ADMINISTRATIVE PROCEEDING
FILE NOS. 3-14872, 3-15116

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

RECEIVED
SEP 20 2013
OFFICE OF THE SECRETARY

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.;
PricewaterhouseCoopers Zhong Tian CPAs Limited

Respondents.

The Honorable Cameron Elliot,
Administrative Law Judge

RESPONDENTS' POST-HEARING REPLY BRIEF

Date: September 20, 2013

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

RULES

REGULATIONS

I. INTRODUCTION AND SUMMARY OF ARGUMENT

The Division of Enforcement's (the "Division") Post-Hearing Brief does not provide a legal or factual basis for this unprecedented proceeding. The Division is attempting to use this Rule 102(e) proceeding to terminate the ability of all the major audit firms in an entire country to issue audit opinions on U.S. listed companies. This draconian result would represent an extraordinary departure from the Commission's longstanding policy of using cooperative mechanisms for obtaining information abroad, and would place billions of dollars of investment capital at risk, block Chinese companies from entering the U.S. capital markets, and have major ripple effects throughout the world economy. The Division seeks this outcome despite the fact that Respondents have acted in good faith and (like dozens of other accounting firms around the world) are simply unable to produce documents directly to the SEC without violating the laws of their home country and thereby risking severe sanctions there. Perhaps most puzzlingly, the Division continues to press for this result despite the fact that the regulator-to-regulator channel for obtaining the requested documents is plainly open—the very thing the Division itself has repeatedly stated would render this proceeding unnecessary altogether.[1]

The Division's position in this proceeding lacks legal and factual support. The applicable Congressional legislation places a heavy burden on the Division to prove that Respondents

---

[1] Just this month, following multiple productions by the CSRC and despite the Division's steadfast insistence that the CSRC is not a viable gateway for the production of documents, the Division reversed course and [redacted] As discussed *infra*, the Division's decision to [redacted] confirms that the CSRC is indeed a viable gateway and an alternative means for the production of workpapers—which likewise underscores the inappropriateness of this action and the Division's request for sanctions against Respondents. [redacted]

"willfully refused to comply" with the SEC requests—which it has not met. The Division continues to advocate a legal standard that is inconsistent with the distinctive language and intent of Section 106, as well as core principles of statutory construction. The Division's factual arguments distort the evidentiary record, or otherwise ignore crucial evidence altogether. And it seeks dramatic sanctions without justifying their undisputed adverse consequences.

On the law, the Division presses for an erroneous legal standard under which Chinese legal impediments are "irrelevant"[2] and Section 106(e) is satisfied simply because "in each instance" Respondents stated their position "in writing." ENF Post-Hearing Brief at 68. But the Division has failed to address the key interpretive arguments raised by Respondents, or otherwise demonstrate that the "willful refusal" standard—which appears nowhere else in the securities laws—can be satisfied without proof of bad faith or conscious wrongdoing: (1) the Division asks this Court to ignore some words in the statute (*i.e.*, focus solely on "willful" rather than "willful refusal"), to abandon the clear and ordinary meaning of others (*i.e.*, read "refusal" to mean "failure"), and to adopt a construction that renders Section 106(e)'s "willful refusal" standard superfluous in its entirety (*i.e.*, interpret Section 106(e)'s "willful refusal" as identical to Rule 102(e)(1)(iii)'s "willful violation"); (2) unlike Congress (which wrote Section 106 with appropriate sensitivity to foreign sovereign interests), the Division refuses to acknowledge the international consequences of what it seeks here, and contends that principles of international comity do not even apply; and (3) the Division resorts to policy arguments that should be directed to Congress, and that ignore the careful balance that Congress intentionally struck when it passed Dodd-Frank. Based on its language, structure, legislative history, and on principles of statutory construction, Section 106(e) requires the

---

[2] *See* ENF Post-Hearing Brief at 3 ("The exact nature of the constraints imposed on Respondents under Chinese law . . . [is] irrelevant to the willfulness inquiry under Section 106.").

Division to prove bad faith or conscious wrongdoing, and at a minimum provides a defense where, as here, the record establishes that Respondents have acted in good faith but are nonetheless precluded from producing the requested documents under foreign law.

On the facts, despite advocating an extreme, erroneous legal standard that could be satisfied by the most limited volitional action, the Division tellingly devotes most of its brief to arguing about "factual bases" that it believes support a finding of liability. But its factual arguments ignore the actual evidence and proceed as if the hearing never occurred.

First, the Division argues that Respondents' mere registration with the PCAOB and subsequent audit work for U.S. issuers is sufficient to establish a "willful refusal." But the record shows that Respondents have consistently and transparently identified potential legal impediments, have shared the PCAOB's belief that they would be able to produce documents to U.S. regulators through Chinese regulators (and, as recent developments show, they were right), and have repeatedly attempted to facilitate the production of the requested documents. The Division is just wrong that these facts—and Respondents' entry into U.S. markets alone—permit a finding of "willful refusal." Compliance with the notice and disclosure procedures established by the PCAOB and the Commission for registration (and the PCAOB's acceptance of the registration applications despite the full disclosure of the foreign law impediments) cannot constitute bad faith. The U.S. Supreme Court and other federal courts have routinely found that foreign parties that availed themselves of U.S. markets, but nonetheless could not produce documents without violating their home country law, acted in good faith and their noncompliance was due to inability and not willfulness. *Société Internationale pour Participations Industrielles et Commerciales v. Rogers*, 357 U.S. 197, 211-212 (1958); *In re Sealed Case*, 825 F.2d 494, 498-99 (D.C. Cir. 1987); *see infra* pp. 30-31. And these courts have

done so irrespective of whether the foreign parties had advance knowledge of the potential impediments. *Id.* Even the Division's own authority makes clear that something more is needed to show bad faith. Yet nothing is available on this evidentiary record.

Second, the Division ignores the substantial evidence showing Respondents' good faith efforts to facilitate production of the documents and otherwise cooperate with the SEC. The various Respondents took an array of actions, all of which show that they intended to cooperate and adhere to the laws of both countries. Those Respondents who were asked promptly produced documents to the CSRC for delivery to the SEC or the PCAOB; other Respondents offered to do so. Respondents sought reconsideration of the CSRC's refusal to allow direct production and efforts to seek clearance from China's State Secrets Bureau ("SSB") and State Archives Administration ("SAA") were rejected. Some Respondents produced non-restricted documents, and made their personnel available for telephonic interviews. All of the Respondents repeatedly met with and asked the CSRC for permission to provide the documents to the SEC. In short, the evidence shows that Respondents took many steps to facilitate production. This evidence is inconsistent with bad faith, and it is telling that the Division ignores this evidence altogether.

Third, the evidence adduced at the hearing has forced the Division to abandon one of its principal arguments against Respondents—namely, that Chinese law did not impede Respondents from unilaterally producing the requested documents directly to the Division. At the hearing, the Division's own expert (1) conceded that Chinese law does prohibit such productions (disagreeing only about which Chinese authorities must be consulted according to written Chinese law), (2) opined that the CSRC has the authority to issue written and oral directives that would prevent Respondents from producing documents, and (3) chose to ignore

the evidence indicating that this is exactly what has occurred. Respondents' Post-Hearing Brief at 29-31. In response, the Division's Post-Hearing Brief just repeats the Division's pre-hearing arguments about the written law, but those arguments are based on an analysis its own expert concedes is insufficient, and is otherwise belied by the evidence. ENF Post-Hearing Brief at 84-95. The Division also tries to cast doubt on the CSRC's and MOF's oral directives, *id.*, but the evidence establishing those directives—including compelling and credible witness testimony that withstood a week of cross-examination by the Division and was corroborated by multiple written documents—is indisputable. Ultimately, the Division itself now repeatedly contends that Chinese law forbade Respondents from producing the requested documents directly to the SEC without prior Chinese government approval.[3]

With its prior position on Chinese law thus refuted, the Division now tries to diminish the significance of this critical turn of events by attempting to characterize—for the first time in this proceeding—the relevant Chinese laws as "blocking statutes." This argument is a non-sequitur: whatever the Chinese government's rationale in passing these laws, Respondents have no choice but to comply with them or face severe punishment for disobeying them. Further, the relevant Chinese laws simply are not blocking statutes. For example, Chinese state secrets laws establish generally applicable protections for certain information that apply both within China and to the transfer of information outside China. And, to the extent that Chinese regulators have now established mechanisms to funnel the production of audit workpapers to foreign regulators through customary regulator-to-regulator channels—just like a multitude of other countries

---

[3] ENF Post-Hearing Brief at 74 ("Chinese legal regime that was designated to block, and did in fact block, the SEC's access to audit workpapers"); *id.* at 80 ("Because audit workpapers are considered archives under Chinese Archives Law, even copies generally cannot be transferred outside of Mainland China without authorization by the Chinese government."); *id.* at 84 ("foreign legal regime that effectuated a total blockade against the SEC's receipt of documents").

around the world—any interim measures to prevent the leakage of state secrets are not blocking statutes.

Similarly, the Division is unable to refute the evidence that principles of international comity render the Section 106 requests unenforceable in the first instance. Most critically, the Division's position that it has "no alternative means of obtaining documents sought by the requests," ENF Post-Hearing Brief at 101-105, has been refuted by recent developments, including the CSRC's voluminous production of the Longtop audit workpapers and other documents [redacted] in July 2013, [redacted], and ultimately the SEC's own decision earlier this month [redacted]. Less than two weeks prior to [redacted], the Division had argued that any further attempts to work through the CSRC would be "futile" and amount to nothing but the Division "spinning its wheels"—a position that has been at the heart of the Division's case. ENF Post-Hearing Brief at 41, 105. Clearly, the recent developments have caused the Division to change its view on the viability of the CSRC as an alternative means—whether it says so in this proceeding or not. The Section 106 requests at issue here simply are not enforceable (under the statute or under principles of international comity) when such a viable alternate means of production is available, and an analysis of the other comity factors weighs against enforcement as well. Ultimately, the Division tries to ignore the overwhelming evidence that alternative means of production exist by arguing that well-established principles of international comity do not apply here, but it can offer no valid basis for such an approach.

Nor can the Division show that, before this case of first impression, Respondents had a clear legal obligation under the "willful refusal" standard of Section 106 to violate Chinese law

in order to respond directly to the Division's requests, and therefore there can be no finding of willfulness under the Supreme Court's decision in *Safeco Insurance Co. of America v. Burr*, 551 U.S. 47 (2007). In response to this critical issue, the Division attempts to distinguish *Safeco*, ENF Post-Hearing Brief at 108-110, but fails to address the central point: it is not possible to find bad faith or even mere willfulness where U.S. law does not clearly and unambiguously require Respondents to violate Chinese law in these circumstances.

As to sanctions, the Division's proposed sanctions are manifestly not in the public interest: they would inflict substantial and unnecessary harm on Respondents, their issuer clients, and investors. At a time when documents are starting to flow from the CSRC, the proposed sanctions would both cause as many as [redacted] issuers with securities traded in the United States to lose their chosen auditors (and any replacements would face the same Chinese legal impediments at issue here) and threaten to disrupt the further flow of documents. Further, the Division's proposed sanctions would be fundamentally unfair and violate long-established Commission policies and practices. And they are unwarranted under the specific factors the Commission traditionally considers.

II. THE DIVISION HAS FAILED TO DEMONSTRATE THAT THE "WILLFUL REFUSAL" STANDARD IS SATISFIED BY MERE VOLITIONAL CONDUCT

A. The Division Continues to Ignore the Relevant Statutory Language, Structure, and Intent of Section 106.

As demonstrated in Respondents' Post-Hearing Brief, Section 106's "willful refusal" standard is unique in the federal securities laws. The plain language, structure and intent of Section 106, as well as the principle of prescriptive comity, do not permit a construction of "willful refusal" under which it is a violation of federal law for foreign firms to comply in good

faith with laws of their home country. Instead, the Division must demonstrate bad faith or consciousness of wrongdoing to establish a violation of Section 106.[4]

In its Post-Hearing Brief, the Division continues to argue for a construction of "willful refusal" that requires nothing more than mere "volitional" conduct. *See, e.g.*, ENF Post-Hearing Brief at 50 ("'willful' under Section 106(e) means only 'volitional'"); *id.* at 2 ("Respondents' *knowing failures* to produce requested documents constituted willful refusals to comply with the Requests. . . ." (emphasis added)). But none of the Division's attempts to justify this construction withstands any scrutiny. Indeed, the Division has ignored altogether the plain language and intent of the statute, as well as applicable canons of statutory construction. The Division's construction must therefore be rejected.

1. The Division Continues to Ignore the Plain Language of Section 106.

The Division argues that "willful" is a term of art used throughout the securities laws to connote "volitional" conduct, ENF Post-Hearing Brief at 46-50; that "when Congress employs a term of art, 'it presumably knows and adopts the cluster of ideas that were attached to each borrowed word'"; and that "repeated uses of specific words should be presumed to have the same meaning," *id.* at 50-51. The fatal flaw in this argument, however, is that there are *no* "repeated uses" of the term "*willful refusal*" anywhere in the federal securities laws. *See* Respondents' Post-Hearing Brief at 14-20. Rather, the *only* use of that term in the federal securities laws is in Section 106.

---

[4] The Division contends that to carry its burden, it must establish three "prongs of a willful Section 106 violation": (1) "[o]ne or more of the triggering conditions of Section 106(b)(1) is met"; (2) the "Commission properly issues to the foreign firm a 'request' for audit workpapers"; and (3) the "foreign firm 'willful[ly] refus[es] to comply." ENF Post-Hearing Brief at 43-44 (alterations in original). It claims the first two prongs are "indisputably met," but that is not the case. As Respondents argued in their Motions for Summary Disposition, the first prong is not satisfied where Respondents did not issue any audit opinions, and the second prong has not been met because the issuance of the requests was not proper because they are unenforceable (and, separately, no federal court has ever passed on that question).

The Division ignores the actual language of Section 106(e), which does not authorize punishment for a merely "willful" act, but rather requires a "willful refusal." Thus, provisions or cases that use "willful" alone do not apply here. And the Division still has not pointed to any provision of the federal securities laws that uses the term "willful refusal" or any similar standard. The Division is therefore wrong that, in enacting Section 106(e), Congress "employ[ed] a term of art" that has "repeated uses" in the federal securities laws, and there is no basis for the Division's assertion that Congress intended that the term "willful refusal" would adopt a "'cluster of ideas that were attached'" to the term "willful" standing alone. *See* ENF Post-Hearing Brief at 51 (citation omitted). If that had been Congress's intent, Congress would have modeled Section 106 after several other provisions relating to the production of documents to the Commission Staff, or used more common formulations like "willful failure" or "willful violation." Instead, Congress chose to employ a phrase found nowhere else in the federal securities laws. This choice must be given meaning, and the Division's attempt to gloss over it must be rejected.

This is the exact lesson of the Supreme Court's decision in *Arthur Andersen LLP v. United States*, 544 U.S. 696 (2005). There, the government's central argument was that the word "corruptly" in the witness tampering statute, 18 U.S.C. § 1512(b), should have been given the same meaning it was traditionally given in the obstruction statute, 18 U.S.C. § 1503. Despite the similarity in context, the Supreme Court tersely dismissed the argument because in § 1512, unlike in § 1503, the word "corruptly" is modified by "knowingly." *Andersen*, 544 U.S. at 705 n.9. The Court concluded that the additional word rendered any statutory analogies "inexact," *id.*, and that it was required to reject the government's construction because the term "corruptly" would do "no limiting work whatsoever." *Id.* at 705, 707. *Andersen* thus instructs that in

construing "willful refusal," this Court cannot rely on the "inexact" statutory analogies offered by the Division, and must not adopt a construction in which one of the terms in the phrase, *i.e.*, "willful" or "refusal," does "no limiting work whatsoever."[5]

Consistent with this approach, the Supreme Court determined in *FPC v. Metropolitan Edison Co.*, 304 U.S. 375 (1938), that when "willful" modifies "refusal," a more demanding standard is appropriate—and liability cannot be established where the defendant has acted in good faith. The Division, however, takes the remarkable position that this decision—in which the U.S. Supreme Court construed a statute in which "willful" modified "refuse"—has "*no bearing* on the issues here." ENF Post-Hearing Brief at 56 (emphasis added). First, the Division contends that *Metro Edison Co.* preceded "decades of judicial precedents uniformly interpreting 'willfully' to mean 'volitionally' in the civil securities law context." *Id.* But, once again, the Division makes the error of ignoring the actual language of the operative standard here—*i.e.*, "willful refusal." "[J]udicial precedents" interpreting the word "willful" standing alone do not impact the holding in *Metro Edison Co.* or otherwise instruct how the term "willful refusal" must be construed. Second, the Division contends that *Metro Edison Co.* is not relevant because the "relevant statutory language" established a standard for misdemeanor (rather than civil) liability. ENF Post-Hearing Brief at 56. But the fact that criminal sanctions were reserved for a "willful refusal" is telling, and demonstrates that this language establishes a heightened standard.[6]

---

[5] The Division contends that *Andersen* is "distinguishable" because it involves a criminal statute, and that statute did not "include the word 'willful.'" ENF Post-Hearing Brief at 56. Those extraneous differences miss the point. The Division has not rebutted (nor could it) *Andersen*'s central tenet, which is described above and is fatal to the Division's efforts to construe "willful refusal to comply" as requiring nothing more than "volitional" conduct.

[6] The Division also suggests that *Safeco* "undermines" Respondents' position because the Supreme Court "rejected the heightened standard of 'willfully' urged by the credit reporting companies" there. ENF Post-Hearing Brief at 55. But the civil provisions considered in *Safeco* used the term "willfully fails," which, as demonstrated below, is entirely distinct from "willful refusal." Moreover, the

Indeed, Congress's decision to borrow a term previously used in the criminal law is perfectly understandable given the exceptional extraterritorial reach of Section 106 and the severe penalties that the Division can seek (and is seeking here) if it is violated.

The Division's attempt to ignore the actual language of Section 106(e) thus cannot be squared with these two important Supreme Court decisions and core canons of statutory construction, and it must be rejected.

2. Contrary to the Division's Contention, the Terms "Refusal" and "Failure" Do Not Mean the Same Thing.

The Division's position that the "willful refusal" standard requires only "volitional" conduct violates the basic canon of statutory construction that courts must "assume that Congress used two terms because it intended each term to have a particular, nonsuperfluous meaning." *Bailey v. United States*, 516 U.S. 137, 146 (1995). Indeed, the Division's construction of "willful refusal" violates this interpretive canon in two ways. First, Section 106(e) pairs the term "willful" with an act, "refusal," that already requires knowing and intentional conduct. The Division's construction does not give any meaning to the pairing of these two words and renders the language superfluous. Second, the Division equates Section 106's "willful refusal" standard with Rule 102(e)(1)(iii)'s "willful violation" standard, and thereby completely reads out the entirety of Section 106(e). *See* Respondents' Post-Hearing Brief at 10-11. Under the Division's interpretation, even absent Section 106(e), any failure to produce documents would be a violation of the securities laws because it would violate Section 106(b)'s command that foreign accounting firms "shall" produce documents upon request. *See* 15 U.S.C. § 7216(b). And a "willful" failure to produce documents would then suffice as a basis for a Rule 102(e)(1)(iii)

---

relevant statute in *Safeco* used the term "willfully" in parallel criminal provisions—something that is obviously not the case here.

proceeding. 17 C.F.R. § 201.102(e)(1)(iii). For Section 106(e) to serve any purpose at all, the term "willful refusal" must mean more than mere "willful" failure.

