piwowar, U.S. Securities and Exchange Commission
Mr. Paul Beswick, U.S. Securities and Exchange Commission
Mr. Russell Golden, Financial Accounting Standards Board
Mr. James Doty, Public Company Accounting Oversight Board
The Honorable Tim Johnson, U.S. Senate
The Honorable Michael Crapo, U.S. Senate
The Honorable Jeb Hensarling, U.S. House of Representatives
The Honorable Maxine Waters, U.S. House of Representatives
The Honorable Scott Garrett, U.S. House of Representatives
The Honorable Carolyn Maloney, U.S. House of Representatives

TOM QUAADMAN
VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
(202) 463-5540
tquaadman@uschamber.com

August 31, 2015

Ms. Phoebe W. Brown
Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, D.C. 20006-2803

Re: PCAOB Supplemental Request for Comment: *Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form* (PCAOB Release No. 2015-004, June 30, 2015; PCAOB Rulemaking Docket Matter No. 029)

Dear Ms. Brown:

The U.S. Chamber of Commerce[1] (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 must have a strong system of internal controls, recognizes the vital role external audits play in capital formation, and supports efforts to improve audit effectiveness. Accordingly, the CCMC appreciates the opportunity to comment on the Public Company Accounting Oversight Board ("PCAOB") Supplemental Request for Comment on *Rules to Require Disclosure of Certain Audit Participants on a New PCAOB Form* ("Supplemental Proposal") and wishes to express serious concerns regarding the Supplemental Proposal.

The Supplemental Proposal represents the latest PCAOB release on these matters and the CCMC has commented on two prior proposals.[2] Our concerns

[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.

[2] See CCMC letter dated March 10, 2014 on PCAOB Exposure Draft on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor's Report of Certain Participants in the Audit* (PCAOB Release No. 2013-009, December 4, 2013; PCAOB Rulemaking Docket Matter No. 029) and CCMC letter dated January 9, 2012 on Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB*

expressed in those two letters remain and we attach them with this letter as an appendix and request that they be made a part of the comment file for the Supplemental Proposal. The CCMC also has concerns that the Supplemental Proposal is not being put forth in a liability neutral fashion and that liability neutrality was not considered as part of the economic analysis. Finally, we also wish to raise the issue that comments are being solicited by the Securities and Exchange Commission ("SEC") on audit committee disclosures and the CCMC requests that the PCAOB defer to the SEC on this matter.

Consistent with our prior comments, the CCMC does not support mandating disclosure of this information. The CCMC believes that any such disclosures should be voluntary and that U.S. regulators should let market forces sort out the consequences of any jurisdictional requirements to disclose this information.

The CCMC also reiterates that in the United States., the Sarbanes-Oxley Act of 2002 ("SOX") created the PCAOB to regulate the accounting firms and individuals that audit public companies and reaffirmed the audit committee's responsibility for oversight of the external audit. There is no need for mandating these disclosures when investors trust these structures and processes created by SOX on their behalf. In addition, mandating these disclosures will never put investors "in the shoes" of the PCAOB or audit committees. Nonetheless, such disclosures may result in investors and others unnecessarily second-guessing decisions of the PCAOB and audit committees—based on partial and incomplete information, which in turn undermines trust in regulatory and governance processes.

The PCAOB issued the Supplemental Proposal to solicit comment on an alternative mechanism for disclosing the name of the engagement partner and information about certain other participants in the audit—namely via a new PCAOB Form AP.[3] The CCMC appreciates that creating a new disclosure Form AP, instead of requiring disclosure in the auditor's report, is intended to respond to concerns

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Auditing Standards and Form 2 (PCAOB Release No. 2011-007, October 11, 2011; PCAOB Rulemaking Docket Matter No. 029).

[3] The Supplemental Proposal indicates that the PCAOB is considering a basic filing deadline of 30 days after the date the auditor's report is first included in a document filed with the SEC, with a shorter deadline of 10 days for initial public offerings (or within 10 days after the registration statement is publicly filed with the SEC for emerging growth companies ("EGCs")).

raised by commenters, including the CCMC, that the PCAOB's proposed disclosures would create both legal and practical issues.

However, the Supplemental Proposal represents a response to such concerns only regarding disclosures in auditors' reports included or incorporated by reference into registration statements under the Securities Act of 1933—specifically in regards to liability under Section 11 and consents required under Section 7.[4] The Supplemental Proposal does not otherwise respond to litigation risks that would be created by the proposed disclosures, including under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

The CCMC reiterates that we strongly believe that liability neutrality represents a minimum threshold for these disclosures. The Supplemental Proposal states this PCAOB rulemaking process was undertaken in response to a recommendation of the U.S. Department of the Treasury's Advisory Committee on the Auditing Profession ("ACAP") that the PCAOB should consider mandating the engagement partner's signature on the audit report. However, as the CCMC has previously emphasized, this ACAP recommendation (regardless of form or placement of the name of the engagement partner) was premised on liability neutrality.

