UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDINGS RULINGS
Release No. 763/April 30, 2013

ADMINISTRATIVE PROCEEDING
File Nos. 3-14872, 3-15116

In the Matter of		
BDO CHINA DAHUA CPA CO., LTD., ERNST & YOUNG HUA MING LLP, KPMG HUAZHEN (SPECIAL GENERAL PARTNERSHIP), DELOITTE TOUCHE TOHMATSU CERTIFIED PUBLIC ACCOUNTANTS LTD., and PRICEWATERHOUSECOOPERS ZHONG TIAN CPAs LIMITED	:	ORDER ON MOTIONS FOR SUMMARY DISPOSITION AS TO CERTAIN THRESHOLD ISSUES

The Securities and Exchange Commission (Commission) instituted these proceedings on May 9, 2012, and December 3, 2012, pursuant to Rule 102(e)(1)(iii) of the Commission's Rules of Practice (Commission Rule).[1] The two proceedings were consolidated on December 20, 2012, pursuant to Commission Rule 201(a). The Orders Instituting Proceedings (OIP) allege that Respondents willfully refused to provide the Commission with audit work papers and other documents relating to their audit or interim review work for certain clients, in violation of Section 106 of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) and the Securities Exchange Act of 1934 (Exchange Act).

Respondents each filed an Answer dated January 7, 2013. At a prehearing conference on January 9, 2013, Respondents were granted leave to file motions for summary disposition as to certain threshold issues. Respondents submitted their motions on February 1, 2013. Each Respondent filed its own motion for summary disposition and joined the motions filed by DTTC (Motion) and PwC Shanghai (PwC Shanghai Motion).[2] The Division of Enforcement (Division)

[1] The May 9, 2012, proceeding was instituted against Respondent Deloitte Touche Tohmatsu Certified Public Accountants Ltd. (n/k/a Deloitte Touche Tohmatsu CPA LLP) (DTTC) (DTTC Proceeding). The Commission instituted the December 3, 2012, proceeding (Omnibus Proceeding) against DTTC and Respondents BDO China Dahua CPA Co., Ltd. (BDO China), Ernst & Young Hua Ming LLP (EYHM), KPMG Huazhen (Special General Partnership) (KPMG Huazhen), and PricewaterhouseCoopers Zhong Tian CPAs Limited (PwC Shanghai).

[2] Respondents' individual motions primarily address the facts of Respondents' respective cases, while the Motion and PwC Shanghai Motion set forth the substance of Respondents' legal arguments.

filed its consolidated Opposition on February 22, 2013. DTTC and PwC Shanghai each submitted a Reply on March 8, 2013, which the other Respondents joined.[3] Accordingly, briefing is complete.

A motion for summary disposition may be granted if there is no genuine issue with regard to any material fact and the party making the motion is entitled to a summary disposition as a matter of law. 17 C.F.R. § 201.250(b). The facts of the pleadings of the party against whom the motion is made shall be taken as true, except as modified by stipulations or admissions made by that party, by uncontested affidavits, or by facts officially noticed pursuant to Commission Rule 323. 17 C.F.R. § 201.250(a).

I. Facts

The basic facts of this case are not in dispute. Respondents are foreign public accounting firms located in China that provide audit services throughout mainland China. Opposition, p. 1; Motion, p. 6. Each Respondent is a member of a global network of accounting firms. Motion, p. 6. In China, Respondents are supervised and regulated by the China Securities Regulatory Commission (CSRC) and China's Ministry of Finance. Id.

Respondents registered with the Public Company Accounting Oversight Board (Board) between 2004 and 2006, and have maintained their Board registrations and file annual reports. Opposition, p. 7; Motion, p. 7. Respondents declined to sign Exhibit 8.1 to the Board registration form, which requires registrants to consent to "cooperate in and comply with any request for . . . production of documents," and provided a legal opinion to the Board stating that Chinese law would prevent them from providing "full cooperation" with overseas document requests, but that they would cooperate to the extent permitted by Chinese law.[4] Motion, p. 7.

Respondents were engaged to conduct or participate in audits for certain clients in China.[5] In March 2011, in connection with a potential accounting fraud investigation, the

[3] This procedure was agreed to by the parties and authorized by my March 7, 2013, Order.

[4] The parties appear to agree that each Respondent declined to sign Exhibit 8.1, but disagree as to the legal effect of such refusal. Opposition, p. 7 n.3; Motion, p. 7. That dispute is irrelevant for purposes of the instant motions.

[5] BDO China audited the financial statements of Client A as identified in the Omnibus Proceeding (Omnibus Client [A]), for the fiscal years ending December 31, 2010, and 2011. BDO China Answer, p. 2. EYHM was engaged to audit the financial statements of Omnibus Client B for the fiscal year ended December 31, 2010, and of Omnibus Client C for the fiscal years ended September 30, 2010, and 2011. EYHM Answer, p. 3. KPMG Huazhen provided assistance to another firm in auditing the financial statements of Omnibus Client D for the fiscal year ended December 31, 2010, Omnibus Client E for the fiscal year ended December 31, 2010, and Omnibus Client F for the fiscal years ended December 31, 2008, 2009, and 2010. Omnibus Proceeding OIP, p. 2; KPMG Huazhen Answer, pp. 2-3. It appears that there may be a dispute as to the amount of assistance KPMG Huazhen provided, but that is irrelevant for purposes of the instant motions. Omnibus Proceeding OIP, p. 2; KPMG Huazhen Answer, pp. 2-3. PwC Shanghai was engaged to audit the financial statements of Omnibus Clients H and I for the fiscal

Commission sent DTTC a demand for audit work papers and related documents for one of its China-based clients, pursuant to Section 106 of Sarbanes-Oxley (Section 106). Opposition, p. 8; DTTC's Motion to Dismiss the Commission's OIP in the DTTC Proceeding, p. 5; Motion, p. 7. Between February and April 2012, the Commission sent Section 106 requests to each Respondent in the Omnibus Proceeding regarding certain of their China-based clients for a total of ten requests. Opposition, p. 8; Motion, pp. 7-8.