The Division now attempts unsuccessfully to sidestep the problems that result from its construction by taking the position that the words "refusal" and "failure" should be given the exact same meaning.[7] But this late-breaking reversal of the Division's interpretation of "refusal"[8] is not only inconsistent with the Division's prior position, it does not solve the superfluity of Section 106(e) under the Division's construction, and also defies the clear and ordinary meaning that courts have given to "refusal," even when (unlike here) it is standing by itself.

Thus, the Division is wrong that construing "refusal" to mean mere "failure" in Section 106 is "consistent with how courts have interpreted 'refusal' in other contexts." ENF Post-Hearing Brief at 52. To the contrary, courts in the United States have long recognized that the term "refusal" itself requires knowing and intentional action, and is distinct from a mere "failure," which can be satisfied through inadvertence or inability. *See, e.g.*, *United States v. Boyle*, 469 U.S. 241, 245 n.3 (1985) (noting that the terms "willful neglect" and "refusal" each "impl[y] *intentional* failure" (emphasis added)); *In re Jordan*, 521 F.3d 430, 434 (4th Cir. 2008) ("[T]he majority of courts have found that the word 'refused' does in fact require the showing of a willful or intentional act, not merely the showing of a mistake or the inability to comply.");

---

[7] The Division meekly suggests that even if "refusal" is "construed to include a volitional component," the term "willful"—under its proffered construction—could still "perform an important clarifying function" by "mak[ing] clear that a foreign firm's refusal to comply . . . must be volitional in the same sense that all other 'willful' conduct must be volitional." ENF Post-Hearing Brief at 56-57. But ensuring that a term with a "volitional component" is construed to be "volitional" is no function at all—it is surplusage. This is particularly true under the Division's own logic, which suggests that the term "willful" standing alone has a well-established meaning and would need no clarification. And in any event, Rule 102(e) itself could already perform a clarifying "function" because it requires that any violation of Section 106 be "willful" before sanctions can be imposed.

[8] *See* ENF Pre-Hearing Brief at 30 (contending that the term "'[r]efusal' implies the positive denial of an application or command, or at least the mental determination not to comply").

United States v. Seigel, 168 F.2d 143, 147 (D.C. Cir. 1948) (contrasting a "refusal" with an "inadvertent failure"); *In re Foster*, 335 B.R. 709, 716 (Bankr. W.D. Mo. 2006) ("The term used in the statute is 'refused' not 'failed.' Accordingly, the Court must find that the Debtors' lack of compliance with the relevant court order was willful and intentional."); *Griffin v. United States*, 618 A.2d 114, 120 (D.C. 1992) ("'Refusal' to [do an act] is to be distinguished from 'failure' to do so . . . . In the words of Chief Justice Marshall, to refuse to do something is 'an act of the will,' while to fail to do it 'may be an act of inevitable necessity.' *Taylor v. Mason*, 22 U.S. (9 Wheat.) 325, 344, 6 L.Ed. 101 (1824).").[9] There is simply no basis to treat these markedly different words—"refusal" and "failure"—as synonymous.

The ordinary meaning of "refusal"—as being distinct from mere "failure"—is not undermined by the holding in *Société Internationale*, as the Division argues. There, the Supreme Court found that, for purposes of a previous version of Federal Rule of Civil Procedure 37, "a party 'refuses to obey' simply by failing to comply with an order." 357 U.S. at 208. Critically, however, that holding is limited to Rule 37 only and based on unique textual considerations not

---

[9] *See also State v. Kaiser*, 65 P.3d 463, 467 (Ariz. Ct. App. 2003) ("[T]he ordinance does contain a *mens rea* requirement: It requires that a person 'refuse' to obey an order. To refuse an order is an affirmative act of rejection, not a bare failure to obey but a knowing and deliberate decision to not obey. Absent a refusal to obey, as opposed to a mere failure to obey, there can be no violation of the ordinance."); *Griffin*, 618 A.2d at 120 ("Refusal is commonly defined as a rejection, a denial of what is asked. It is a volitional act. 'Refusal' to admit the police is to be distinguished from 'failure' to do so." (internal quotation marks and citations omitted)); *Commonwealth v. James*, 392 A.2d 732, 735 (Pa. Super. Ct. 1978) ("In order to demonstrate a refusal to pay . . . , the Commonwealth must show more than a mere failure to pay."); *Smith v. Godby*, 174 S.E.2d 165, 171 (W. Va. 1970) ("It is significant that the statute uses the words 'fail' or 'refuse' in the disjunctive and manifestly attaches a different meaning to each word. *Obviously they are not synonyms*. The word 'refuse'. . . implies an intentional or deliberate failure or unwillingness to discharge the duty imposed as distinguished from 'failure' through inattention, inaction or inadvertence in the discharge of such duty." (emphasis added)); *State v. Harland*, 105 N.E.2d 293, 295 (Ohio Com. Pl. 1951) ("'Refusal' means a denial, a declination to do what is requested or ordered. A 'refusal' is a willful, conscious and deliberate act."); *Walker v. English*, 17 So. 715, 716 (Ala. 1895) ("The complaint does not count upon his refusal to enter the satisfaction, but upon his failure. The refusal involves more than the failure. The one is positive, the other may be negligent or inadvertent.").

present here.[10] Specifically, the Court found that the words "failure" and "refusal" were used interchangeably throughout Rule 37. *See, e.g.*, *id.* at 207 n.1 (explaining that "[d]ifferent subsections refer to '*Refusal* to Answer' (a), 'Expenses on *Refusal* to Admit' (c), '*Failure* of Party to Attend or Serve Answers' (d), and '*Failure* to Respond to Letters Rogatory' (e)." (emphasis in original)); *see also* Fed. R. Civ. P. 37 advisory committee's note (1970) (describing the "rather random use of these two terms" in the previous version of Rule 37). Indeed, the relevant use of the term "refusal" in that case fell under a subsection of Rule 37 that was entitled "*Failure* to Comply With Order." *Société Internationale*, 357 U.S. at 207-08 (emphasis added). As such, the Court detected "no design in the Rules evidenced by this pattern of words" that could "establish the clear distinction" between "failure" and "refusal."[11] *Id.* at 207 n.1. There are no similar textual bases in Section 106 to require departure from the well-settled meaning of "refusal" as it appears in Section 106(e).

Furthermore, following *Société Internationale*, Rule 37 was revised (with approval by the Supreme Court itself) to replace the word "refusal" with "failure" in all instances. *See* Fed. R. Civ. P. 37 advisory committee's note (1970). This was done with the express purpose of addressing the fact that "refusal" and "failure" normally have different meanings, and courts—

---

[10] The Division's Post-Hearing Brief omits key language that shows the limits of the Court's holding to the unique circumstances presented by the previous version of Rule 37. For example, the Division contends that the Court held the "term 'refusal' 'clearly refers in several instances . . . to noncompliance for any reason.'" ENF Post-Hearing Brief at 52. But the ellipsis omits the phrase "in subsection (a) of the Rule." *Société Internationale*, 357 U.S. at 207 n.1. Similarly, the Division contends that "[t]he Court stated, 'we think a party 'refuses to obey' simply by failing to comply with an order." ENF Post-Hearing Brief at 52 (emphasis omitted). But it omits an introductory clause that reads: "For purposes of subdivision (b)(2) of Rule 37. . . ." *Société Internationale*, 357 U.S. at 208. Read in their proper context, these quotations reveal the extremely limited scope of the decision.

[11] Despite holding that the previous version of Rule 37 did not employ the ordinary meaning of the term "refusal," *Société Internationale* went on to hold that a foreign party does not act willfully (and should not face sanctions of default, contempt, or dismissal) when it is unable to produce documents due to foreign legal impediments. That holding was not limited to the previous version of Rule 37, and at minimum provides a dispositive defense in the instant case.

including the Fifth Circuit—had continued to interpret "refusal" and "failure" in Rule 37 as having different meanings despite the decision in *Société Internationale*. *Id.* As a result, Rule 37 was revised and the word "failure" was used throughout to avoid the potential "confusion" given the otherwise commonly recognized difference between "refusal" and "failure." *Id.* The Division's citation of *Société Internationale* as precedent establishing "refusal" and "failure" as synonyms therefore falls flat and is directly belied by the subsequent history of Rule 37.

The Division's reliance on *In the Matter of the Application of R.E. Bassie & Co. & R. Everett Bassie, C.P.A.*, Exchange Act Rel. No. 3354, 2012 WL 90269 (Jan. 10, 2012), is similarly misplaced. *Bassie* did not involve interpretation of Section 106's "willful refusal" standard, which is applicable solely to foreign audit firms, but instead the different standards applicable to Section 105.[12] 15 U.S.C. § 7215(b)(3) (authorizing sanctions "[i]f a registered public accounting firm . . . *refuses* to testify, produce documents, or otherwise cooperate with the Board" (emphasis added)). Thus, in the *Bassie* decisions, the Board and Commission each held that respondents' "intentional or knowing conduct" constituted a "refusal" under Section 105. The Board and Commission held that a "refusal" under Section 105 "need not be express," and that a "refusal" could be inferred from the respondents' conduct in that case. *See* Respondents' Post-Hearing Brief at 17-18. But, contrary to the Division's assertions, ENF Post-Hearing Brief at 53-54, neither the Board nor the Commission ever held that the respondents in *Bassie* had violated—or could violate—Section 105 by mere failure, *e.g.*, through inadvertence or mistake. Indeed, the *Bassie* respondents' disregard of the PCAOB's investigatory efforts, unaccompanied

[12] Accordingly, the Division is simply wrong when it asserts that "without any statutory basis, . . . Respondents would arrogate to themselves a special status, by denying the SEC the type of cooperation that domestic accounting firms routinely provide under other statutory mechanisms." ENF Post-Hearing Brief at 63. As the very title of Section 106 makes clear, it was Congress itself that imposed a different set of rules regarding "Foreign Public Accounting Firms," and created a different, elevated standard ("willful refusal," a standard not found in Section 105) before sanctions for nonproduction may be imposed on Respondents and other foreign public accounting firms.

by any mitigating circumstances (such as foreign legal impediments) that might have justified nonproduction, is not remotely comparable to the conduct of Respondents, who consistently and transparently advised the Division of the obstacles to production and sought every means of complying. Further, any PCAOB rules permitting the initiation of non-cooperation proceedings on the basis of a "fail[ure] to comply with an accounting board demand" are beside the point here. *See* Respondents' Post-Hearing Brief at 18. The Commission has engaged in no rulemaking with respect to Section 106. The "willful refusal" standard is thus indisputably applicable. The Division must satisfy that Congressionally-enacted standard—not any lower regulatory standard.

Under the long line of authority described above, the term "refusal" requires "knowing" and "volitional" conduct, and the Division's position that "refusal" be equated with mere "failure" must be rejected. In any event, the Division's proposal that this Court adopt an unnatural meaning of the term "refusal" does not alleviate the equally problematic surplusage and circularity that results from interpreting Section 106(e)'s "willful refusal" as identical to Rule 102(e)(1)(iii)'s "willful violation" so that Section 106(e) does not serve any purpose. *See* Respondents' Post-Hearing Brief at 10-11. The Division's Post-Hearing Brief only exacerbates these problems, and underscores the circularity of the Division's position. *See, e.g.*, ENF Post-Hearing Brief at 6 (Respondents "willfully violated the securities laws under Rule 102(e) by willfully refusing to comply with the Section 106 requests."). The mere fact that the Division is seeking sanctions under Rule 102(e) does not automatically transform the legal standard for the predicate act. For example, when a violation of Section 10(b) is the predicate for a Rule 102(e) proceeding, the Division still must establish the predicate standard (in that case, scienter) for there to be any violation—"willful" or

otherwise. So too here. The Division simply has not offered any way out of the impermissible superfluity that results from its proposed construction of Section 106(e).

3. Contrary to the Division's Position, Principles of Comity Must be Considered in Construing Section 106(e).

The principle of prescriptive comity instructs courts to interpret statutes in a manner that "avoid[s] unreasonable interference with the sovereign authority of other nations." *F. Hoffmann-La Roche Ltd. v. Empagran, S.A.*, 542 U.S. 155, 164 (2004) ("This rule of statutory construction cautions courts to assume that legislators take account of the legitimate sovereign interests of other nations when they write American laws.").[13] The Division argues, however, that principles of prescriptive comity are "*irrelevant* to the proper construction of willful refusal" because (i) "these proceedings do not seek to compel Respondents to produce documents"; and (ii) "[n]one of the remedies sought by the Division even arguably implicates any foreign laws." ENF Post-Hearing Brief at 58 (emphasis added). The notion that this internationally sensitive proceeding "would make no intrusion whatsoever into a foreign country," *id.* at 59, is utterly misguided. Respondents (and hundreds of other foreign accounting firms, each independently subject to regulation by their home country regulators) were required to register with the PCAOB and, as a result, were subjected to certain U.S. laws and regulations. From the time of such registrations, the SEC has known that a number of these U.S. legal requirements conflict with foreign law, and

---

[13] *See also Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 817 (1993) (Scalia, J., dissenting) (explaining that the principle of "prescriptive comity" is "the respect sovereign nations afford each other by limiting the reach of their laws," which is "exercised by legislatures when they enact laws, and courts assume it has been exercised when they come to interpreting the scope of laws their legislatures have enacted"); *Morrison v. National Australia Bank Ltd.*, 130 S. Ct. 2869, 2885 (2010) (given that "foreign countries regulate their domestic securities exchanges and securities transactions occurring within their territorial jurisdiction" and that "the regulation of other countries often differs from ours as to," *inter alia*, "what discovery is available," the "probability of incompatibility with the applicable laws of other countries is so obvious" that Congress would have specifically addressed the subject if it had intended foreign application of U.S. law).

a multitude of foreign audit firms face restrictions on their ability to produce documents directly to the SEC.

This particular proceeding arose because Respondents have been unable to comply with the Division's demands that they produce documents directly to the SEC in violation of Chinese law and the express directives of Chinese regulators—and, years after learning of that inability, the Division made a strategic decision to move forward at this particular time. That decision was made against the backdrop of ongoing negotiations between U.S. and Chinese regulators about cross-border securities enforcement and supervisory cooperation—including with respect to the very documents at issue here. The Division seeks a sanction that would very likely have a substantial economic impact on China, including the de-listing from U.S. exchanges of more than one hundred China-based companies and substantial obstacles to multinationals that seek to do business in China. Any suggestion that this proceeding "implicates only the Respondents' prerogatives within the United States," ENF Post-Hearing Brief at 58 (emphasis omitted), and that therefore comity principles are irrelevant, is a fiction that must be rejected outright.

Indeed, the Division's position is inconsistent with decades of judicial precedent uniformly taking into account concerns for international comity when declining to enter sanctions of default, dismissal, or contempt against foreign parties that act in good faith but nonetheless are unable to produce documents due to foreign legal impediments. *See, e.g.*, *Société Internationale*, 357 U.S. 197. The sanctions sought in these cases would not have required the production of documents in violation of foreign law; rather, these cases considered the appropriate sanctions (if any) in U.S. court for not doing so. Nonetheless, because of the substantial impact such decisions have on foreign sovereign authority, the Supreme Court has held that U.S. courts are constrained by comity principles in issuing severe sanctions in those

circumstances. These cases therefore require the Court to reject the Division's contention that principles of prescriptive comity are inapplicable because no documents are being sought, as well as the spurious claim that the sanctions impact only Respondents' prerogatives within the United States.

4. The Division's Fallback Policy Arguments Are Misguided and Properly Directed to Congress In Any Event.

Ultimately, the Division resorts to a series of policy arguments, contending that construing Section 106 to establish a heightened culpability standard would produce a "harmful result." ENF Post-Hearing Brief at 61-63. As an initial matter, the plain language and intent of the statute, and applicable canons of statutory construction, all demonstrate that Congress intended to establish a heightened standard in Section 106(e). If the Division disagrees with that Congressional judgment, that is an argument for Congress. But those arguments do not justify the Division's strained construction of Section 106 here.

In any event, given the legislative history and statutory context, it is evident why Congress specifically chose a heightened standard of liability. Congress fully appreciated the novel and extraterritorial effect of Dodd-Frank's provisions regarding SEC requests for documents located outside the United States. Further, Congress had been specifically apprised that hundreds of foreign firms faced legal impediments on their ability to produce documents directly to the SEC. In this novel circumstance, rather than make it illegal for these firms to abide by their home country laws, Congress struck a balance by setting an appropriately high bar before punishing foreign firms, while concurrently amending the Sarbanes-Oxley Act of 2002 ("SOX") in 2010 to support the SEC's efforts to establish cooperative mechanisms with foreign regulators to obtain information. *See* Respondents' Post-Hearing Brief at 11-13.

Similarly, the heightened "willful refusal" standard provides appropriate safeguards given the broad scope of documents that foreign firms may be required to produce under Section 106(b). 15 U.S.C. § 7216(b)(1)(A) (foreign firms, upon request, shall "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" (emphasis added)). It is very likely that "audit workpapers" and "all other documents of the firm related to any such audit work" could contain materials protected by the attorney-client privilege or attorney work product doctrines. And the Division has readily admitted that, under its construction of "willful refusal," the SEC could initiate Rule 102(e) proceedings against foreign accounting firms for a "failure" to produce them. Division's Opposition to Motions for Summary Disposition at 39 n.22 (contending that the Commission could "institut[e] an administrative proceeding based specifically on an audit firm's failure to produce privileged documents"). *That* is a legal standard that would produce "harmful results." However, by establishing a heightened culpability standard in Section 106(e), Congress protected firms—like Respondents—that have a good faith and valid basis for not producing documents to the Staff.[14] This is an eminently reasonable policy decision by Congress, and undermines the Division's contention that "[t]here is no valid reason" to construe "willful refusal" to require proof of bad faith. *See* ENF Post-Hearing Brief at 63.

---

[14] Similar concerns animated the Supreme Court's textual analysis of the legal standard at issue in *Andersen*. As described above, the applicable statute made it a crime to "'knowingly . . . corruptly persuade another person . . . with intent to . . . cause' that person to 'withhold 'documents from, or 'alter' documents for use in, an 'official proceeding.'" 544 U.S. at 698. The Court explained that the need to give effect to each word in the statute (*i.e.*, "knowingly" and "corruptly"), and to apply the resulting heightened standard of culpability, was "particularly appropriate here, where the act underlying the conviction—'persuasion'—is by itself innocuous." *Id.* at 703 (explaining that "'persuading' a person 'with intent to . . . cause' that person to 'withhold' testimony or documents from a Government proceeding or Government official is not inherently malign," and providing as examples "a mother who suggests to her son that he invoke his right against compelled self-incrimination" and "a wife who persuades her husband not to disclose marital confidences").