Further, the precondition of liability neutrality should also be part of an economic analysis. The CCMC has emphasized the importance of the PCAOB conducting substantive and robust economic analysis. Although consisting of 27 pages of qualitative discussion, the "Economic Considerations" section of the Supplemental Proposal does not address liability considerations at all.

The Supplemental Proposal does not resolve other concerns discussed in our prior comments. While we do not restate these concerns, please consider them to be incorporated by reference in this letter.

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[4] Section 11 of the Securities Act of 1933 imposes liability on certain participants in a securities offering, including every accountant who, with his or her consent, has been named as having prepared or certified any part of the registration statement or any report used in connection with the registration statement. Section 7 of the Securities Act of 1933 requires that the consent of every accountant so named in a registration statement must be filed with the registration statement.

Lastly, it is important to recognize that on July 1, 2015, the SEC voted to publish a Concept Release on *Audit Committee Disclosures* ("SEC Concept Release"). Among other matters, the SEC Concept Release solicits public comment on whether the SEC should require audit committees to disclose the name of the engagement partner and information about certain other participants in the audit.

While the CCMC does not support mandating disclosure of this information, as we have stated in our prior letters, the CCMC believes that any such disclosure is better suited for inclusion in a report by the audit committee in the proxy statement. Given the SEC has taken up considering the disclosure of this information, the CCMC urges the PCAOB to defer to the SEC on this matter.

Once again, the CCMC appreciates the opportunity to comment on the Supplemental Proposal. Thank you for your consideration and the CCMC stands ready to assist in these efforts.

Sincerely,

Tom Quaadman

CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

TOM QUAADMAN
VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
(202) 463-5540
tquaadman@uschamber.com

January 9, 2012

Mr. J. Gordon Seymour
Secretary
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006-2803

Re: PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29)

Dear Mr. Seymour:

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 must have a strong system of internal controls and recognizes the vital role external audits play in capital formation. The CCMC appreciates the opportunity to comment on the Public Company Accounting Oversight Board's ("PCAOB") Proposed Rulemaking on ***Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2*** ("the Proposal").

The CCMC is concerned that the Proposal will undermine the foundation of the audit process impairing transparency and accountability. The CCMC believes that the Proposal in its current form will obfuscate essential responsibilities thereby harming accountability. Because of these concerns and the lack of any tangible demonstrated benefit, the CCMC believes that the Proposal should be reassessed through a public roundtable of all interested stakeholders and additional outreach such as field testing.

Rather than moving forward on this Proposal, the CCMC believes that the PCAOB should concentrate its efforts on updating its quality control standards that are long overdue for updating.

Discussion

The Proposal would amend the PCAOB standards and rules to require registered public accounting firms to make two new disclosures in the audit report:

1. The name of the engagement partner for the most recent period's audit; and

2. Information on other independent public accounting firms and other persons that took part in the audit. In addition, the name of the engagement partner would also be required to be disclosed in Form 2 filed with the PCAOB for each audit report already required to be reported on the Form.

A foundational precept of independent audits is that the audit firm has ultimate responsibility for the audit report, while the opinion rendered represents the combined efforts of a team of individuals. Proposing disclosure requirements that could undermine and confuse this essential responsibility would impair transparency and accountability. It is also unclear what the objectives of the Proposal are, how the Proposal furthers the mission of the PCAOB, and what the consequences of the Proposal are in terms of its costs and benefits.

1. <u>Disclosing the Name of the Engagement Partner</u>

The proposal to disclose the name of the engagement partner for the most recent period's audit evolved from the PCAOB's ***Concept Release on Requiring the Engagement Partner to Sign the Audit Report*** issued on July 28, 2009. Among the concerns expressed by commenter's on that Concept Release was that partner signatures would suggest the engagement partner is responsible for the audit engagement and increase engagement partner legal liability.

The CCMC commends the PCAOB for responding to these concerns by not pursuing the original Concept Release. However, the CCMC believes that these fundamental concerns regarding the Concept Release hold equal weight with the current Proposal.

It is also problematic that the PCAOB continues to move in the direction of expecting engagement partners to somehow build their own individual reputations for audit quality, independent of their firm's reputation, undermining accountability in the audit process and harming investor protection.