Respondents met with the CSRC and were informed that they were prohibited from producing audit work papers to the Commission without authorization. Motion, pp. 7-8. In October 2011, the CSRC issued a written directive reiterating that prohibition. Id. Respondents contend that there would be legal consequences, and potentially criminal sanctions, if they were to violate the CSRC's prohibition.[6] Id., p. 8. Respondents informed the Commission of the CSRC's prohibition. Id. Respondents did not provide the requested documents to the Commission, and these proceedings were instituted. Opposition, p. 9; Motion, p. 8.

II. Legal Issues

a. Service of the OIPs

Respondents first contend that these proceedings must be dismissed because the Commission failed to serve them with the OIPs. Motion, p. 9. The Commission included an express directive in each of the OIPs, providing for the manner in which the OIPs should be served. The OIP in the Omnibus Proceeding (Omnibus OIP) stated:

> Under the authority conferred by Rule 141(a)(2) of the Commission's Rules of Practice, 17 C.F.R. § 201.141(a)(2), this Order shall be served upon Respondents through the respective domestic registered public accounting firms or other United States agents that Respondents have designated for service under Section 106(d) of Sarbanes-Oxley, 15 U.S.C. § 7216(d), or by any other method reasonably calculated to give notice to a Respondent, provided that the other method of service used is not prohibited by the law of the foreign country in which the Respondent is located.

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year ended December 31, 2010. PwC Shanghai Answer, pp. 5-6. DTTC was engaged to audit the financial statements of Omnibus Client G for the fiscal year ended June 30, 2010. DTTC Answer to Omnibus Proceeding OIP, p. 5. DTTC performed audit services for Client A as identified in the DTTC Proceeding. DTTC's Motion to Dismiss the Commission's OIP in the DTTC Proceeding, p. 5.

[6] The Division argues that it is irrelevant to the present motions whether Chinese law prohibits Respondents from producing audit work papers and it "does not concede that compliance with the Section 106 demands 'would potentially expose Respondents to 'severe sanction in China.'" Opposition, p. 9 n.5.

Omnibus OIP, p. 6. The Omnibus OIP was sent by mail to Respondents' U.S. member firms, which Respondents had designated as their agents for service of process under Section 106(d). Opposition, pp. 9-10; Motion, pp. 2, 9 n.5.

The OIP in the DTTC proceeding (DTTC OIP) contained a different express directive regarding service. It stated: "[t]his Order shall be served forthwith upon [DTTC] through its designated agent." DTTC OIP, p. 4. The DTTC OIP was sent to Deloitte's U.S. member firm, which was designated as Deloitte's agent under Section 106(d).[7] DTTC's Motion to Dismiss the DTTC OIP, pp. 17-18.

Respondents argue that the Division's service of the OIPs in this manner violated Section 106(d) of Sarbanes-Oxley, Commission Rule 141, and Chinese law. Motion, pp. 9-11. Section 106(d), which the Commission cited when directing service in the Omnibus OIP, requires foreign public accounting firms that perform certain types of audit work to designate an agent in the United States "upon whom may be served any request by the Commission or the Board under [Section 106] or upon whom may be served any process, pleadings, or other papers in any action brought to enforce this section." 15 U.S.C. § 7216(d)(2). Respondents argue that they designated agents pursuant to Section 106(d) only for the two purposes expressly recognized in that section: service of Section 106 requests and actions to enforce them. Motion, pp. 9-10. Because service of the OIPs falls into neither of these categories, Respondents argue, service on their Section 106(d) designated agents was improper. Id., p. 10.

Respondents also assert that service of the OIPs was not done in accordance with the Commission's Rules of Practice because Commission Rule 141(a)(2)(iv), which provides for service upon persons in a foreign country, only allows service to be made by a "method reasonably calculated to give notice," if the "method of service used is not prohibited by the law of the foreign country." Id., pp. 9-10; see 17 C.F.R. § 201.141(a)(2)(iv). Respondents argue that service of the OIPs was not in accordance with Chinese law and offer the Declaration of James V. Feinerman (Feinerman Declaration), the James M. Morita Professor of Asian Legal Studies at Georgetown University Law Center, as evidence of Chinese law regarding service of process. Motion, p. 10; Motion, Exhibit A. Respondents argue that China is a party to the Hague Service Convention and therefore foreign service of process must be transmitted through the Chinese central authorities and the courts; attempts to serve parties in China without following these procedures, such as through the mail, are prohibited. Motion, pp. 10-11.

The Division argues, on the other hand, that it properly served the OIPs on Respondents by mailing them to Respondents' agents in the United States because the Commission expressly directed this method of service when it authorized the filing of the Omnibus OIP. Opposition, pp. 3-4, 11. The Division contends that it is irrelevant whether Respondents specifically designated their Section 106(d) agents to receive service of the OIPs because service was reasonably calculated to provide notice to Respondents in accordance with Commission Rule 141(a)(2)(iv). Id., p. 11. The Division argues that it is also irrelevant whether the method of service was prohibited by Chinese law because service on Respondents' agents occurred entirely within the United States, and that rule was not intended to "render service that occurs solely *within the U.S.* subject to the dictates of foreign law." Id., p. 4 (emphasis in original). The

[7] The most natural reading of "designated agent" in the DTTC OIP is that it means "agent under Section 106(d)."