B. Respondents' Conduct Cannot Even Satisfy the Division's Proposed "Volitional" Standard.

Even if the Division were correct (and it is not) that Section 106's "willful refusal" standard does not require that the Division establish a lack of good faith by Respondents, and instead should be construed as mere "willfulness," it is well-established that the good faith inability to comply with document demands is at a minimum a *defense* to mere "willfulness." But the Division's one-sided reading of the law does not permit even that much. ENF Post-Hearing Brief at 60 (Section 106(e) does not "permit *any defense* based on a good-faith inability to comply" (emphasis added)). That position flies in the face of well-settled legal authority, including the Supreme Court's decision in *Société Internationale* (on which the Division itself relies), and the Division offers no valid reason why such an extreme departure from precedent is warranted here. Even under the Division's proffered construction of "willful refusal," requiring mere "willfulness," Respondents cannot be punished because they were *unable* to comply with the SEC's document requests based on foreign legal impediments.[15]

U.S. courts are not authorized to enter sanctions of default, dismissal, or contempt in *civil* matters for "failure" to comply with a discovery order unless such "failure" is due to "'willfulness, bad faith, or any fault'" of the noncomplying party. *See, e.g., NHL v. Metro. Hockey Club*, 427 U.S. 639, 640 (1976) (per curiam) (citation omitted). It is also well-settled that there is a "distinction" between "instances where the failure to produce documents was caused by *inability* on the part of a party, as opposed to *willfulness*." *Attorney General of United States v. Irish People, Inc.*, 684 F.2d 928, 952 (D.C. Cir. 1982) (emphasis added); *see also Klein-*

---

[15] The Division's position that inability to comply with foreign law is not even a permissible defense is also contrary to *Bassie*, in which both the Board and the Commission found the respondents liable (under Section 105) and imposed sanctions in part because the respondents had failed to point to any "mitigating circumstances" justifying their non-production. 2012 WL 90269, at *12; PCAOB File No. 105-2009-001, at 12 (Oct. 6, 2010).

Becker USA, LLC v. Englert, 711 F.3d 1153, 1159 (10th Cir. 2013) (distinguishing "willful failure" from "involuntary noncompliance" (internal quotation marks omitted)); *Gocolay v. New Mexico Fed. Sav. & Loan Ass'n*, 968 F.2d 1017 (10th Cir. 1992) (no finding of willfulness where health issues rendered party unable to complete deposition); *Searock v. Stripling*, 736 F.2d 650 (11th Cir. 1984) (no finding of willfulness where party unable to produce documents that were lost); *Thomas v. Gerber Prod.*, 703 F.2d 353 (9th Cir. 1983) (no finding of willfulness where party unable to pay monetary sanction for separate violation of court order); *Bon Air Hotel, Inc. v. Time, Inc.*, 376 F.2d 118 (5th Cir. 1967) (no finding of willfulness where party unable to produce witness for deposition because that person is no longer employed by party and cannot be located); *Baraz v. United States*, 181 F.R.D. 449 (C.D. Cal. 1998) (no finding of willfulness where party residing outside the U.S. is unable to attend deposition because INS prohibited entry to the U.S.).

Consistent with this authority, the U.S. Supreme Court and other federal appellate courts have held that when foreign parties are constrained by foreign legal impediments, their failure to produce documents is due to *inability* rather than "willfulness." *See Société Internationale*, 357 U.S. at 212 (reversing sanction of dismissal where non-complying party asserted "inability to comply because of foreign law" and the failure to comply was therefore not due to "willfulness, bad faith, or any fault of petitioner"); *In re Westinghouse Elec. Corp. Uranium Contracts Litig.*, 563 F.2d 992, 994 (10th Cir. 1977) (where Canadian law prohibited disclosure, it was necessary to consider whether the defendant's failure to comply was due to inability, and not to willfulness, bad faith, or any fault of the petitioner); *Shcherbakovskiy v. Da Capo Al Fine, Ltd.*, 490 F.3d 130, 139 (2d Cir. 2007) ("the inquiry into *Russian law* . . . will inform a finding as to appellant's *willfulness*, or lack thereof," in not producing the documents (emphasis added)). Indeed, the

seminal case in this circuit, *In re Sealed Case*, reversed a contempt order issued in connection with a criminal investigation and expressed deep reservations about ever sanctioning a foreign party that is unable to comply with document demands due to foreign legal impediments. 825 F.3d at 498.

The Division tries to distinguish these cases by suggesting that they do not involve "application of the securities-law meaning of the word 'willfulness,'" and do not involve "application of a specialized statutory scheme." ENF Post-Hearing Brief at 61. But the Division's arguments fall flat. First, the Division cites no actual cases in which the alleged "securities-law meaning of the word 'willfulness'" has been construed to exclude an "inability" defense. In fact, to the contrary, the Division's proffered construction—*i.e.*, the "intent to do the act which constitutes the violation of law," *In the Matter of Peak Wealth Opportunities LLC*, Exchange Act Rel. No. 69036, Admin. Proc. 3-14979, 2013 WL 812635 (ALJ Order March 5, 2013)—obviously would not be satisfied where a party was unable to comply and therefore lacked the requisite "intent" to commit the act. In any event, the "act which constitutes the violation of law" here is a "willful refusal," and so this formulation merely restates the question rather than answering it. Second, the Division ignores the fact that, like the purported "securities-law meaning" of mere willfulness that the Division advocates here, courts have construed "willful" (standing alone) in the civil discovery context to require "intentional" conduct, but not necessarily a showing of "wrongful intent." *See., e.g.*, *Klein-Becker USA*, 711 F.3d at 1159 (internal quotation marks and citation omitted). Nonetheless, those cases still recognize an exception for "involuntary noncompliance" or justifiable excuse. *See id.* The Division can offer no valid reason why its (incorrect) "volitional" standard should not then be

controlled by *Société Internationale* and its progeny and at least permit a defense based on good faith inability.

The Division is wrong about the proper construction of "willful refusal." But it offers no basis to conclude that its own proffered "volitional" standard—even if it were applicable—would be satisfied by a party's inability to produce documents without violating foreign law.

III. THE DIVISION HAS NOT CARRIED ITS BURDEN OF PROVING THAT RESPONDENTS WILLFULLY REFUSED TO COMPLY WITH THE REQUESTS

The Division has failed to carry its burden of proving that Respondents' inability to produce documents directly to the SEC constitutes a "willful refusal." The Division has argued for an extreme legal standard under which Chinese legal impediments are "legally irrelevant," ENF Post-Hearing Brief at 46, and Respondents "willfully refused" simply because "in each instance" Respondents stated their position "in writing," *id.* at 68. But the Division implicitly recognizes that is not enough under Section 106's heightened standard, and so it spends the bulk of its 130-page brief attempting to establish a number of "factual bases for Respondents' liability." *Id.* at 3; *see id.* at 6-42, 63-110. However, the Division has not come close to carrying its burden regarding these "factual bases":

- The Division's primary argument—that Respondents violated Section 106 by "purposefully entering U.S. markets while determining not to comply with U.S. rules," *id.* at 72—ignores the factual record and runs headlong into well-established legal precedent.
- The Division completely ignores the extensive evidence of Respondents' good faith efforts to facilitate the production of documents and otherwise cooperate with the Division's investigations.

- With its prior position on Chinese law thoroughly refuted at the hearing, the Division (i) repeats its discredited pre-hearing arguments about Chinese written law; (ii) unsuccessfully tries to cast doubt on the CSRC's and MOF's oral directives; and (iii) tries to diminish the relevant Chinese laws by characterizing them as "blocking statutes" (an argument that, even if correct, has no bearing on whether Respondents "willfully refused")—but ultimately, the Division admits that there *were* Chinese legal impediments that prevented Respondents from producing the requested documents directly to the SEC.

In the end, the Division has not identified any valid basis to find that Respondents have "willfully refused."

A. The Willful Refusal Standard Is Not Satisfied Merely By Respondents' Registration with the PCAOB and Subsequent Audit Work for U.S. Registrants.

1. The Division's Sole Remaining Theory of Bad Faith Fails.

The Division has retreated to a position in which it attempts to demonstrate Respondents' bad faith based on their registration with the PCAOB and performance of audit work in the United States. ENF Post-Hearing Brief at 72-73. In doing so, the Division argues that Respondents "deliberately courted legal impediments," and that they "cannot now claim good faith when they knew all along that their own purposeful, profit-motivated conduct could land them in precisely the circumstances in which they now find themselves." ENF Post-Hearing Brief at 72-73; *see also id.* at 65 (Respondents "knew at the time of their registration" with the PCAOB "that PRC legal impediments could prevent their compliance with their production obligations under U.S. law"). Nothing could be further from the truth. The Division's Post-Hearing Brief portrays a factual scenario that bears no resemblance to the actual evidence at the hearing, and its arguments are precluded by controlling legal precedent.

The full context of Respondents' registration with the PCAOB and subsequent audit work is detailed in Respondents' Post-Hearing Brief (at 53-60), and makes clear that the following key facts have been established beyond dispute:

- When Respondents applied for registration, they transparently disclosed potential Chinese legal impediments to their production of documents directly to U.S. regulators in full compliance with the procedures adopted by the PCAOB and the Commission for the registration of foreign accounting firms. Respondents' Post-Hearing Brief at 53-54.[16]
- Hundreds of foreign accounting firms from jurisdictions around the world faced similar potential legal impediments to producing documents. *Id.* at 54.
- In this context, the PCAOB (with SEC oversight) made the policy decision to approve these firms' registrations based on the expectation that any foreign legal impediments could be resolved by working cooperatively with foreign regulators.[17] *Id.* at 56-58; *see* Respondents Ex. 607, at 1-2, ENF Exs. 6-10.

---

[16] *See* Respondents Ex. 205, Item 8.1, Ex. 99.2 (DTTC Application for PCAOB Registration (April 6, 2004)); Respondents Ex. 40, Item 8.1, Ex. 99.2 (Dahua Application for PCAOB Registration (Sept. 25, 2005)); Respondents Ex. 1, Item 8.1, Ex. 99.2 (EYHM Application for PCAOB Registration (May 25, 2004)); Respondents Ex. 365, Item 8.1, Ex. 99.2 (PwC Shanghai Application for PCAOB Registration (Apr. 26, 2004)); Respondents Ex. 513, Item 8.1, Ex. 99.2 (KPMG Huazhen Application for PCAOB Registration (Apr. 26, 2004)).

[17] The policy decision made by the SEC and PCAOB must be considered against the backdrop of the SEC's longstanding objective of attracting foreign private issuers to U.S. markets. *See* Respondents Ex. 216 (SEC Posts Text of Rules Facilitating Foreign Private Issuer Deregistration Under the Exchange Act (2007-55)) (former Director of the Division of Corporation Finance lauding rules that should "promote capital formation in the U.S. and make our markets more attractive to foreign companies"); Respondents Ex. 217 ("U.S. investors benefit from the investment opportunities provided by foreign private issuers registering their securities with the Commission"); Ethiopis Tafara, *Testimony Concerning Foreign Government Investment in the U.S. Economy and Financial Sector* (Mar. 5, 2008) ("[A]s Chairman Cox, Secretary Paulson, and others have noted on many occasions, the United States welcomes foreign investment."); *see also* Respondents' Post-Hearing Brief at 113 n. 91 (discussing the SEC's acceleration of Chinese issuer registration statements *after* the start of these proceedings). Of course, to accomplish this objective successfully, the SEC also needs qualified foreign accounting firms to perform the audits of these foreign issuers. *See, e.g., International Reporting and Disclosure Issues in the Division of Corporation Finance* (Nov. 1, 2004), Section V.K

- Respondents shared this exact same expectation, and firmly believed their workpapers would be made available to the PCAOB and SEC via cooperative arrangements among regulators. Respondents' Post-Hearing Brief at 55-56.[18] This expectation has proven well-founded, as the PCAOB entered into an enforcement memorandum with the CSRC and the MoF, and audit workpapers are now being produced from China through regulator-to-regulator channels. *Id.* at 58-59.[19]
- At the same time, when Respondents registered with the PCAOB, it was not at all clear under the original version of Section 106 that the inability to produce audit workpapers to the SEC would constitute a violation of law. *Id.* at 55. Indeed, the original version of Section 106 did not provide that any kind of noncompliance with SEC requests for documents would constitute a violation of the federal securities laws, and even after the Dodd-Frank amendments in 2010, only a "willful refusal" constitutes a violation of SOX.

These facts decisively refute any suggestion that Respondents "purposefully enter[ed] U.S. markets while determining not to comply with U.S. rules," and "hid behind Chinese law to avoid compliance with U.S. rules." ENF Post-Hearing Brief at 72. Tellingly, however, the Division ignores them altogether, and suggests that by registering, in accordance with the law,

---

(the Staff may "question the location from which the audit report was rendered if there does not appear to be a logical relationship between that location and the location of the registrant's corporate offices or place where the registrant conducts its principal operations").

[18] *See* George Tr. 1627:22-1628:9, 1630:24-1633:13 ("We presumed, I think, that stakeholders in all of this, in particular the regulators working cooperatively together, would develop the platforms that would enable effective cross-border regulation to take place."); Leung Tr. 1503:5-12, 1506:5-12; Wong, J. Tr. 2162:24-2163:5.

[19] *See, e.g.*, Respondents Ex. 631; Respondents Ex. 633 (Notice to the Court, *U.S. Securities and Exchange Commission v. Deloitte Touche Tohmatsu CPA Ltd.*, 11 Misc. 512 OK/DAR (D.D.C. July 10, 2013); Respondents Ex. 632A (July 3, 2013 request from the CSRC to EYHM for Client C workpapers); Leung Tr. 1579:17-1581; Respondents Ex. 649A (confirming July 22, 2013 delivery of Client C workpapers to CSRC); Respondents Ex. 650A (July 19, 2013 request from CSRC to KPMG Huazhen for Client D and F workpapers); Yan Tr. 1927:1-13 (testifying that a team of people has started to review the materials); Wong, J. Tr. 2192:18-24.

Respondents were acting in bad faith, apparently because their expectations that the legal impediments they identified would be resolved were not realized quickly enough.[20]

Further, the Division grossly twists the testimony of Respondents' representatives to argue that Respondents "chose affirmatively ***not*** to produce the documents sought by the Requests." ENF Post-Hearing Brief at 70-72 (emphasis in original); *see also id.* at 3 ("Respondents confirmed that they chose to comply with the alleged dictates of Chinese law, rather than with their obligations to produce documents under U.S. law."). As demonstrated in Respondents' Post-Hearing Brief, however, the witnesses specifically testified that they had *no choice* but to comply with Chinese law and the directives of their home country regulators. *See* Respondents' Post-Hearing Brief at 59-60. Indeed, while the Division attempts to cherry-pick sound-bites from the testimony, the fact is that upon continued questioning from the Division, Respondents' witnesses explained innumerable times that they had "no choice" but to comply with Chinese law and could not produce documents directly to the SEC.[21] Nonetheless,

---

[20] The Division suggests that Respondents' position "blame[s]" the PCAOB "for permitting [Respondents] to register." ENF Post-Hearing Brief at 65. But that misses the point. "Blame" aside, the decision to approve the registration applications of Respondents (and similarly situated firms) was a policy decision based on full information and the expectation (by all involved parties) that sovereign-to-sovereign mechanisms would work. That is not a context in which any party can be found to have acted in bad faith. Yet the Division seeks to ignore all of this critical context, and instead act as if U.S. regulators had no role whatsoever in the events that gave rise to this proceeding.

[21] *See, e.g.*, Chao Tr. 1358:10-17 (testifying that any "decision not to produce documents directly to the SEC" was "made by the MOF and CSRC," that "[w]e have to follow the laws of the PRC," and "[t]he decision [PwC Shanghai] made was let's cooperate to the extent we can, let's do as much as we can to satisfy the request of the SEC within the constraints consistent with the Chinese law. . . . And I was also hopeful that the current impasse between the two regulators can be resolved very quickly."), 1358:1-3, 1359:1-9, 1387:10-21; Leung Tr. 1522:21-1523:7 (testifying that EYHM "did not have the choice" whether to produce documents directly by the SEC because it was "told by the PRC regulator that [it] should not directly provide working paper to the foreign regulators," that it was "hoping that there will be a solution and indeed a solution actually has come," and that EYHM is "very willing to provide those working papers to the SEC or PCAOB so long as we're permitted by PRC representatives and eventually we actually provide those working paper."), 1523:12-14, 1523:15-16, 1525:10-18, 1526:11-18, 1555:19-1556:3, 1556:10-15, 1556:16-23, 1557:11-24; George Tr. 1715:12-1716:18, 1716:24-1717:4, 1717:7-25 (testifying that "[w]e have a clear direction from [the CSRC and

Respondents engaged in extensive efforts to obtain permission to produce the documents or otherwise facilitate production to the SEC. *See* Section III.B, *infra.*[22]

The Division also attempts to make an issue of Respondents' "increasing their number of U.S. issuer audit clients over time." ENF Post-Hearing Brief at 67. First, that statement is not even factually accurate as to Dahua; Dahua decreased the number of its issuer clients from 2011 to 2012. *See* ENF Post-Hearing Brief at 13. And, in 2013, Dahua completely ended its work for U.S. issuers. Ji. Tr. 2051: 7-24.

Second, as demonstrated above, Respondents took on these engagements with the reasonable expectation that documents could be produced to the SEC, either with the permission of Chinese regulators or through regulator-to-regulator channels. Critically, this expectation has been borne out, as the CSRC has produced the Longtop audit workpapers to the SEC, [redacted], and is preparing the DTTC Client A and Client G workpapers for production to the SEC and Client C workpapers for production to the PCAOB. Presumably in recognition of these major developments, the Division itself has

---

MOF] not to produce. There is no decision being made here."), 1718:6-1719:6, 1720:16-19 ("There was no decision made [not to produce] because there was no choice involved."); Wong, D. Tr. 1819:14-21 (when asked if PwC Shanghai "decided that they would not provide those documents directly to the SEC," responding that "our firm was directed not to produce the working papers to the SEC directly by the Chinese authorities, the CSRC, and the MOF. So we believe we had to abide by those Chinese laws and the directions of those two regulators."), 1890:25-1891:4, 1900:7-1901:5 ("I don't actually think of it as a choice that was being made either way. I don't think we had a choice."); Yan Tr. 2001:19-2002:7 ("Q: . . . your firm elected not to produce documents to the SEC in response to the Section 106 requests, correct? A: I don't think there is an election as such. I think we simply have no choice. As I said, our firm is facing the PRC, our people are facing the PRC. We simply have to comply with the PRC regulations."), 2002:8-12, 2003:8-11; Ji Tr. 2125:12-21 ("I think Dahua has no decision power in deciding anything in this mater, just enter the Chinese laws and regulations. Dahua had no choices."); Wong, J. Tr. 2263:3-13, 2265:19-2266:1 ("Q: Your firm chose not to produce the documents to the SEC, correct? A: No. CSRC gave us a directive that if we were to produce the documents directly to the SEC or foreign regulator, that we would be subject to PRC sanctions and they advised that the route to get the work papers was with foreign regulators to contact the CSRC and to seek their assistance."), 2266:6-20.