In reality, the firm's quality control system, in accordance with the PCAOB's "interim" quality control standards, provides the foundation for the efficacy of the work performed on the engagement by the team of individuals in rendering the audit opinion. The CCMC believes that the PCAOB's quality control standards are long overdue for updating. Investors would likely be better served by the PCAOB focusing its efforts on updating these standards rather than diverting its time and resources on the Proposal.

a. Legal Liability

The potential for the disclosure of the name of the audit partner to increase engagement partner legal liability was recognized by Board Member Dan Goelzer in his Statement on the Proposal and his comments at the PCAOB's open Board meeting on October 22, 2011. The duties and relationships established by federal securities laws, Securities Exchange Act Rule 10b-5 and Securities Act Section 11 are the basis of those concerns. The June 2011 decision of the U.S. Supreme Court in *Janus Capital Group, Inc.*[1] has added to the uncertainty over legal liability under Rule 10b-5 in the context of this Proposal. In addition, it remains to be seen whether the Securities and Exchange Commission ("SEC") would require issuers to file not only the consent of the accounting firm that prepared the audit report but also a separate

[1] See *Janus Capital Group, Inc. v. First Derivative Traders,* 131 S.Ct. 2296 (2011).

consent of the engagement partner whose name is disclosed in the audit report.[2] If this requirement unfolds, this would subject the partner, along with the accounting firm, to potential Section 11 liability. Further, the CCMC understands liability issues could potentially extend to disclosure of the name of the engagement partner in PCAOB Form 2.

Given these legal uncertainties, the CCMC believes it would be premature of the PCAOB to proceed with this Proposal. The Board needs to fully understand the liability implications and have persuasive evidence that disclosure of the name of the engagement partner would be liability neutral. Neutrality is consistent with the recommendation of the Advisory Committee on the Auditing Profession ("ACAP") that was the genesis for the Proposal.[3] The ACAP recommendation was premised on the condition that the requirement not impose on the engagement partner "any duties, obligations or liability that are greater than the duties, obligations and liability imposed on such person as a member of an auditing firm."[4]

b. Objectives

The Proposal reiterates that the objectives from the Concept Release on partner signature—namely transparency and accountability—continue to be the objectives for disclosing the name of the engagement partner in the audit report and on PCAOB Form 2. Unfortunately, these objectives lack clarity in the context of this Proposal.

While the Proposal articulates the "means" of disclosing more information, it fails to state the "ends" it seeks to achieve. The Proposal fails to articulate the problem that needs to be addressed and how disclosing the name of the engagement partner will enhance financial reporting for investors.

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[2] If this scenario was to unfold, it is unclear if an issue of consent would be created for others participating in the audit.
[3] ACAP recommended that the PCAOB "undertake a standard-setting initiative to consider mandating the engagement partners' signature on the auditor's report (*Final Report of the Advisory Committee on the Auditing Profession to the* U.S. *Department of the Treasury*, (2008), VII: 19, VII: 20).

[4] *Ibid* at VII: 20. The ACAP Report also noted that this language is similar to safe harbor language the SEC promulgated in its rulemaking pursuant to The Sarbanes-Oxley Act of 2002 ("SOX") for audit committee financial experts.

Such an articulation is important as the Proposal simply provides conjectures for some of which the Board seeks comments on. For example, the Board asks whether the additional transparency could promote auditor independence by discouraging audit clients from inappropriately pressuring the firm to remove an engagement partner sooner than is required under the partner rotation requirements in SOX and SEC rules[5]. Yet, there are many substantive reasons for changes in engagement partners. And, without additional information disclosed about the reason for a change in the engagement partner an "inappropriate" partner change could not be discerned from a change in the name alone.

At the November 2011 meeting of the PCAOB's Standing Advisory Group ("SAG"), PCAOB staff emphasized that no such additional disclosure regarding a change in engagement partners is proposed or planned. Indeed, current disclosure requirements on auditor change reside within the SEC's jurisdiction and strongly suggest that any rulemaking along these lines would be better left to the SEC.

In the Proposal, accountability is described in terms of the original Concept Release with the added proviso that disclosure may make partners feel more accountable for the quality of the work and, therefore: "Disclosing the name of the engagement partner may be one means of promoting better performance"[6]. Not all agree with that statement and at the November 2011 SAG meeting; one SAG member took strong issue with this notion.

Reinforcing the speculative and likely illusory nature of any such improvements, the PCAOB has provided no evidence related to how this Proposal might improve audit quality. This is important because audit quality is the PCAOB's mission. As Dan Goelzer stated at the PCAOB's open Board meeting on October 11, 2011: "Unless engagement partner disclosure can be directly linked to improving audit quality, or to promoting understanding of the financial statement audit or of the Board's inspection program, the issue would seem to fall in the SEC's bailiwick."[7]

[5] PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29), Page 9.
[6] Ibid.
[7] See "Statement on Proposed Amendments to Improve Transparency Through Disclosure of Engagement Partner and Certain Other Participants in Audits" at the October 11, 2011 PCAOB Open Board Meeting by Daniel L. Goelzer, Board Member.

c. *Improving Audit Quality*

Evidence linking the Proposal with improvements to audit quality is a necessary condition for PCAOB rulemaking and for SEC approval of such rulemaking. The absence of any such evidence is likewise troublesome because the PCAOB considers collecting such evidence through its inspection process as one of its unique strengths. For example, the PCAOB's Strategic Plan for 2011-2015 (the "Strategic Plan") states: "We possess unique data and analysis related to audits based on eight years of inspections and enforcement experience, as well as a sophisticated research and analysis function".[8] Yet, there is no PCAOB data or analysis in evidence to support this Proposal and the Proposal makes no reference to the PCAOB having either collected or analyzed any relevant data.