Division contends that even if foreign-law restrictions did apply to service, Respondents have not established that the Division's method of service violates Chinese law. Id., p. 15. The Division attached the Declaration of Donald Clarke, a professor of law at the George Washington University Law School, as Exhibit 1 to its Motion, which addresses the issues raised by the Feinerman Declaration. Id.

It is important to recognize at the outset that Respondents received actual notice of these proceedings. The purpose of service is to provide actual notice of a proceeding; nonetheless, actual notice is not required to satisfy due process. See, e.g., Jones v. Flowers, 547 U.S. 220, 226 (2006) ("Due process does not require that a property owner receive actual notice before the government may take his property."). Where there has been actual notice, however, due process has been satisfied, at least in Commission administrative proceedings. See Dan Rapoport, Exchange Act Release No. 63744, 100 SEC Docket 37050, 37056-58 (Jan. 20, 2011) (finding that respondents' actual notice of the law judge's authorized service on him was sufficient and, therefore, he could not have reasonably believed that he could disregard the ruling and ignore the service effected on him), vacated and remanded on other grounds, 682 F.3d 98 (D.C. Cir. 2012); see also Hector Gallardo, Administrative Proceedings Rulings Release No. 694 (Mar. 6, 2012), 103 SEC Docket 51937, 51938 (denying motion to set aside default because respondent had received actual notice of proceeding); Alchemy Ventures, Inc., Administrative Proceedings Rulings Release No. 702 (Apr. 27, 2012), 103 SEC Docket 53938, 53940.

In the Omnibus Proceeding, the Commission directed that service of the OIP be effected in a particular way, "[u]nder the authority conferred by [Commission] Rule 141(a)(2)," and service was made in accordance with those instructions. Likewise, the DTTC OIP was served on DTTC's agent in accordance with the Commission's directive in that proceeding. As between the hearing officer and the Commission, the Commission's interpretation of its own Rules of Practice regarding service of OIPs ultimately governs. See 17 C.F.R. §§ 201.360, .411(a) (Commission Rules pertaining to the appeal process and the Commission's scope of review); 5 U.S.C. § 557(b) (stating, in pertinent part, that "[o]n appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision except as it may limit the issues on notice or by rule"); Steven Altman, Exchange Act Release No. 63665 (Jan. 6, 2011), 100 SEC Docket 36625, 36626 (stating that "[o]nce the Commission granted the parties' petitions for review, the initial decision ceased to have any force or effect," and "[o]n review, the Commission was vested with all of the powers which it would have had in making the initial decision"). Therefore, I lack the authority to determine whether such an express directive violates the Commission's Rules of Practice,[8] and Respondents' arguments regarding service must be rejected.

[8] Compare Gregory M. Dearlove, CPA, Initial Decision Release No. 315 (July 27, 2006), 88 SEC Docket 1808, 1872 ("[A]ny claim that the Rules of Practice are unconstitutional must be addressed to the Commission.") with Gregory M. Dearlove, CPA, Exchange Act Release No. 57244 (Jan. 31, 2008), 92 SEC Docket 1867, 1920 ("The law judge declined to rule on Dearlove's claim that the Rules of Practice are unconstitutional. He asserted that 'any claim that the Rules of Practice are unconstitutional must be addressed to the Commission.'"), petition for review denied, 573 F.3d 801 (D.C. Cir. 2009). In Dearlove, the Commission declined to remand

Finally, even if I had determined that service on Respondents was improper, dismissal would not be the remedy. See Alchemy Ventures, Inc., 103 SEC Docket at 53939. While insufficient service of process may be a ground for dismissal under the Federal Rules of Civil Procedure (FRCP), there is no analogous provision in the Commission's Rules of Practice. See id.; Fed. R. Civ. P. 12(b)(4), (5). Nor has the Commission established any deadline or presumptive time limit within which service must occur, in contrast to FRCP 4(m). In the absence of dismissal, the Division would be required to continue its efforts to serve Respondents for an unspecified period of time. Pursuing alternative methods of service in this case would be a waste of time and resources, particularly where Respondents have received actual notice of this proceeding.[9]

The Commission extended the deadline for filing an initial decision in the DTTC Proceeding until October 11, 2013. BDO China Dahua CPA Co., Ltd., Exchange Act Release No. 69094 (Mar. 8, 2013). Although DTTC contested the propriety of service in that proceeding, it agreed that it received the OIP on May 14, 2012.[10] Id.; see also Brief in Support of Joint Motion for Adjournment of Hearing and Prehearing Conference, Admin. Proc. File No. 3-14872 (May 24, 2012). Accordingly, the date of service of the DTTC OIP is deemed to be May 14, 2012.

The record is not entirely clear as to the dates of service in the Omnibus Proceeding. However, all Respondents were served between December 3, 2012, the date the Omnibus OIP was issued, and December 19, 2012, the date Administrative Law Judge Foelak issued an order postponing the hearing date in that proceeding. December 15, 2012, is 300 days before October 11, 2013. Accordingly, so that the due dates for the two Initial Decisions will be uniform between the DTTC and Omnibus Proceedings, the service date in the Omnibus Proceeding is deemed to be December 15, 2012.

b. Enforcement of Section 106 Requests in Federal Court

Second, Respondents argue that the OIPs must be dismissed because the Division has not enforced the Section 106 requests in federal court. Motion, p. 12. They contend that a federal court must first rule that the Section 106 requests are enforceable before the Commission can discipline Respondents for willfully refusing not to comply with them. Id., pp. 12, 18. Respondents assert that by bypassing judicial enforcement, the Division has violated separation

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the issue back to the administrative law judge, which is consistent with the administrative law judge's finding that he lacked authority to reach the issue of due process.