[22] *See also, e.g.*, George Tr. 1622:14-22, 1626:4-8, 1627:9-18, 1658:1-4; Wong, J. Tr. 2163:23-2164:4; Wong, D. Tr. 1852:4-9.

reversed course and [redacted] (less than two weeks after arguing that such efforts would be "futile"). The Division may, for litigation purposes, continue to try to downplay these developments here, but its position that the CSRC is not a viable gateway—and that it must single out Respondents among scores of similarly situated firms around the globe—is crumbling under its feet.

Further ignoring the actual evidence and context, the Division attempts to support its "bad faith" argument by noting that when approving the registration applications of foreign firms (including Respondents), the PCAOB sent letters explaining that the legal impediments identified in their applications did not necessarily relieve Respondents of the responsibility to comply with Board demands. ENF Post-Hearing Brief at 64-70. Notably, these letters thus confirm that the PCAOB and SEC clearly understood the existence of foreign legal impediments but nonetheless chose to approve Respondents' registration applications. In any event, as addressed in Respondents' Post-Hearing Brief at 58 n.43, to the extent these letters may have constituted a technical reservation of the PCAOB's authority, the PCAOB and SEC otherwise gave every indication that foreign firms like Respondents would not be placed in the middle of conflicting laws and instead regulator-to-regulator solutions would be achieved. The letters therefore do not change the fact that Respondents acted in good faith and shared the PCAOB's expectations about cooperative solutions to these issues.[23] *Id.*

---

[23] The Division also continues to focus on Respondents' Section 106(d) consents, in which Respondents naturally did not identify potential legal impediments to producing documents. As explained in Respondents' Post-Hearing Brief at 54 n. 37, these documents had nothing to do with Respondents' ability to produce documents; rather, they designated agents for service. Indeed, the Division's attempt to contrast the Section 106(d) consents with the Section 106(b) consents, ENF Post-Hearing Brief at 67 n.31, makes the point: the latter specifically related to the ability to produce documents, and Respondents accordingly included a clear reservation of rights in that document. In any event, after nearly a decade of registrations, legal opinions, and the SEC's own correspondence (with the

Beyond the factual record, well-settled law does not permit a finding of bad faith based solely on a foreign party (subject to foreign law) availing itself of U.S. markets. That factual scenario is present in every single U.S. court decision involving foreign legal impediments, yet there are numerous cases—including the seminal, binding case from this circuit (*In re Sealed Case*)—finding that foreign parties have acted in good faith under those circumstances. *See, e.g.*, *Cochran Consulting, Inc. v. Uwatec USA, Inc.*, 102 F.3d 1224, 1228-30 (Fed. Cir. 1996) (Swiss company that manufactured and sold computers (and the allegedly infringing product) in the U.S. acted in good faith); *In re Sealed Case*, 825 F.2d at 498-99 (banks that conducted business in the United States acted in good faith); *United States v. First Nat'l Bank of Chi.*, 699 F.2d 341, 346 (7th Cir. 1983) (U.S. bank that established branches in Greece and could not respond to IRS subpoena under Greek law acted in good faith); *Westinghouse*, 563 F.2d at 994 (finding that Delaware corporation doing business in Utah had acted in good faith where it was prohibited by Canadian law from obeying discovery orders); *Tiffany (NJ) LLC v. Qi*, 276 F.R.D. 143, 160 (S.D.N.Y. 2011) (Chinese banks with offices in New York, and which accepted desposits from customers in the United States, acted in good faith).

Société Internationale itself involved a Swiss bank that had brought an action in a U.S. court against the U.S. Attorney General, which, under the Trading with the Enemy Act, had seized cash from its branches in the U.S. and stock it held in a Delaware corporation. 357 U.S. at 198-99. Notwithstanding the fact that the Swiss bank had clearly "availed itself of business activities" in the United States (and even initiated the legal action), the Supreme Court found that it had acted in good faith and its inability to comply with discovery requests without violating Swiss law did not constitute "willfulness." *Id.* at 212. The Court did not even address whether

---

firms and with the Chinese regulators themselves), there is no doubt that the SEC understood the legal impediments and any suggestion to the contrary is baseless. *See* Respondents' Post-Hearing Brief at 54 n. 37.

the Swiss bank had been aware of potential foreign legal impediments before entering U.S. markets (though there could be no doubt that a Swiss bank would be aware of Swiss banking secrecy laws).

In the face of this authority, the Division relies on outlier decisions that are easily distinguishable. Indeed, each of the cases cited by the Division involves exacerbating conduct—beyond the foreign parties merely availing of the U.S. markets—that supported a finding of bad faith. *See Richmark Corp. v. Timber Falling Consultants*, 959 F.2d 1468, 1479 (9th Cir. 1992) (noncomplying party had "fought disclosure for several months before raising the foreign law problem"); *SEC v. Banca Della Svizzera Italiana*, 92 F.R.D. 111, 114 (S.D.N.Y. 1981) (noncomplying party "made deliberate use of Swiss nondisclosure law to evade" U.S. insider trading laws that otherwise prohibited its conduct); *Minpeco, S.A. v. ContiCommodity Servs., Inc.*, 116 F.R.D. 517, 528-29 (S.D.N.Y. 1987) (noncomplying party failed to take basic steps that would have allowed it to produce documents).[24] No such conduct is present here: the record is clear that Respondents have long been transparent about the potential Chinese impediments, have made no attempt to hide behind Chinese law or use it to their strategic benefit, and have worked diligently to facilitate production of the documents.

Ultimately, the Division's theory is simply unsustainable and proves too much: it would mean that the hundreds of other foreign firms in exactly the same situation have also acted in bad faith, as well as the PCAOB and SEC themselves, which shared Respondents' expectations and permitted the instant circumstances to materialize. If there were some flaw in Respondents'

---

[24] The Division also cites *In re Dominick & Dominick, Inc.*, 50 S.E.C. 71, 1991 WL 294209 (1991), for this proposition. *See* ENF Post-Hearing Brief at 49. As shown in Respondents' Post-Hearing Brief at 16 n.13, that proceeding did not involve the "willful refusal" standard applicable here. Moreover, *Dominick & Dominick* involved a non-litigated, settled order. "[A]s the Commission has many times stressed, settlements are not precedent." *In re Finnerty*, 2009 WL 2013415, at *53 (SEC Initial Decision July 13, 2009) (citing several Commission opinions).

registration process with the PCAOB, it is the PCAOB's responsibility to address any deficiencies, not the SEC's responsibility to do so through this disciplinary proceeding. And, indeed, the only action taken by the PCAOB with respect to Respondents was to *permit* newly-created legal entities to succeed to the valid registration of the Respondents. Respondents Ex. 267 (PCAOB Form 4 (Jan. 2, 2013)). More generally, under the Division's logic, U.S. law trumps foreign law with respect to any foreign person or entity that does business in the United States. No case so holds, and the implications of that position are breathtaking.[25] The Division has failed to establish bad faith and, consequently, any violation of Section 106.[26]

2. The Evidence Concerning Respondents "Entering U.S. Markets" Does Not Even Satisfy the Division's Own "Volitional" Standard.

Recognizing that the factual record concerning Respondents "entering U.S. markets" does not establish bad faith, the Division deploys these same facts in support of its lower (and erroneous) "volitional" standard of "willful refusal." *See, e.g.*, ENF Post-Hearing Brief at 3 ("Given all of this voluntary conduct, their knowing refusals to comply with the Requests were 'willful' under Section 106."). But the Division has failed in that effort as well.

The Division argues that Respondents' noncompliance with the Section 106 requests was "intentional" because when they registered with the PCAOB, they "indisputably knew that Chinese law potentially could impair their ability to comply with these demands." ENF Post-Hearing Brief at 64. But as demonstrated above, Respondents followed exactly the registration

---

[25] The Division's position also smacks of the "my way or the highway" approach to international enforcement cooperation that Chairman White expressly disavowed in a recent speech. *See* Respondents' Post-Hearing Brief at 69. According to the Division, the Chairman's call to "find common ground with our counterparts abroad" and to "collaborate on everyday matters like enforcement" was nothing more than "platitudes." ENF Post-Hearing Brief at 82.

[26] The Division's argument makes little sense as Respondents chose to disclose these impediments rather than conceal them. In the Division's view, disclosing or concealing these impediments constitutes the same evidence of "bad faith."

requirements and (like the PCAOB itself) acted on the sincerely held and reasonable expectation that (i) any theoretical possible conflicts between U.S. and Chinese legal requirements would be resolved on a sovereign-to-sovereign basis; and (ii) their audit workpapers would be made available (either directly or through a Chinese regulator) to U.S. regulators upon request. At the same time, it was (and remains) unclear whether Respondents' obligations under U.S. law require them to violate Chinese law in order to comply with an SEC request. Such facts do not support a finding that Respondents "*intentionally* committed the act that constitutes the violation." *Id.* (emphasis added).

The Division is thus left with no choice but to argue that "complying with directions from Chinese regulators, and withholding documents from the SEC, are by their very nature volitional acts." ENF Post-Hearing Brief at 72. But that statement is inconsistent with U.S. law. As demonstrated in Section II.B, the Supreme Court has specifically held that a party's noncompliance with a discovery order because of foreign legal impediments constitutes "inability" rather than "willfulness." *Société Internationale*, 357 U.S. at 211-12. Thus, Respondents' compliance with Chinese law and inability to produce documents directly to the SEC does *not* satisfy the Division's "volitional" standard.

B. The Division Fails to Address the Extensive Evidence of Respondents' Good Faith Efforts to Facilitate the Production of Documents to the SEC.

The Division has ignored—and leaves undisputed—the substantial evidence demonstrating Respondents' good faith efforts to facilitate the production of documents to the SEC or otherwise cooperate in the underlying investigations. The evidence completely undermines any suggestion that Respondents did not act in good faith.

As demonstrated in Respondents' Post-Hearing Brief, despite facing Chinese legal impediments, Respondents' good faith efforts were extensive and included, *inter alia*:

- Promptly producing workpapers to the CSRC the first time they were requested, with the expectation that they would be delivered to the SEC, Respondents' Post-Hearing Brief at 49;[27]
- Repeatedly requesting and attending meetings with the CSRC and MOF to determine if Respondents could produce documents directly to the SEC or otherwise facilitate a regulator-to-regulator production, and offering to produce documents to the CSRC to accomplish that objective, *id.* at 49;[28]
- Seeking permission from the CSRC to produce documents directly to the SEC (promptly after receiving the relevant requests), and requesting reconsideration of the CSRC's directives to the contrary, *id.* at 49-50;[29]
- Seeking guidance (to no avail) from the SSB and SAA in an attempt to facilitate production, *id.* at 50-51;[30]
- Producing certain documents that were not restricted under Chinese law, *id.* at 51-52;[31]
- Arranging telephonic interviews with members of the audit team, *id.* at 52;[32] and

---

[27] *See also* Respondents Ex. 72, at DTTC-CS-000098 (July 6, 2010 request from CSRC to DTTC for DTTC Client A workpapers); Respondents Ex. 74 (confirming July 23, 2010 delivery of DTTC Client A workpapers to CSRC); Josephs Tr. 107:6-10 (when the SEC made the request for assistance for the DTTC Client A workpapers, it "didn't expect Deloitte to somehow circumvent the CSRC and produce documents directly to the SEC").

[28] *See, e.g.*, Chao Tr. 1297:25-1298:14, 1309:24-1310:4; Leung Tr. 1411:7-22, 1467:8-17; George Tr. 1614:7-17; Wong, D. Tr. 1872:22-1873:19, 1877:9-20.

[29] *See, e.g.*, Respondents Ex. 116A ("Because of the seriousness of the SEC staff's recommendation and the potential consequences should the SEC authorize an action against DTTC and move forward to preclude DTTC from auditing Chinese companies listed on United States exchanges, we respectfully request that you reconsider your earlier decision and authorize DTTC to produce its 2009 [DTTC Client A] audit working papers (or a copy thereof) directly to the SEC in the United States."); *see also* Josephs Tr. 133:14-17 ("Q: And Deloitte was asking the CSRC to reconsider the earlier decision and allow the direct production just as the SEC wanted; is that correct? A: Yes.").

[30] *See* Respondents Ex. 551A; Wong, J. Tr. 2178:11-2179:9.

[31] *See, e.g.*, Hubbs Tr. 484:2-15.

- Devoting substantial resources to the screening process that has been established to allow the CSRC to produce workpapers to the SEC and other foreign regulators, *id.* at 52-53.[33]

Similarly, the Division ignores the uncontroverted evidence that Respondents were properly discharging their role as auditors and, in most instances, were the very entities that identified and reported the issues that have become the focus of the Division's investigations. Respondents' Post-Hearing Brief at 60-61.[34] The Division offers no explanation for how a finding of bad faith is possible in light of this evidence. Indeed, the record is clear that Respondents have nothing to hide and would promptly produce the requested documents directly to the SEC if permitted under Chinese law. They have done all they could under the circumstances, and a finding of willful refusal is not available on this record.

---

[32] *See* Wong, D. Tr. 1839:22-1843:1 (Client H), 1851:17-1853:5 (Client I); Respondents Ex. 371; London Tr. 867:9-18, 887:1-8.

[33] *See, e.g.*, George Tr. 1635:11-1637:23 (confirming that Longtop, DTTC Client A, and Client G workpapers were produced to the CSRC in accordance with the new procedures implemented by the Chinese government); Chiu Tr. 1784:2-11, 1791:3-1792:22 (confirming that DTTC has subjected the Longtop and DTTC Client A documents to the new CSRC process, and devoted 9,000 hours to the effort); Respondents Ex. 632A (July 3, 2013 request from the CSRC to EYHM for Client C workpapers); Leung Tr. 1579:17-1581; Respondents Ex. 649A (confirming July 22, 2013 delivery of Client C workpapers to CSRC); Respondents Ex. 650A (July 19, 2013 request from CSRC to KPMG Huazhen for Client D and F workpapers); Yan Tr. 1927:1-13 (testifying that a team of people has started to review the materials); Wong, J. Tr. 2192:18-24 (testifying that KPMG started preparing documents for production to the CSRC).

[34] *See, e.g.*, Chang Tr. 712:1-714:11 (acknowledging DTTC's substantial role in identifying the issues at Client G on which the SEC based its subsequent investigation); Chang Tr. 716:24-717:15 ("Q: And it looks like the issues, the questions that Deloitte raised were critically important, right? A: Correct. Q: Their work was very valuable to you, wasn't it? A: Yes."); ENF Ex. 92, Item 4.01 (SEC filing indicating problems that DTTC identified with Client G); Leung Tr. 1404:19-23, 1406:5-8 (confirming that EYHM sent 10A letters to Clients B and C and resigned as Client C's auditor); ENF Ex. 54 (10A letter from EYHM to Client B); Wong, D. Tr. 1833:2-14, 1835:17-25 (testifying that PwC Shanghai raised concerns about issues at Clients H and I); Respondents Ex. 380, 103-04; Respondents Ex. 407, at 2.

C. The Division's Prior Position on Chinese Law Has Been Thoroughly Refuted, And So the Division Resorts to Labeling the Operative Chinese Laws As "Blocking Statutes."

Prior to the hearing, the Division repeatedly asserted that no Chinese laws prevented Respondents from unilaterally producing the requested documents directly to the SEC. ENF Pre-Hearing Brief at 46-49. However, the evidence presented at the hearing thoroughly refuted that position, and has forced the Division to change abruptly one of the central components of its case. On the one hand, the Division attempts to cast doubt on the oral directives, ENF Post-Hearing Brief at 76-77, and continues to repeat its discredited pre-hearing arguments about Chinese written law. But these arguments are entirely divorced from the testimony and documents submitted at the hearing, including the opinion of the Division's own Chinese law expert.[35] As such, the Division spends most of its own brief acknowledging that Chinese law does, in fact, prohibit Respondents from responding directly to the Section 106 requests. *See, e.g.*, *id.* at 3 ("Respondents uniformly confirmed that they knew when they first registered with the PCAOB . . . that Chinese law might impair their ability to comply with U.S. law obligations."); *id.* at 73-84 (arguing that Chinese law "effectuated a total blockade against the SEC's receipt of the documents that it sought"). However, in an attempt to minimize the significance of this critical turn of events, it now argues that the relevant Chinese laws constitute "blocking statutes." The Division's newest argument is incorrect, and in any event it has no bearing on Respondents' good faith (or even whether their conduct was "volitional").

---

[35] Similarly, the Division complains that Respondents "provided the Division with 'a laundry list of possible PRC provisions that might prohibit turning over the documents,'" which lacked "any specificity." ENF Post-Hearing Brief at 17-18. This is just a characterization not supported by the actual evidence. In any event, it of course has no bearing on whether Chinese law in fact prohibited unilateral production by Respondents—which has now been proven beyond dispute. And the number of Chinese laws that could be implicated by a direct production of workpapers to a foreign regulator underscores the complexity of the Chinese legal regime and the need for Respondents to coordinate with the Chinese regulators in navigating it.

1. The Division Offers No Valid Reason to Ignore the Binding Oral Directives.

During the hearing, the Division put on *no case at all* concerning the oral instructions. It offered no evidence that called the oral instructions into question. And its Chinese law expert repeatedly disclaimed any attempt to opine on them. Clarke Tr. 2357:11-14 (acknowledging that his opinion is limited solely to written materials); *id.* at 2360:8-12 (agreeing that his opinion "does not address the impact, if any, of any oral instructions"); *id.* at 2365:20-25 (same).[36] Indeed, counsel for the Division stressed as much. Feinerman Tr. 2556:7-9 (asking, during the cross-examination of Respondents' expert, "[a]nd isn't it true, sir, that Professor Clarke was addressing written Chinese law and *not all Chinese directives issued orally*?" (emphasis added)). Nonetheless, the Division makes a number of desperate arguments aimed at ignoring the overwhelming evidence that Respondents received binding oral instructions from the CSRC and MOF on multiple occasions. These arguments fail.

First, the Division claims that the oral instructions should be disregarded here because they are "incapable of independent verification," "inherently unreliable," and based on hearsay testimony. ENF Post-Hearing Brief at 91. Respondents have already demonstrated as a matter of law that this testimony is not hearsay, Respondents' Post-Hearing Brief at 31-32, and the Division remains unable to refute that showing. At any rate, Respondents presented compelling, consistent, and credible witness testimony that established beyond any doubt that the oral instructions were given. *Id.* at 24-27. And, contrary to the Division's argument, the testimony was corroborated by multiple contemporaneous letters to the SEC and CSRC itself describing the

---

[36] *See also* Clarke Expert Report ¶ 43 ("In particular, Respondents highlight meetings in October 2011 in which they state that they received directions not to produce documents directly to the SEC. *I do not address these contentions in this Report*, except to note that the referenced letters do not contain any such explicit direction." (emphasis added)); *id.*at ¶ 55 ("Putting aside other oral instructions from the CSRC (assertions about which, as noted above, I do not express an opinion in this Report. . . .") (emphasis added)).

oral instructions, as well as the broader factual record (including the lengthy discussions between the SEC's OIA and the CSRC concerning the production of audit workpapers).[37] *Id.* at 27-29. There is nothing "unreliable" or "flimsy" about this evidence, and the Division does not offer any evidence or reason to believe that the oral instructions were not given.