Paradoxically, the objective for the disclosure of the name of the engagement partner, particularly the Form 2 disclosures, appears to be to facilitate analysis *by others,* not for the benefit of the PCAOB. For example, the Proposal states the purpose of the Form 2 disclosures is to compile this information in one place that could be easily accessed[9]. This implies that meaningful analysis of this data is possible and useful, which in reality is problematic given the complex nature of audit quality. This also ignores the facts that a thorough analysis of any such data requires such data to be considered in conjunction with information that may not be available or relevant to investors.[10]

Finally, it is worth noting that the PCAOB has not yet developed audit quality indicators—another ACAP recommendation. It would seem that the development of such indicators should occur in advance of any rulemaking on disclosing the name of the engagement partner as, at least implicitly, the Proposal is suggesting that the name of the engagement partner is somehow a quality indicator.

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[8] See Public Company Accounting Oversight Board Strategic Plan: *Improving the Relevance and Quality of the Audit for the Protection and Benefit of Investors 2011-2015* (November 30, 2011), Page 8.

[9] PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29), Page 17.

[10] Additionally, the Proposal fails to take into account that various actors aggregate a variety of data from SEC filings that they find relevant.

d. Other Costs and Benefits

An additional motivation for disclosing the name of the engagement partner appears to be to provide useful information for audit committees. For example, the Proposal reiterates a point made in the Concept Release that "providing financial statement users, audit committees, and others with the name of the engagement partner might provide them the opportunity to evaluate, to a degree, an engagement partner's experience and track record. If so, audit committees might increasingly seek out engagement partners who are viewed as performing consistently high quality audits, and the resulting competition could lead to an improvement in audit quality"[11]. However, this rationale cannot serve as a basis for rulemaking as audit committees already have access to this information and would need to use it in conjunction with a variety of other information, both public and private, for assessing quality on their audits.

As expressed in previous letters to the PCAOB,[12] the CCMC continues to be concerned that this Proposal provides yet another illustration of the PCAOB's skepticism regarding the role of audit committees and that this and other PCAOB proposals may actually interfere with the prerogatives, discretion and duties of audit committees. For example, with this Proposal, the PCAOB seems to be expecting investors to second guess the work of audit committees based on "one" data point – the name of the engagement partner.

2. <u>Disclosing Information on Others Participating in the Audit</u>

Somewhat ironically the Proposal combines a disclosure focused on one individual with a requirement to disclose more information about others participating in the engagement not employed by the auditor. The Proposal calls for disclosure, with limited exceptions, of other participants in the audit for whose audit the auditor takes responsibility or whose audit procedures the auditor supervises. The Proposal

[11] Ibid, Page 6.
[12] For example, see the September 14, 2011 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on the *Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements* (PCAOB Release No. 2011-003, June 21, 2011, Rulemaking Docket Matter No. 34) and the October 20, 2011 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on the *Concept Release on Auditor Independence and Audit Firm Rotation* (PCAOB Release No. 2011-006, August 15, 2011, PCAOB Rulemaking Docket Matter No. 37).

would require the auditor to disclose in the audit report, the names, location, and percentage of hours attributable to the other participants for those whose participation is 3% or greater of total hours. Disclosures would also be required when the auditor divides responsibility with another independent public accounting firm.

The Proposal suggests that these disclosures would "enable investors and other users of the audit report to determine whether a disclosed independent public accounting firm is registered with the Board and has been subject to PCAOB inspection, and whether a disclosed independent public accounting firm or another person has had any publicly available disciplinary history with the Board or other regulators"[13]. However, this is information that the audit committee has access to and can consider in exercising its oversight responsibilities. Further, the auditor either takes responsibility for the work of others or divides responsibility. In the case of the later, current disclosures to investors do not appear wanting for assessing audit quality and the applicability of PCAOB inspection information.

Essentially the "new" information proposed to be disclosed involves work for which the auditor assumes responsibility. As such, the proposed disclosures are likely to only cause confusion over who has responsibility for the audit. The CCMC notes that avoiding such confusion is an important objective of current auditing standards. This suggests that investors would be better served with more targeted disclosures founded on some meaningful objective.

The potential for confusion is exacerbated by the low threshold for disclosure of 3% being proposed. The basis for this threshold is unclear as the Proposal provides no meaningful rationale for it. Further, a 3% threshold is much lower and in marked contrast to the 20% threshold already incorporated in PCAOB rules to determine others performing a substantial role in audits and thus subject to PCAOB registration and inspection. So, why should investors be interested in what the PCAOB is not?