[9] The Division filed a March 25, 2013, Motion for Leave to File Supplemental Declaration of Donald Clarke (Motion for Leave) requesting leave to file an additional declaration relating to its analysis of Chinese law. Respondents submitted a joint response to the Motion for Leave on March 29, 2013, stating that they do not oppose the request, but arguing that the supplemental declaration does not add anything of substance to the briefing. I did not analyze Chinese law in reaching a conclusion and therefore the Division's Motion for Leave will be denied as moot.

[10] Because I am ruling in favor of the Division, I need not address the Division's argument that DTTC waived its objection to service in the DTTC proceeding.

of powers and due process, which could lead to an abuse of subpoena power by the Commission. Id., pp. 18-19. They analogize the Section 106 requests to the Commission's investigative subpoenas, which they argue must be enforced in federal court, and they point to language in Section 106(b)(1)(B) stating that the "'courts of the United States' have 'jurisdiction . . . for purposes of enforcement of any request.'" Id., pp. 12-14.

The Division argues that it is not seeking to enforce the Section 106 requests or seeking production of any documents. Opposition, p. 31. Instead, its purpose in instituting these proceedings was to "protect the integrity of the Commission's processes by imposing remedial relief in response to Respondents' failure to satisfy their statutory obligations under Section 106." Id., pp. 31-32. The Division argues that it is therefore irrelevant to this proceeding whether it could have sought to enforce the Section 106 requests in federal court. Id.

The Division was not required to obtain a ruling from a federal court regarding the enforceability of the Section 106 requests before instituting these proceedings. The Division is plainly not seeking to enforce the requests or obtain documents through these proceedings and therefore it is irrelevant whether such an enforcement action must be adjudicated by a federal court.[11] The Commission instead instituted these proceedings pursuant to Commission Rule 102(e)(1)(iii), which authorizes the Commission to censure or deny a person, temporarily or permanently, the privilege of practicing before it if the person is found to have willfully violated a provision of the federal securities laws. 17 C.F.R. § 201.102(e)(1)(iii). The purpose of Commission Rule 102(e)(1)(iii) is remedial and the rule is directed at protecting "the integrity of the Commission's own processes" and "the confidence of the investing public in the integrity of the financial reporting process." Marrie v. SEC, 374 F.3d 1196, 1200-01 (D.C. Cir. 2004); Steven Altman, Exchange Act Release No. 63306 (Nov. 10, 2010), 99 SEC Docket 34405, 34423 n.39, petition for review denied, 666 F.3d 1322 (D.C. Cir. 2011).[12]

[11] Because it is irrelevant to my conclusion, I do not express any views on the enforcement of Section 106(b) requests, including whether the requests must be enforced in federal court.

[12] The U.S. District Court for the District of Columbia's recent ruling in SEC v. Deloitte Touche Tohmatsu CPA Ltd., is consistent with my findings. No. 1:11-mc-00512 (D.D.C. Apr. 22, 2013) (order adopting magistrate judge's conclusion to grant petitioner's motion to lift the stay). In that case, the Commission moved for an order to show cause why DTTC should not be ordered to comply with an administrative subpoena served on DTTC in connection with a Commission investigation. The case was stayed to allow for negotiations between the Commission and the CSRC, and following the conclusion of those discussions, the Commission moved to lift the stay. DTTC requested that the stay remain in place "'pending the expeditious resolution of a parallel, consolidated, and profession-wide administrative proceeding,'" i.e., this proceeding. Id., p. 2. Although the subpoena at issue in the district court did not involve any of the clients implicated in this administrative proceeding, and dealt with the Commission's general subpoena powers found in Section 19(c) of the Securities Act of 1933 (Securities Act) and Section 21(b) of the Exchange Act, DTTC argued that there was significant overlap between the two proceedings. Id., p. 3-5. The district court rejected that argument, reasoning in part that "[t]he remedy sought in the Administrative Proceeding differs greatly from what is sought in this case. In the former, the [Commission] seeks to bar the five firms from 'appearing or practicing' before the

It may well be more common in Commission Rule 102(e) cases for a respondent to have already received a judicial determination that it has violated the securities laws, leaving me to determine whether respondent has any defenses and the appropriate sanction to impose. However, Commission Rule 102(e)(1)(iii) plainly permits me to adjudicate the threshold question of whether a respondent has violated the securities laws. See, e.g., Philip L. Pascale, Securities Act Release No. 8555 (Mar. 18, 2005), 85 SEC Docket 2; Steven Altman, 99 SEC Docket 34405; Robert W. Armstrong, Exchange Act Release No. 51920 (June 24, 2005), 85 SEC Docket 3011. With respect to the alleged violations in this case, Section 106(b)(1) provides that foreign public accounting firms that meet certain conditions shall produce audit work papers and other related documents to the Commission or the Board upon request. 15 U.S.C. § 7216(b)(1). Section 106(e) makes a "willful refusal to comply" with such a request a violation of Sarbanes-Oxley. Id. § 7216(e). Taken together, these two provisions provide a basis for me to determine whether Respondents have willfully violated the securities laws for purposes of Commission Rule 102(e)(1)(iii).