The Division further complains that it has "virtually no recourse effectively to challenge such an out-of-court statement." ENF Post-Hearing Brief at 92. But it had the opportunity to, and in fact did, cross-examine Respondents' witnesses *for an entire week.* The fact that the witness testimony withstood the Division's scrutiny does not mean the Division cannot "protect its processes" (*id.* at 92), but rather proves that the testimony is credible.

Ultimately, the Division suggests that oral instructions are somehow categorically incapable of establishing the existence of foreign legal impediments, and that only a "written or sworn statement by the Chinese government" will do. *Id.* at 91. But the Division simply invented this standard to serve its current purposes.[38] Ruling out oral directives entirely would be inconsistent with the uncontroverted reality of Chinese law. Oral directives—often confidential—"remain one of the most common forms of binding regulatory guidance in China." Feinerman Rebuttal Report ¶ 4; Feinerman Tr. 2518:23-2519:9; *see also* Feinerman Expert Report ¶ 37 ("The vast majority of administrative guidance provided by Chinese regulators to regulated entities is still largely unwritten or 'internal' (in Chinese *'neibu'*)."). The evidence supporting the oral instructions is powerful, and there is no basis to ignore them.

---

[37] The Division's contention that, in its view, the "alleged oral directives" differ from the content of the October 2011 written directives is wrong. *See* ENF Post-Hearing Brief at 92. Like the oral instructions, the written directives make clear that Respondents are prohibited from producing documents to the SEC without approval, and that any such productions must go through the CSRC. *See, e.g.*, Feinerman Tr. 2547:10-14 (testifying that he believes the written directives "reflect[] what was conveyed orally").

[38] In any event, written Chinese law also establishes that Respondents are unable to produce documents directly to the SEC without violating Chinese law. *See infra* Section III.C.2.

Second, the Division contends that the question "whether the Chinese government's oral statements would be binding" remains open. ENF Post-Hearing Brief at 93. That contention has no merit. Professors Tang and Feinerman unequivocally explained the mandatory and binding nature of the oral directives, and their testimony was unrebutted. Tang Tr. 2412:8-2413:5 (oral directives from the CSRC "have a legal binding effect"); Feinerman Tr. 2518:3-2519:9 ("I believe that those oral instructions [given to Respondents], along with the written guidance and the statutory and regulatory provisions I have mentioned before, clearly have a binding force of law."). Indeed, Professor Clarke's own report seems to concede that such directives have the force of law. Clarke Expert Report ¶ 17 n.28 (acknowledging that oral directions can be categorized as "'law'"); *accord* Clarke Tr. 2397:14-20 (acknowledging that "assertions about the functioning of the Chinese legal system can never stop simply with observations about what the formal law says"). The Division broadly suggests that the binding nature of oral directives may depend on "facts and circumstances." ENF Post-Hearing Brief at 93. But it does not identify a single piece of evidence that rebuts the position of Professors Tang and Feinerman or that otherwise shows that the oral directives at issue in this case are not binding. This red herring should be dismissed outright.

Third, the Division contends that the oral directives were given under "dubious circumstances" and resulted from "some level of collusion between Respondents and the Chinese government." ENF Post-Hearing Brief at 93-94. Such indiscriminate allegations—which impugn the integrity of another sovereign government and the five major accounting firms in China—are baseless and irresponsible. They rest in part on the Division's unsupported premise that "Respondents with potential liability for U.S. securities laws violations (or who otherwise want to avoid scrutiny) obviously have an interest in shielding their documents." *Id.* at 93. But

the record shows just the opposite. Respondents discharged their professional obligations and identified the very issues that jumpstarted the Division's investigations in the first place. *See supra* Section III.B. They have done everything possible to facilitate production of the documents, including producing them to the CSRC on multiple occasions with the intent that they would be delivered to U.S. regulators. *See id.* As professional accounting firms, Respondents have a significant interest in maintaining compliance with legal and regulatory requirements—it is a critical part of their business and reputation. *See, e.g.*, George Tr. 1673:4-24. Facing an effort to shut them out of the U.S. markets altogether, Respondents would undoubtedly produce the documents directly to the SEC if they could. *See, e.g.*, Leung Tr. 1407:9-22.

Nor can a finding of collusion possibly rest on the mere fact that "during the relevant period, Respondents had repeated contacts with the CSRC through in-person meetings, phone calls, and emails." ENF Post-Hearing Brief at 93-94. Of course, there is nothing untoward about a regulated entity communicating with its regulator, and, in these circumstances, that was the only prudent course. Feinerman Report ¶ 44 (opining that, based on "PRC's cultural assumptions, the discretion inherent in its legal system as a civil law regime, its heightened sensitivity to the release of information, and its often non-public actions and legal interpretations, among other reasons[,] no responsible audit firm operating in China would produce documents from China to a foreign regulator without first alerting its regulator"). Indeed, the record is replete with evidence of Respondents' contacts with Division staff, which were equally proper. Further, these "contacts" with the Chinese government were made with the knowledge and approval of Commission Staff and with the specific purpose of facilitating production of the documents. *See, e.g.*, Josephs Tr. 146:15-149:13 (confirming that she told Mr. Warden that the

delay in initiating the Rule 102(e) proceeding was "so that Deloitte could work with the CSRC to try to facilitate the production," that Mr. Warden and Ms. Josephs "started talking weekly, sometimes every day, about progress that Deloitte had made," and that she "think[s]" that DTTC was working with the CSRC to facilitate a production during that time).[39] The Division cannot now twist this into evidence of "collusion."

Finally, the Division suggests that based on KPMG Huazhen's correspondence with the CSRC about the October 18, 2011 written directive (Respondents Ex. 545; ENF Ex. 335A), it "must be inferred" that *all of the Respondents* colluded with the CSRC. ENF Post-Hearing Brief at 94. This "conspiracy theory" is unsupported by any evidence. In reality, the record shows that KPMG Huazhen proposed a limited edit to one line of the written directive—a proposed edit that KPMG Huazhen believed would make the letter even more clearly in line with the tone of the repeated oral instructions it had received. Wong, J. Tr. 2176:6-13; Yan Tr. 1918:7-11 (explaining that KPMG Huazhen proposed a minor revision—adding a single "clause"—to "make the letter clearer"), 2029:23-2030:7. KPMG Huazhen acted on its own and with the involvement of highly regarded U.S. counsel (who now serves as Chief Counsel in the SEC's

---

[39] *See also* Josephs Tr. 104:4-18 (agreeing that the SEC "hoped" the CSRC "would reach out to Deloitte and ask for the production of documents" and that there is "nothing wrong or inappropriate" about such contact between the CSRC and DTTC); *id.* at 117:5-17 (testifying that she was "aware" that DTTC "contacted the CSRC about the 106 request," that DTTC's then-counsel notified the Staff it planned to do that, and that the Staff "didn't raise any objection to that"); *id.* at 118:6-16 (testifying, with respect to DTTC's contacts with the CSRC, "[w]e were certainly not unwilling to explore any possibility that would get us the documents. And if Deloitte had better access, then let them have the contact"); *id.* at 126:1-9 (confirming she "didn't object in any way to Deloitte going to the CSRC" and that she did not "suggest in any way that Deloitte should have gone to another part of the Chinese government"); *id.* at 141:8-11 (confirming that during a January 2012 meeting between the SEC and DTTC, "[t]here was . . . a discussion about the efforts that Deloitte could make to facilitate the production of documents by the CSRC"); *see* ENF Ex. 162 (DTTC Wells Submission) (attaching correspondence between DTTC and the CSRC); ENF Ex. 128 (letter from counsel for DTTC to the SEC relaying DTTC's interactions with the CSRC); Respondents Ex. 137 (letter from DTTC's counsel detailing the October 10, 2011 meeting with the CSRC and MOF and attaching the October 11, 2011 written directive); Respondents Ex. 140 (briefing the SEC Staff on DTTC's ongoing correspondence with the CSRC).

OIA, after having served as Senior Counsel to Chairman White and, before that, General Counsel of the Commission). Yan Tr. 2019:3-12; Wong, J. Tr. 2279:21-24.[40] And the CSRC *rejected* KPMG Huazhen's proposed revision. Yan Tr. 2017:19-25. These facts reflect reasonable and common interactions between regulator and regulated entity—no different from the sort in which the SEC regularly engages.[41] Far from showing collusion, the evidence shows just the opposite: it shows a Chinese regulator that, as part of its regulatory function, was resistant to the requests of its regulated entities—a fact also demonstrated by the CSRC's continued unwillingness to allow Respondents to produce the requested documents directly to the SEC.

The Division has thus failed to refute the overwhelming evidence that Respondents received oral instructions barring them from producing the requested documents directly to the SEC. That fact alone is dispositive, and precludes a finding of "willful refusal."

2. It is Beyond Dispute That Chinese Written Law Prohibits Respondents' Direct Production of the Documents to the SEC.

The Division repeats its pre-hearing argument that Respondents "have not cited a single, written law or rule requiring that Respondents' primary regulator in this area—the CSRC—approve Respondents' production to the SEC of any of the specific documents sought by the requests." ENF Post-Hearing Brief at 84. That argument has been thoroughly discredited. Indeed, it carefully sidesteps the key issue: all of the Chinese legal experts agree that it is illegal

---

[40] Dahua, for example, did not even see written instructions from the CSRC until June 2012. Ji Tr. 2088:16-2089:25. There is simply no evidence of any "conspiracy."

[41] The Division's position in these proceedings demonstrates the reasonableness of KPMG Huazhen's course of action and belies any inference of collusion. Even in the face of overwhelming evidence, the Division continues to claim that oral instructions should be ignored altogether and that the written directives are ambiguous and do not mean what they say. Given the Division's win-at-all-costs approach, it is entirely understandable that KPMG Huazhen would want the written directive to be as closely aligned with the repeated oral instructions as possible.

in China for Respondents to produce audit workpapers to foreign regulators without permission. *See* Clarke Tr. 2390:15-2391:15 (agreeing that approval from "some Chinese regulatory authority" is required before workpapers can be transferred abroad). The only dispute among the experts is whether written Chinese law—apart from any oral instructions—requires approval by the CSRC or by the SAA and SSB (none of whom have, in fact, approved any direct productions here). *See id.* at 2391:7-2392:3. The question whether Respondents "willful[ly] refus[ed]" cannot turn on such a minor difference of opinion over complex Chinese legal issues.

In any event, the Division has offered no new arguments—let alone identified any evidence—that support its erroneous construction of Chinese written law. First, the evidence is clear that the CSRC has asserted its authority over productions of audit workpapers to foreign regulators. That assertion of authority is based upon and completely consistent with Articles 6, 7 and 8 of Regulation 29, as well as Article 179 of the Securities Law and Article 3.12 of the Provisions on Function Allocation, Internal Department Arrangement and Personnel Make-up of the China Securities Regulatory Commission.[42] Respondents' Post-Hearing Brief at 34-35. Professor Clarke ignores some of these provisions, views the meaning of others as unclear, and bases his entire opinion to the contrary on a "structural analysis" of one subparagraph of Regulation 29. Clarke Tr. 2347:7-2349:18. As demonstrated in Respondents' Post-Hearing Brief, this cramped, context-free analysis of Chinese law is not sufficient, as Professor Clarke himself ultimately acknowledges. Respondents' Post-Hearing Brief at 34-34; *see also* Clarke Tr. 2396:22-2397:20. Not surprisingly then, Professor Clarke is alone in his position, and is wrong.

Further, the Division can no longer contend that Respondents' audit workpapers do not contain state secrets, and it concedes that all of the audit workpapers constitute "archives" under

---

[42] Even if the CSRC's assertion of authority had been inconsistent with these laws, Respondents would have had no ability to challenge it. Clarke Tr. 2362:23-2363:3.

Chinese law that cannot be produced without authorization. ENF Post-Hearing Brief at 40; *see also* Clarke Expert Report ¶ 14 ("Audit work papers are deemed archives by the State Archives Administration. Such archives may generally not be transferred abroad without approval."). Thus, the Division merely claims that Respondents did not do enough to obtain the approval of the SSB and SAA to produce their workpapers. But, in the context of requests from foreign regulators, the CSRC has taken charge of coordinating with other Chinese authorities, and those authorities have specifically declined to deal directly with the CSRC's regulated entities (the Respondents).[43] Respondents' Post-Hearing Brief at 36-38.

The notion that Respondents themselves could have unilaterally identified and produced documents that "clearly did not implicate state secrets" without the involvement of the Chinese authorities, *see* ENF Post-Hearing Brief at 86, is divorced from reality. First, other directives and Chinese laws prohibit direct production of any documents, and so screening for state secrets would not have permitted Respondents to produce the workpapers without authorization in any event. Second, given the heightened sensitivities present in this context, it would have been unreasonably risky for Respondents to try to determine which documents constitute state secrets without the involvement of the Chinese authorities. *See* Respondents' Post-Hearing Brief at 40 n.26. Indeed, under the CSRC's new screening procedures, the CSRC has provided Respondents with guidance on state secret issues, and has the opportunity to review the screened documents before they are produced. *Id.* at 39. That process has made clear that workpapers did, in fact, contain state secrets. Bypassing this process would have exposed Respondents to severe and unreasonable risks of criminal punishment.

---

[43] Tellingly, Professor Clarke concedes that the CSRC is authorized to require notice and approval when foreign regulators request audit workpapers from China-based firms. Clarke Tr. at 2361:20-2363:3, 2364:14-20; Clarke Expert Report ¶¶ 51, 54.

In another stretch regarding state secrets, the Division contends that "[p]rotection of state secrets was a (distant) secondary concern," apparently because "[o]nly a few documents . . . have been determined to contain state secrets." ENF Post-Hearing Brief at 4. But this is both a non-sequitur and rank speculation—the Division has offered absolutely no evidence on the importance the Chinese authorities attached to the "protection of state secrets"—and the expert testimony is uniformly to the contrary. *See, e.g.*, Clarke Expert Report ¶ 23 ("The unauthorized disclosure of state secrets can lead to criminal penalties."); Clarke Tr. 2397:21-25 (same); Feinerman Expert Report ¶ 31 (explaining China's "longstanding interest in protecting sensitive information," including "a huge body of what are classified as 'state secrets'"). Certainly, the quantity of documents that contained state secrets says nothing about the degree of Chinese governmental interest in the information that *was* deemed state secret. Until the entirety of Respondents' documents were subject to the newly-established screening process approved at the highest levels of the Chinese government, there was no way to know what documents contained, in the Chinese government's view, state secrets. Contrary to the Division's position, the combined actions of the Chinese authorities make clear that protection of state secrets and other sensitive information was (and is) of paramount importance.[44]

Finally, the Division continues its efforts to muddy the otherwise unambiguous October 2011 written directives. ENF Post-Hearing Brief at 88-90. As demonstrated in Respondents' Post-Hearing Brief, the evidence firmly establishes that these directives themselves require

---

[44] The Division implies that purported productions by issuers and other audit firms suggest that the applicable Chinese laws are not serious or otherwise may permit direct production to the SEC. *See* ENF Post-Hearing Brief at 21, 23, 29, 30, 79-80. That suggestion is completely unsupported. As discussed in Respondents' Post-Hearing Brief at 43-46, the evidence supporting the Division's assertions about any such productions is wholly lacking. In any event, there is no question that to the extent such productions involved the unauthorized transfer of archives (workpapers) or state secrets outside of China (as any production by Respondents undeniably would), they were in violation of Chinese law.

Respondents to obtain approval from the CSRC before producing audit workpapers to foreign regulators. Respondents' Post-Hearing Brief at 38-40. Indeed, the very fact that the CSRC issued a written letter at all is significant. *Id.* at 38. Ultimately, however, even if the Division were correct (which it is not) that the letters "simply instruct[] recipients to follow existing law," ENF Post-Hearing Brief at 88, the evidence establishes that "existing law" does not permit direct production of audit workpapers without the permission of the relevant Chinese authorities—in this case, the CSRC.[45]

3. The Division's Attempt to Diminish the Chinese Laws as "Blocking Statutes" is Unfounded and Legally Irrelevant.

Ultimately, with no other choice but to acknowledge the existence of Chinese legal impediments, the Division now argues that because the "Chinese legal regime" was allegedly "designed to block, and in fact did block, the SEC's access to audit workpapers," Respondents' inability to produce workpapers constitutes a "willful refusal." ENF Post-Hearing Brief at 73-74. This argument is also inconsistent with the law and the evidence.

As an initial matter, the Division's argument is a non-sequitur. The labeling of the relevant Chinese legal regime has no bearing on Respondents' good faith, or even whether their

---

[45] The Division argues that Respondents' "reliance on the Reply is undercut by their own desperate attempt during the hearing to substitute a new English translation," *i.e.*, Respondents Ex. 246A. ENF Post-Hearing Brief at 90. Respondents did no such thing. At the request of the Division and the Court, Respondents submitted certified translations to complement the informal versions that were already on their exhibit list. The certified translation was prepared by a professional translator, and did not include the phrase "in violation of the relevant laws," which the Division has focused upon. That suggests the Division has overemphasized that language. But none of this changes the fact that the Division's view of the directives (i) admittedly renders the phrase "without authorization" redundant and (ii) is contradicted by Professors Tang and Feinerman and all of Respondents' percipient witnesses. *See* Respondents' Post-Hearing Brief at 38 n.25. At bottom, Respondents' witnesses testified to their understanding of the letters (written in Mandarin), which confirmed their understanding that they could not produce workpapers directly to the SEC.

conduct is "volitional."[46] Respondents obviously bear no responsibility for the enactment of particular Chinese laws or the strategic decisions of their Chinese regulators. Respondents must follow these laws regardless of their purpose and, to paraphrase Professor Clarke, are in no position to challenge them. *See* Clarke Tr. 2362:23-2363:3. The Division's suggestion that Respondents' "good faith" (or even "volitional" conduct) turns on factors entirely beyond their control is inconsistent with well-settled law. *See, e.g.*, *Société Internationale*, 357 U.S. at 211 (no finding of willfulness where "failure to satisfy fully the requirements of [a] production order was due to inability fostered neither by [party's] own conduct nor by circumstances within its control"). Further, if the Division were correct that the Chinese authorities had set out to block the SEC's access to audit workpapers, that would only underscore the risks Respondents would face for violating those laws, including the severity of punishment. *See* Respondents' Post-Hearing Brief at 42-43.