Further, there is no indication that the PCAOB has field-tested the 3% threshold to determine the relevance of the information to be disclosed. For example,

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[13] PCAOB Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29), Page 20.

the Proposal contains no useful illustrations based on real-world data. The absence of these data to inform stakeholders about the implications of the Proposal is surprising, given the PCAOB has access to the necessary data through its inspection process and, as previously noted, the PCAOB emphasizes this in its Strategic Plan as strength of the organization.[14]

Conclusion

The CCMC appreciates the opportunity to comment on the Proposal. However, the CCMC believes that the Proposal will disseminate information that is non-material, lacks relevance that could undermine the fundamental foundations of the audit function hampering the ability of investors to make informed decisions. Without a clear articulation of the problems to be solved and the benefits of the proposal, the CCMC does not believe that the proposal should move forward.

Furthermore, based on the statements and comments by Board members at the October 11, 2011 open Board meeting, it appears that the majority of Board members strongly support enacting the Proposal raising potential due process questions. The CCMC hopes that the PCAOB will take the concerns expressed in this letter under consideration when deliberating on the Proposal.

Thank you for your consideration and the CCMC stands ready to discuss these concerns in further detail.

Sincerely,

Tom Quaadman

[14] While the CCMC does not believe that it is in the best interests of financial reporting to move forward on this proposal, one alternative the PCAOB may wish to consider is that the Form 2 would be a more useful location for such disclosures, as the determination of information in SEC filings is more appropriately maintained within the SEC's jurisdiction, Form 2 disclosures would not lengthen issuer and broker-dealer filings with tangential information, and Form 2 disclosures would not be subject to the estimation of hours necessitated by the short time constraints for SEC filings. In addition, disclosure in Form 2, instead of the audit report, might help mitigate potential liability issues and confusion over auditor responsibility, as previously discussed.

CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

TOM QUAADMAN
VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
(202) 463-5540
tquaadman@uschamber.com

March 10, 2014

Ms. Phoebe W. Brown
Secretary
Public Company Accounting Oversight Board
1666 K Street, NW
Washington, D.C. 20006

Re: PCAOB Exposure Draft on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor's Report of Certain Participants in the Audit* (PCAOB Release No. 2013-009, December 4, 2013; PCAOB Rulemaking Docket Matter No. 029)

Dear Ms. Brown:

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 must have a strong system of internal controls and recognizes the vital role external audits play in capital formation. The CCMC supports efforts to improve audit effectiveness and appreciates the opportunity to comment on the Public Company Accounting Oversight Board ("PCAOB") Exposure Draft on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards to Provide Disclosure in the Auditor's Report of Certain Participants in the Audit* ("the Proposal").

The CCMC has serious concerns that the PCAOB has not met the minimum thresholds needed to move forward on the Proposal, namely the failure to demonstrate how the Proposal will provide investors with decision useful information and what investor interests are being addressed. While the CCMC applauds the PCAOB for establishing the Center for Economic Analysis, the Proposal's cost-benefit analysis is insufficient as it fails to provide stakeholders with an analysis to comment on, nor is any analysis provided to meet the statutory requirements as to why Emerging Growth Companies ("EGCs") should be subject to the Proposal if adopted. Finally, the issues raised in our January 9, 2012 comment letter to the Proposal's predecessor ("2012 letter") remain unaddressed. Accordingly, we have attached the 2012 letter as an appendix to this letter and ask that it also be considered a part of the record.

Our concerns are discussed in more detail below.

I. Background

The Proposal would require disclosure in the auditor's report of the following:

- The name of the engagement partner;

- The names, locations, and extent of participation of other independent public accounting firms that took part in the audit; and

- The locations and extent of participation of other persons not employed by the auditor, whether an individual or a company, ("other participants") that took part in the audit.

The Proposal represents the latest PCAOB release on these matters. In July 2009, the PCAOB issued a Concept Release on *Requiring the Engagement Partner to Sign the Audit Report.* In October 2011, the PCAOB proposed a rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2*. The CCMC provided comments on the proposed rulemaking.[1]

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[1] *See* the January 9, 2012 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on Proposed Rulemaking on *Improving the Transparency of Audits: Proposed Amendments to PCAOB Auditing Standards and Form 2* (PCAOB Release No. 2011-007, October 11, 2011 and PCAOB Rulemaking Docket Matter No. 29).

II. Naming the Engagement Partner

While the Proposal calls for audit firms to disclose the name of the engagement partner in the auditor's report, it does not provide a meaningful rationale for why this should be done. The Proposal states that this information "***could*** be valuable to investors in making investment decisions as well as if they are asked to vote to ratify the company's choice of registered firm as its auditor" (emphasis added).[2] However, there is a marked failure to show how this change in disclosure will benefit investors and the arguments in support of the Proposal, including those related to audit quality, are superficial.[3]

The Proposal states the "means" of more disclosure but fails to demonstrate the "ends" it seeks to achieve. The Proposal does not articulate the problem that will be resolved through the adoption of the Proposal, or how the Proposal is the best option to solve the undefined problem. Moreover, the Proposal fails to show how investor needs will be enhanced through the naming of the engagement partner.

a. Audit Quality

As we expressed in the 2012 letter, regardless of their nature and size, audits are performed by a team of individuals. In reality, the audit firm's quality control system, in accordance with the PCAOB's "interim" quality control standards, provides the foundation for the efficacy of the work performed on audits. The CCMC continues to believe that investors would be better served by the PCAOB focusing its efforts on updating its quality control standards rather than naming the engagement partner.