It is not the case, as Respondents appear to contend, that they will be "subject to sanction without any judicial process." DTTC Reply, p. 10. The current proceedings constitute the judicial process that Respondents are entitled to, and the burden is placed on the Division to prove that Respondents willfully violated the federal securities laws. See 17 C.F.R. § 201.102(e)(1) ("The Commission may censure a person or deny . . . the privilege of appearing or practicing before it . . . after notice and opportunity for hearing."). Respondents have identified no meritorious no constitutional issues presented by my adjudication of this case. See Gregory M. Dearlove, CPA, 92 SEC Docket at 1926 (finding, in response to a request for a postponement, that "the process provided" to respondent accountant in a Section 102(e)(1)(iv) case to be adequate under Mathews v. Eldridge, 424 U.S. 319 (1976)).

Respondents cite several federal court cases to support their contention that because Congress enacted Section 106 "against the backdrop of a well-developed body of law protecting foreign entities from being punished for their inability to produce documents without violating the laws of their home country," Congress therefore intended to include similar procedural protections in Section 106. Motion, pp. 14-15. These cases are inapposite. The ability to practice or appear before the Commission is a privilege and Congress has codified the Commission's authority to deny that privilege to any person who is found to have willfully violated the federal securities laws. See 17 C.F.R. § 201.102(e)(1)(iii) (codified at 15 U.S.C. § 78d-3). The purpose of these proceedings is to determine whether Respondents have abided by the rules set forth by the Commission and Congress as a condition to practicing or appearing before the Commission, and none of the cases cited by Respondents present similar circumstances.

Commission; in this case, the [Commission] merely seeks production of documents." Id., p. 7. The district court also rejected DTTC's concern that there may be inconsistent rulings on the application of Chinese law, reasoning that "the final decisions emanating from both the [Commission] [in the administrative proceeding] and this Court would both be resolved by the same decision-maker, our Court of Appeals." Id., p. 6.

Respondents argue that bypassing judicial enforcement will result in domestic firms being treated differently than foreign firms because domestic firms are not subject to sanction for failing to produce documents without a federal court first ruling on the enforceability of the request. Motion, pp. 17-18; DTTC Reply, pp. 13-14. They contend that this result is "flatly inconsistent" with Section 106(a)(1)'s statement that foreign firms are subject to Sarbanes-Oxley and the rules of the Board and the Commission "in the same manner and to the same extent" as domestic firms. Motion, pp. 17-18; DTTC Reply, pp. 13-14; see 15 U.S.C. § 7216(a)(1).

Respondents' argument is not persuasive. Section 106(b)(2) requires "*[a]ny registered public accounting firm* that relies, in whole or in part, on the work of a foreign public accounting firm in issuing an audit report, performing audit work, or conducting an interim review" to produce the audit work papers of the foreign public accounting firm upon request. 15 U.S.C. § 7216(b)(2) (emphasis added). Therefore, domestic firms can similarly be charged with a violation of Sarbanes-Oxley if they willfully refuse to comply with a Section 106 request, even in the absence of judicial enforcement. See id. § 7216(b)(2), (e).

In addition, the Board has enacted Rule 5103(a) which authorizes it to issue "a demand for the production of audit work papers or any other document or information in the possession of a registered public accounting firm . . . wherever domiciled, that the Board or its staff considers relevant or material to [a Board] investigation."[13] If a registered public accounting firm refuses to produce the documents, the Board may suspend or revoke the registration of the registered public accounting firm or impose other sanctions. See 15 U.S.C. § 7215(b)(3). Furthermore, Section 3(b)(1) of Sarbanes-Oxley makes a violation of a Board Rule also a violation of the Exchange Act, and therefore the Commission may choose to institute proceedings pursuant to Commission Rule 102(e)(1)(iii) against a domestic registered public accounting firm if it determines that the firm has willfully violated a Board Rule, and therefore violated the Exchange Act. 15 U.S.C. §§ 78d-3(a)(3), 7202(b).

Next, Respondents argue that the Division's decision not to seek judicial enforcement of the Section 106 requests is arbitrary and capricious because it cannot be reconciled with the Commission's existing practices. Motion, p. 19. Respondents contend that Section 106 requests are "effectively equivalent in every relevant respect" to investigative subpoenas, and cite to a provision of the Division's publicly-available Enforcement Manual, which provides, "'[i]f a person or entity refuses to comply with a subpoena . . ., the Commission may file a subpoena enforcement action in federal district court.'" Id., p. 20. Respondents assert that the Commission represented to them that sanctions for noncompliance with Section 106 would not be imposed until a federal court enforced the requests, and offer Commission Form 1662, which was sent to Respondents with the Section 106 requests, as evidence of this representation. Commission Form 1662 states:

> If you fail to comply with the subpoena, the Commission may seek a court order requiring you to do so. If such an order is obtained

[13] Section 105(b)(2)(B) of Sarbanes-Oxley permits the Board, by rule, to "require the production of audit work papers and any other document or information in the possession of a registered public accounting firm or any associated person thereof, wherever domiciled, that the Board considers relevant or material to the investigation . . . ." 15 U.S.C. § 7215(b)(2)(B).

> and you thereafter fail to supply the information, you may be subject to civil and/or criminal sanctions for contempt of court.

Id., p. 20.

Respondents' arguments are not convincing. They have not provided any evidence, beyond mere argument, that Section 106 requests are "effectively equivalent" to investigative subpoenas and therefore any Commission procedures related to investigative subpoenas are irrelevant. See Motion, pp. 13-14. Unlike investigative subpoenas, a Section 106 request "seeks a statutorily-identified category of documents from a statutorily-identified recipient" and the statute specifically provides that a "'willful refusal to comply'" with any request by the Commission or the Board is deemed a violation of Sarbanes-Oxley. See Opposition, pp. 43-44.