In any event, the evidence overwhelmingly establishes that the relevant Chinese laws do not meet the Division's (or any other) definition of "blocking statute." The Division itself defines a "blocking statute" as a law "designed to take advantage of the foreign government compulsion defense . . . by *prohibiting* the disclosure, copying, inspection or removal of documents located in the territory of the enacting state in compliance with orders of foreign authorities." ENF Post-Hearing Brief at 74 (emphasis added). The Division acknowledges, however, that China's state secrets and archives laws have general application outside the context of producing documents to foreign regulators. ENF Post-Hearing Brief at 80 ("Because

---

[46] For this reason, U.S. courts consider the respective sovereign interests in initially determining the *enforceability* of document requests that require violation of foreign law, and not when considering sanctions for noncompliance. *See, e.g.*, *United States v. First Nat'l Bank of Chi.*, 699 F.2d 341, 345 (7th Cir. 1983) (requiring consideration of "the competing interests of the nations whose laws are in conflict" in determining the enforceability of a document demand, rather than in considering any sanctions for noncompliance).

audit workpapers are considered archives under Chinese Archives Law, even copies generally cannot be transferred outside of Mainland China without authorization."); Clarke Report ¶¶ 19, 35-36; Clarke Tr. 2397:21-25; Tang Tr. 2416:16-22, 2427:1-6; Feinerman Tr. 2542:18-21. These laws are certainly not "designed to take advantage of the foreign government compulsion defense," but instead to protect China's sovereign interests in information located within its borders. Feinerman Report at ¶¶ 31-32; Tang Report at ¶¶ 39-40. They prohibit all forms of unauthorized disclosure, as demonstrated by prior criminal prosecutions for violation of China's state secrets law. *See, e.g.*, *China Jails US Geologist for Stealing State Secrets*, BBC News, July 5, 2010, http://www.bbc.co.uk/news/10505350 (describing an American geologist sentenced to eight-year prison sentence for violating State secrets laws by arranging for the sale of an "openly available database about China's largely state-controlled oil industry" to his U.S. consulting firm); John Lee, *The Uncurious Case of Xue Feng's Jail Sentence*, Forbes.com, July 7, 2010, http://www.forbes.com/2010/07/07/xue-fengstern-hu-state-secrets-opinions-contributors-john-lee.html (describing a Chinese-born American convicted for violating state secrets law for obtaining and using "information about the Chinese steel industry that he apparently received while attending a conference"—"seemingly legitimate information . . . obtained from the normal course of business activities"). Both Professor Tang and Professor Feinerman have opined that because these Chinese laws have equal force to the disclosure of state secrets within China as they do to disclosure outside of China, they are not "blocking statutes." Tang Expert Report ¶¶ 15, 58; Feinerman Rebuttal Report ¶ 13. Those opinions stand unrebutted.

Nor is there any merit to the Division's contention that Respondents' alleged "abandonment of procedures" by which the SSB and SAA can screen the documents "further contributed to the overall blocking effect." ENF Post-Hearing Brief at 78-79, 80-81. As

demonstrated in Respondents' Post-Hearing Brief (at 50-51), Respondents never "abandoned" any such procedures. Instead, in the context of a request from foreign regulators, the CSRC has asserted its authority as the facilitating agency responsible for interacting with other Chinese authorities to ensure that documents are properly screened before they are produced. The SSB and SAA thus declined Respondents' efforts to seek determinations from them in this context. There is nothing further that Respondents could (or should) have done.

Similarly, the Division is wrong that Regulation 29 and the CSRC's and MOF's oral and written directives constitute "blocking statutes." Those laws and directives are not designed to "block" foreign regulators' access to workpapers, but instead to direct such workpapers through customary regulator-to-regulator channels. Indeed, this is exactly what the CSRC said in its oral directives to Respondents. *See* George Tr. 1602:12-18 (the CSRC "indicated that the appropriate channel for the production of . . . working papers would be through the CSRC themselves"). And it is clear from the face of the three written directives issued by the CSRC in October 2011.[47] Far from a "disfavored" blocking statute, this approach is common across the globe. *See* Respondents' Post-Hearing Brief at 74-75. In fact, it is the same approach adopted by such countries as the United Kingdom and Germany, and the Division has acknowledged the legitimacy of the foreign sovereign interests underlying that approach. *Id.*

Ultimately, recent developments demolish the Division's attempt to categorize these laws as "blocking statutes." In July 2013, the CSRC produced 20 boxes of hard-copy audit

---

[47] *See* Respondents Ex. 245A ("Any foreign securities regulatory agency who seeks audit and other documents . . . shall consult with its Chinese counterpart to find a solution through regulatory cooperative mechanism."); Respondents Ex. 546A ("Where foreign securities regulatory authorities request relevant audit work papers and other documents . . . , they should consult and seek resolution with the PRC regulatory authority based on established audit oversight cooperation."); Respondents Ex. 246A ("Any foreign regulatory authority seeking access to archive files (including audit work papers) . . . shall consult with its Chinese counterpart to find a solution through regulatory cooperation mechanism.").

workpapers and a disc of electronic files at the request of the SEC. Respondents Ex. 642; George Tr. 1636:8-23. The CSRC has been actively working with Respondents and other Chinese authorities to facilitate the production of the DTTC Client A, Client G, Client C, Client D, and Client F workpapers. *See* George Tr. 1636:24-1637:23 (discussing DTTC Client A and Client G); Leung Tr. 1480:20-25 (Client C); Respondents Exs. 632, 649A, 650A; Yan Tr. 1926:3-1927:13. [redacted] The Division's own conduct acknowledges the significance of these developments—as they have apparently caused the Division to reverse course and [redacted] after arguing throughout the hearing that such efforts would be "futile."

The record plainly demonstrates that the relevant Chinese laws are not blocking statutes. In any event, the Division's "blocking statute" analysis is not relevant to Respondents' good faith.

IV. THE SECTION 106 REQUESTS ARE UNENFORCEABLE

The Division cannot establish a "willful refusal to comply" with the Section 106 requests if those requests themselves are not enforceable, and Respondents therefore would have no legal obligation to comply with them. Respondents' Post-Hearing Brief at 63-75. And the enforceability of these requests depends on a number of factors derived from principles of international comity. Nonetheless, the Division contends that (1) principles of international comity are not applicable to this case, ENF Post-Hearing Brief at 95-96; (2) the record has not

established the existence of Chinese legal impediments to production, *id.* at 96-97; and (3) the factors would permit enforcement of the requests in any event, *id.* at 97-108. The Division is wrong on every count.

A. The Division Incorrectly Contends that Well-Settled Principles of International Comity Do Not Apply to this Proceeding.

The Division's position that traditional comity principles do not apply in this proceeding is contrary to the law and the evidence. First, it does not matter that the Division purports not to seek enforcement of the Section 106 requests in this proceeding. ENF Post-Hearing Brief at 95-96. The Division attempted to skip that step and to seek to impose sanctions based on non-compliance. Not even the Division would suggest that Respondents could be sanctioned based on invalid or otherwise unenforceable requests, but that is precisely what the Division is asking this Court to do. Therefore, the question whether these requests are enforceable remains, and the comity analysis must be used to answer it. *See* Restatement (Third) of Foreign Relations Law of the U.S. § 442 (1987) (providing that a "court *or agency of the United States*" must address these considerations of international comity in determining the enforceability of document demands (emphasis added)); *In re Sealed Case*, 825 F.2d at 498 (considering comity principles in relation to grand jury subpoena); *Banca Della*, 92 F.R.D. at 117-19 (considering comity principles in relation to SEC subpoena).

Second, as discussed in Section II.A.3, *supra*, the circumstances of this proceeding particularly require resort to principles of international comity. As discussed, the Division's claim that this proceeding does not "'touch[]'" the "'interests'" of China is wrong. ENF Post-Hearing Brief at 96. Congress was clearly sensitive to foreign sovereign interests in enacting Section 106 and amending it in Dodd-Frank, including by codifying the "alternate means" approach and providing that only a "willful refusal to comply" will constitute a violation of the

federal securities laws. In this proceeding, the Division seeks to punish Respondents for complying with the laws of their home country. And the sanctions sought by the Division would destroy Respondents' ability to provide services to a meaningful segment of their clients and prevent China-based U.S. issuers from maintaining their listings on U.S. exchanges. Therefore, both Respondents and China-based issuers would lose the extensive investments they have made to comply with U.S. exchange requirements. Thus, for the same reasons outlined in Section II.A.3, *supra*, comity considerations must be evaluated in considering the enforceability of the Section 106 requests.

B. The Division Has Acknowledged That Chinese Law Prohibits Respondents' Direct Production of Documents to the SEC.

As demonstrated in Section III.C, *supra*, there can be no legitimate claim that Chinese legal impediments to direct production do not exist, and the Division has conceded the point in its Post-Hearing Brief. The Division's Chinese law expert recognized that we can "agree that approval is generally required by some Chinese regulatory authority before [workpapers] can be transferred abroad." Clarke Tr. 2390:15-2391:15.[48] Accordingly, there is now no question that direct production is prohibited; rather, the only dispute relates to which Chinese agency is responsible for the review, approval, and transmission of productions. That debate has been settled by China's State Council, which placed the CSRC at the forefront of the newly approved process, precisely as contemplated by Regulation 29. Respondents' Post-Hearing Brief at 39, 64-65. Accordingly, the Section 106 requests can only be enforced if the relevant comity factors allow it.

---

[48] *See also* ENF Post-Hearing Brief at 80 ("Because audit workpapers are considered archives under Chinese Archives Law, even copies generally cannot be transferred outside of Mainland China without authorization by the Chinese government.").

C. Traditional Comity Analysis Demonstrates That the Section 106 Requests Are Unenforceable.

The evidence presented at the hearing fully supports Respondents' previous assertions regarding the correct analysis as to the application of the comity factors, while the Division simply ignores the facts that it views as unfavorable. As Respondents demonstrated in their Post-Hearing Brief at 63-76, the availability of an alternative means for obtaining the documents (which seems to become clearer with each passing day) and the other comity factors support a finding that the instant Section 106 requests are not enforceable. Indeed, binding precedent in this Circuit sets a particularly high bar for the Division to meet in enforcing the Section 106 requests, even when an alternate means of production is not so readily available. See *In re Sealed Case*, 825 F.2d at 499 ("Though we recognize that the grand jury's investigation may nonetheless be hampered, perhaps significantly, we are unable to uphold the contempt order against the bank."). Nothing in the Division's Post-Hearing Brief satisfies this high bar.

Alternative Means. The ability to obtain requested documents through an alternative means substantially undermines the enforceability of document demands that would require the violation of foreign law. Here, there is now no doubt that the requested documents can be obtained through the CSRC, and the Section 106 requests therefore cannot be enforced under well-settled principles of international comity. Respondents' Post-Hearing Brief detailed the testimony and documentary evidence that decisively undermined the Division's position to the contrary, including but not limited to the voluminous production of Longtop documents and the CSRC's efforts to produce the DTTC Client A and Client G workpapers as soon as the CSRC process is complete. The Division clings to its position that the CSRC is not a viable gateway to obtain the requested audit workpapers. But in the days since that brief was filed, any remaining support for the Division's position has evaporated.

Specifically, on September 11, 2013, [redacted] And recent correspondence produced by the Division makes clear that, [redacted]. Most significantly, on September 13, 2013, the SEC itself [redacted]. Those [redacted] reflect a significant reversal of the Division's position. At the hearing, the Division's witnesses repeatedly testified that, based on discussions with OIA, they concluded that formal requests to the CSRC would not bear fruit. *See, e.g.*, Rana Tr. 182:23-183:14, 186:12-187:5; Peavler Tr. 276:11-16; Kaiser Tr. 385:4-13; Weinstein Tr. 623:9-24; Kazon Tr. 757:19-758:4. The Division itself has consistently taken the position—as recently as two weeks before [redacted]—that "making additional requests to the CSRC would be a waste of its time, as the CSRC had shown that it was simply not a viable gateway for obtaining assistance."[49] *See, e.g.*, ENF Post-Hearing Brief at 41.

Presumably, the SEC has recognized the importance of these recent developments, and has re-evaluated its position about the viability of the CSRC as an alternative means of production. The Division (along with OIA) has repeatedly contended that this proceeding would be rendered altogether unnecessary if such developments occurred.[50] [redacted]

---

[49] This position was based in part on the Division's contention that the CSRC had failed to meet its obligations under the IOSCO MMOU. ENF Post-Hearing Brief at 102. But the SEC could not even agree internally on what the IOSCO MMOU required in this context, with the OIA Director concluding that the IOSCO MMOU did not apply here. Respondents' Post-Hearing Brief at 69 n. 53. Accordingly, such a broad statement is mere rhetoric and lacks any probative value.

[50] *See, e.g.*, Respondents Ex. 482 [redacted]

[redacted][51] OIA again affirmed it by [redacted] The Division is right on this score. The availability of a regulator-to-regulator path has rendered this proceeding unnecessary and inappropriate; indeed, the Section 106 requests themselves are not even enforceable in the circumstances.[52] Further, as set forth in Respondents' Post-Hearing Brief at 70 n. 55, the availability of an alternate means has statutory implications under Section 106. Having chosen to pursue alternate means of production under Section 106(f), the Division cannot now punish Respondents for the failure to produce documents that are available through the CSRC. *Id.*

Sovereign Interests. Yet again, the Division has mischaracterized the sovereign interests at stake in this proceeding. It claims that the "U.S. has a stronger interest in preventing non-transparent audits than China has in blocking regulators' full access to workpapers." ENF Post-Hearing Brief at 98 (initial capitals deleted). But the only thing that the current PRC regime prevents is Respondents' *direct* production of workpapers to the SEC. There is a new process

---

[51] Respondents Ex. 638 [redacted]

[52] Previous time lapses related to requests for assistance from the CSRC are now immaterial, and were at least partially based on the fact that prior to the SEC's request for the DTTC Client A workpapers, the CSRC had never received a request for workpapers from a foreign regulator. *See* Respondents Ex. 469 (E-mail from D. Tong to E. Tafara and K. Brockmeyer (Mar. 30, 2012)) (stating that the DTTC Client A request "is the first time that a Chinese regulator is trying to provide to a foreign regulator Chinese audit working papers"). Furthermore, the SEC did not assist in expediting the production process as it rejected an interim approach that would have allowed it to view documents and pursue items and issues found in those documents through other avenues. Respondents' Post-Hearing Brief at 68-70.

that allows the SEC to obtain documents from the CSRC, and it has resulted in the production of workpapers and other documents. Moreover, the Division understates the validity of China's decision to channel through its regulators all document requests from foreign regulators, which contradicts the Division's own previous statements[53] and which the SEC has respected as recently as [redacted]. Respondents' Post-Hearing Brief at 75. Such a regime can hardly be considered a blocking statute, as explained in Section III.C.3, *supra*. Although the Division might prefer to obtain documents directly from Respondents, the existence of a viable alternative means for obtaining the documents minimizes the U.S. interest at issue.

As explained in Section III.C.2, *supra*, the Division's attack on China's policy of protecting state secrets also falls short. The Division's assertion that "[o]nly a few documents sought by the Requests have been determined to contain state secrets" misses the mark entirely. ENF Reply at 4. The Division fails to acknowledge that state secrets have been identified in *every* set of workpapers produced to the CSRC to date. Respondents' Post-Hearing Brief at 39-40. In any event, there is no connection between the quantity of documents identified as containing state secrets within a given set of workpapers, and the importance of the state secret information and process. The CSRC's new procedures reflect a significant investment of time and attention by Chinese regulators to these issues, and leave no doubt of the importance of these issues.

---

[53] SEC's Reply Memorandum in Support of Its Application for Order Requiring Compliance with Subpoena at 3, *SEC v. Deloitte Touche Tohmatsu CPA Ltd.*, 11 Misc. 512 GK/DAR (D.D.C. Dec. 3, 2012) ("For example, DTTC notes that Germany and the United Kingdom take analogous positions to that of the CSRC with regard to direct production of certain documents abroad. And we agree that, in that case, Germany's and the United Kingdom's sovereign interests are valid and, generally speaking, should be respected." (internal citation omitted)).

Ultimately, the Chinese government has a legitimate interest in coordinating all document requests from foreign regulators and protecting state secrets. Meanwhile, a new process has been deployed that will provide U.S. regulators with a viable gateway to obtain documents, thereby significantly limiting their interest in requiring Respondents to produce them directly.

Importance of the Requested Documents. The Division's conclusory claims aside, the documents at issue in this proceeding cannot be considered as important as they otherwise might be where the Division has abandoned any attempt to enforce the requests—a fact that it repeats on numerous occasions. *See, e.g.*, ENF Post-Hearing Brief at 58, 95, 96-97. Furthermore, until just days ago, the PCAOB and SEC had sought documents from the Chinese government in only half of the ten investigations at issue in this proceeding. Respondents' Post-Hearing Brief at 72. Indeed, several of the Division's witnesses—those same witnesses who insisted that getting the documents was critical—had not even read the PCAOB MOU that would have entitled the Division to get them otherwise, and one was not even aware of it. *See* Josephs Tr. 89:6-91:4; Weinstein Tr. 683:4-23; London Tr. 922:17-923:1; *see also* Arevalo Tr. 1106:23-1107:19 (explaining that he "read [the MOU] very quickly"); Kaiser Tr. 452:19-453:14 (unaware of PCAOB MOU). Against that backdrop, the Division cannot credibly claim that Respondents' inability to produce the requested documents directly has "egregiously disrupt[ed]" the ten enforcement investigations that it has continued to pursue. ENF Post-Hearing Brief at 6. The evidence clearly shows otherwise: as the Division's own witnesses testified, those investigations have yielded multiple complaints, formal actions, and relief such as injunctions, civil penalties, and officer-and-director bars. *See* ENF Post-Hearing Brief at 68 n.32 (recounting the various successful civil suits filed by the SEC against Respondents' issuer clients); Respondents' Post-Hearing Brief at 73-74; *see also, e.g.*, Rana Tr. 199:19-200:6.

The Division also fails to acknowledge Respondents' roles in bringing potential issues at the issuers to the attention of the appropriate company personnel, the investing public, and the SEC itself. It simply states that "[t]he underlying investigations were begun based largely on cursory public announcements by the issuers." ENF Post-Hearing Brief at 106. That ignores the fact that several of the "public announcements" were required based on Respondents' actions. Respondents contacted the clients' audit committees, issued Section 10A letters, and resigned as auditors when appropriate—facts that the Division conveniently ignores. Respondents' Post-Hearing Brief at 61.

Hardship of Compliance. The Division's arguments also fail to properly appreciate the potential hardships that Respondents would face if the Section 106 requests were deemed enforceable and they were required to produce the requested documents. As explained in Respondents' Post-Hearing Brief, each of the Chinese law experts confirmed that the Chinese authorities could dissolve Respondents, revoke their licenses, or subject their personnel to criminal penalties. Respondents' Post-Hearing Brief at 41-43.[54] Such penalties are devastating and amount to a corporate "death penalty." There is no reason to expose Respondents to such risks when the documents can be obtained through the CSRC.[55] The record clearly demonstrates—and the Division is unable to refute—that Respondents and their personnel would

---

[54] *See also* Clarke Tr. 2397:21-25; Tang Tr. 2416:16-22, 2427:1-6; Feinerman Tr. 2542:18-21; Tang Expert Report ¶¶ 68-79; Tang Rebuttal Report ¶ 3; Tang Tr. 2415:7-17, 2424:23-2425:5; Feinerman Expert Report ¶¶ 47-48; Feinerman Rebuttal Report ¶ 10; Clarke Tr. 2403:3-2405:11 (agreeing that the MOF has "the power in certain circumstances to dissolve or revoke the license of accounting firms," and "therefore, accounting firms need to worry about what the MOF thinks"); Clarke Rebuttal Report ¶ 23 (same).