The Proposal states that the PCAOB has noticed through its inspection process variation in the quality of audits performed. While the inspections process can and should be a useful tool in setting priorities for the PCAOB, the justification for the Proposal falls short. The Proposal states that, while many factors contribute to this variation, the role of the engagement partner is an important factor to

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[2] *See* page 3 of the Proposal.

[3] Setting aside the conceptual flaws with the Proposal, from a practical standpoint, the CCMC notes that naming the engagement partner in the auditor's report is retrospective and does not necessarily disclose to investors the identity of the engagement partner for the *upcoming* period that applies to the shareholder vote on ratification of the audit firm.

consider.[4] Unfortunately, this is not a compelling argument for this Proposal. If a variation of audit quality is found because of a variety of factors, either that combination of factors must be addressed in a policy response, or a clear and demonstrable showing must be made of how naming the engagement partner is the over-riding cause of such a variation.

The Proposal does not make either case.

Naming the engagement partner does not enable investors or other third-parties to even begin to approach "stepping into the shoes" of the PCAOB or audit committee. Indeed, third-parties may instead get an incorrect view of the role of the engagement partner related to audit quality based on the information available from the name of the engagement partner. Investors are better served by relying on the regulatory and governance processes rather than trying to second guess these processes based on a disclosure of the name of the engagement partner.

Reinforcing this point, the CCMC notes that another current PCAOB initiative focuses on developing audit quality indicators ("AQIs"). The PCAOB staff Discussion Paper for the May 15-16, 2013 meeting of the Standing Advisory Group ("SAG") describes this initiative. The definition of audit quality in the Discussion Paper includes "meeting investors' needs for independent and reliable audits."[5] In this regard, the SAG Discussion Paper provides 40 different AQIs involving operational inputs (13), the audit process (15), and audit results (12). The name of the engagement partner is not among these 40 AQIs. Thus, the PCAOB's own initiative on audit quality does not recognize the relevance of disclosing the name of the engagement partner to investors.

b. Legal Liability

The Proposal calls for placing the disclosure of the name of the engagement partner in the auditor's report. In the 2012 letter, the CCMC expressed concern that disclosing the name of the partner could increase engagement partner legal liability. Disclosure in the auditor's report is a major contributor to the liability increase.

[4] *See* page 6 of the Proposal.
[5] *See* pages 3 and 4 of the Discussion Paper on AQIs for the May 15-16, 2013 SAG meeting.

The CCMC appreciates that the Proposal contains a section on liability considerations, including under Section 11 of the Securities Act and Section 10(b) and Rule 10b-5 of the Exchange Act.[6] As explained in the Proposal, Section 11 of the Securities Act imposes liability for material misstatements or omissions in a registration statement, subject to a due diligence defense, on "every accountant … who has with his consent been named as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement … which purports to have been prepared or certified by him."[7]

In turn, Section 7 of the Securities Act requires issuers to file with the Securities and Exchange Commission ("SEC") the consent of any accountant who is named as having prepared or certified any part of the registration statement or any valuation or report included in the registration statement. The Proposal recognizes that engagement partners (and participating accounting firms) named in the auditor's report would have to consent to the inclusion of their names in such reports filed with the SEC, or included by reference in another document filed under the Securities Act with the SEC.[8]

As to Section 11 liability, the Proposal acknowledges litigation-related costs would increase, but conjectures that these costs should "not be substantial."[9] As to liability under Section 10(b) of the Exchange Act, the Proposal acknowledges concerns similar to those we expressed in our letter of January 9, 2012 and states that the Board "cannot conclude with certainty whether its approach might increase liability."[10]

The CCMC continues to strongly believe that "liability neutral" represents a minimum threshold for proceeding with any initiative that would involve disclosing the name of the engagement partner. The CCMC urges the PCAOB to recognize this important pre-condition as anything other than liability neutral standards will ultimately harm investors. Such a precondition should also be a part of an economic

[6] *See* pages 20-26 of the Proposal.
[7] *See* page 21 of the Proposal.
[8] *See* pages 21-22 of the Proposal.
[9] *See* page 23 of the Proposal.
[10] *See* page 25 of the Proposal.

analysis.[11] Economic analysis should be used to determine if a proposed standard or revision to a standard is liability neutral and if not what the costs to investors and businesses will be.

c. Placement of Disclosures

While the CCMC does not support a requirement to disclose the name of the engagement partner, we would also like to comment on the Proposal in regards to the placement of any such disclosure. If any such requirement ensues from this initiative, disclosures should not be in the audit report. Rather than being part of the auditor's report, any such disclosure seems better suited for inclusion in a report by the audit committee in the proxy statement.