While the Division admits that Commission Form 1662 does not apply to Section 106 requests, Respondents have suffered no prejudice from receiving this form. Respondents were not misled into believing that their failure to comply with a Section 106 request might lead to an enforcement action in federal court because, in fact, it did not. The Commission's authority to discipline accountants pursuant to Commission Rule 102(e) is well established, and Respondents have been on notice since the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) in July 2010 that a willful refusal to comply with a Commission request pursuant to Section 106 would constitute a violation of Sarbanes-Oxley. See Touche Ross & Co. v. SEC, 609 F.2d 570 (2d. Cir. 1979) (decided under the predecessor to Rule 102(e)); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929J, 124 Stat. 1376, 1859 (2010) (codified as amended at 15 U.S.C. § 7216(e)).

Commission Form 1662 simply does not speak to disciplinary actions that the Commission may impose for a willful refusal to comply with the federal securities laws, and therefore it does not address any Commission practices or procedures relevant to a Commission Rule 102(e)(1)(iii) proceeding. Moreover, Respondents do not dispute that they received Wells Notices months before the institution of these proceedings warning them of the possibility of these disciplinary proceedings and the imposition of administrative sanctions. See Opposition, p. 45.

c. Applicability of Section 106(a) to These Proceedings

Finally, Respondents argue that the Omnibus Proceeding must be dismissed, at least in part, because they did not "prepare" or "furnish" an audit report for some of the clients identified in the OIP.[14] PwC Shanghai Motion, pp. 8-9. They contend that Section 106(a), which provides

[14] Specifically, DTTC and PwC Shanghai argue that the Omnibus OIP should be dismissed entirely as to them because they did not prepare or furnish audit reports for Omnibus Clients G, and H and I, respectively. PwC Shanghai Motion, p. 9; PwC Shanghai Answer, pp. 5-6; Motion, p. 1 n.1; DTTC Answer, p. 18. EYHM and KPMG Huazhen argue that the Omnibus OIP should be dismissed partially as to them because they did not prepare or furnish audit reports for Omnibus Clients B and E, respectively. EYHM Answer, p. 12; EYHM Motion, p. 11; KPMG Huazhen Motion, pp. 4-5, 8 ("the OIP must be dismissed as to [Omnibus] Client E because Section 106 does not apply since neither KPMG Huazhen nor its affiliate prepared or furnished an audit report").

that a foreign public accounting firm that "prepares or furnishes an audit report with respect to any issuer" is subject to Sarbanes-Oxley, serves a gatekeeping function, and therefore Section 106(b) requests cannot be made for those clients for whom the requirements of Section 106(a) are not met. Id. Respondents argue that Section 106(a)'s gatekeeping function is supported by its title, "Applicability to Certain Foreign Firms," and is confirmed by the organization of Section 106, which begins with provisions of broad applicability and ends with provisions of specific applicability. Id., pp. 9-10.

Respondents argue that Section 106(b) cannot be untethered from the requirements of Section 106(a) because it could result in a foreign firm having to produce documents to the Commission where the firm is not registered with the Board, the client has no connection to the United States, and the audit was not conducted under Generally Accepted Auditing Standards. Id., p. 11. Respondents emphasize that the purpose of Section 106(b) is to "protect the ability of U.S. investors to rely on audit reports," and imposing the requirements of that section when no audit report has been furnished or prepared does not serve that policy goal. Id., pp. 12-15.

The Division takes a different view. It asserts that Section 106(b) applies to all foreign public accounting firms, and not just registered firms, that meet one of the four triggering conditions specified by that provision ("performs material services upon which a registered public accounting firm relies in the conduct of an audit or interim review," "issues an audit report," "performs audit work," or "conducts interim reviews") for each of its issuer-clients, regardless of whether the firm also prepares or furnishes an audit report under Section 106(a). Opposition, p. 20. The Division argues that Congress deliberately expanded Section 106(b) and added the new triggering conditions when it amended Section 106 as part of Dodd-Frank in 2010 and that the statute therefore contemplates the production of documents in the absence of an audit report. Id., pp. 20-21. To find otherwise, the Division argues, would read the triggering conditions "performs audit work," "conducts interim reviews," and "performs material services" entirely out of the statute. Id.

The Division asserts that construing Section 106(b) as a stand-alone provision is not untenable because it applies only to documents related to U.S. issuers by virtue of its use of the term "audit." Id., pp. 23-24. Because an "audit" is defined as an examination of an "issuer," and "issuer" is further defined as an entity that has securities registered with the Commission, is required to file reports under Section 15(d) of the Exchange Act, or that has filed and not withdrawn a registration statement under the Securities Act that is not yet effective, Section 106(b) plainly confines its reach to documents related to U.S. issuers. Id. The Division acknowledges that the term "interim review" is not defined by Sarbanes-Oxley, but argues that "it is clear from the context that the provision relates to an interim review of an issuer" since the Commission can only request work papers from foreign firms relating to audits of U.S. issuers. Id., p. 24 n.12.

The Division does not have to show that Respondents prepared or furnished an audit report for the clients identified in the OIPs as a prerequisite to this proceeding or as a threshold requirement to their requests under Section 106(b). I base this conclusion on a careful reading of Section 106.

Section 106(b)(1), which is entitled "Production by Foreign Firms," provides:

> If a foreign public accounting firm performs material services upon which a registered public accounting firm relies in the conduct of an audit or interim review, issues an audit report, performs audit work, or conducts interim reviews, the foreign public accounting firm shall – (A) produce the audit work papers of the foreign public accounting firm and all other documents of the firm related to any such audit work or interim review to the Commission or the Board, upon request . . .