[55] The Division misconstrues *Richmark* and *Banca Della* as discussed in Section III.A, *supra*, to suggest that the mere fact that Respondents were involved in the U.S. market means their hardship should be ignored. Every case involving comity analysis involves foreign actors that have contact with the U.S., otherwise they would not be subject to the jurisdiction of U.S. courts. *See id.* Such a simplistic view of this factor is incorrect.

face severe criminal, administrative, and civil sanctions for violating Chinese law in these circumstances. *See id.* at 41-43.

Location of Information and Parties. Despite acknowledging that "the extent to which the required conduct is to take place in the territory of the other state" and "the nationality of the person" are relevant to the comity analysis, the Division does not address these factors. ENF Post-Hearing Brief at 97. Presumably, this is an admission of the obvious by the Division: production of the requested documents would require China-based audit firms and individuals to violate written Chinese law and explicit, binding oral directives from Chinese regulators on Chinese soil. These facts weigh heavily against enforcement.

Application of the traditional comity analysis thus dictates the conclusion that the Section 106 requests at issue are not enforceable. Each factor weighs in favor of non-enforcement, an unsurprising result considering the scope and novelty of the Division's efforts in this proceeding. Ultimately, when a national regulator has the ability to legally obtain documents from its foreign counterpart, comity considerations should not, and do not, allow it to require a foreign citizen to violate foreign law on foreign soil.[56] *See In re Sealed Case*, 825 F.2d at 497-98.

V. BECAUSE THE DIVISION STILL HAS NOT OFFERED ANY EVIDENCE THAT RESPONDENTS' LEGAL OBLIGATIONS WERE OBJECTIVELY CERTAIN, SAFECO PRECLUDES SANCTIONS

The Division takes the remarkable position that the "objective reasonableness" of Respondents' conduct is "legally irrelevant." ENF Post-Hearing Brief at 108. That contention is directly contrary to the Supreme Court's holding in *Safeco*, 551 U.S. 47, and the Division's weak efforts to escape that holding are entirely without merit.

---

[56] Respondents' good faith is addressed throughout Section III, *supra*.

First, the Division suggests that the "question whether the company's conduct was 'objectively reasonable' was germane to liability only because the Supreme Court held that the civil liability provisions of the FRCA included reckless conduct." ENF Post-Hearing Brief at 108. That is wrong. The Court made clear in *Safeco* that a party cannot be found to have acted "willfully" under *any* interpretation of that term—including the "knowing" standard and not merely under the "recklessness" subcategory of *mens rea*—where its legal obligations were objectively ambiguous. *See* 551 U.S. at 70 n. 20 ("To the extent that they argue that evidence of subjective bad faith can support a willfulness finding even when the company's reading of the statute is objectively reasonable, their argument is unsound. Where, as here, the statutory text and relevant court and agency guidance allow for more than one reasonable interpretation, it would defy history and current thinking to treat a defendant who merely adopts one such interpretation as a *knowing or reckless* violator." (emphasis added)). Indeed, there is nothing about *Safeco*'s holding that suggests a sensible distinction between these fine gradations of intent. To the contrary, if a party cannot act recklessly where its obligations are uncertain, its conduct certainly cannot satisfy a higher "knowing" standard. The uncertainty of Respondents' legal obligations is therefore directly relevant to the analysis here. *Accord AFL-CIO v. FEC*, 628 F.2d 97, 101 (D.C. Cir. 1980) ("It is clear that uncertainty as to the meaning of the law can be considered in assessing the element of willfulness in a violation of the law.").

Second, the Division has offered no evidence to rebut the plainly obvious point that Respondents' legal obligations were unsettled at the time that they were unable to produce documents to the SEC. The Division points only to the fact that Respondents designated U.S. agents under Section 106(d) to accept service of document requests, ENF Post-Hearing Brief at 67, but that has no bearing on the fundamental question whether such demands—directing

Respondents to violate the laws of their home country—would be enforceable in the first instance or if failure to produce the documents in those circumstances would constitute a "willful refusal." (If anything, it is only further evidence of Respondents' good faith efforts to comply to the fullest extent possible with the procedures set out by U.S. regulators.)[57] Indeed, Respondents made known from the very outset the obstacles under Chinese law to any direct production of workpapers.[58] Although the PCAOB, in approving Respondents' registrations, reserved the right to "contest[] the invocation of any particular non-U.S. law that [Respondents] might raise as an obstacle to complying with a Board demand or as a defense to a Board sanction for noncooperation," ENF Exs. 6-10, it has never done so.[59]

The Division's other apparent contention—that the issuance of Wells notices by SEC Staff somehow "ma[de] clear that" Respondents "were obligated to produce documents to the SEC in response to the Requests"—is similarly misguided. ENF Post-Hearing Brief at 109. Contrary to the Division's apparent view of its authority, the Wells notice is the beginning, not the end, of the process of determining a party's legal obligations. The very purpose of a discretionary Wells notice is to "provide[] the recipient the opportunity to set forth his version of the law or facts." *SEC v. Internet Solutions for Bus., Inc.*, 509 F.3d 1161, 1163 n. 1 (9th Cir. 2007) (citation and internal quotation marks omitted); *see generally* SEC Enforcement Manual § 2.4 ("The Wells Process") (Nov. 2012), available at http://www.sec.gov/divisions/enforce/

---

[57] In fact, no Respondent has disputed service of the Section 106 requests in accordance with Section 106(d).

[58] Respondents Ex. 205, Ex. 99.2; Respondents Ex. 40, Ex. 99.2; Respondents Ex. 1, Ex. 99.2; Respondents Ex. 365, Ex. 99.2; Respondents Ex. 513, Ex. 99.2.

[59] Instead, the PCAOB has continued to work with the Chinese government to obtain documents. It executed its own MOU with the CSRC, Respondents Ex. 274, and has made requests pursuant to that MOU, Respondents Ex. 632A; Respondents Ex. 650A.

enforcementmanual.pdf. It cannot also serve to establish Respondents' otherwise uncertain legal obligations under *Safeco*.

The Division makes no attempt to dispute this Circuit's presumption against the enforceability of document demands that require a violation of foreign law on foreign soil. *See, e.g., In re Sealed Case*, 825 F.2d at 498. Nor has it made any effort to overcome that presumption by seeking enforcement in federal court of the Section 106 requests underlying this proceeding. The Division likewise does not dispute that this is a case of first impression, because in *every* other instance the Commission has consistently *refrained* from forcing foreign firms to violate the laws of their home countries, opting instead to pursue sovereign-to-sovereign solutions in earnest with its foreign counterparts. *See* Atkins Tr. 2654:7-21. Finally, whatever construction of "willful refusal" the Court decides to adopt at this stage, it "def[ies] history" and common sense to suggest that Respondents' legal obligations under Section 106(e) were susceptible only to *the Division's* understanding prior to this novel proceeding. *Safeco*, 551 U.S. at 70 n. 20; *see* Tr. 1228:13-22 (Judge Elliot noting, a week into the Hearing, that the interpretation of "willful refusal" was "wide open").

Because Respondents acted reasonably in the face of "less-than-pellucid statutory text" and a "dearth of guidance," they cannot be found to have committed a *willful refusal* to produce documents in violation of Section 106, or a "willful violation" under Rule 102(e)(1)(iii). *Safeco*, 551 U.S. at 70.

VI. IMPOSING SANCTIONS WOULD BE INAPPROPRIATE AND WOULD HARM THE PUBLIC INTEREST

As shown in Respondents' Post-Hearing Brief, the sanctions the Division seeks pursuant to Rule 102(e)—(1) a censure, (2) a permanent bar from issuing audit reports for issuers with securities traded in the United States, and (3) a permanent bar from playing a 50 percent or

greater role in the audits of such issuers (the "Proposed Bar")—are inappropriate and would be manifestly contrary to the public interest. Nothing in the Division's Post-Hearing Brief supports any of these proposed sanctions.

The Division's Post-Hearing Brief focuses on a point-by-point analysis of the so-called "*Steadman*" factors that the Commission traditionally considers in deciding whether to impose sanctions. *See Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979). As shown below and in Respondents' Post-Hearing Brief at 84-89, application of the *Steadman* test weighs heavily against imposing sanctions. But the Division's focus on *Steadman* misses the more fundamental point: that the Proposed Bar would not serve—and would actually disserve—the overriding objectives of sanctions, namely, preventing future misconduct and serving the public interest.

It speaks volumes that the Division devotes its attention to what happened in the past but spends little if any time discussing either the likelihood of future "misconduct" or why the Proposed Bar is necessary to prevent any such future "misconduct." The reason is simple: the Division has nothing to say about either of these topics. Now that workpapers and other documents are being produced by the CSRC to the SEC pursuant to the IOSCO MMOU and now that the SEC can avail itself of the PCAOB's MOU with the CSRC and the MOF,[60] there is no reason to believe either (1) that there would be any future "misconduct" (*i.e.*, nonproduction of

---

[60] The Division pains itself to explain why the PCAOB's MOU changes nothing, yet none of its arguments goes to the question of whether the MOU will actually be effective, *see* ENF Post-Hearing Brief at 122-23, and every indication is that it will be. By its plain terms, it covers audit workpapers and permits the PCAOB to share them with the SEC, which can then use the workpapers in enforcement matters. *See* Respondents' Post-Hearing Brief at 73-74. Moreover, the Division's representation of the SEC as operationally independent from the PCAOB conflicts with the Government's own representation before the Supreme Court that the Commission "could govern and direct the Board's daily exercise of prosecutorial discretion by promulgating new SEC rules, or by amending those of the Board." *Free Enterprise Fund v. Pub. Co. Accounting Oversight Bd.*, 130 S.Ct. 3138, 3159 (2010).

documents to the SEC), or (2) that the severe sanctions the Division seeks are the only or best means to obtain documents from China.

Similarly, the Division has little if anything to say about the effect of its Proposed Bar on the public interest as a whole. To the extent the Division engages in any analysis of its Proposed Bar, its discussion is remarkably weak. For example, it asserts tepidly that Respondents' clients at issue "would not necessarily" be forced to delist if the Proposed Bar were ordered (ENF Post-Hearing Brief at 125), a dubious assertion that depends on the willingness of "substitute auditors" to violate China law and the Division's implicit approval of such conduct. In the end, the Division acknowledges that its Proposed Bar will have collateral impacts, claiming that the Proposed Bar is "tailored to limit collateral effects on other market participants" [redacted] *Id.* at 125, 128. Yet, the Division, eschewing thoughtful analysis, advocates that these costs are worth it in order to put Respondents out of the business of auditing U.S. issuers, even though Respondents' past conduct was dictated by Chinese law and the directives of the Chinese government and even though there is no reasonable basis for believing that future "misconduct" will occur.

There are several other sound reasons to reject the Division's Proposed Bar, discussed in more detail below. First, the Division's proposed sanctions are unwarranted under the *Steadman* factors. Respondents did not act egregiously or in bad faith. They were and remain ready and willing to produce workpapers in response to the Division's requests, but have been unable to do so because of legal impediments imposed by Chinese law, including express directives from Chinese regulators that production directly to the SEC would violate Chinese law and subject Respondents to serious legal liability, and the lack of agreement between the CSRC and SEC for

the production of documents. Second, the Division's proposed sanctions would be fundamentally unfair and violate long-established Commission policies and practices, because the Commission has long relied on inter-regulator cooperation to obtain documents in foreign countries. Third, the Division's proposed sanctions would inflict substantial—and unnecessary—harm on Respondents, their issuer clients, and investors. As shown at the hearing, the Division's Proposed Bar would cause as many as [redacted] issuers with securities traded in the U.S. to lose their chosen auditors. These issuers face a high likelihood of being unable to find qualified replacement auditors and of being delisted from the exchanges on which they currently trade. The impact on investors from such delisting is undeniable: [redacted]

A. Sanctions Are Not Warranted Under the *Steadman* Test.

"The Commission may impose sanctions for a remedial purpose, but not for punishment." *McCurdy v. SEC*, 396 F.3d 1258, 1264 (D.C. Cir. 2005). For this reason, any sanction must focus principally on—and be rationally related to—preventing future misconduct. *See SEC v. Patel*, 61 F.3d 137, 141-42 (2d Cir. 1995). To guide this inquiry, the Commission has traditionally followed the multi-factor "*Steadman*" balancing test as part of its assessment of whether sanctions are warranted.[61]

Despite the D.C. Circuit's clear instructions in cases such as *McCurdy* and *Patel*, the Division's primary argument in support of sanctions is that Respondents allegedly committed "serious infractions that warrant a stringent" sanction. ENF Post-Hearing Brief at 116. The question in Rule 102(e) proceedings, however, is not whether Respondents were "bad" and

---

[61] *Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981).

"must be punished." *Blinder, Robinson & Co. v. SEC*, 837 F.2d 1099, 1113 (D.C. Cir. 1988). It is whether sanctioning Respondents is "necessary to protect the investing public and the Commission from the future impact on its processes of professional misconduct." *In the Matter of William R. Carter, et al.*, Exchange Act Release No. 17597, 1981 WL 384414, at *5 (Feb. 28, 1981) (emphasis added). As set forth in Respondents' Post-Hearing Brief and below, under these standards the Division has not shown it is entitled to the harsh sanctions it seeks.

1. Respondents' Actions Were Not Egregious.

The Division argues that Respondents' conduct in this case was "egregious" based *solely* on the harm it claims the Commission's investigative processes suffered from being unable to obtain workpapers directly from Respondents. *See* ENF Post-Hearing Brief at 118. The Division overlooks, however, that whether a respondent's actions should be considered "egregious"—*i.e.*, "shocking" or "outstandingly bad"[62]—normally depends not just on what happened, but also on *why* it happened.[63] For this reason, courts focus on the respondent's state of mind and typically find conduct to be egregious only in cases of intentional or reckless misconduct. *See, e.g., SEC v. Bankosky*, No. 12 Civ. 1012, 2012 WL 1849000, at *2 (S.D.N.Y. May 21, 2012) (collecting cases). Respondents did not engage in intentional or reckless misconduct in this case. As shown at the hearing, they did not produce documents directly to the Division in response to its Section 106 requests only because doing so would have violated Chinese law and express instructions from their Chinese regulators. This factor favors Respondents.

---

[62] *Egregious,* Oxford Dictionaries, Oxford Univ. Press, http://oxforddictionaries.com/definition/american_english/egregious (last visited Sep. 16, 2013).

[63] The Division also would treat a respondent's inability to produce documents because of legal or other impediments the same as a respondent who has in fact acted in bad faith by intentionally refusing to cooperate or respond to the Division's requests.

The Division also attempts to rewrite the traditional standard of egregiousness applied in Rule 102(e)(1)(iii) proceedings by arguing that Respondents' motives are irrelevant and that even *negligence* is sufficient to support sanctions if the Commission's processes were harmed. *See* ENF Post-Hearing Brief at 118 (quoting *In the Matter of Gregory M. Dearlove, CPA*, 92 SEC Docket 1427, 2008 WL 281105, at *30 (Jan. 31, 2008)). The decision the Division cites for this proposition, however, was brought under the "improper professional conduct" prong of Rule 102(e)(1)(iv), a different subsection of Rule 102(e) that—unlike Rule 102(e)(1)(iii)—permits accountants to be sanctioned for "[r]epeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards, that indicates a lack of competence to practice before the Commission." *See Dearlove*, 2008 WL 281105, at *30. *Dearlove* is inapplicable to these Rule 102(e)(1)(iii) proceedings.

2. Respondents' Actions Were Isolated.

The Division argues that Respondents' conduct was "recurrent" because four (out of five) Respondents were unable to produce workpapers in response to Section 106 requests regarding multiple audit clients. ENF Post-Hearing Brief at 118-19. This argument fails on several fronts.

First, the Division does not explain how, under this standard, the conduct of Dahua could be considered "recurrent." As shown at the hearing, Dahua received only a single Section 106 request related to a single audit client. *See* Respondents Ex. 51; OIP ¶ 8; Ji. Tr. 2089:9-14.

Second, the Division omits to mention that eight of the ten Section 106 requests issued to Respondents were issued in a single wave between February 1 and February 16, 2012.[64] As

[64] Respondents Ex. 48 (Section 106 Request for Dahua Client A (Feb. 1, 2012)); Respondents Ex. 23 (Section 106 Request for Client C (Feb. 2, 2012)); Respondents Ex. 548 (Section 106 Request for Client D (Feb. 6, 2012)); Respondents Ex. 549 (Section 106 Request for Client E (Feb. 9, 2012); Respondents Ex. 547 (Section 106 Request for Client F (Feb. 3, 2012)); Respondents Ex. 141 (Section 106 Request for Client G (Feb. 14, 2012)); Respondents Ex. 382 (Section 106 Request for Client H (Feb. 8, 2012)); Respondents Ex. 408 (Section 106 Request for Client I (Feb 16, 2012)).

shown at the hearing, these requests were issued immediately after a January 31, 2012 meeting between the Division and DTTC's representatives in what appears to have been an orchestrated effort by the Division to bring its conflict with the CSRC to a head. *See* Josephs Tr. 139:14-143:14. And the Division issued them despite having been made fully aware that Respondents were prevented by Chinese law from complying. *See* DTTC's Pre-Hearing Brief at 10-14 (detailing events preceding Division's issuance of Section 106 requests). Indeed, many of the requests were the first contact Respondents had had from the SEC in months. *See id.* Respondents' actions to respond to this wave of requests were not "recurrent" conduct—if anything, they were "concurrent." To take one example, KPMG Huazhen responded to all three of the Section 106 requests it received in a single, 20-page letter explaining the legal impediments it faced and imploring the Division to seek the requested work papers through the CSRC. Respondents Ex. 556. Simply put, although the Division asked for work papers for multiple audit clients in its wave of Section 106 requests, each Respondent's inability to respond was a single event, not a recurring course of conduct. This factor, thus, favors Respondents.

3. Respondents Did Not Act With Scienter.

The Division does not seriously argue that Respondents acted with scienter. The closest it comes is to contend that Respondents acted "willfully" by registering with the PCAOB while knowing "that Chinese law *could* impair their compliance with U.S. rules" and then "consciously" not producing documents. ENF Post-Hearing Brief at 119 (emphasis added).

This argument fails by its own terms. The Division asserts (erroneously) that "willfully" means nothing more than "volitionally," by which it means an intent to do the act that constitutes a violation of law. *See id.* at 47-50. But acting "volitionally" is a far cry from acting with "scienter," a term that the Supreme Court defines as "a mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976).

Moreover, as shown *supra* at III.A, and in Respondents' Post-Hearing Brief at 53-60, the evidence shows that Respondents did not intend to, nor did they in fact, deceive or defraud anyone or act in any kind of bad faith when they registered with the PCAOB. To the contrary, they were completely transparent and candid about the limitations imposed by Chinese law on the production of documents. *See supra* at Section III.A.1. And they acted no differently from scores of other audit firms from countries with data privacy laws and other restrictions on the production of documents directly to a foreign government agency. *See id.* This factor weighs strongly in Respondents' favor.