Importantly, the PCAOB could have circumvented some of the Section 11 liability concerns previously discussed by not proposing the name of the engagement partner (and other participants involved in the audit) be disclosed in the auditor's report. An alternative mode of naming the engagement partner would be a disclosure on the PCAOB's website through the use of Form 2.

In this regard, it is worth recalling that the PCAOB's October 2011 Proposed Rulemaking would have required disclosure of the name of the engagement partner in both the audit report and PCAOB Form 2. Instead of focusing the initiative on disclosures in Form 2, the current Proposal would require the disclosure only in the audit report. Apparently this focus was premised on arguments that disclosures in the audit report on the SEC's website would be more timely and accessible for investors. However, these arguments are not at all compelling.

It is unclear as to why a posting on both the SEC's and PCAOB's websites would not be the preferable route of disclosure. If the decision to make this disclosure on the SEC website alone is because the PCAOB's website is not "user friendly", that is a problem that can be fixed by the PCAOB. It cannot be used as a rationale to impose costs on all stakeholders. Moreover, according to the PCAOB's Strategic Plan and statements by Board members at the PCAOB's November 25,

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[11] Liability neutrality is not a new concept; it was also included in the *Final Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury* (2008), VII: 19-20.

2013 open meeting on the PCAOB budget,[12] the PCAOB already has an initiative underway to leverage its technology, improve the "usability" of its website, and enhance communication to public constituencies. Thus, this technology "impediment" seems fixable in the near term; and, it is under the purview of the PCAOB to do so.

Further, the notion that investors would have all necessary information in-hand with disclosure of the name of the engagement partner in the audit report is flawed. Setting aside that the name of the engagement partner is unlikely to provide any actionable information for investors, there is no information content in the name of the engagement partner per se. Indeed, it is unclear how the disclosure of a name, which on its face will be of no utility to an investor, will help the reasonable investor make an investment decision. Indeed, the PCAOB acknowledges in the Proposal that this disclosure would have to be considered in combination with other information.[13]

It appears that the PCAOB envisions some of this other information would come from the SEC's website, but it would also involve information on the PCAOB's existing website as well. In addition, according to the Proposal, much of this other information would have to be obtained (and only available over time) from academic research and databases developed by third-parties.[14] Thus, the argument that the name of the engagement partner needs to be included in the audit report in order for investors to have all necessary information readily available in one place falls apart in practice.

Not disclosing the name of the engagement partner (and other participants in the audit) in the auditor's report would likewise avoid the complex and costly administrative nightmare that would be imposed on audit firms and issuers from needing to obtain Section 7 consents from engagement partners (and other participating accounting firms) so that issuers could file required consents with the SEC. The Proposal fails to recognize the multiple difficulties that would arise in trying to obtain such consents. These difficulties would likely hinder the ability of issuers to make timely filings with the SEC, thereby harming investors.

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[12] For example, see *PCAOB Strategic Plan: Improving the Quality of the Audit for the Protection and Benefit of Investors 2013-2017* (November 26, 2013), pages 16-17.
[13] *See* page 11 of the Proposal.
[14] *See*, for example, pages 12-13 of the Proposal.

As just one example of the difficulties that could arise from needing Section 7 consents, assume that an engagement partner is rotated off an audit because of the Sarbanes-Oxley Act of 2002 ("SOX") mandatory partner rotation requirement and the SEC's rules implementing this requirement. Also assume that the partner's initial consent needs to be reissued. On one hand, the partner would need to do additional work in order to allow the reissuance of the consent.[15] On the other hand, the partner would be precluded from doing any additional work because it would cause the audit firm to be in violation of the SEC's independence rules. Moreover, this example assumes the partner would be willing and able to reissue the consent and does not consider the need to address the myriad of circumstances when this would not be the case.

The Proposal appears to set up a dynamic whereby PCAOB requirements would force the SEC to waive its requirements (as a matter of policy) for audit partners (and other participants in audits) to reissue their consents in a broad array of circumstances in order to make our markets function efficiently.

All things considered, the arguments in the Proposal for disclosing the name of the engagement partner (and other participants in the audit) in the audit report are simply not convincing. The proposed placement of the disclosures significantly increases the costs of the Proposal, including legal and administrative costs, for no substantive benefit. The CCMC strongly urges that the PCAOB reconsider the Proposal in this regard.

III. Other Participants in the Audit

In addition to disclosing the name of the engagement partner, the Proposal would also require that the audit report disclose the names, locations, and extent of participation of other independent public accounting firms that took part in the audit and the locations and extent of participation of other persons not employed by the auditor. The proposed threshold for these disclosures is any public accounting firm or other participant performing 5% or more of the total hours in the most recent period's audit. This threshold is designed to demonstrate if an accounting firm plays a substantial role in the audit. The current threshold is 20%.