15 U.S.C. § 7216(b)(1). By its express terms, Section 106(b)(1) authorizes the Commission to request audit work papers and related documents from a foreign public accounting firm that, among other activities, "performs audit work" or "conducts interim reviews." Section 106(b)(1) contains no requirement that the firm prepare or furnish an audit report in connection with the audit work or interim review. Indeed, it would render much of Section 106(b)(1) meaningless if work papers could only be requested in instances where the audit work or interim review was done in connection with the preparation or furnishing of an audit report. Therefore, if such a requirement does exist, it must be contained in some other provision.

Respondents contend that Section 106(a)(1) sets forth this threshold requirement, however, there is nothing in Section 106(a)(1) that contradicts or overcomes the express terms of Section 106(b)(1). Section 106(a), which is entitled "Applicability to Certain Foreign Firms," only addresses the authority of the Board and the jurisdiction of U.S. Courts. It sets forth the general rule that any foreign public accounting firm that "prepares or furnishes an audit report with respect to any issuer" shall be subject to Sarbanes-Oxley and the rules of the Board and the Commission, in the same manner and to the same extent as a U.S.-based public accounting firm, even without being registered with the Board. It also contains a limitation on jurisdiction, stating that registration pursuant to Section 102 of Sarbanes-Oxley by itself is not sufficient to subject a foreign public accounting firm to U.S. jurisdiction, other than with respect to controversies between the firm and the Board. There is nothing in Section 106(a)(1) to indicate Section 106(a) was intended to serve as a "gatekeeper" or "prerequisite" for Section 106(b).[15] Respondents' assertions that the title of Section 106(a), "Applicability to Certain Foreign Firms," and the structure of Section 106, moving from general applicability to specific applicability, confirms Section 106(a)'s role as a gatekeeper, are simply not persuasive and do not overcome the plain meaning of the statute.

Nor is there any support for Respondents' argument in any other provision of Section 106. Indeed, Section 106(d)(2) repeats verbatim much of the language used in Section 106(b)(1). It provides in part that:

[15] Section 106(a)(2) provides the Board with discretion to treat foreign public accounting firms that do not issue audit reports, but nonetheless play a substantial role in the preparation and furnishing of audit reports, as public accounting firms for purposes of registration. Presumably, such a "substantial role" would include engaging in activities triggering Section 106(b), such as performing audit work and conducting interim reviews. There is nothing in Section 106(a)(2) to indicate Section 106(a) was intended to set forth threshold requirements for purposes of Section 106(b).

> Any foreign public accounting firm that performs material services upon which a registered public accounting firm relies in the conduct of an audit or interim review, issues an audit report, performs audit work, or, performs interim reviews, shall designate to the Commission or the Board an agent in the United States upon whom may be served any request by the Commission or the Board under this section . . . .

15 U.S.C. § 7216(d)(2). Just as in Section 106(b), there is no suggestion in Section 106(d) that its applicability is contingent upon the foreign public accounting firm meeting the requirements set forth in Section 106(a).

In their Reply brief, Respondents admit that Dodd-Frank expanded the scope of Section 106(b); however, their interpretation of this expansion is illogical. PwC Shanghai Reply, p. 3. Their position appears to be that, prior to Dodd-Frank, a Section 106(b)(1) request concerning a particular client was valid only if the foreign public accounting firm prepared or furnished an audit report for that client pursuant to Section 106(a), as well as "issued" an audit report for that client as required by pre-Dodd-Frank Section 106(b).[16] Id. Following Dodd-Frank, Respondents contend that a Section 106(b)(1) request may be valid if the foreign public accounting firm performed audit work, or met one of that Section's three other triggering conditions, if the foreign firm also prepared or furnished an audit report for that client.[17] Id.

Respondents' explanation allows for no meaningful expansion of Section 106(b). The only additional authority the Commission and the Board gain under Respondents' construction of the Dodd-Frank amendments is that they are able to request documents from foreign public accounting firms that have prepared or furnished an audit report, but have not issued it yet. Under Respondents' construction, it does not matter whether the firm has performed audit work or conducted an interim review, because Section 106(b) is still not applicable until the firm, at minimum, prepared an audit report for purposes of Section 106(a). It renders the Dodd-Frank amendments essentially meaningless. While Respondents argue that the primary change Dodd-Frank effected on Section 106(b) was to expand the production requirement from just "audit work papers" to "audit work papers . . . and all other documents," that argument is unpersuasive in light of the clear import of the Dodd-Frank amendments to Section 106(b). See PwC Shanghai Reply, p. 3 n.5.

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[16] Prior to Dodd-Frank, Section 106(b)(1) provided: "[i]f a foreign public accounting firm *issues an opinion* or otherwise performs material services upon which a registered public accounting firm relies in issuing all or part of any audit report or any opinion contained in an audit report, that foreign public accounting firm shall be deemed to have consented – (A) to produce its audit workpapers for the Board or the Commission in connection with any investigation by either body with respect to that audit report." 15 U.S.C. § 7216(b)(1) (emphasis added).

[17] Respondents acknowledge that both before and after Dodd-Frank, Section 106(b) covered situations where a foreign firm "performs material services upon which a registered public accounting firm relies," but their analysis does not address that issue. PwC Shanghai Reply, p. 3.