4. Respondents Are Sincere in Their Assurances Against Future Violations.

The Division argues that this *Steadman* factor favors the Division because Respondents have not provided assurances against future violations. *See* ENF Post-Hearing Brief at 119. The Division, however, misstates Respondents' position. As shown at the hearing, Respondents' inability to provide workpapers directly to the Division in response to the Section 106 requests was dictated by express instructions from Chinese regulators and the lack of a working cooperative agreement between the regulators. Respondents have repeatedly assured the Division that to the extent U.S. and Chinese regulators now appear to have agreed on information-sharing mechanisms, Respondents will respond to future requests in whatever manner they are instructed under Chinese law.[65] In fact, workpapers recently have been produced to the SEC by the CSRC and the testimony at the hearing showed that the CSRC has adopted new procedures to facilitate sharing such documents with the SEC in the future.[66] As to

---

[65] *See, e.g.*, Wong, D. Tr. 1900:21-1901:5.

[66] Respondents Ex. 642; George Tr. 1635:4-1636:23 (describing the new procedures and noting that "Longtop working papers have now been produced by the CSRC to the SEC"); Leung Tr. 1476:18-1477:3; Chiu Tr. 1786:23-1787:5.

Dahua, as the Court is aware, that firm has exited this line of business and does not plan to re-enter until these issues are resolved. This factor, thus, favors Respondents.

5. The "Recognition of Wrongfulness" Factor Is Inapplicable.

The Division argues that the fifth *Steadman* factor—whether Respondents recognize their actions as "wrongful"—favors the Division. In this case, complying with the Division's Section 106 requests by producing work papers directly to the Division would have required Respondents to violate Chinese law on Chinese soil. The Division acknowledges as much: "[t]he Division does not argue that Respondents should have chosen to violate Chinese law, nor does the Division now seek to compel Respondents to do so." ENF Post-Hearing Brief at 120. Respondents had no ability to choose a course of action. This factor is, accordingly, inapplicable.

6. Respondents Will Not Have Opportunities For Future Violations Owing To Their Occupation.

The Division argues, without citation or elaboration, that the likelihood of future violations by the Respondents is "very high" and that its Proposed Bar is the "only" means of preventing the "near certainty of future violations by some or all of these Respondents." ENF Post-Hearing Brief at 120. This argument simply ignores the facts.

Respondents were not unable to produce documents in response to the Commission's Section 106 requests because they were predisposed to flouting their obligations. They were unable because providing the workpapers directly to the Division would have violated Chinese law and, as shown *supra* at Sections III and IV.B, the Division now has conceded that Chinese law and Chinese governmental directives did in fact prevent Respondents from directly producing requested documents to the SEC. Respondents were unable to provide the workpapers to the Division through the CSRC because the Division and the CSRC had not yet developed a

mechanism for sharing information. As shown at the hearing and evidenced by the Division's post-hearing disclosures, *see supra* at Section IV.C, the CSRC has now developed new procedures for producing documents to the SEC. This new protocol provides the Commission with an effective means of obtaining the documents from Respondents in the future. Under these new procedures, there is nothing about Respondents' status as China-based audit firms that suggests a risk of future violations different from other China-based audit firms or audit firms in the many other countries that place legal impediments on the production of documents directly to the Commission.[67]

Even if that were not the case, the Division's claim that its Proposed Bar is necessary to reduce the risk that it will be unable to obtain workpapers from China in the future is not supported by the evidence or even logic. The Division has offered no evidence suggesting that any of the audit firms that might replace Respondents would have a greater ability to produce workpapers directly to the Division than Respondents, and there is no reason to think that they would in fact produce such workpapers. In short, Respondents do not pose a heightened risk of future violations compared to the firms that might replace them. This factor, thus, favors Respondents.

B. Imposing Sanctions Would Be Fundamentally Unfair and Inconsistent With the Commission's Long-Standing Policies and Practices.

The Division maintains that Respondents made a "calculated gamble" and that they seek preferred treatment as compared to other audit firms around the world. The Division is wrong on both accounts. Respondents at all times acted openly and in good faith. They did so against the backdrop of repeated pronouncements from U.S. and China regulators regarding the need for

---

[67] Again, Dahua is not currently performing audits of U.S. issuers, and has no intention of doing so unless and until these issues are resolved.

collaboration and with an awareness of successful, collaborative agreements with other foreign governments.

1. Respondents Fully Disclosed the Foreign Legal Impediments In Their Registrations with the PCAOB.

In connection with their registrations, Respondents declined to sign Item 8.1 on their registration forms, which requested their unqualified consent to produce documents to the PCAOB upon request. Respondents Exs. 1; 40; 205; 365; and 513. The registrations included analysis of the applicable Chinese laws as well as offers to cooperate to the fullest extent permitted under applicable law. *Id.* Respondents were not alone, as accounting firms from more than 50 jurisdictions likewise faced legal restrictions. *See* Respondents Exs. 309 – 364.

The PCAOB—over which the Commission exercises comprehensive control—approved Respondents' registrations with the full knowledge that Respondents might be legally prohibited from producing documents upon request. As discussed *supra*, the PCAOB has similarly approved the registrations of dozens of other accounting firms from other countries that are in the same position. *See* Respondents Ex. 602. Clearly the PCAOB, and implicitly the Commission, have made a calculated decision that the benefits of allowing these firms to register and to keep their registrations, and allowing U.S. issuers in these countries to file audit reports, outweigh possible complications with document production down the road. It is incorrect to suggest that Respondents took a gamble or otherwise acted in bad faith in this situation.

2. For Three Decades the Commission Has Relied on Inter-Regulator Cooperation to Obtain Documents from Foreign Countries.

Respondents are among the dozens of accounting firms that work for U.S. issuer clients around the world in countries with strict data privacy, official secret or other similar laws. *See, e.g.,* Respondents Exs. 309-364. As discussed at length in Respondents' Pre- and Post-Hearing Briefs, these restrictions are so commonplace that the Commission and its counterparts in more

than 20 other countries have developed a web of Memoranda of Understanding ("MOUs") designed to help authorities navigate the laws and pursue effective cross-border enforcement of securities laws. *See* KPMG Huazhen's Pre-Hearing Brief at 18-21; Respondents' Post-Hearing Brief at 112-116. The efforts are consistent with recent statements from the Chairman of the Commission regarding the reconciliation of the U.S. regulatory system with requirements of the Commission's foreign counterparts. *See* Mary Jo White, Speech on Regulation in a Global Financial System (May 1, 2013), *available at* http://www.sec.gov/news/speech/2013/spch050313mjw.htm ("A defining fact of life at the SEC today is that we are not alone in the global regulatory space. And our duty to the investors, entrepreneurs, and other market participants who rely on us means that we must find common ground with our counterparts abroad, collaborate on everyday matters like enforcement and accounting, and knit together a regulatory network that offers protection, consistency, and stability to market participants—especially in the United States but abroad as well.").

The MOUs have resulted in a well-developed framework for handling exactly the kinds of requests at issue in this proceeding: work papers and other similar documents that are subject to data privacy protections in accounting firms' home countries. *See* KPMG Huazhen's Pre-Hearing Brief at 18-21. No other accounting firm has faced the kind of sanctions Respondents face here for simply abiding by the laws and directives of its home regulator. Instead, the Division has consistently worked through intergovernmental channels when requesting document productions from countries with data privacy controls. Pursuing documents directly—and threatening Respondents with sanctions for their inability to comply directly with the Division's impossible requests—is wholly inconsistent with the Commission's historical approach in this arena and its long-standing policies regarding cross-country collaboration. In

this regard, Respondents do not purport to "unilaterally exempt themselves from compliance" with U.S. law, but rather ask the Division to treat them as it treats all other similarly situated accounting firms.

The arbitrariness of the proposed sanctions is reflected not only in the Division's departure from the SEC's decades-long approach to cross-border regulatory cooperation, but in the Division's insistence that its proposed sanctions are justifiable based on their aggregate impact on Respondents collectively. *See* ENF Post-Hearing Brief at 129-30 ([redacted]). In fact, the impact of the proposed sanctions on Respondents is disproportionate and has no link to the alleged Section 106 violations. See Respondents' Post-Hearing Brief at 109-11.

3. Recent Production Developments Must Be Considered As A Viable Alternative.

The Division is wrong in stating that the CSRC's recent production of documents in the Longtop matter provides no evidence that inter-governmental channels might provide a means of obtaining the workpapers at issue here. ENF Post-Hearing Brief at 122. The production of the Longtop materials as well as the May 2013 MOU between the PCAOB and the CSRC, which explicitly allows the PCAOB to share with the SEC documents obtained pursuant to the agreement, certainly are relevant and demonstrate that a viable alternative exists. *See, e.g.,* KPMG's Pre-Hearing Brief at 20-21; *see also* Tr. 2319:12-2320:17 (the ALJ noted that the production of Longtop materials is relevant). And, as noted earlier, recent correspondence produced by the Division reveals that the SEC issued five new requests for assistance to the CSRC for the production of audit workpapers at issue in this proceeding. The SEC clearly interprets the Longtop production as proof of the CSRC's willingness to cooperate.

Moreover, the Division's claim that "the need remains to remedy Respondents' violations and make clear that future recipients of Section 106 requests must comply with them," ENF Post-Hearing Brief at 122, suggests that the proposed sanctions are intended as a general deterrent, which is—on its own—insufficient to support the imposition of sanctions and smacks of a punitive rather than remedial purpose. *See PAZ Sec., Inc. v. SEC,* 494 F.3d 1059, 1066 (D.C. Cir. 2007); *see also Touche Ross & Co. v. SEC,* 609 F.2d 570, 579 (2d Cir. 1979).

C. Sanctions Would Have Substantial Negative Consequences For Affected Issuers and Investors.

The Commission is required to engage in "reasoned decisionmaking," *Allentown Mack Sales & Serv., Inc. v. NLRB*, 522 U.S. 359, 374-75 (1998), in deciding whether imposing sanctions would be in the public interest. This requires it to consider all important aspects of the problem that the sanctions are meant to address. *See, e.g., Saad v. SEC*, No. 10-1195, 2013 WL 2476807, at *5 (D.C. Cir. 2013). It must also give reasoned consideration to the collateral impact sanctions would have on Respondents and on third parties, including issuers and investors. *See, e.g., PAZ*, 494 F.3d at 1065 ; *Saad*, 2013 WL 2476807, at *5.

The Division concedes that third parties would suffer negative collateral consequences from the sanctions it seeks. *See* ENF Post-Hearing Brief at 125. But it urges that these consequences should be ignored because (it claims) they are "tailored to limit collateral effects," ENF Post-Hearing Brief at 125, or because (it otherwise claims) quantifying them is "highly speculative," *id.* at 126. In effect, the Division argues that Respondents should be sanctioned without considering the costs to issuers, investors, or the securities markets. That position is not supported by the evidence or the law.

1. More Than [redacted] Issuers Would Be Affected by the Proposed Bar and Lose Their Auditors.

The evidence adduced at the hearing shows that at least [redacted] issuers with shares traded in the United States would be affected by the Division's Proposed Bar and would be forced to find new auditors or face delisting. [redacted][68]

[68] The Division attempts to disguise the impact of its Proposed Bar on the affected issuers by presenting its numbers as a percentage of Respondents' client base. [redacted] Whether these issuers constitute a large or small percentage of Respondents' clients is irrelevant. The impact of the Proposed Bar on *the issuers* is the same. In any event, to the extent it is relevant, the Division's calculations understate the percentage of Respondents' clients (for 2011) that would be affected by ignoring the issuers for which they served as principal auditor; [redacted]

[redacted]

2. There Are No Adequate Substitutes for Respondents.

The Division acknowledges that imposing the Proposed Bar against Respondents would cause numerous issuers to lose their chosen auditors. *See* ENF Post-Hearing Brief at 126. But it has given little consideration to, and has little concern for, what would happen after that. *See, e.g.,* Josephs Tr. 163:21-164:21.

In fact, the Division's response to the enormous gap that disbarring the vast bulk of the auditing profession from an entire country would create is simply to ignore the issue. [redacted]

[redacted]

[69] The Division fails to appreciate that there is no evidence as to what these firms might do if faced with a request for documents from the SEC or PCAOB. As the evidence at the hearing showed, these firms would be required to contact Chinese regulators upon receipt of a request, and there is no good reason to believe that these firms would not heed the directions of their Chinese regulators not to produce documents directly to the SEC – just as Respondents did here.

[redacted]

[redacted] As discussed at length in Respondents' Post-Hearing Brief, even assuming, *arguendo*, that these firms would be willing to replace Respondents and produce documents directly to the SEC upon request in violation of Chinese law, they are woefully inexperienced in auditing U.S. issuers when compared to Respondents and they lack the capacity to service a huge influx of new clients. They are not adequate substitutes. *See* Respondents' Post-Hearing Brief at 91-95.

[redacted]

[redacted] However, as discussed in Respondents' Post-Hearing Brief, to the extent that non-Chinese firms have produced workpapers to the SEC that actually were created in mainland China, they did so in violation of Chinese laws and regulations. *See* Respondents' Post-Hearing Brief at 43-46; *see also id.* at 95-96. The Division's suggestion that auditors that are ignorant of or willing to violate Chinese law would be regarded as adequate replacements for Respondents by the affected issuers—or could be so regarded by the Commission—is not worthy of consideration.

3. The Proposed Bar Will Very Likely Force Impacted Issuers to Delist or to Be Delisted.

[redacted]

[redacted] Instead, it offers only a sleight of hand, arguing that "at any rate, the vast majority of *Respondents' clients*"—as opposed to Respondents' clients *affected* by the Proposed Bar—"would not face this situation." *Id.* (emphasis added).

The reality is that each issuer affected by the Proposed Bar would be forced to try to obtain a replacement auditor from a small pool and, if those efforts fail, either delist or be delisted. Becker Tr. 2617:23-2618:25. Obviously, whether an individual issuer will be successful in this scramble against [redacted] other issuers cannot be predicted with specificity. [redacted] Thus, the risk that a substantial number of issuers will find themselves without auditors must be regarded as being quite high and must be taken into account in determining whether sanctioning Respondents is in the public interest.

4. Delisting Would Harm U.S. Investors.

Academic research shows that companies that delist and transition to the "Pink Sheets" or other over-the-counter markets experience a significant decline in share price. *See* Simmons Expert Report ¶ 45. Dr. Simmons demonstrates that the most relevant literature predicts an average drop of 50 percent for stocks listed on the NYSE and 19 percent for stocks listed on the

Nasdaq. *See id.* Based upon those figures, [redacted] *See id.*

The Division does not dispute that delistings caused by the Proposed Bar would inflict substantial harm on investors. It does not question that delisting of a company's shares results in a drop in the price of those shares. *See, e.g.*, Becker Tr. 2639:17-23. Instead, it argues that the drop in the share prices of the affected issuers would be smaller than that estimated by Dr. Simmons. *See, e.g.*, Becker Tr. 2584:14-2585:7. For the reasons stated in Respondents' Post-Hearing Brief, the studies relied upon by Dr. Simmons provide the best estimate of the likely magnitude of the drop associated with what would occur here: involuntary delistings for failure to file audited financial statements. *See* Respondents' Post-Hearing Brief at 100-02. But even if a delisting forced by the Proposed Bar could (as Dr. Becker advocates) be likened to a voluntary delisting by an issuer, the Division's expert still estimated that the likely price drop would be between 0.85 and 10 percent. *See* Becker Report ¶¶ 34-37. [redacted][70]

In short, regardless of which academic study is the most relevant to estimating the impact of delistings resulting from the Proposed Bar, the harm to third parties would be substantial. The

---

[70] The Division contends that these losses to investors in the issuers affected by the Proposed Bar should be weighed against the purported benefits to the securities markets as a whole from "rigorous enforcement of disclosure obligations." ENF Post-Hearing Brief at 129. The studies showing these purported benefits did not deal with the production of workpapers by auditors. *See* Becker Tr. 2637:13-19. In any event, the Division makes no attempt either (1) to show how sanctioning Respondents for failure to produce documents would result in greater or more compliant disclosure by issuers (the focus of the studies on which Dr. Becker relied) or (2) to quantify the benefits to the markets from sanctioning Respondents in this case. Thus, the Division offers no reason to think that those benefits would remotely offset the multi-billion dollar losses individual investors would likely suffer as a result of the Proposed Bar.

Commission cannot ignore the collateral impact of a proposed sanction on third parties. *See, e.g.*, *PAZ*, 494 F.3d at 1065; *Saad*, 2013 WL 2476807, at *5. Instead, it must take it into account in deciding whether sanctions truly are in the public interest or would instead amount to punishment of Respondents. When the natural and probable consequences of the Proposed Bar are fully considered, it is evident that it is not in the public interest and should not be imposed.

VII. CONCLUSION

For the foregoing reasons, the Division failed to meet its burden of proving that Respondents willfully refused to comply with the Section 106 requests, and in any event, any sanction against Respondents in these circumstances would be impermissibly arbitrary and capricious, unwarranted, and contrary to the public interest.

Dated: September 20, 2013

Respectfully submitted,

(*Signatures on next page*)

Dated: September 20, 2013

Respectfully submitted,

DLA PIPER LLP
Deborah R. Meshulam
Grayson D. Stratton
500 8th Street, N.W.
Washington, D.C. 20004
Tel: (202) 799-4000

Counsel for Respondent Dahua CPA Co., Ltd. (Formerly BDO China Dahua CPA Co., Ltd.)

ORRICK, HERRINGTON & SUTCLIFFE LLP
Richard A. Martin
Robert G. Cohen
James A. Meyers
51 West 52nd Street
New York, New York 10019
Tel: (212) 506-5000

Counsel for Respondent Ernst & Young Hua Ming LLP

SIDLEY AUSTIN LLP
Neal E. Sullivan
Griffith L. Green
Timothy B. Nagy
1501 K Street, N.W.
Washington, D.C. 20005
Tel: (202) 736-8000

Counsel for Respondent KPMG Huazhen (Special General Partnership)

LATHAM & WATKINS LLP
Miles N. Ruthberg
Jamie L. Wine
Latham & Watkins LLP
885 Third Avenue
New York, New York 10022
Tel: (212) 906-1200

James J. Farrell
Latham & Watkins LLP
355 South Grand Avenue
Los Angeles, California 90071
Tel: (213) 485-1234

SIDLEY AUSTIN LLP
Michael D. Warden
Sidley Austin LLP
1501 K Street, N.W.
Washington, D.C. 20005
Tel: (202) 736-8000

David A. Gordon
Sidley Austin LLP
One South Dearborn
Chicago, Illinois 60603
Tel: (312) 853-7000

Counsel for Respondent Deloitte Touche Tohmatsu Certified Public Accountants Ltd.

DAVIS POLK & WARDWELL LLP
Michael S. Flynn
Gina Caruso
450 Lexington Avenue
New York, New York 10017
Tel: (212) 450-4000

Counsel for Respondent PricewaterhouseCoopers Zhong Tian CPAs Limited Company