[15] Our discussion sets aside any considerations related to determining the nature of and standards for this work.

While the CCMC appreciates that the Proposal does raise the threshold from the 2011 proposal of 3% to 5%, we believe that the Proposal does not provide a compelling case for why the current 20% threshold should not be used instead.

As expressed in our 2012 letter, we do not believe that it is in the best interests of financial reporting to move forward on these matters. And, as previously discussed in this letter, we continue to be concerned that any such disclosures do not belong in the auditor's report.

IV. Cost Benefit Analysis

The Proposal recognizes that the Jumpstart Our Business Startups Act ("JOBS Act") now makes economic analysis a necessary pre-condition for applying new PCAOB auditing standards and rules to an audit of any emerging growth company ("EGC"). Specifically, Section 103(a) (3) of SOX as amended by Section 104 of JOBS Act requires that rules adopted by the Board after the date of enactment of JOBS Act shall not apply to an audit of any EGC, unless the SEC determines that the application of such additional requirements is necessary or appropriate in the public interest, after considering the protection of investors and whether the action will promote efficiency, competition, and capital formation. The Proposal recommends that EGCs follow the requirements if adopted.

At the outset, we commend the PCAOB for establishing the Center for Economic Analysis to help fulfill the statutory requirements of the JOBS Act. The CCMC has been a strong advocate of economic analysis as a means of using empirical evidence to guide smart regulation and standard setting.[16]

However, in our view, the economic analysis provided with the Proposal fails to provide commenters with any information to comment on and fails to delineate the costs or benefits to EGCs if they are to follow the requirements of the Proposal. Indeed there is no analysis to provide an articulation of the benefits or of the costs to

[16] For example, see the December 9, 2013 letter from the U.S. Chamber of Commerce CCMC to the PCAOB on Proposed Auditing Standards on *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 and PCAOB Rulemaking Docket Matter No. 34).

EGCs. This not only calls into question the ability of the Proposal to meet the economic analysis requirements needed for the Proposal to be approved through the SEC's rulemaking process, it also raises questions regarding the level of the PCAOB's commitment to economic analysis.

A review of some academic studies of companies in jurisdictions that do not have similar legal, regulatory, governance, market, and cultural environments and structures with the United States does not pass muster as an economic analysis. The Proposal contains no analysis or articulation of the direct costs to issuers, the direct costs to auditors, possible liability costs to issuers, possible impacts on stock price, possible impacts on returns to investors, potential discussion of benefits, if any public companies in the United States voluntarily disclose the name of the engagement partners and the costs and benefits comparing those companies to similarly situated companies. This is by no means an exhaustive list, but it is the type of analysis that accompanies proposed regulations when required by law. As such an analysis is required by the JOBS Act and as this Proposal must go through the SEC rulemaking process which will require an analysis of the impacts on competition and capital formation a more thorough study subject to public comment is necessary to move forward in applying the Proposal to EGCs.

The CCMC notes that the PCAOB's Strategic Plan for 2013-2017 states the PCAOB has developed "internal" guidance on economic analysis.[17]. The CCMC strongly urges the PCAOB to release its internal guidance on economic analysis for public comment so that stakeholders can be informed of the PCAOB's understanding of the role of economic analysis and how it can be used. Such public commentary can create a useful dialogue on the issue that all sides can benefit from. The merits of the PCAOB's analysis of costs and benefits in any particular proposal cannot be evaluated without understanding the essentials of the guidance being applied by the PCAOB for economic analysis.

The CCMC is very disappointed with the level of economic analysis provided in the Proposal and believes that it cannot pass the requirements of the JOBS Act and other statutory provisions that must be met for the Proposal to be approved and

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[17] For example, see page 13 of the PCAOB *Strategic Plan: Improving the Quality of the Audit for the Protection and Benefit of Investors 2013-2017* (November 26, 2013).

become operational. Economic analysis, with a thorough weighing of the costs and benefits, can and should be used as a means of using empirical evidence to develop smart regulations. That goal has not been met.

V. Conclusion

Once again, the CCMC appreciates the opportunity to comment on the Proposal. However, the CCMC has serious concerns that the Proposal in its current form is flawed.

The Proposal fails to demonstrate how naming an engagement partner will improve audit quality, will provide investors with decision-useful information, and what investor interests are being addressed. Additionally, the cost-benefit analysis is insufficient as it fails to provide stakeholders with an analysis to comment on, nor is any analysis provided to meet the statutory requirement that must be fulfilled for the Proposal to be applied to EGCs. Indeed, we are concerned about the commitment of the PCAOB to a robust economic analysis as envisioned by the bipartisan JOBS Act.

Thank you for your consideration and the CCMC stands ready to assist in these efforts.

Sincerely,

Tom Quaadman