Respondents claim that "untethering" Section 106(b) from Section 106(a)'s requirements could lead to the Commission requesting documents relating to a firm's private foreign clients, which are not U.S. issuers, and have no connection with the United States. In these proceedings, however, Respondents do not dispute that all of the Section 106 requests relate to clients that were issuers of securities registered in the U.S. The full scope of the term "issuer," within the context of Section 106, is not properly before me and I need not reach the question.

I also reject Respondents' theory that the Division's construction of Section 106(b) would render subsection 106(b)(2) unnecessary. Section 106(b)(2) provides:

> Any registered public accounting firm that relies, in whole or in part, on the work of a foreign public accounting firm in issuing an audit report, performing audit work, or conducting an interim review, shall – (A) produce the audit work papers of the foreign public accounting firm and all other documents related to any such work in response to a request for production by the Commission or the Board; and (B) secure the agreement of any foreign public accounting firm to such production, as a condition of the reliance by the registered public accounting firm on the work of that foreign public accounting firm.

15 U.S.C. § 7216(b)(2). Respondents argue that it is their understanding that Section 106(b)(2) applies where a foreign firm has not prepared or furnished an audit report, and in this circumstance, the Commission or Board may seek production of the foreign firm's work papers from a registered firm that relies on the work of the firm. PwC Shanghai Reply, p. 5. They argue that under the Division's interpretation, Section 106(b)(2) is superfluous because Section 106(b)(1) would already cover the circumstances in which a foreign public accounting firm has not prepared or furnished an audit report and therefore there would be no need to request audit work papers through a registered public accounting firm. Id.

Sections 106(b)(1) and (b)(2) create two distinct alternatives by which the Board or the Commission can request documents from accounting firms. The former authorizes demands to a "foreign public accounting firm," which, according to the definition provided by Sarbanes-Oxley, does not necessarily have to be registered with the Board, while the latter authorizes requests to a "registered public accounting firm."[18] See 15 U.S.C. § 7216(g) (defining "foreign public accounting firm" as a "public accounting firm that is organized and operates under the laws of a foreign government or political subdivision thereof"); 15 U.S.C. § 7201(a)(12) (defining "registered public accounting firm" as a "public accounting firm registered with the Board in accordance with this Act"). Section 106(b)(2) is not superfluous, it simply creates an alternative by which the registered public accounting firm can be held accountable for the work of a foreign public accounting firm that it relies upon, and creates another means by which the Commission or the Board can request documents.

Respondents contend that because the policy underlying Section 106 is to ensure that U.S. investors can rely on publicly-filed audit reports, requiring foreign public accounting firms

[18] However, there is nothing in the statute indicating that a "foreign public accounting firm" cannot be registered with the Board. See 15 U.S.C. § 7216(g).

to produce documents where no audit report has been prepared or furnished is inconsistent with that goal. PwC Shanghai Motion, pp. 2, 10-11, 12-15. As the Division notes, however, Respondents read the applicable policy considerations far too narrowly. See Opposition, pp. 27-30. In addition to combatting fraud in audit reports, Section 106(b) assists the Commission in carrying out its statutory oversight role over auditors and combatting fraud generally. See id., pp. 28-29. Specifically, the Division points out that access to audit work papers allows the Commission to determine whether an auditor has complied with the standards of conduct set forth in Exchange Act Section 10A, address fraud that may preclude or delay the filing of an audit report, and assist the Commission in determining the accuracy of previous audit reports prepared by the issuer. Id. The fact that none of these policies may be implicated in the case of these specific Respondents is irrelevant. See PwC Shanghai Reply, p. 1. Respondents do not dispute that they were engaged to audit the financial statements of issuers of securities registered in the U.S., or in the case of KPMG Huazhen, provided some level of assistance to another firm in auditing financial statements, and that they performed certain audit work in the course of those engagements. Imposing the requirements of Section 106(b) on Respondents is not only consistent with the plain language of the statute, but also the policy considerations of Sarbanes-Oxley and the federal securities laws.

d. Motion to Dismiss the DTTC Proceeding

DTTC filed a June 20, 2012, Motion to Dismiss the Commission's OIP in the DTTC Proceeding (Motion to Dismiss), and the Division submitted a Memorandum of Law in Opposition on July 5, 2012. Shortly thereafter, the DTTC proceeding was postponed, and the due date for the filing of DTTC's reply brief was extended several times, in light of discussions between the Commission and CSRC, the filing of the Omnibus Proceeding, and the consolidation of the DTTC and Omnibus Proceedings. As a result, no reply brief was ever filed and DTTC's Motion to Dismiss remains pending.

DTTC's primary arguments in support of dismissal, that service of the OIP was improper and that the Division has improperly bypassed judicial enforcement of the Section 106 requests, were raised in the Omnibus Proceeding and are addressed by this Order. DTTC also argued that the proceeding should be dismissed because it was being singled out for "differential treatment for which [the Commission] has proffered no rational basis," and that the proceeding "imperil[ed] DTTC's right to equal protection." Motion to Dismiss, p. 17. DTTC has only offered argument, and no evidence, in support of this claim, and given that the Omnibus Proceeding was instituted against four additional public accounting firms in addition to DTTC, this argument is rejected.

ORDER

It is ORDERED that Respondents' motions for summary disposition are DENIED.

It is FURTHER ORDERED that the Division's Motion for Leave to File Supplemental Declaration of Donald Clarke is DENIED AS MOOT.

It is FURTHER ORDERED that Respondent DTTC's June 20, 2012, Motion to Dismiss the Commission's OIP in the DTTC Proceeding is DENIED.

It is FURTHER ORDERED that the parties shall confer and inform this Office of at least two suggested dates and times for a prehearing conference.

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Cameron Elliot
Administrative Law Judge